# Annual Report
## Rheinmetall AG

# 2011

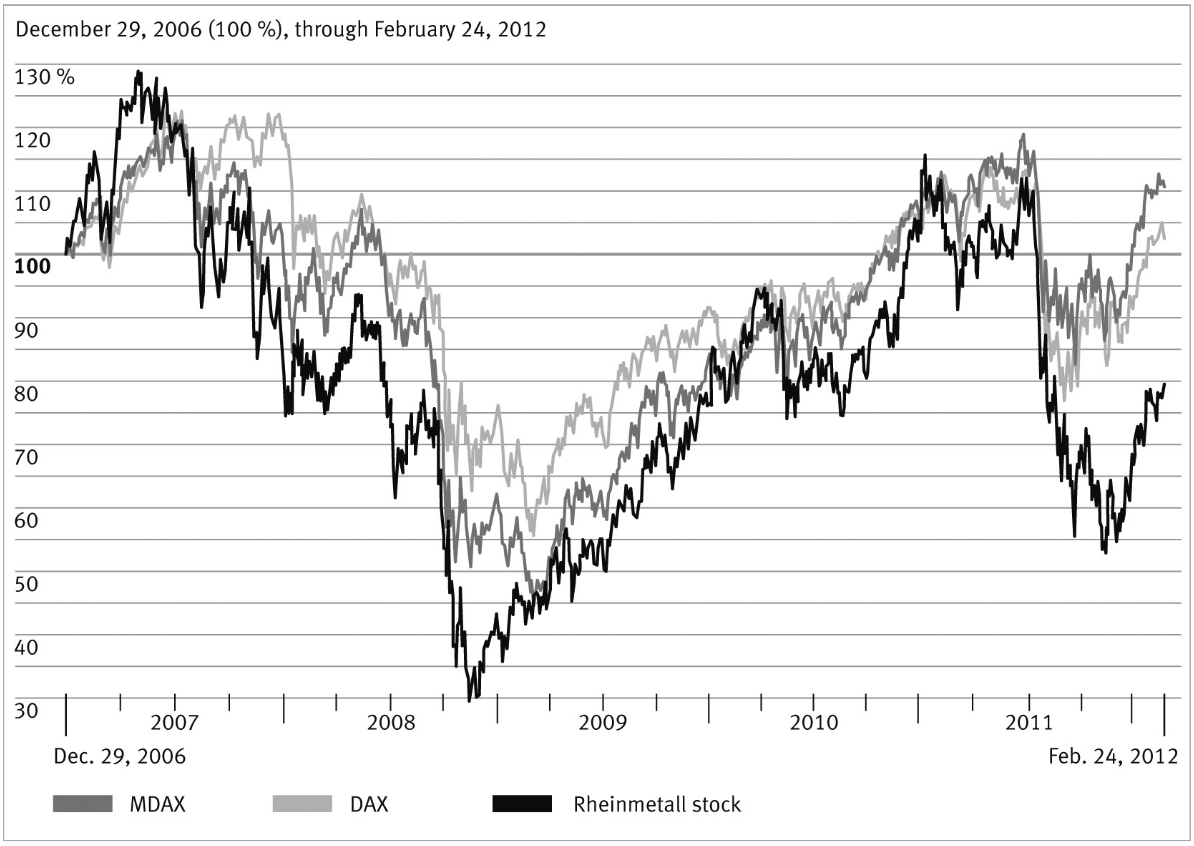
# Rheinmetall in figures

## Rheinmetall Group indicators

| | | 2007 | 2008 | 2009 | 2010 | 2011 |
|---|---|---|---|---|---|---|
| Sales | *€ million* | 4,005 | 3,869 | 3,420 | 3,989 | 4,454 |
| Order intake | *€ million* | 4,040 | 3,780 | 4,649 | 3,974 | 4,189 |
| Order backlog (Dec. 31) | *€ million* | 3,239 | 3,683 | 4,940 | 5,136 | 4,950 |
| EBITDA | *€ million* | 438 | 411 | 180 | 464 | 538 |
| EBIT [1] | *€ million* | 270 | 245 | 15 | 297 | 354 |
| EBT [1] | *€ million* | 213 | 193 | (46) | 229 | 295 |
| Net income [1] | *€ million* | 150 | 142 | (52) | 174 | 225 |
| Cash flow | *€ million* | 352 | 308 | 120 | 344 | 402 |
| Capital expenditures | *€ million* | 202 | 200 | 145 | 189 | 207 |
| Amortization/depreciation/impairment | *€ million* | 168 | 166 | 165 | 167 | 184 |
| Total equity [1] | *€ million* | 1,059 | 1,080 | 1,134 | 1,355 | 1,546 |
| Total assets [1] | *€ million* | 3,448 | 3,612 | 3,835 | 4,460 | 4,832 |
| EBIT margin | *in %* | 6.7 | 6.3 | 0.4 | 7.4 | 7.9 |
| ROCE [1] | *in %* | 14.5 | 12.5 | 0.8 | 14.6 | 14.9 |
| | | | | | | |
| Stock price, annual high | € | 74.12 | 53.81 | 44.74 | 60.17 | 66.46 |
| Stock price, annual closing | € | 54.38 | 22.90 | 44.74 | 60.17 | 34.24 |
| Stock price, annual low | € | 48.04 | 16.82 | 20.41 | 42.50 | 30.35 |
| Earnings per share (EpS) [1] | € | 4.15 | 4.09 | (1.60) | 4.23 | 5.55 |
| Dividend per share | € | 1.30 | 1.30 | 0.30 | 1.50 | 1.80 |
| Employees (Dec. 31) according to capacity | | 19,185 | 21,020 | 19,766 | 19,979 | 21,516 |

[1] *From 2008, recognition in equity of actuarial gains/losses*

## Rheinmetall stock price trend in comparison to DAX and MDAX



# An overview of the Rheinmetall Group


## Defence

### Weapon and Munitions
Direct fire
Indirect fire
Infantry
Protection systems
Plant engineering

### Propellants
Propellant systems
Civil chemistry

### Land Systems
Wheeled vehicles
Tracked vehicles
Turret systems
Service

### Air Defence
Air defence systems

### C4ISTAR
Reconnaissance
Command
Fire control
Airborne systems

### Simulation and Training
Flight simulation
Land simulation
Maritime and process simulation


# Automotive

## KS Kolbenschmidt
Passenger car pistons
Commercial vehicle pistons
Large-bore pistons
Piston systems

## Pierburg Pump Technology
Oil pumps
Vacuum pumps
Water circulation
and coolant pumps

## KS Gleitlager
Metallic plain bearings
Permaglide®
Continuous castings
Large bearings

## Pierburg
Air management
Actuators
Emission reduction
Solenoid valves
Commercial diesel systems

## KS Aluminium-Technologie
Aluminum alloy
engine blocks
Cylinder heads
Final machining

## Motor Service
Aftermarket components

# Contents

# Report of the Supervisory Board

**»Close cooperation between the Supervisory Board and Executive Board«**

In the 2011 fiscal year, the Supervisory Board once again performed the advisory and supervisory duties for which it is responsible in accordance with the law, the Company bylaws, the German Corporate Governance Code and the Supervisory Board rules of procedure with the utmost diligence. In order to ensure good corporate governance, constructive cooperation between the Executive Board and Supervisory Board was characterized by trusting and open dialog. In four scheduled ordinary Supervisory Board meetings and two extraordinary Supervisory Board meetings, as well as eight committee meetings, the members of the Supervisory Board focused on the position of the Rheinmetall Group and its Defence and Automotive sectors. The members of the Supervisory Board performed their activities with a great sense of responsibility and dedication. No member of the Supervisory Board attended fewer than half the meetings. With two exceptions, all committee meetings in the year under review were attended by all members.

A number of key issues and various transactions requiring approval were addressed in the consultations and discussions held by the Supervisory Board. In addition to the development of the business trend, earnings and financial position of the Rheinmetall Group, the operating and economic performance of the Defence und Automotive sectors, the HR situation, the risk situation and risk management were discussed, as well as compliance in the Company. Economic trends and general conditions in the international competitive environment, as well as opportunities and risks in key growth markets, were also examined. Topics discussed also included the potential consequences of the natural disaster in Japan for the Automotive business and the development of global defence expenditure and procurement budgets and the associated impact on the business activities of Rheinmetall Defence. The turmoil on the financial and foreign exchange markets and the resulting changes and uncertainty in the economic environment were also discussed. As part of its reports on the business situation, the Executive Board also provided information on measures taken to improve efficiency and productivity and on change processes taking place within the organization, with the aim of ensuring the competitiveness of the operating units.

All developments, measures and decisions of significance to the Rheinmetall Group were discussed and deliberated on in detail in the Supervisory Board based on information provided by the Executive Board verbally and in writing. The Executive Board informed the Supervisory Board in good time of any matters requiring approval in accordance with the law, the Company bylaws or the rules of procedure. Following thorough discussion and examination, the Supervisory Board cast its vote on the detailed and informative draft resolutions.

Between meetings, the Supervisory Board was informed of the economic and financial situation of the Rheinmetall Group by means of the quarterly written reports.

In addition to the Board meetings, the Supervisory Board Chairman and CEO were in regular close contact and communicated on the progress of business activities, significant developments and corporate options in a number of work meetings.

Based on detailed reports and presentations and the information provided by the Executive Board, the Supervisory Board carried out a critical examination of the Company's management. It is convinced of the legality and propriety of management by the Executive Board and of the performance of the organization. This includes the effectiveness of the compliance organization, the internal control system and the risk management system.

### »Focus of discussions and reviews carried out by the Supervisory Board«

At its extraordinary meeting held on January 31, 2011, the Supervisory Board addressed the increase in the stake held in ADS Gesellschaft für aktive Schutzsysteme mbH, a specialist in protection technology, from the stake held up to then of 25% to 74%. The Executive Board presented the strategic approach and the technological and operational advantages associated with this measure to be taken under company law. Following in-depth discussion, the Supervisory Board followed the recommendation of the Executive Board and approved the acquisition of further shares.

The focus of the annual accounts meeting on March 22, 2011 was discussion of the single-entity and consolidated financial statements certified by PricewaterhouseCoopers (PwC) together with the summarized management report for Rheinmetall AG and the Rheinmetall Group as at December 31, 2010 and the Executive Board's proposal for the appropriation of net income for the year. The auditors reported on the audit approach and development of the audit, material findings and the results of their audits. Both the Executive Board and PwC provided comprehensive answers to the questions of the Supervisory Board. Taking into account the expectations of shareholders and the capital market, and after considering the Company's financial situation, the Supervisory Board approved the Executive Board's proposal for appropriation of net income. As part of its reports on the business situation, the Executive Board gave an account of the potential impact of the earthquake and nuclear incident in Japan on international automotive business. It explained the precautions taken by the Automotive sector in the event that automotive manufacturers decided to reduce the requisition level for parts. The agenda for the 2011 Annual General Meeting, including the draft proposals, was approved by the Supervisory Board. Following in-depth discussion, the Supervisory Board determined that current Executive Board remuneration was appropriate.

In its meeting on May 9, 2011, the Supervisory Board discussed the Annual General Meeting which had been convened for the following day. Business development in the first quarter of 2011 was also presented and the current business situation was discussed. The results of the shareholder analysis carried out in January 2011 were presented. The Executive Board also gave a review of the annual meeting of the senior management of Rheinmetall AG, which includes around 270 staff. This event, which is traditionally held in April, focused on the themes of operational excellence, innovation and internationalization.

At the second extraordinary meeting on July 28, 2011, the items on the agenda included the future strategic and corporate orientation of the Rheinmetall Group together with its Defence and Automotive sectors. The Executive Board outlined the prospects, challenges and opportunities for successfully strengthening the Company's competitive position in each of its industries and stated that, due to limited financial capacity, it may not be possible to invest sufficient amounts of funds in all divisions equally on a long-term basis in order to exploit these opportunities evenly. The Executive Board explained its decision to review the sustainability of the two-pillar strategy of the Rheinmetall Group and to analyze potential courses of action. It stated that, within this context, options including an IPO of the Automotive subsidiary KSPG AG were being examined, as well as continuing with the current corporate structure. The Supervisory Board acknowledged and approved the course of action which was presented in detail.

At the Supervisory Board meeting on August 31, 2011, the Executive Board presented the half-yearly financial report and its assessment of the overall expected business development for 2011. The Executive Board also informed the Supervisory Board of the results of the review into the sustainability of the two-pillar strategy, the pros and cons of the alternative courses of action determined and the status of its deliberations. The development of national and international defence budgets and the status of various major projects in the Defence sector were also discussed.

# Report of the Supervisory Board

The Supervisory Board convened for its fourth ordinary meeting on December 13, 2011. The Executive Board presented its report for the third quarter of 2011. It informed all those present of the current business situation of the Rheinmetall Group and presented its projected key figures for the 2011 fiscal year. The Supervisory Board was then informed in detail of the medium-term corporate planning for 2012 to 2014, including financial, capex and HR planning, and the assumptions made by the Executive Board in preparing this corporate plan were discussed extensively. Following in-depth discussion, the Supervisory Board acknowledged the corporate planning for 2012 to 2014 and approved the framework capex plan for 2012. It also passed a resolution to mandate PwC, which was elected at the Annual General Meeting on May 10, 2011, to audit the single-entity financial statements, the consolidated financial statements and the summarized management report for Rheinmetall AG and the Rheinmetall Group for the 2011 fiscal year. The Supervisory Board approved the Executive Board's request to integrate a Defence product group into a joint venture to be established with an industrial partner. It also approved a new syndicated loan of €500 million, with which a €400 million syndicated loan facility dating from April 2005 is to be replaced earlier than scheduled. At the recommendation of the Personnel Committee, the Supervisory Board appointed Armin Papperger, who has up to now been a member of the Management Board Defence, as a member of the Executive Board of Rheinmetall AG for five years with effect from January 1, 2012, where he will be responsible for the Defence sector. The Supervisory Board also carried out its annual review of the efficiency of its activities, which included looking at organizational workflows, the distribution of duties and communication between the Board and its committees, the routing of information from the Executive Board and the interaction of the two boards. The form, manner and content of this interaction were given a positive assessment, and further possibilities for optimizing the work of the Supervisory Board were discussed. The Supervisory Board considers the Board to have a sufficient number of independent members.

### »Activities in the committees«

The work of the Supervisory Board is supported by four permanent committees which it has established. The members of these committees relieve the burden of work of the Supervisory Board by preparing time-consuming topics requiring extensive discussion as well as meetings of the Board, and examining draft proposals in advance. The committees act in accordance with the law, the Company bylaws, the rules of procedure adapted to the duties of the Supervisory Board and the rules of procedure of the respective committee. Where legally possible, the committees also have decision-making powers if these are transferred by the Supervisory Board. With the exception of the Nomination Committee, which consists of two shareholder representatives, all committees are based on equal representation, with two shareholder representatives and two employee representatives. The Supervisory Board Chairman presides over all committees. He informed the Supervisory Board of each of their activities in the subsequent plenary meeting. The composition of these committees is presented on page 57.

The Personnel Committee, which prepares personnel decisions of the Supervisory Board and resolution recommendations regarding the remuneration system for the Executive Board, met once in March and twice in November 2011. In the year under review, the Committee dealt with topics including legal regulations and current developments relating to remuneration for Executive Board members. It discussed issues concerning the structure and amount of Executive Board remuneration as well as targets for the Executive Board. The Committee also made preparations for the appointment of Armin Papperger as a member of the Executive Board of Rheinmetall AG from January 1, 2012.

At its meetings in March, May, July, November and December 2011, the Audit Committee addressed the single-entity and consolidated financial statements and the Executive Board's proposal for the appropriation of net income and the dividend, monitoring the accounting process and the effectiveness of the internal control system, the risk management system and the internal auditing system. Before the publication of the quarterly accounts, the quarterly results were discussed in detail with the Executive Board. The Audit Committee obtained the declaration of independence from the auditors required in accordance with the German Corporate Governance Code and prepared the Supervisory Board's proposal to the Annual General Meeting for the election of the auditor for fiscal 2011.

Other important issues at the meetings included the conditions of the new syndicated loan concluded in fiscal 2011 and the further development of risk management and compliance management. At its December meeting, reports on the audits carried out during the year were submitted and the Internal Auditing progress report was presented. As part of this review, the Audit Committee was informed of the implementation status of the improvement measures established in the 2010 fiscal year. The Chief Compliance Officer also presented the compliance report for 2011 and gave an overview of the status of the compliance organization.

It was not necessary to convene the Mediation Committee formed in accordance with Section 27 (3) of the German Codetermination Act (MitbestG) during the past fiscal year.

The Nomination Committee, which comprises shareholder representatives and which submits to the Supervisory Board a slate of suitable Supervisory Board candidates for election by the Annual General Meeting in the event of upcoming re-elections, did not meet in 2011.

### »Corporate governance«

At its meeting on December 13, 2011, the Supervisory Board examined the contents of the German Corporate Governance Code as amended up to May 26, 2010. The annual declaration of conformity to be submitted together with the Executive Board in accordance with Section 161 of the German Stock Corporation Act (AktG) regarding compliance with the recommendations of the German Corporate Governance Code at Rheinmetall AG was approved and made permanently available for shareholders to view on the Internet at www.rheinmetall.com. It is also published on page 54 of this annual report. The Company confirms that, since it issued its last declaration in December 2010, it has carried out, continues to carry out and will in future carry out all recommendations of the German Corporate Governance Code. In their combined corporate governance report, the Executive Board and Supervisory Board provide information on corporate governance at Rheinmetall in accordance with Item 3.10 of the current German Corporate Governance Code on pages 54 to 60.

There have been no indications of conflicts of interest relating to mandates among members of the Supervisory Board or Executive Board in fiscal 2011 in connection with advisory activities or positions on the boards of other companies which would need to be disclosed to the Supervisory Board immediately and notified in the Annual General Meeting. No former members of the Executive Board of the Company belong to the Supervisory Board.

The auditor submitted a declaration of independence in accordance with Item 7.2.1 of the German Corporate Governance Code. The requirements of Item 7.2.3 of the German Corporate Governance Code regarding the contractual relationship between the Company and the auditor have been fulfilled. During the audit of the annual financial statements, no inaccuracies were noted in the declaration submitted by the Executive Board and Supervisory Board regarding the German Corporate Governance Code.

### »HR matters«

No changes were made to the composition of the Rheinmetall AG Supervisory Board and Executive Board during the period under review.

### »Adoption of the single-entity and consolidated financial statements 2011«

In December 2010, in accordance with the resolution of the Annual General Meeting of May 10, 2011, the Supervisory Board mandated PwC, Frankfurt am Main, Düsseldorf branch, to audit the single-entity and consolidated financial statements for the 2011 fiscal year. The scope and focal areas of the audit had been decided on in advance by the Audit Committee.

# Report of the Supervisory Board

The single-entity financial statements prepared by the Executive Board in accordance with German GAAP and the consolidated financial statements prepared on the basis of Section 315a of the German Commercial Code (HGB) in conformity with the International Financial Reporting Standards (IFRS) as required in the European Union, together with the summarized management report for Rheinmetall AG and the Rheinmetall Group for fiscal 2011, including the accounts, were audited by PricewaterhouseCoopers in accordance with statutory regulations and were issued with an unqualified auditor's opinion. The auditor conducted the audit in accordance with German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW).

All members of the Supervisory Board were presented with the single-entity and consolidated financial statements documentation, the resolution on the appropriation of net income and the audit reports submitted by the auditors in good time in order to ensure an in-depth, thorough review. The statutory auditors who signed the audit reports attended both the Audit Committee proceedings held on March 13, 2012 and the annual accounts meeting of the Supervisory Board held on March 20, 2012. They reported on the scope of their audit and areas that they focused on as well as any significant findings and answered questions put forward by the Supervisory Board.

The statutory audit report contains no mention of, or reference to, any misstatement or misrepresentation in the declaration of conformity according to the German Corporate Governance Code.

The audit performed in line with Section 91 (2) AktG concluded that the Company has an appropriate early risk identification system that conforms to statutory regulations. The auditor confirmed that the methods defined by the Company for the management, identification and monitoring of risks incurred are suitable for these purposes and that the summarized management report for Rheinmetall AG and the Rheinmetall Group presents a true, fair and reasonable view of the risks and opportunities of Rheinmetall's future development.

In accordance with the conclusive findings of its own review and on the basis of the Audit Committee's report and recommendation, the Supervisory Board concurred with the statutory auditor's conclusions and approved the single-entity and consolidated financial statements for fiscal 2011. The single-entity financial statements have thus been adopted under the terms of Section 172 AktG. The Supervisory Board approved the summarized management report, particularly the assessment of Rheinmetall's further development. It also approved the Executive Board's proposal for the appropriation of net income for the year, including the distribution of a dividend of €1.80 per share for the year under review.

Rheinmetall ended the demanding and challenging 2011 fiscal year with a very good result. The members of the Supervisory Board wish to thank the customers of companies in the Rheinmetall Group and shareholders for the confidence they have shown in such diverse ways. The Supervisory Board would like to express its gratitude to the Executive Board, executives and employees for their enthusiastic involvement and their high level of personal commitment and thanks them for their successful work in ensuring the well-being of the Company and the shareholders.

Düsseldorf, March 20, 2012
On behalf of the Supervisory Board

Klaus Greinert
Chairman

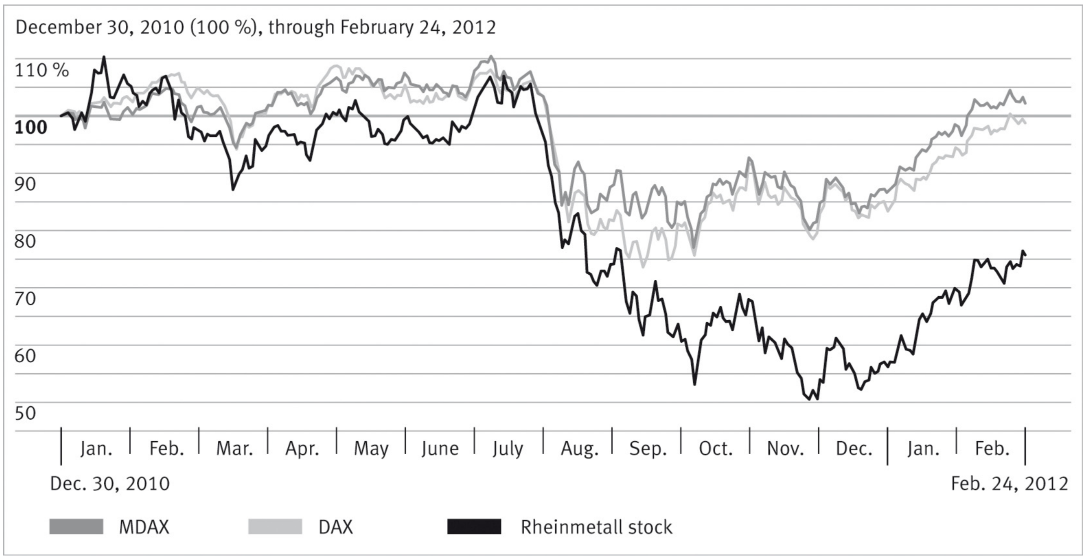
# Rheinmetall on the capital markets

**»Performance on the stock markets«**

Following extremely successful development during the 2010 trading year, which followed the global economic crisis of 2008/2009, the DAX and MDAX indices recorded a sideways movement in the first six months of 2011. From mid-February 2011 onwards, these indices fell by almost 10 % – a fall which was amplified by the natural disaster in Japan – but then began to recover quickly. The DAX posted its annual high on May 2, 2011 at 7,528 points, while the MDAX reached its annual peak of 11,187 points around two months later on July 7, 2011.

The ongoing problems in the euro zone, which came to bear in the form of downgrades of the ratings of several nations and discussions regarding the prevention of state bankruptcies, particularly in Greece, meant that fears surrounding the effects of the financial and state budget crisis on the real economy mounted in summer. Numerous investors began to anticipate a recession. Due to this culmination of negative expectations, the previously positive sentiment on the stock exchange shifted and led to severe share price losses in August and September 2011. The DAX fell in value by around 30 % within six weeks and posted its annual low on September 12, 2011 at 5,072 points. The MDAX experienced a similar development, reaching its lowest point on October 4, 2011 with 7,783 points.

As confidence in the action being taken to overcome the crisis grew in the wake of several EU summit meetings and government changes, a slight upward trend was seen on the capital markets, which was nevertheless characterized by high volatility. However, the indices no longer succeeded in closing the gap on the level seen in the first six months of the year. The DAX closed the trading year on December 30, 2011 at 5,898 points and the MDAX at 8,898 points. This meant significant losses in value for the indices in 2011 – the DAX fell by 15% and the MDAX by 12%.



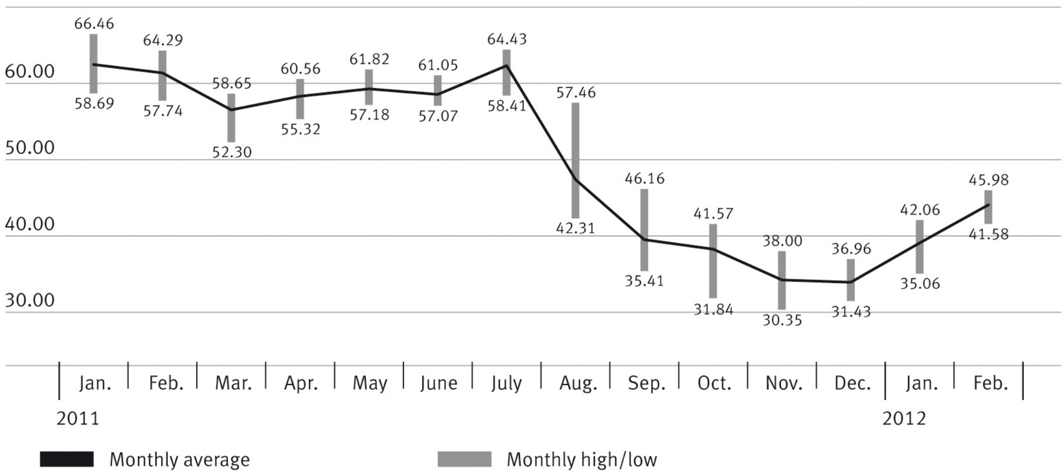

**»Rheinmetall share price performance«**

In 2011, the Rheinmetall share initially continued with the rapid price rise seen in December 2010 – posting an increase of over 20% in this month alone – whereby the share price shot up to its annual high of €66.46 by January 18, 2011. The listing then performed largely parallel to the MDAX up to the start of May. Following the publication of figures for the first quarter of 2011, the capital market priced Rheinmetall at below average compared to the indices. However, the share caught up fully again by July 2011. In the wake of the sharp price decline on the stock exchanges, triggered by the severe uncertainty of the stock markets and the growing fear of recession, the share price fell considerably below the level of the DAX and MDAX from August 2011 onwards. While the Rheinmetall share was forced to contend with fears regarding falling defence budgets of Western nations back in the first six months of the year, added to this now were concerns on the part of investors regarding an economic downturn and, associated with this, fears of a fall in earnings in the Automotive business.

# Rheinmetall on the capital markets

Both assessments put the share under pressure, meaning that it experienced an above-average fall in value from July 2011 onwards. It reached its annual low on November 25 at €30.35, after which it began to recover again. The share price stood at €34.24 on the last trading day of 2011, which corresponds to a decline of 43 % in fiscal 2011. However, the more pessimistic assessment gradually began to diminish again at the end of the fiscal year and the price rose to €45.98 by February 24, 2012.

January 2011 through February 2012




**»Ranking in the MDAX«**

The above-average loss in the price of the Rheinmetall share was also reflected in the market capitalization. The Rheinmetall share took 17th place in the rankings of Deutsche Börse at the end of the year under review, following its 10th place ranking on the balance sheet date of the previous year. With a constant number of 39,599,000 shares and a free float of almost 97 %, this resulted in a stock market value of €1.3 billion as at the end of 2011.

Significant improvement was seen in the other key criterion for MDAX membership, the share trading volume. The average daily trading volume of the Rheinmetall share rose significantly, from approximately 234,000 shares in 2010 to 276,000 shares in the year under review. The liquidity of the share, which increased again as a result of this, and which is also an important investment criterion for institutional investors, led to an improvement in the share's position in the rankings for stock exchange turnover, rising from 14th place in 2010 to 12th place in 2011.

**»Dividend distribution«**

The Rheinmetall Group will continue its shareholder-friendly distribution policy in fiscal 2011. The Executive Board and Supervisory Board will propose a dividend of €1.80 for the year under review, which corresponds to a dividend yield of 5.3 % based on the 2011 closing price of €34.24. The payout ratio, i.e. the dividend in relation to earnings per share, will therefore stand at over 30 % once again.

**»Shareholding structure«**

The results of the shareholder analysis commenced in November 2011 showed a broad and diversified shareholding structure with a focus on European investors. Investors from this region held 57 % of the shareholdings in Rheinmetall AG, while 30 % of the capital related to North American investors and 3 % of shares were owned by Rheinmetall AG.

### »Disclosures regarding changes in the share of voting rights«

In fiscal 2011, investors informed the Company that they had exceeded or dropped below the reporting thresholds for changes in the share of voting rights that need to be disclosed in accordance with Section 21 of the German Securities Trading Act (WpHG). Rheinmetall AG notified the capital markets of this in accordance with Section 26 of the German Securities Trading Act (WpHG) and also informed the general public of these changes on its homepage in the Investor Relations section. At the end of 2011, the investment companies Black Rock Inc., New York, USA, and Harris Associates L.P, Chicago, USA, respectively held more than 5% and more than 10% of Rheinmetall shares.

### »Treasury stock«

Rheinmetall AG continued to exercise its right to repurchase treasury shares in fiscal 2011. The proportion of own shares held as treasury stock was 3.4 % (1,350,842 shares) at the end of the 2011 fiscal year, compared to 3.3% or 1,293,198 shares on the previous year's balance sheet date. In 2011, the Company purchased 333,025 shares, of which 169,743 shares entered the employee share purchase program and 105,638 shares entered the long-term incentive program. On February 9, 2012, Rheinmetall AG held 1,547,842 shares or 3.9%.

### »Share purchases by the management«

Members of the Supervisory Board and Executive Board and related parties together held 437,853 shares or 1.1% of the common stock as at December 31, 2011 as was also the case on the 2010 balance sheet date. The Executive Board holds 89,313 shares or 0.2%, the Supervisory Board 348,440 shares or 0.9%.

### »Employees as shareholders«

The option to purchase Rheinmetall shares at special rates was offered in April and November 2011. On these occasions, eligible staff purchased 169,743 shares which are subject to a two-year lockup period. Since the first employee share purchase program in 2008, Rheinmetall employees have purchased 680,454 shares in total, of which 54,502 shares have been taken up by European employees since the introduction of the European employee share purchase program in 2010.

### »Communication with capital market participants«

The aim of the Rheinmetall Group's capital market communication is to ensure ongoing and open dialog with shareholders, potential investors and financial analysts and, in so doing, to lay the groundwork for a fair and realistic assessment of the Rheinmetall share on the capital market. In order to achieve this aim, Rheinmetall held more than 230 meetings with investors and analysts in fiscal 2011. A large proportion of these took place at a total of 15 investor/analyst conferences and road shows. Destinations comprised the major financial centers in Europe and North America, including London, Frankfurt am Main, Paris, Zurich, Edinburgh and New York. In addition to these, a number of one-on-one discussions were held during investor visits and telephone conferences. Here, the management – in most cases with the direct involvement of an Executive Board member – actively provided comprehensive information regarding the business development, corporate strategy and future prospects of the Company.

These extensive activities have helped to generate a great deal of interest in Rheinmetall on the capital market and also mean that international brokers are still extremely interested in ensuring active coverage by equity research analysts. As at December 31, 2011, a total of 23 equity research analysts reported regularly on the business development of Rheinmetall AG in comprehensive studies. Here, the analysts perform an important task in informing investors of current events and developments. Trusting and open communication with these institutes represents a key aspect of the investor relations work of the Rheinmetall Group. With 14 buy recommendations at the end of the year, around two thirds of the analysts assessed the potential of the Company as high. Eight analysts gave the share a "hold" recommendation, while just one analyst gave the share a "sell" rating.

# General economic conditions

### »Robust real economy in 2011 – debt crisis weighs on the global economy«

Following a dynamic phase of growth between January and June 2011, the turmoil seen on the financial and foreign exchange markets since August led to a gradual slowdown in the global economy. Despite robust development in the real economy compared to that seen during the 2008/2009 global economic crisis, the second half of the year was characterized by growing concerns regarding the stability of the euro zone and an increased risk of recession. In September, the International Monetary Fund (IMF) lowered its forecast for growth in the global economy in 2011 to 4.0 % from the 4.3 % it had been expecting in June 2011.

In November 2011, the Organization for Economic Cooperation and Development (OECD) confirmed that the global economy had “deteriorated significantly” since its Economic Outlook the previous year. Here, it stated that the euro crisis was the biggest threat to global economic development, and that the risk potential was heightened by the fact that contagion had now spread to countries with finances that were previous regarded as relatively stable.

Economic experts at the OECD calculated economic growth of 1.9% in 2011 for its 34 member states. As the largest economy amongst the mature industrialized nations, the USA achieved growth of 1.7 % according to the OECD study, while Japan saw a 0.3% decline in gross domestic product as a result of the earthquake and tsunami disaster in March 2011. Economic output in the euro zone increased by 1.6% in 2011, led by the economic driving force that is Germany, where the gross domestic product achieved strong, above-average growth of 3.0%. Here, the German economy benefited in particular from the ongoing strength of domestic demand, as private consumer spending rose, and companies invested more in machinery and vehicles. The ifo business climate index, which serves as a leading indicator of economic development in Germany, also posted a positive surprise towards the end of the year. In November 2011, the business expectations of trade and industry had improved slightly for the first time in four months. The ifo Institute therefore came to the conclusion that the German economy was continuing to do comparatively well against the backdrop of international jitters. Nevertheless, the economic experts all agreed that even the German economy would not be able to completely distance itself from the negative effects of the economic uncertainties brought about the euro crisis and debt crisis. Tellingly, the report for fall issued by the leading German economic research institutes was published under the heading of “Adverse Effects on the German Economy from the European Debt Crisis”.

The emerging countries continued to achieve strong growth in 2011, although momentum also began to slow. After still achieving low double-digit growth in 2010, the OECD calculated growth of 9.3% for the Chinese economy in 2011. According to the OECD, the gross domestic product in India was up 7.7% year-on-year in 2011.

### »Slight growth in global defence expenditure once again in 2011«

In the year under review, in addition to the need to consolidate budgets in a number of countries, the development of global defence expenditure was also characterized by the mission-specific ongoing need for substantial modernization of military equipment. According to the calculations of experts at IHS Jane’s, global defence expenditure rose slightly once again in 2011 to USD 1,570 billion. While cuts were reported in expenditure for military personnel and in the area of military research and development, global expenditure for the procurement of equipment increased by over 4 % in 2011 to USD 362 billion.

According to analysts from IHS Jane's, emerging countries such as Brazil and India in particular saw large increases in defence budgets in 2011. Some budgets in countries in the Middle East and North Africa (MENA) region also increased significantly in the year under review. In the USA, the country with the highest defence spending in the world, the 2011 defence budget was almost 2.6% down on the figure for the previous year, at approximately USD 711 billion, despite the considerably intensified debt situation. In Germany, the available defence budget for 2011 stood at €31.6 billion, slightly up on the previous year's figure of €31.1 billion. At €6.2 billion, expenditure for the procurement of military equipment and research and development in Germany was at almost the same level as the previous year's figure of €6.4 billion.

In the context of the fundamental reorganization of the German military, 2011 will go down as a significant year in history of the German armed forces. With the adoption of the reform concept, the path was set for the realignment of Germany's troops. Since July 2011, the German armed forces have been made up entirely of volunteers as a result of the abandonment of compulsory military service. Furthermore, the staffing level is to be gradually reduced from approximately 211,000 to no more than 185,000 soldiers, and to no more than 55,000 civilian staff and civil servants. The cornerstones of the German armed forces reform also include the reorganization of procurement processes, which the defence technology industry had also advocated in order to boost the potential for improvements in efficiency.

### »Best possible protection and effective engagement represent growth segments in the Defence sector«

In the year under review, ground troops continued to bear the brunt in key foreign deployments of the western nations. Investments in the protection and engagement of land forces were therefore high up on the list of priorities for procurement projects in Germany and a number of other friendly states. As one of the world's leading systems suppliers for armed forces technology, Rheinmetall Defence has consistently exploited the opportunities for growth resulting from this. For example, Rheinmetall Landsysteme is involved in the largest ongoing land forces procurement project in the UK – the modernization of the UK's Warrior infantry fighting vehicle. There was also positive news from Australia at the end of 2011. In December 2011, the Australian Department of Defence announced that Rheinmetall MAN Military Vehicles had been chosen as its preferred bidder for the procurement of logistical wheeled military vehicles. The Wheeled Vehicles division also recorded another significant international success with the large order placed by the Algerian Ministry of Defence to supply Fuchs 2 armored personnel carriers in a range of models.

As well as armored vehicles, the Simulation and Training division also continued to play a more significant role. In the year under review, the Simulation and Training division acquired a large order for the construction of a combat training center in Russia. When it is commissioned in 2014, this training center will be the world's first live, virtual and constructive combat training center.

The Scandinavian subsidiary Rheinmetall Nordic also made a significant achievement in exports: A contract was signed with Malaysia to equip a new personnel carrier with state-of-the-art Rheinmetall reconnaissance systems.

In Germany, the Ministry of Defence announced lower unit figures for certain major projects, yet it also made it clear that any freed-up funds would not be saved, but were to be made available for new investments.

# General economic conditions

### »Strong automotive year in 2011«

The automotive industry can look back on a successful fiscal year, despite setbacks resulting from the natural disaster in Japan and growing uncertainty due to the euro crisis. “The turmoil on the financial markets, which became even stronger around the middle of the year, high commodity prices and even the high inflationary pressure have barely showed any signs of slowing down as yet,” was the summary given by the Association of the German Automotive Industry (VDA) in its economic barometer released in November 2011.

According to the VDA, 2011 for the German automotive industry was dominated by new records in sales, production and exports. Even on a global level, the automotive industry proved distinctly robust in the period under review. According to the calculations of industry experts at IHS Automotive, global automotive production of passenger cars and light commercial vehicles up to 3.5t increased once again compared to the 2010 boom year by 2.9% and achieved a new high with approximately 75 million units. As such, the automotive industry far outperformed the 2009 crisis year, when only around 58 million vehicles were produced. In the triad markets of Western Europe, NAFTA and Japan, production increased by just 0.7 % in 2011. However, it should be taken into consideration here that production figures in Japan fell by 14.2 % as a result of losses due to the earthquake and tsunami disaster. The North American market grew by 9.1% in 2011, while Western Europe still achieved an increase in production of 2.9% despite the euro crisis. The main driving force behind the positive development in Europe was the German automotive industry, which saw an increase in production figures of 5.3 %. According to the VDA, as well as sustained high domestic demand, German automotive manufacturers have also continued to grow in the key foreign markets – for example, in China, where German manufacturers sold more than 2 million passenger cars for the first time.

Overall, the Chinese market did not build on the huge growth rates of previous years, yet it remained at a high level according to IHS Automotive, with an increase in production of 3.6%. Growth momentum in the Indian automotive industry remained strong, with production figures exceeding those of the previous year by 10.4 %. However, following a strong previous year, the Brazilian market posted a slight fall in production in 2011 of 0.9%.

### »Automotive with the support of the economy behind it – an active driver of industry trends«

In 2011, the Automotive sector benefited not only from the generally positive mood of the automotive industry, but, in times when commodities are becoming increasingly scarce and demands for emission controls are growing, it also benefited in particular from consistently following market trends in terms of reducing consumption and lowering pollution. As such, the Automotive subsidiary, which has traded under the name of KSPG AG since the International Automobile Fair (IAA) 2011, acquired orders from renowned European and US automotive manufacturers in the year under review for fully variable electrical main coolant pumps with a sales volume of over €200 million. These pumps are to be used in newly-developed, particularly fuel-efficient generations of engines, and are also to be used in a new generation of hybrid engines by one US customer. KSPG also presented a promising transitory technology aimed at increasing the acceptance of electric vehicles: The Range Extender, which considerably increases the range of electric vehicles. This is a particularly compact combustion engine which powers a generator, which in turn provides the battery and electric motor with energy.

# Rheinmetall Group business trend

### »Key events in fiscal 2011«

In July 2011, in an ad hoc notification Rheinmetall announced that it would be reviewing the sustainability of the two-pillar strategy of the Company with its Automotive and Defence sectors. The aim is to allow Automotive and Defence each to develop their competitive positions with a greater degree of flexibility. In this context, Rheinmetall is examining in particular the option of an IPO of KSPG AG, which represents the Automotive sector in the Rheinmetall Group. In this process, the Executive Board remains open to the possibility of retaining the current two-pillar strategy. At the start of November 2011, as part of its report on the third quarter of 2011, the Executive Board of Rheinmetall AG announced that, in view of the current instability on the capital markets and the high volatility in listings, it does not believe that the requirements for an IPO of the Automotive sector are currently in place.

### »Rheinmetall Group sales at €4.5 billion«

The Rheinmetall Group achieved sales of €4,454 million in the past fiscal year, compared to €3,989 million in the previous year. This represents an increase of 12%. Rheinmetall Defence accounted for 48% of total sales (previous year: 50%), while Automotive accounted for 52% (previous year: 50%).

Sales *€ million*

| | 2010 | 2011 |
|---|---|---|
| **Rheinmetall Group** | **3,989** | **4,454** |
| Defence | 2,007 | 2,141 |
| Automotive | 1,982 | 2,313 |

Rheinmetall Defence achieved sales of €2,141 million in the past fiscal year, exceeding the previous year's figure by €134 million or 7%. Adjusted for changes in the scope of consolidation, growth was 3%. The activities of Rheinmetall Laingsdale (Pty) Ltd. (from January 2011), ADS Gesellschaft für aktive Schutzsysteme mbH (from February 2011), MarineSoft GmbH (from October 2011) and Swiss SIMTEC AG (from October 2011), included for the first time in the 2011 fiscal year, contributed to the volume of business with sales of €9 million.

In 2011, the Automotive sector achieved sales of €2,313 million, following €1,982 million in fiscal 2010. This therefore exceeded the previous sales record of €2,249 million achieved in fiscal 2007 prior to the outbreak of the global economic crisis in 2008. With this 17 % year-on-year improvement in sales, the Automotive sector not only significantly exceeded the global level of light vehicle production growth of 2.9%, but was also well above the levels in the core markets of Western Europe (+2.9 %) and NAFTA (+9.1%).

At 70 %, the international share of consolidated sales in fiscal 2011 was above the level of the previous year (69 %). Alongside the German market (30%), the key regions in terms of sales volumes were Europe excluding Germany (40%), followed by North and Central America (15%) and Asia (12%). In the Defence sector, 63 % of sales were generated abroad (previous year: 66 %). In the Automotive sector, the proportion of sales achieved with customers abroad rose from 72 % to 76%.

# Rheinmetall Group business trend

### »Order intake in the Rheinmetall Group reaches €4.2 billion«

The order intake reached €4,189 million in fiscal 2011, following €3,974 million in the previous year. Here, the Defence sector was 7 % or €146 million down on the previous year's figure, with an order intake of €1,831 million. The order intake of the Automotive sector rose from €1,997 million in 2010 to €2,358 million in 2011.

Order intake *€ million*

| | 2010 | 2011 |
|---|---|---|
| **Rheinmetall Group** | **3,974** | **4,189** |
| Defence | 1,977 | 1,831 |
| Automotive | 1,997 | 2,358 |

### »Group order backlog of €5.0 billion«

At €4,950 million, the Rheinmetall Group achieved an order backlog that was slightly down on the level of the previous year. At the end of fiscal 2011, the order backlog in the Defence sector stood at €4,541 million (previous year: €4,772 million). In the Automotive sector, the order backlog as at the balance sheet date totaled €409 million, following €364 million in the previous year.

Order backlog *€ million*

| | 2010 | 2011 |
|---|---|---|
| **Rheinmetall Group** | **5,136** | **4,950** |
| Defence | 4,772 | 4,541 |
| Automotive | 364 | 409 |

### »Rheinmetall consolidated EBIT at a record level«

The earnings before interest and tax (EBIT) of the Rheinmetall Group rose by €57 million or 19 % to €354 million in fiscal 2011. The EBIT margin was 7.9 %, compared to 7.4 % in the previous year. The Rheinmetall Group also achieved a new record in earnings before taxes (EBT) with €295 million. EBT increased by €66 million or 29 % year-on-year.

The Defence sector reported a slight decline in EBIT, which totaled €223 million, following €234 million in the previous year. The EBIT margin remained at a high level at 10.4 % (previous year: 11.6 %). At €207 million, EBT was around the same level as the previous year.

The Automotive sector achieved a new record with an improvement in EBIT of €70 million or 86 %, rising from €81 million in the previous year to €151 million in fiscal 2011. As such, the Automotive sector followed on seamlessly from the positive earnings performance of the previous year, to which all divisions contributed once again. The EBIT margin saw a significant increase of 2.4 percentage points to 6.5 % due to the disproportionately large increase in earnings in comparison to sales. At €135 million, EBT more than doubled (previous year: €63 million).

The EBIT for the area Others/Consolidation includes the results for Rheinmetall AG and was burdened in fiscal 2011 and 2010 by expenses of €5 million in each of these years, resulting from changes in the fair value of interest rate derivatives that are not reported in hedge accounting.

EBIT *€ million*

| | 2010 | 2011 |
|---|---|---|
| **Rheinmetall Group** | **297** | **354** |
| Defence | 234 | 223 |
| Automotive | 81 | 151 |
| Others/Consolidation | (18) | (20) |

### »Group net income totals €225 million«

With net interest up €9 million and after deduction of income taxes of €70 million, Group net income of €225 million was achieved in 2011, which exceeded the previous year's figure by €51 million. After deducting profit attributable to minority interests of €12 million, this brings earnings per share to €5.55 (previous year: €4.23), which corresponds to a 31% improvement compared to the previous year.

Group net income *€ million*

| | 2010 | 2011 |
|---|---|---|
| **EBIT** | **297** | **354** |
| Net interest | (68) | (59) |
| **EBT** | **229** | **295** |
| Income taxes | (55) | (70) |
| **Group net income** | **174** | **225** |
| of which: | | |
| Minority interests | 12 | 12 |
| Rheinmetall AG shareholders | 162 | 213 |
| **Earinings per share** (in €) | **4.23** | **5.55** |

### »Cash flow statement«

With an improvement of €51 million in Group net income, 2011 saw a cash flow of €402 million (previous year: €344 million). The cash flow from operating activities was €290 million, up €143 million on the previous year. The build-up in working capital seen during both years led to a higher cash outflow in 2010; around €40 million was also paid out for restructuring measures in the Automotive sector in 2010.

# Rheinmetall Group business trend

Operating free cash flow (defined as cash flow from operating activities less capital expenditure on intangible assets, property, plant and equipment and investment property) amounted to €93 million (previous year: €-39 million). After accounting for cash receipts from the disposal of fixed assets and divestments and payments for acquisitions, the free cash flow came to €39 million (previous year: €-111 million), which was up €150 million year-on-year.

Cash flow statement *€ million*

| | 2010 | 2011 |
|---|---|---|
| **Gross cash flow** | **344** | **402** |
| Changes in working capital and other | (197) | (112) |
| **Net cash provided by operating activities** | **147** | **290** |
| Investments in intangible assets and property, plant and equipment | (186) | (197) |
| **Operating free cash flow** | **(39)** | **93** |
| Cash receipts from the disposal of intangible assets, property, plant and equipment and investment property | 12 | 14 |
| Net cash outflow from financial investments in/divestments of consolidated subsidiaries and other financial assets | (84) | (68) |
| **Free cash flow** | **(111)** | **39** |

### »Asset and capital structure«

In September 2010, Rheinmetall successfully placed a seven-year bond with a volume of €500 million and a coupon of 4.0 % with institutional investors in Germany and abroad. This bond will strengthen the liquidity cushion on a sustainable basis and will secure favorable interest rates in the long term.

Asset and capital structure *€ million*

| | Dec. 31, 2010 | % | Dec. 31, 2011 | % |
|---|---|---|---|---|
| Noncurrent assets | 2,037 | 46 | 2,271 | 47 |
| Current assets | 2,423 | 54 | 2,561 | 53 |
| **Total assets** | **4,460** | **100** | **4,832** | **100** |
| | | | | |
| Equity | 1,355 | 30 | 1,546 | 32 |
| Noncurrent liabilities | 1,547 | 35 | 1,557 | 32 |
| Current liabilities | 1,558 | 35 | 1,729 | 36 |
| **Total equity and liabilities** | **4,460** | **100** | **4,832** | **100** |

In fiscal 2011, the Rheinmetall Group's total assets increased by €372 million or 8 % to €4,832 million. The changes in the consolidated balance sheet were essentially due to the acquisitions in the Defence sector, the implementation of the second stage of the joint venture Rheinmetall MAN Military Vehicles GmbH, Munich, and the associated integration of the Vienna production plant (MAN) at the end of 2011, and the build-up of working capital, owing to the expansion of the volume of business. Non-current assets represented 47 % of total assets as at December 31, 2011, compared with 46 % in the previous year. They rose by €234 million to €2,271 million. This increase was mainly due to an increase in intangible assets, which also included goodwill. These rose by €208 million to €902 million, largely owing to the acquisitions that were carried out and the integration of the Vienna production plant. Current assets rose by €138 million in total year-on-year, which was due in particular to an increase of €77 million in inventories and of €118 million in trade receivables.

The equity ratio is 32 %, following 30 % in the previous year. In fiscal 2011, the equity of the Rheinmetall Group increased by €191 million or 14 % to €1,546 million. This increase was primarily due to the net income (€225 million) and to changes in the scope of consolidation (€112 million). This was countered by actuarial gains and losses from pension provisions recognized in equity (€45 million) and dividend payouts (€62 million). Of the €10 million increase in non-current liabilities to €1,557 million, €52 million is attributable to the increase in pension provisions and €31 million to deferred taxes. This was countered by the early repayment of promissory note loans (€65 million). The €171 million rise in current liabilities relates primarily to trade liabilities and other current liabilities totaling €180 million.

In terms of the total assets adjusted for cash and cash equivalents, the equity ratio is at 36 % compared to 35 % in the previous year. Financial debts fell by €40 million or 6 % year-on-year. This decline is attributable to the early repayment of promissory note loans. As at the balance sheet date, cash and cash equivalents totaled €535 million following €629 million on the balance sheet date of the previous year. The net financial debts for 2011 totaled €130 million, following €76 million in the previous year. The proportion of net financial debts in relation to adjusted total assets is 3 % in the fiscal year 2010, compared to 2 % in the previous year.

Capital structure *€ million*

| | Dec. 31, 2010 | % | Dec. 31, 2011 | % |
|---|---|---|---|---|
| **Equity** | **1,355** | **35** | **1,546** | **36** |
| | | | | |
| Current financial debts | 34 | 1 | 45 | 1 |
| Noncurrent financial debts | 671 | 18 | 620 | 14 |
| **Total financial debts** | **705** | **19** | **665** | **15** |
| Cash and cash equivalents/financial resources | (629) | (17) | (535) | (12) |
| **Net financial debts** | **76** | **2** | **130** | **3** |
| **Total assets adjusted for cash and cash equivalents** | **3,831** | **100** | **4,297** | **100** |

# Rheinmetall Group business trend

**»Improvement in value added«**

In fiscal 2011, the Rheinmetall Group generated added value of €1,636 million. The Group's total operating performance came to €4,868 million, compared with €4,343 million in the previous year. At 34%, the ratio of value added to total operating performance was almost at the previous year's level of 35%. Value added per employee amounted to €80,000 (previous year: €75,000). The workforce benefited from the largest share of value added in fiscal 2011 at 78 %. 5 % was apportioned to the Treasury. Interest payable to lenders in the year under review was 4%. At €69 million, the shareholders of Rheinmetall AG received a 4% share of value added. 9% or €156 million remained within the Rheinmetall Group, following value added of €117 million or 8% in the previous year.

Source and use of value added *€ million*

| | 2010 | % | 2011 | % |
|---|---|---|---|---|
| **Source** | | | | |
| Group's total operating performance | 4,343 | 100 | 4,868 | 100 |
| Input | (2,670) | | (3,048) | |
| Amortization and depreciation | (167) | | (184) | |
| **Value added** | **1,506** | 35 | **1,636** | 34 |
| | | | | |
| | | % | | % |
| **Use** | | | | |
| Employees | 1,197 | 79 | 1,268 | 78 |
| Treasury | 62 | 4 | 78 | 5 |
| Lenders/banks | 72 | 5 | 65 | 4 |
| Shareholders | 58 | 4 | 69 | 4 |
| Companies | 117 | 8 | 156 | 9 |
| **Value added** | **1,506** | **100** | **1,636** | **100** |

The Group's total operating performance comprises all income, i.e. total operating performance, other operating income, income from equity holdings, interest income and other financial income. Input includes all expenses excluding personnel expenses, interest and taxes.

# Rheinmetall Group business trend
# Defence sector

**»Key events in 2011«**

With effect from January 4, 2011, Rheinmetall Defence has taken over the assets and liabilities of the Laingsdale Engineering division of Tellumat (Pty) Ltd., Cape Town, South Africa, as part of an asset deal. The assets and liabilities have been acquired by the newly-established Rheinmetall Laingsdale (Pty) Ltd., Cape Town, South Africa, in which Rheinmetall Waffe Munition GmbH, Unterlüß, holds a 51% stake and Rheinmetall Denel Munition (Pty) Ltd., Somerset West, South Africa, a 49% stake. Its business activities encompass the development and production of precision components for fuses and will supplement Rheinmetall Defence's technology portfolio in the field of ammunition. This acquisition will strengthen distribution activities in South Africa and other customer nations.

Rheinmetall Defence has further extended its expertise in the field of sophisticated protection technology and thus its market position as a systems supplier for land forces. With effect from February 1, 2011, the stake held in ADS Gesellschaft für aktive Schutzsysteme mbH, Lohmar, was increased from the previous level of 25% to 74% by exercising the option which had been contractually agreed back in 2006. As the majority shareholder, Rheinmetall took over management of the business. A 26% stake in the company is still held by IBD Deisenroth, Lohmar. ADS Gesellschaft für aktive Schutzsysteme has successfully developed the "Active Defence System" (ADS), one of the world's most innovative and powerful technologies in the field of military protection. The Active Defence System belongs to a new generation of standoff protection technologies and is used in the protection of military vehicles of practically all weight classes against threats in the field, particularly antitank hand weapons and guided missiles, along with improvised booby-traps.

In the year under review, Rheinmetall Italia S.p.A., Rome, Italy, focused entirely on its strategic core competencies in the area of defence and, in this context, sold its Space product group, in which its satellite activities were bundled, to Telematic Solutions S.p.A., Milan, Italy, with effect from May 1, 2011.

Rheinmetall Simulation Australia Pty Ltd., Canberra, Australia, was founded on September 12, 2011. With this new company the Simulation division is consolidating its market presence in Australia.

The Simulation and Training division also expanded its competitive position further with two acquisitions in October 2011. Rheinmetall Defence Electronics GmbH, Bremen, acquired 49% of shares in MarineSoft Entwicklungs- und Logistikgesellschaft mbH, Rostock. MarineSoft specializes in software solutions and services for maritime simulation and the development of specific e-learning software. Rheinmetall Defence Electronics also acquired 100 % of shares in Swiss SIMTEC AG, Thun, Switzerland, which develops and manufactures components and concepts for simulation and training systems.

Rheinmetall MAN Military Vehicles GmbH, Munich, a joint venture between Rheinmetall and MAN, has been active on the market since May 1, 2010. Rheinmetall AG holds 51% of shares in the joint venture, while MAN Truck & Bus AG owns 49% of the company. This joint venture has given rise to a full-service provider covering the full range of armored and unarmored transport vehicles, command vehicles and multipurpose vehicles for armed forces in Germany and abroad, which makes a significant contribution towards national and European consolidation in the field of military commercial vehicles. In a first step, the development and distribution activities of Rheinmetall Radfahrzeuge GmbH and MAN Truck & Bus AG in the field of wheeled military vehicles were merged in Rheinmetall MAN Military Vehicles in fiscal 2010. As of December 31, 2011, the second stage of the joint venture – as had been contractually agreed back in December 2009 – was completed with the integration of the two production sites in Kassel (Rheinmetall) and Vienna (MAN) into the joint venture.

# Rheinmetall Group business trend Defence sector

**»Rheinmetall Defence posts further sales growth«**

The Defence sector recorded sales of €2,141 million in fiscal 2011, exceeding the previous year's figure of €2,007 million by €134 million or 7 %. The activities of Rheinmetall Laingsdale (Pty) Ltd. (from January 2011), ADS Gesellschaft für aktive Schutzsysteme mbH (from February 2011), MarineSoft GmbH (from October 2011) and Swiss SIMTEC AG (from October 2011), included for the first time in the year under review, contributed to the volume of business with sales of €9 million. The proportion of sales achieved abroad fell by 3 percentage points to 63 % compared to 2010. Alongside the German market (37 %, previous year: 34 %), the key regions in terms of sales volumes were Europe excluding Germany (29 %, previous year: 30 %), followed by the Middle East and Asia (18 %, previous year: 20 %) and North America (11%, previous year: 11%). Other regions accounted for 5% of sales (previous year: 6%).

Sales in the Weapon and Munitions division increased by 15 % year-on-year in the year under review to €872 million. Significant export sales were generated with 40 mm practice ammunition for the US Marine Corps and the United Kingdom, the 40 mm CASW (close-area suppression weapon) weapon system for Canada and with remote control weapon stations for the US CROWS II (common remote operating weapon station) procurement project. Further sales were generated with protection components for a transport vehicle (armored security vehicle – ASV) for a North American customer. 120 mm HE ammunition was also supplied to the USA, while 81 mm mortar ammunition with modern propellants and active charges was delivered to Sweden. In Germany, 120 mm DM78 practice ammunition was supplied to the German armed forces.

Deliveries of propellant powders for artillery and tank ammunition to the United Kingdom dominated sales in the Propellants division. With sales totaling €104 million, this exceeded the previous year's figure by 14 %. The market position in Europe was also consolidated in the year under review on the basis of contracts held with French customers and a Turkish customer to supply propellant powder for artillery ammunition.

The Tracked Vehicles division reported sales of €337 million in the year under review, corresponding to a year-on-year increase of 13 %. Key products in terms of sales abroad included the armored engineering vehicle 3 for Sweden and the Netherlands and the armored recovery vehicle 3 with associated ancillary services for an Asian customer. In the context of the Puma infantry fighting vehicle project, sales were generated in Germany as part of the series contract as well as invoicing for the pre-production run. The state-of-the-art mortar combat system based on the air-portable Wiesel 2 tracked vehicle was also delivered for the first time to the German armed forces. The transfer of state levies of German armed forces vehicles, together with the associated repairs and maintenance services, contributed to the sales of the service division.

The Wheeled Vehicles division achieved sales of €255 million in fiscal 2011, corresponding to a year-on-year increase of 31 %. In the area of tactical vehicles, the acceleration of Boxer series production for Germany and the Netherlands accounted for approximately €113 million of sales. Sales were also generated with deliveries of NBC assemblies for the Fox and Stryker wheeled vehicles for the US armed forces and from modernization services for the Fuchs armored transport vehicle for the German armed forces. Deliveries were invoiced for customers in the area of logistical vehicles, particularly in the United Kingdom, Singapore and Hungary.

Sales in the Air Defence division totaled €313 million in the year under review (previous year: €326 million). Further partial invoicing of air defence systems and associated ammunition for major projects in the Middle East made a significant contribution to sales. Upgrades to radar systems for naval air defence systems constituted further key sales areas.

Sales in the C4ISTAR division totaled €200 million in 2011 (previous year: €258 million). The air force uses the state-of-the-art Heron 1 unmanned aircraft system in Afghanistan. This "system for conducting long-range reconnaissance missions" (SAATEG) is used for airborne monitoring and reconnaissance without a time delay in the area of operations of the German ISAF contingent. Partial invoicing for this unmanned aerial vehicles contract accounted for a significant proportion of sales in the year under review. National sales were also achieved with fire control systems of the mount-adapted aiming device type and through services for the cargo loading systems of the Airbus A400M and A380. The delivery of laser light modules for Germany and the United Kingdom accounted for further sales.

In the year under review, sales in the Simulation and Training division exceeded the previous year's figure by 8% at €166 million. Significant sales were associated with the operation of the German armed forces' combat training center in Letzlingen as well as with partial invoicing for a combat training center in the Middle East. Further sales resulted from the national follow-up orders for the Eurofighter 2000 flight simulator. In the area of maritime simulation, invoices were issued for the modernization of a training system enabling training in the command and weapon engagement system and for a simulator providing training in tactical engagement on board a submarine.

### »Rheinmetall Defence order intake dominated by small to medium orders«

At €1,831 million, the order intake in fiscal 2011 was 7 % down on the previous year's figure of €1,977 million. Whereas the year under review was dominated by a number of small and medium-sized orders, the previous year's figure included three large orders with a total volume of €450 million.

In the year under review, the Weapon and Munitions division was commissioned to supply remote control weapon stations for the US CROWS II (common remote operating weapon station) procurement project and protection components for transport vehicles of a US customer. As well as stepping up a long-term partnering agreement with the UK Ministry of Defence and orders for 40 mm practice ammunition for the US Marine Corps, an order was also received to supply the Vingtaqs II long-range surveillance, observation and reconnaissance system for all-terrain vehicles of the Malaysian armed forces. The Vingtaqs II accurately determines coordinates at long distances and can be integrated at low cost into a wide variety of vehicles. This order also includes services in the area of training, system integration and documentation. Orders were also received to supply 120 mm DM78 practice ammunition to Switzerland and a customer in the Middle East. In Germany, orders were posted for protection systems for the Puma infantry fighting vehicle and to supply 120 mm HE ammunition which can be used in all installed 120 mm smoothbore guns. This HE DM 11 ammunition sets new standards as regards precision, range and impact, and stands out in terms of its technology thanks to features including the ability to program the loaded round.

Extensive contracts to supply propellant powder for artillery ammunition to French customers were of particular importance in the Propellants division. As part of the follow-up order received in 2009 for the Munitions Acquisition Supply Solution (MASS) project, orders were received from the UK to supply propellants for 105 mm ammunition and for other calibers. Further noteworthy orders in the area of propellant systems came from Switzerland, Turkey and a customer in Asia.

# Rheinmetall Group business trend
# Defence sector

The Tracked Vehicles division received an order in the year under review to supply eight armored engineering vehicles 3 to the Canadian armed forces. Rheinmetall Defence has been commissioned to supply at short notice key protection systems as part of mission-specific immediate requirements for the German armed forces in order to improve the safety of forces in Afghanistan further. For this purpose, some support vehicles of the German armed forces have been extensively modernized in order to provide effective protection of crews against ballistic threats, mines and IEDs (improvised explosive devices). IEDs in particular pose one of the biggest threats to the ISAF forces in Afghanistan. The extensive renovation of armored vehicles also involves modernization in the area of command systems and improvements in ergonomics.

The Air Defence division primarily received only smaller orders from Europe and the Middle East in fiscal 2011, unlike previous years which were dominated by the intake of orders for individual large projects. As well as the modification of optronics in existing guns, orders were also received for 20 mm naval guns in particular.

In the Wheeled Vehicles division, a large order was received in the year under review to supply Fuchs 2 armored personnel carriers in a range of models to the Algerian Ministry of Defence. An order placed by the US armed forces for NBC assemblies for the Fox and Stryker wheeled vehicles constituted another significant order from abroad. A range of orders were also generated as part of the modernization of the equipment of the German armed forces. As part of a follow-up order in the current upgrade program of the German armed forces for the Fuchs armored transport vehicle, Rheinmetall Defence will modernize a further 31 vehicles by the end of 2012. The new Fuchs 1A8 version guarantees significantly better protection against mines and IEDs and expands the deployment spectrum for armored wheeled vehicles. The retrofitting contract also provides for the creation of new versions for different functions, for example for fire protection and the disposal and clearing of weapons. In this context, eleven Fuchs 1A8 field ambulances were ordered in the year under review. An additional order was also received in Germany to supply a lightweight NBC reconnaissance system for civil use.

The C4ISTAR division received an order in the year under review to supply the first two batches of MPCS (multi-purpose combat system) launcher modules to a customer in the Middle East. Entry onto this market offers potential for future acquisitions in connection with use in other systems such as the Leopard 2 or Boxer. Furthermore, a significant volume of orders was received from Germany and the UK for laser light modules. Orders were also received in the year under review from the German Federal Office of Defence Technology and Procurement to supply additional required fire control systems of the mount-adapted aiming device type and to supply the target detection drone (KZO) system. Orders were also received for the series production of cargo loading systems for the Airbus A380.

In the year under review, the Simulation and Training division acquired a large order for the construction of a combat training center in Russia. When it is commissioned in 2014, this training center will be the world’s first live, virtual and constructive combat training center. Two smaller orders were also received for the construction and expansion of combat training centers in the Middle East. National orders were also placed for the maintenance of Tiger helicopter simulators as well as follow-up orders for the Eurofighter 2000 flight simulator of the German air force. The support, maintenance and repair contract, which is conducted together with two cooperation partners, covers a total of six Eurofighter flight simulators in Rostock-Laage, Neuburg an der Donau and Nörvenich and has a term up to 2015.

### »High order backlog at Rheinmetall Defence remains unchanged«

The order backlog of the Defence sector amounted to €4,541 million as at December 31, 2011, falling below the previous year's figure of €4,772 million by €231 million. This includes a number of large-volume projects spanning several years. The most important projects are still the contract for the series production of the Puma infantry fighting vehicle and the series contracts for the Boxer armored transport vehicle from the Netherlands and Germany with a total volume of €1.7 billion. Rheinmetall Laingsdale (Pty) Ltd., ADS Gesellschaft für aktive Schutzsysteme mbH, MarineSoft GmbH and Swiss SIMTEC AG, which were included in the consolidated financial statements for the first time in the year under review, reported a total order backlog of €11 million as at December 31, 2011. The order backlog of €188 million acquired from the implementation of the second stage of the Rheinmetall MAN Military Vehicles GmbH joint venture was also included as at December 31, 2011. Due to the reduction in unit figures for the Puma infantry fighting vehicle from 405 to 350 vehicles, the order backlog was revised and adjusted downwards by €148 million to €4,541 million as at December 31, 2011. As in previous years, the sales expectations of Rheinmetall Defence for fiscal 2012 are already largely ensured thanks to the current order backlog.

### »Slight fall in earnings at Rheinmetall Defence«

The Defence sector recorded earnings before interest and taxes (EBIT) of €223 million in fiscal 2011, down €11 million or 5% on the previous year's figure of €234 million. Earnings performance in 2011 was largely influenced by the year-on-year increase in the depreciation of intangible assets identified through the purchase price allocation. This amounted to €17 million in 2011 and was thus significantly higher than the prior-year figure of €8 million.

Income from the first-time consolidation of acquisitions is also included in both fiscal years. In 2011, income of €11 million was generated from increasing the book value of the 25% stake initially held in ADS Gesellschaft für aktive Schutzsysteme mbH to the current fair value following the majority acquisition of shares in the company. In the previous year, this still included a one-off effect in the form of badwill of €8 million from the first-time consolidation of RWM Italia S.p.A., which has taken over the defence technology activities of Società Esplosivi Industriali S.p.A.

As well as influencing factors from the acquisitions, there were further one-off effects in both fiscal years which had a comparable impact year-on-year. In 2011, additional costs of €11 million arose in connection with project processing in the Wheeled Vehicles division. The previous year's EBIT included income of €5 million from a currency rate-hedging transaction of an investment. This was countered by processing an expense of €15 million from write-downs on inventories, which had to be carried out in connection with the restructuring of a product portfolio in the C4ISTAR division.

After adjustment for the increase in depreciation of intangible assets identified through the purchase price allocation, one-off effects from the first-time consolidation and other one-off effects, the EBIT of Rheinmetall Defence totaled €240 million, down 2 % or €4 million on the previous year's figure of €244 million. The EBIT margin reached 10.4% in 2011, following 11.6% in the previous year.

EBIT Rheinmetall Defence before one-off effects *€ million*

| | **2010** | **2011** |
|---|---:|---:|
| EBIT | 234 | 223 |
| Write-downs resulting from purchase price allocations | 8 | 17 |
| Income from changes in the scope of consolidation | (8) | (11) |
| Project costs | 15 | 11 |
| Income from currency rate-hedging transactions | (5) | - |
| EBIT before one-off effects | **244** | **240** |

# Rheinmetall Group business trend Automotive sector

### »Key events in 2011«

In the first quarter of 2011, Pierburg Pump Technology GmbH and Mikuni Corporation, Tokyo, Japan, founded the sales and development joint venture Pierburg Mikuni Pump Technology Corp., Japan, in which Pierburg Pump Technology holds a 51 % stake. The company operates on the Asian market in the field of electrical coolant pumps and variable oil pumps. Since mid-2011, preparations have been underway for the establishment of a production line for a variable oil pump which is to be supplied to the Chinese plant of a global automotive customer. Production is set to commence as early as the second half of 2012.

The Automotive sector stepped up its presence on the automotive growth market that is India in the year under review. At the start of October 2011, KSPG Automotive India Private Ltd. acquired the plain bearing operations of Kirloskar Oil Engines Ltd. (KOEL), Pune, India, which sells chiefly to the domestic market and employs approximately 500 staff at the two production facilities in Ahmednagar and Pune. The scope of production includes motor bearings, bushings and thrust washers for the passenger car and commercial vehicle sectors as well as the agricultural machinery sector. The company’s customers include Maruti Suzuki, Mahindra & Mahindra, Tata Motors and Tata Cummins. Another area at the company is supplying the spare parts market. In the 2010/2011 fiscal year, KOEL generated sales of approximately €20 million in the plain bearings sector.

### »Automotive sector with record sales«

In 2011, the Automotive sector achieved sales of €2,313 million, following €1,982 million in fiscal 2010. This therefore exceeded the previous sales record of €2,249 million achieved in fiscal 2007 prior to the outbreak of the global economic crisis in 2008. With this 17 % year-on-year improvement in sales, the Automotive sector not only significantly exceeded the global level of light vehicle production growth of 2.9%, but was also above the levels seen in the core markets of Western Europe (+2.9 %) and NAFTA (+9.1%). Production in the triad markets of Western Europe, NAFTA and Japan increased by just 0.7 % in the year under review due to the fact that Japan was forced to absorb a fall in production of 14.2 % in 2011 as a result of the natural disaster in March 2011. All divisions, each of which enjoyed double-digit percentage improvements in sales compared to the previous year, contributed to the strong increase in sales. The ongoing positive development of sales at the Chinese joint ventures carried at equity (50 % stake), which, based on 100 %, recorded growth of €40 million to €298 million (+16 %), is not included in the sales for the Automotive sector.

Thanks to higher sales revenue, primarily in the context of the large PSA order, sales in the Pierburg division increased by 17 % year-on-year to €600 million in the year under review. New projects in the area of divert-air valves, in which Pierburg is a global market leader, highlighted the dynamic growth of the Solenoid Valves business unit, which also saw significant increases in sales in its two other product groups of electric switchover valves and electropneumatic valves. The Actuators business unit expanded its business activities with new projects in the areas of throttle bodies and electrical actuators for exhaust gas flaps. The systematic establishment of the Commercial Diesel business unit over the past few years led to the launch of the first products specifically developed for the needs of heavy-duty customers in the year under review. Pierburg saw a significant increase in output at the US site in Greenville, South Carolina, thanks to new orders to supply EGR valves to a major US manufacturer. The two Asian sites located in Pune, India, and Shanghai, China, contributed to growth with projects for local Asian customers in the area of exhaust gas reduction.

In the Pierburg Pump Technology division, sales increased by 15 % in 2011 compared to fiscal 2010, reaching €431 million. This sales increase of €55 million was primarily achieved with pumps of high technological quality such as electrical coolant pumps, water circulation pumps and variable oil pumps. The need for these pumps is the result of automotive manufacturers' challenging aims to reduce fuel consumption and to comply with strict emissions regulations. This includes in particular the use of electrical water pumps for turbocharger cooling (downsizing) by German premium manufacturers and the accelerated production of variable oil pumps for the optimization of consumption in the new generations of engines of European high-volume manufacturers. Thanks to this, sales in this area increased by more than 45 % compared to the previous year. Sales of conventional pumps increased only slightly by around 3 % compared to 2010. Despite considerable falls in sales of non-variable oil pumps in the wake of the changeover to variable oil pumps, good economic performance and new business in the area of conventional vacuum/water and oil pumps more than made up for this effect. In Europe, the high market share, which stands at between 30 % and 50 % depending on the product, was retained despite fierce competition. With an 88 % share of sales, Europe is the most important market for the division. Initial orders received from the Asian and North American markets led to significant increases in sales in these regions. This success confirmed to the Pierburg Pump Technology division its strategic orientation and its aim to participate to a greater degree in the Asian and American markets, some of which are experiencing strong growth.

Sales in the KS Kolbenschmidt division rose in the year under review by 11 % to €669 million, following €605 million in 2010. As well as further improvement in the economic situation of the small-bore pistons product group, the 13 % increase in sales in the large-bore pistons group also contributed to growth in fiscal 2011. Here, sales growth in the large-bore pistons group was distributed roughly evenly between the two locations in Europe and North America. The small-bore pistons group posted an increase in sales of 10 % compared to 2010. With the exception of the Japanese company, all operating companies and all regions contributed to this development. Sales increased significantly year-on-year particularly in Europe and South America, whereas sales Japan remained static at the previous year's level as a result of the natural disaster. In China, the positive market development seen in previous years continued. When broken down according to product, demand across the entire small-bore pistons business proved to be higher than the previous year in the wake of the ongoing good economic situation, and in particular demand for commercial vehicle pistons (+26 %) and other pistons (+16 %), which include, for example, pistons for off-road vehicles and motorized watersports equipment. Sales of pistons for passenger car diesel engines and gasoline engines rose by 6 % and 2 % respectively compared to 2010.

Sales in the KS Aluminium-Technologie division increased by 29 % year-on-year in 2011, rising from €160 million to €207 million. This increase was mainly due to volume increases in series production business activities. Price increases were also successfully implemented. The first sales of products manufactured as part of the KS ATAG Trimet Guss joint venture according to the extended workbench principle and distributed by KS Aluminium-Technologie were also posted. After adjustment for these sales, sales in the division increased by 21 %. The growth achieved over previous years in the Chinese joint venture continued in the year under review. All product groups contributed to an overall increase in sales of €47 million. Low-pressure casting remained the product group with the highest sales, followed by the die casting group. Products manufactured using a high-pressure casting process and supplies of spare parts produced using a squeeze-cast process accounted for only a small proportion of total sales in the year under review. Compared to the previous year, sales in the area of external tools and development work fell considerably because various projects have not yet been completed and have also not yet been invoiced.

# Rheinmetall Group business trend
# Automotive sector

Following €187 million in sales in 2010, the KS Gleitlager division posted a 17 % increase in sales to €218 million in the year under review thanks to growth in volumes and sales in all product groups. The metallic plain bearings product group, the products of which are mainly used in engine applications, achieved sales growth of 12 %. As well as positive sales effects from existing customer orders as a result of the good performance of the automotive industry, particularly in Europe, this sales growth is also attributable to new product launches and increased production in a range of customer projects. Maintenance-free or low-maintenance non-motor plain bearings in the Permaglide product group saw a 7 % increase in sales compared to 2010 thanks to increased volumes in existing customer projects, such as for use in diesel injection pumps. In the year under review, the price of copper was up considerably compared to the previous year. Passing on increased copper prices to customers led to positive effects in the continuous castings product group, which reported an overall increase in sales of 33 % compared to the previous year. The sales of KOEL have been consolidated since October 2011. After adjustment for this acquisition, sales growth in this division was 15 %.

With sales of €259 million in the year under review, the Motor Service division exceeded the sales of €221 million posted in 2010 by 17 %. In addition to the contributions to sales from BF Germany GmbH and Intec France S.A.S which were acquired at the end of 2010, Motor Service also benefited from increased sales in its core business, which were primarily generated thanks to the recovery of business activities in Eastern Europe, high sales growth in Western Europe, the Middle East and Africa and price increases. In Brazil, sales experienced stable development thanks to the acquisition of new customers in the local market, despite intensified competition. After adjustment for acquisitions, sales growth in this division was 5 %.

### »Order intake in the Automotive sector increases further«

Influenced by the positive trend on the automotive markets, the sector recorded an order intake of €2,358 million in the year under review, exceeding the previous year's figure by €361 million or 18 %.

The order backlog in the Automotive sector comprises only short notice call orders under long-term contracts with automotive manufacturers. Compared to €364 million as at December 31, 2010, the order backlog at the end of the 2011 fiscal year stood at €409 million.

### »Increase in earnings at record level thanks to sales«

The Automotive sector achieved a new record in fiscal 2011 with an improvement in earnings before interest and taxes (EBIT) of €70 million or 86 %, rising from €81 million in the previous year to €151 million. As such, the sector followed on seamlessly from the positive earnings performance of the previous year, to which all divisions contributed once again. The sales margin saw a significant increase of 2.4 percentage points to 6.5 % due to the disproportionately large increase in earnings in comparison to sales. The earnings growth is primarily the result of additional profit contributions from increased sales in connection with a moderate increase in the level of fixed costs. In addition to new project launches and increased production in new customer projects, project costs from the acquisition of the plain bearing operations of KOEL in India and the merging of the North and South American production sites of the KS Gleitlager division in Mexico – which will lead to significant cost savings in the future – also constituted negative impacts on earnings. Earnings in the Automotive sector were also impacted – to the extent intended – by factors including expenditure for the Univalve and Range Extender development projects.

# Rheinmetall Group business trend
# Financing

**»New €500 million syndicated loan facility concluded with a duration to the end of 2016«**
The majority of financing in the Rheinmetall Group takes place centrally via Rheinmetall AG. Against the backdrop of the ongoing financial market crisis and the euro crisis, securing the provision of liquidity and bank guarantees for the Group on a sustainable basis is and will remain the strategic aim of Treasury activities. The Rheinmetall Group traditionally follows an extremely conservative financial policy, geared towards sustainability, diversification and internationalization. The cornerstone of this policy is ensuring a balance between the use of the capital market on the one hand and lending from relationship banks on the other. As well as organizing the Rheinmetall Group's presence on the capital market, communicating and managing its relationship with the banks is also a key responsibility of the Group Treasury based at Rheinmetall AG in Düsseldorf. In this context, the regular, face-to-face exchange of information with representatives from these banks on all levels has once again been stepped up in view of the ongoing tension on the banking market in 2011, with the aim of safeguarding and strengthening the relationship of mutual trust.

After successfully issuing a seven-year €500 million corporate bond in fall 2010, Rheinmetall AG refinanced the former syndicated loan facility of €400 million concluded in 2005 and maturing in April 2012 earlier than scheduled in December 2011. Despite a difficult market environment, Rheinmetall succeeded in setting up a new syndicated loan facility with a duration of five years up to December 2016. Thanks to good oversubscription, the volume was increased by €100 million to €500 million as intended. As was previously the case, this loan will serve as a key facility in organizing relationships with the banks. As part of this concept, Rheinmetall guarantees these long-term financing partners an appropriate participation in the deposits business and fees and commission business that reflects their respective financing contribution.

As well as a number of relationship banks already associated with the Group and which had already participated in the former syndicated loan, prestigious national and international banks were also acquired as new long-term partners in this transaction structured by Rheinmetall AG as a club deal. This is of key significance, especially against the backdrop of the internationalization and growth of the Rheinmetall Group.

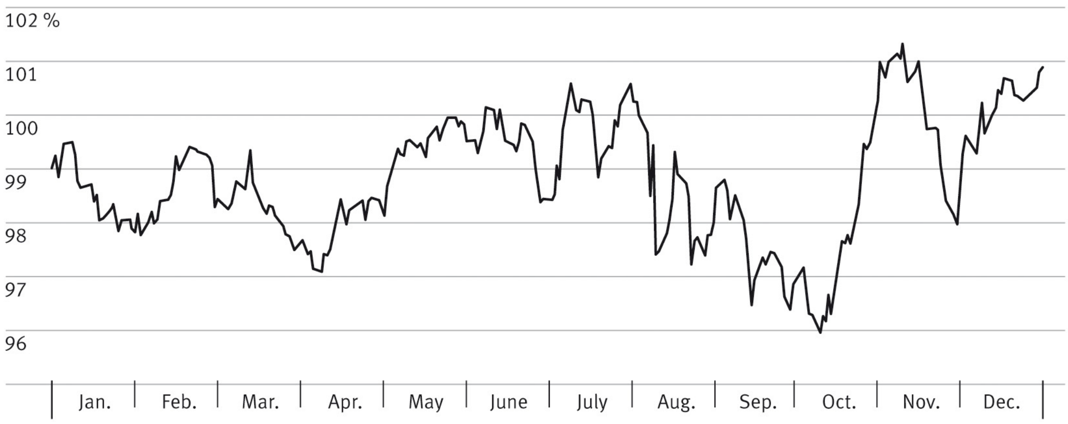
With this syndicated loan facility, Rheinmetall secured itself a long-term credit line for general corporate financing and as a back-up facility for the commercial paper program which has been in place since 2002 and also has a volume of €500 million. The maturity profile of the financing facilities of the Group has thus been shifted significantly into the future – over the next five years, it will be possible to raise cash by means of drawings on the new syndicated loan facility and issues of short-term money market securities. Rheinmetall AG also has considerable bilateral loan commitments from a number of financing partners. These commitments comprise both cash and guarantee facilities.

With this new syndicated loan facility, in combination with the bond that was successfully issued in 2010, the Rheinmetall Group has further secured its continuous solvency on a sustainable and long-term basis. This bond, which also has a volume of €500 million, matures in September 2017. The agreed fixed rate of interest is 4.0 % p.a. The bond with the code number (ISIN) XS0542369219 is listed in Luxembourg and on several German exchanges. The smallest tradable unit is €1,000. In 2011, Moody's continued to rate the bond with the investment grade rating Baa3 stable.

# Rheinmetall Group business trend
# Financing

The performance of the bond on the secondary market since the date of issue (99.122 %) reflects the good development and the trust held by investors in the Rheinmetall Group. The closing price of the bond on the last trading day of the fiscal year (December 30, 2011) was 100.90 %, which resulted in a spread above the mid swap rate of 171.1 basis points (sources: Markit Group bid price, Bloomberg swap rates).

Rheinmetall Bond – Price Development 2011




A significant proportion of the promissory notes issued on the German market in 2009 with a volume of €150 million and comparatively high interest rates maturing in 2013 or 2014 were either repaid in the year under review or their interest rates were lowered.

In addition to the above cash facilities, the Rheinmetall Group also has access to extensive bilateral guarantee facilities with banks and insurance to cover the need for surety bonds and guarantees required for operating activities, particularly in the Defence sector. As at December 31, 2011, a granted credit volume of more than €1 billion was available to the Rheinmetall Group from these bilateral facilities.

The asset backed securities program (ABS) offered for the first time in 1998 also serves to ensure diversified financing of the Group. Here, 14 companies from four European countries in both sectors sell customer trade receivables on a monthly and non-recourse basis to a special purpose entity as part of a program arranged by a Rheinmetall relationship bank. On the balance sheet date, the contractually agreed maximum volume of the program – €170 million – had been utilized in full. The contract is fixed until 2013 and will be extended automatically by one year unless one of the parties gives notice.

The funds available to the Group on a permanent basis and beyond the end of the fiscal year thanks to the bond, promissory notes, amortizing loan facilities and the ABS program also led, in combination with the typically strong operating cash flow in the last quarter of the year, to a significant level of cash and cash equivalents on December 31, 2011, which will primarily be used to finance the seasonal build-up of working capital in the first quarters of the following fiscal year as is customary at Rheinmetall Defence.

Since 2000, Rheinmetall has continuously had an investment grade rating from Moody’s. This rating is a key prerequisite for a successful presence on the money and capital markets in the long term. The agency currently rates Rheinmetall’s creditworthiness with Baa3 stable/Prime 3.

# Rheinmetall Group business trend
# Capital expenditure

### »Capital expenditure – a building block for sustainable success«

The Rheinmetall Group's capex program was, as in previous years, dominated by the implementation of the growth strategy. The strategic and operating objectives for expanding market share and securing technological competence were the guiding factors in various areas, including the allocation of funds. Targeted investments were made in areas that offer opportunities for growth, that will strengthen profitability on a sustainable basis and that will increase international competitiveness. In order to strengthen operating performance capacity, investments were made in the expansion and modernization of infrastructure, facilities, equipment, processes and product manufacturing capacity.

Even in economically challenging times, Rheinmetall was committed to continuity and invested funds at a consistently high level. The Group's capital expenditure on property, plant and equipment and intangible assets (excluding goodwill) amounted to €207 million in 2011, compared to €189 million in the previous year. This is equivalent to 4.6 % of consolidated sales (previous year: 4.7 %). Capital expenditure was met with amortization and depreciation of €184 million (previous year: €167 million).

Capital expenditure *€ million*

| | 2010 | 2011 |
|---|---:|---:|
| **Rheinmetall Group** | **189** | **207** |
| Defence | 93 | 102 |
| Automotive | 96 | 104 |
| Others/Consolidation | 0 | 1 |

### »Capital expenditure volume at Rheinmetall Defence still at a high level«

In fiscal 2011, the Defence sector invested €102 million in property, plant and equipment and intangible assets, compared to €93 million in the previous year. Of the total capital expenditure volume, €25 million (previous year: €26 million) related to development costs for ongoing large-scale projects capitalized in line with IAS 38. This is equivalent to 4.8 % of sales in the Defence sector (previous year: 4.6 %).

Here, capex activities focused on replacing and rationalizing production plants and machinery, factory and office equipment as well as buildings and construction. Capex measures aimed at optimizing site infrastructure and production processes were the main focus.

Capital expenditure on property, plant and equipment at companies in the Defence sector was spread between a number of smaller individual projects in the year under review. Numerous investments were made in the expansion and rationalization of production plants and machinery as part of an extensive modernization program spanning several years at the South African company Rheinmetall Denel Munition. Capital expenditure focused on infrastructure and production machinery as well as targeted measures at the Boksburg and Wellington sites. Modernization activities were also carried out at the Somerset West site and 40 mm production at the former Philippi site was relocated to a new building at Somerset West. American Rheinmetall Munitions Inc. continued the process of building up local ammunition production at the site in Camden, Arkansas, by expanding the capacity of the assembly line for 40 mm ammunition, with the aim of expanding the strategic competitive position in the USA. Rheinmetall Canada invested in mechanical production and the assembly line as part of the Canadian combat support vehicle program based on Leopard 2. Capex funds were also used for a new assembly line at the Silberhütte site in Germany for Mithras handheld rockets.

# Rheinmetall Group business trend
# Capital expenditure

In addition, development costs from the continuation of development projects for an innovative 30 mm weapon for the Puma infantry fighting vehicle, 120 mm DM88 practice ammunition and 120 mm HE service ammunition with an impact fuse as well as the purchase of a manufacturing license for 60 mm mortar ammunition were capitalized in the year under review. The Weapon and Munitions division also invested in the basic development of a grenade launcher, which is to be installed on the Puma infantry fighting vehicle as a secondary armament.

At the production site in Aschau in Germany, the Propellants division completed its capex measures in the expansion of production facilities for the production of Vinnol. Since April 2011, the Swiss company Nitrochemie Wimmis has been operating the scrap wood heating facility of an energy supplier in order to secure future energy supplies and long-term independence of continually rising fuel prices. The company provides staff to operate the facility and currently obtains the majority of the energy being almost the only customer. This is a finance lease project, meaning that the scrap wood heating facility was recognized in the balance sheet of Nitrochemie Wimmis AG in the year under review.

The Tracked Vehicles division concentrated on the development of a tracked armored personnel carrier (APC), for which a hardware demonstrator was manufactured. This vehicle model, derived from the Marder infantry fighting vehicle, offers the best possible protection for a crew of up to ten soldiers with equipment.

In the Wheeled Vehicles division, funds were invested in the reorganization of IT systems commenced back in 2010 at Rheinmetall MAN Military Vehicles as part of the integration measures. Capex funds were also used to further develop the Ede site of Rheinmetall Nederland in connection with the acceleration of local series production for the Dutch Boxer program.

In fiscal 2011, significant projects were continued and pro rata development costs from these projects were capitalized as part of the technological developments. One focal area was the continuation of the development of the new generation of lightweight armored multipurpose vehicles (AMPV) carried out together with another German armaments company as a cooperation partner, which was commenced back in 2008. Here, particular focus was placed on the commencement of development for series production in the past fiscal year.

Additional capex funds related to the further development of a close-range protection system in the Air Defence division, capable of engaging small targets such as rockets, artillery and mortar rounds.

In the C4ISTAR division, capital expenditure focused on capitalized development work for the Leopard 2 turret demonstrator (MBT Revolution). Here, the previous analogue system of the Leopard 2 turret for sensors and effectors can be replaced with modern, digital systems. Other work performed by the enterprise for the SEOSS demonstrator (stabilized electro-optical sighting system) was also capitalized. This involves the development of a compact, digital fire control unit with a thermal imaging device, a daylight camera and a laser rangefinder that can be installed on various weapon mounts.

In the Simulation and Training division, the Score project launched in 2007 for the development and provision of a new basic simulator system was continued.

With a view to ensuring the future capacity and competitiveness of the company, Rheinmetall Soldier Electronics invested in a plot of land and the construction of a new company building at the Stockach site in 2011. The previous premises were no longer adequate for current business volumes in terms of size and layout. The former property was sold to the City of Stockach.

### »Capex up year-on-year in the Automotive sector«

KSPG invested €104 million in the year under review, following €96 million in 2010. This increased expenditure compared to the same period of the previous year was primarily used to carry out the planned expansion of business activities in India and Mexico and to realize strong sales growth. The investment ratio in the year under review was 4.5%, compared with 4.8% in the previous year.

In the year under review, the Pierburg division focused its capital expenditure on the development of capacity for the production of products to reduce emissions and $CO_2$ in the area of passenger cars, but also in the area of trucks, where the range of products on offer for the reduction of emissions has attracted a great deal of interest. Capex funds in Germany were primarily used for capacity expansion in the production of solenoid valves, equipment for the manufacture of actuators as part of new customer projects and investments in truck projects. In Spain, expenses were incurred in particular for the expansion of production facilities for electrical secondary air valves and EGR valve projects for the Euro 5 and Euro 6 emissions standards. In the Czech Republic, capex activities focused on the purchase of manufacturing facilities for a new generation of secondary air valves and assembly facilities for exhaust gas flaps. Work also commenced here on the first phase of construction of the third production hall. In the USA, capacity was expanded for the production of EGR systems and throttle valves. A new production building was constructed at the Pune site in India. Capex funds were also invested here in the expansion of the production of EGR valves and EGR cooler modules.

Capex in the Pierburg Pump Technology division in Germany focused primarily on expanding capacity in the growth areas of water circulation pumps and electrical coolant pumps and expanding capacity for the electric motor supplied to Pierburg for commercial vehicle EGR valves, as well as on capitalized development work for electrical coolant pumps. The majority of capex funds both at the French site and in Italy were invested in the production of variable oil pumps. As part of the upcoming plant expansion in Mexico, capex funds were invested here in a plot of land and the construction of a new building.

Capital expenditure in the KS Kolbenschmidt division in 2011 concentrated on the expansion of the diesel engine line at the Brazilian plant. In Japan, machine accessories were purchased for the existing gasoline engine line. Kolbenschmidt de México expanded the production of pistons for a prestigious US manufacturer. In the other companies, activities included the purchase of tools and investments in smaller projects.

The KS Aluminium-Technologie division invested large amounts of capex funds in machinery for the production of an engine block commissioned by a German premium manufacturer. The final installment for the Romanian production site acquired in fiscal 2008 also fell due in the year under review.

In the KS Gleitlager division, purchases of further cleaning facilities at the two German sites were associated with increased requirements on the part of customers with regard to the cleanliness of plain bearing systems. Capex in Germany also primarily concerned the procurement of replacement tools, machinery and facilities. Projects commenced in India were continued. The construction of the new production location in Mexico was accompanied by investments in a new facility for the upstream production of sintered materials.

The Motor Service division primarily invested in tools, production facilities and software licenses in 2011.

# Rheinmetall Group business trend
# Research and development

**»Technology and production developments open up growth potential«**
Innovative strength and technological expertise are indicators of competitiveness in a rapidly changing business world. Tradition and innovation – the Rheinmetall Group can draw on specialist knowledge and industrial experience built up over more than 100 years in its Defence and Automotive sectors. Ongoing and targeted research and development activities are the prerequisite for active involvement in technological change and for successful entrepreneurial participation in diverse, technologically challenging markets on a sustained basis. Market, industry and technological developments are constantly monitored and analyzed so that trends can be identified at an early stage. Thanks to close networking and the exchange of knowledge between Sales, Development, Production, Service and Marketing as well as project work in partnership with customers, new requirements in terms of products and systems are also quickly identified, which are rapidly acted upon with a high degree of flexibility and in the shortest possible development periods. Existing product lines are constantly improved and expanded, and new or associated business areas are gradually opened up further by means of innovative products, future-oriented systems and customized services. The Group's own research and development work is supplemented by specialist exchanges with industrial partners, renowned scientists and skilled experts.

In fiscal 2011, €212 million was spent on research and development across the Group, following €208 million in the previous year. Of this, €174 million (previous year: €170 million) was immediately billed as expenses and €38 million (previous year: €38 million) capitalized as development costs. The share of R&D expenditure in the Rheinmetall Group was 4.8 % (previous year: 5.2 %), 5.6 % in the Automotive sector (previous year: 6.1 %) and 3.8 % in the Defence sector (previous year: 4.4 %) – here this relates to the share of self-financed projects. At Rheinmetall Defence, developments commissioned by customers were also carried out. On December 31, 2011, 3,099 engineers (previous year: 3,048) were employed in the research and development departments of the Defence and Automotive sectors.

R&D by corporate sector *€ million*

| | **2010** | % of sales | **2011** | % of sales |
|---|---|---|---|---|
| **Rheinmetall Group** | 208 | 5.2 | 212 | 4.8 |
| Defence (self-financed) | 88 | 4.4 | 82 | 3.8 |
| Automotive | 120 | 6.1 | 130 | 5.6 |

The **Defence sector** consistently gears its R&D activities toward the national capability focal areas specified by the German armed forces and the mission requirement profiles of international armed forces. The armed forces of the 21st century are faced with growing challenges and complex threats. Multinational deployments to avert conflicts and manage crises are increasing. In soldier deployment scenarios, modern and task-specific equipment of a high technological standard can make a crucial contribution to improving survivability, command capability, endurance, mobility and effectiveness in the field.

Rheinmetall Defence, with its globally recognized core competencies, stands for capability-oriented innovation: New generations of vehicles with optimized protection concepts, network-enabled sensors and optronics, platform-independent weapon systems and air defence systems designed to combat very small targets. Whether the task at hand is meeting the specific requirements of air, ground or naval forces, facilitating joint operations or assuring internal or external security, Rheinmetall Defence's ability to integrate components to create effective comprehensive solutions makes it a strong partner of the German armed forces, its allies and friendly armies as well as civil national security forces. To ensure that it is competitive and to reinforce its leading position on the market, Rheinmetall Defence continually supplements developments commissioned by customers with self-financed projects.

### »New reconnaissance technologies and unmanned ground vehicles«

In the category of integrated reconnaissance, command and control, engagement and support systems, research carried out as part of the Distributed Integrated Testing Environment (VintEL) overall project is focused on areas including processes for generating and preparing geodata and environmental data and the integration of sensor data in higher-level simulation architecture. In a multinational project looking into the intelligent networking of a wide range of information sources for the purpose of intelligence gathering, reconnaissance and surveillance, Rheinmetall Defence is making a significant contribution to integration and image data processing thanks to its expertise in the simulation of unmanned airborne sensor carriers.

Decision-making and support in time-critical situations constitutes a focus of its research and development activities. Research is being conducted into new reconnaissance technologies and their integration into real-time cause-and-effect chains in order to relieve the burden on armed forces in critical threat situations. Here, the focus is on the gradual implementation of acoustic reconnaissance systems aimed at fire detection both for soldier-borne and platform-based applications. In research work that has already been ongoing for several years, optronic processes were also included in the year under review. A project aimed at identifying targets, tracking targets and commencing engagement was launched together with the German armed forces. The plan is to equip deployment vehicles with modular comprehensive solutions in future and thus to support crews in detecting and defending themselves against moving targets when travelling during the daytime and at night.

Rheinmetall Defence and the German authorities are working together as part of the “Unmanned ground vehicle prototype” study, which is to be carried out over several years. The medium-term aim is to prepare for the development of an autonomous transport vehicle based on the 6x6 MAN HX58, which is able, for example, to deliver supplies independently to warehouses by means of waypoint navigation. To do this, a wide range of sensors are being tested for suitability. Various universities are involved in this project and are contributing their expertise and experience in the field of obstacle and environment detection.

In the research field regarding engagement of targets using alternative weapons, studies are being carried out into potential weapons and their effectiveness, for example in protecting against the threat of IEDs. Following the successful completion of research into the potential applications of high-power microwaves, the developers are working on a new type of combined process, by means of which the electronics of IED trigger systems can be detected and disabled using microwaves.

### »Vehicle-supported technology solutions for weapons defence«

The first two systems of the new explosive ordnance clearance system “Route Clearance System” together with the Fuchs command vehicle, the Wiesel detection vehicle and the Minewolf manipulator vehicle have been delivered to the German authorities. The next step will be the expansion of the Route Clearance System with a vehicle used for weapons reconnaissance and identification. A vehicle will be developed by Rheinmetall Defence based on a Fuchs 1A8, which will be equipped with an electronically controlled and hydraulically powered manipulator arm with a maximum radius of 14 meters that can compensate for vibrations. As well as the basic tool for digging and grasping, other tools, sensors (e.g. explosive detectors) and a rescue platform for rescuing injured persons can be also be adapted. At the end of 2011, a demonstrator was produced which is to be examined by the Wehrtechnische Dienststelle der Bundeswehr (Technical Center of the German armed forces) in Koblenz from January 2012, and the procurement of seven further systems is to be initiated in 2012.

# Rheinmetall Group business trend
# Research and development

### »Highly mobile transport vehicles for deployment«

The HX truck series was successfully introduced onto the market for logistical military vehicles by the UK procurement program “Support Vehicles UK” in 2005. To date, over 6,000 vehicles have been delivered to a range of customers worldwide. The HX can also be equipped with a modular armor kit that is compatible across the fleet and offers protection against ballistic infantry ammunition threats and land mines. In 2011, Rheinmetall Defence expanded the successful HX series further and will offer an integrated armored driver’s cab in the next generation of vehicle, the HX2. By combining the vehicle and protection expertise of Rheinmetall Defence, new standards have been set in this vehicle category as regards the protection of crews, particularly against mines and IEDs. Several prototypes are currently undergoing a demanding testing program in order to ensure the standard high level of operational availability, performance and reliability of the vehicles. The optimized HX series thus represents the future core element of a globally deployable fleet of highly mobile, armored transport vehicles. The fact that the range meets a large number of military requirements and the modular HX concept also make it possible to derive further customer-specific models and chassis that are also suitable for tactical military vehicles.

### »Acoustic fire detection equipment«

During the deployment of armed forces, hand weapon or sniper attacks – often from a partially covered or raised position, in urban or open areas – represent a direct threat both to crews and dismounted soldiers in the area of the vehicle. Acoustic reconnaissance aimed at locating the threat constitutes an important capability in warding off this type of attack. When equipped with an acoustic reconnaissance component, this considerably improves the protection of the vehicle crew as well as the protection and effectiveness of command, multipurpose and combat vehicles when on deployment. For this purpose, Rheinmetall Defence has developed the Acoustic Shooter Locating System (ASLS). The basic version for use on wheeled vehicles has been made ready for the market. It comprises a powerful acoustic sensor platform (microphone antenna) with integrated analysis electronics and a compact control and display device which can be installed flexibly and independently of other systems in the vehicle. A quick-mounting device eliminates the need for a vehicle-specific installation kit. The system can be mounted in less than 15 minutes, even in small vehicles, with very little effort. The analysis results can be transmitted to the control and display device in the vehicle either by wireless link or cable. The modularity of the ASLS assures high growth potential. Numerous enhancements and integration options in higher-level system environments are currently being examined.

### »Standoff protection system for deployment vehicles«

In the 2011 fiscal year, a Fuchs armored transport vehicle was equipped with the “Active Defence System” (ADS) standoff protection system and successfully underwent extensive tests into system compatibility, including a vehicle technology test at the Technical Center of the German armed forces in Trier. It was established that the integration of ADS in no way negatively affected the handling performance. A live demonstration of the performance of this innovative sensor system in the protection of military vehicles of practically all weight classes against threats in the field was shown to more than 100 guests from ten countries in September 2011. Based on real-life conditions in the field, an antitank hand weapon was fired at the Fuchs armored transport vehicle in an ambush from just 18 meters away. The approaching missile was independently detected, located and destroyed by the ADS as intended. In order to do this, the ADS activated a defence area within microseconds and destroyed the approaching missile with targeted pyrotechnic energy immediately before it was to reach its target. The audience also had the opportunity to make sure of the roadworthiness and full operational capability of the armored transport vehicle following the successfully averted attack.

### »Reconnaissance and target tracking system«

The reconnaissance and target tracking system “Air-Ground Surveillance and Alert System” (AGSAS) allows for uninterrupted surveillance of the lower airspace from the ground up to heights of a few kilometers, thus covering a surveillance gap left by traditional radar surveillance chains. The system combines the performance of tried and tested electro-optical high-performance sensors with newly developed image data processing technologies. This creates a visually-monitored safety barrier which no threats can penetrate unnoticed. AGSAS automatically detects targets and determines their geographical coordinates, direction of motion, speed and height. The system can be used on a stationary basis, as well as on a mobile basis when installed on small off-road vehicles. Several weeks’ testing in North Africa in the climatic conditions present there demonstrated impressively the performance capability of the system up to distances of 40 kilometers. As well as border surveillance, typical applications for AGSAS include the protection of units at sea and vital infrastructure from intruders and attacks on the ground, from the sea and from the lower airspace, such as rapid, low-flying rockets or small drones. It is therefore an ideal addition to existing air defence systems.

### »Mobile tactical training system«

Global multinational deployments in crisis regions with predominantly asymmetrical threats and conditions similar to those seen in civil war constitute the military challenges of today. Joint armed forces missions will continue to demand a high degree of interoperability and communicative ability of the military in the future. This will result in new performance requirements for future training systems. For this purpose, Rheinmetall Defence has developed the mobile tactical training system Advanced Network Trainer (ANTares). This system allows for entire mission contingents to be provided with tactical mission preparation in the country of deployment, in addition to flight crew coordination training. Thanks to its technologically advanced design, the modular cubicle concept allows for a wide range of weapon system simulators from all the armed forces to be networked, thus enabling tactical training in an integrated simulation system. Up-to-date databases are essential in ensuring efficient preparation in a simulated deployment environment. For this purpose, an intelligent build process automatically generates a virtual 3D world from reconnaissance data gathered shortly before this time in just a few hours. The cubicles are assembled as required as plug & play units in a container configuration, thus forming the highly mobile training system. The containers can be transported to the country of deployment by road, air or sea. The modern system design makes a significant contribution to reducing lifecycle costs thanks to the consistent use of components available on the market.

### »Future Soldier – Expanded System«

The technological program “Future Soldier – Expanded System” represents one of the most important modernization projects in the German armed forces. It is designed to increase comprehensively the performance capacity of infantry troops across the whole deployment spectrum while also minimizing risks to the soldiers. The modular combat equipment “Expanded System”, which was developed by Rheinmetall Defence and is currently considered the best of its kind in the world, integrates infantry forces – equipped with reliable communication systems and robust weapons – and their vehicles, including the base station, in network-enabled operations. Future Soldier – Expanded System allows soldiers to gain a complete overview of the situation in hand and to exchange information rapidly. This makes a vital contribution to protecting ground troops and significantly increases their operational effectiveness on deployment. In the year under review, the technical and commercial prerequisites were established for commencing series production in 2012.

# Rheinmetall Group business trend
# Research and development

The **Automotive sector** continued to gear its research and development activities strictly towards the ongoing requirements of the automotive industry. Focal points include the reduction of consumption and $CO_2$, the fulfillment of strict emissions standards such as Euro 6, the implementation of more stringent environmental requirements and further cost reductions through improvements to products and optimized manufacturing processes.

### »Research and Technology central department«

The Research and Technology central department which was established in 2010 continued its activities aimed at creating advance product developments and integrating technical services in the year under review. Cross-division development activities took place in the areas of simulation, engine test stands and electronics development. As well as realizing synergies, this also significantly improved exchanging experience and balancing capacities.

In the area of alternative drive systems, and in particular electric mobility, the Company's own technological position was determined and the future product portfolio defined by means of internal and external studies. The development of a Range Extender as a transitory technology for electric mobility attracted a great deal of interest at the International Automobile Fair in Frankfurt am Main.

The development of new products in individual business areas was continued in close cooperation with the divisions. In 2011, new customer orders were obtained as early as the advance product development stage. Significant progress was also made in the development of variable valve controls. In this context, promising contacts were established with further customers and tenders submitted for prototype development. Initial endurance tests carried out on the UniValve system were successful.

### »Pierburg focuses on reduction of emissions and consumption«

In the Pierburg division, development activities continued to focus on products to reduce consumption and emissions. Legal regulations, such as the Euro 6 emissions standard for type approval that is to come into effect on September 1, 2014, define the minimum requirements for this. The fulfillment of these requirements calls for EGR systems with increased performance, among other things. Pierburg is pursuing various development strategies in order to achieve this. The development of the second generation motorized EGR valve as a stand-alone version and as a highly integrated version in aluminum EGR cooler modules has now been completed and entered series production for a range of applications and customers.

Particularly in terms of the high pressure EGR applications, another focus was on the development of applications for a new, even more compact valve, the requirements of which were defined based on experience to date combined with advance developments for gasoline and diesel engines. A German premium manufacturer is set to commence series production of the first application for an initial order in mid-2013. Further developments and new developments were also carried out with regard to applications for low pressure EGR systems. Here is to be highlighted the high-flow low-pressure EGR valve, which allows greater EGR rates with minimal loss of pressure, along with a new exhaust gas flap that increases the EGR rates by means of higher dynamic pressure whilst simultaneously optimizing the regeneration of the diesel particle filter. From a present day perspective, a further development in the form of a double flap with an intelligent positioning mechanism also offers potential applications in the context of thermal management, e.g. by using the exhaust gas heat to heat the inside of the vehicle more quickly.

As a combination of these two types of valves, the combined valve offers the possibility of fulfilling both functions, i.e. the regulation of the EGR rate and the simultaneous restriction of fresh air, in order to increase exhaust gas recirculation. In order to expand the portfolio of EGR valves, work is being carried out on the development of a high pressure EGR flap valve to meet increased leak tightness requirements based on a low pressure EGR valve.

It can generally be assumed that, as a result of stricter legal requirements in terms of reducing $CO_2$ and lowering fuel consumption, especially in the USA, greater emphasis will be placed on the use of EGR systems in the future, even in gasoline engines.

Pierburg has further expanded its market position as regards throttle, control and swirl valves. In order to realize its growth targets, the division is expanding its activities further, particularly in Asia. The basis for this is the modular system for the fourth generation throttle body – a cost-effective, high-quality series concept. Non-contact, low-cost sensor technology, which is used to position the throttle valves, is used across the board. The actuators of associated applications such as intake manifold actuators and electrical exhaust gas flaps are increasingly benefiting from this modular system. Significant growth has been seen in the area of actuators and the market position has been expanded. Particularly high-performance control valves for commercial vehicle applications, which will extend the product family, are soon to be launched on the market. The use of brushless engines and the application of special designs which increase vibration and temperature resistance ensure a product geared to requirements. In view of the ongoing trend for downsizing and the growing market for turbochargers, the portfolio has been expanded to include electrical actuators for wastegate systems.

The continued trend for charged turbo engines is creating a growing market for solenoid valves from Pierburg. The division is the global market leader for electro-pneumatic valves used to control wastegates and variable turbine geometry in turbochargers for passenger car diesel engines. The fourth-generation electrical divert-air valve for compressors in the turbochargers of passenger car gasoline engines has successfully entered series production. The next step is to develop a low-cost, weight-optimized compact divert-air valve, which is currently undergoing testing in collaboration with customers. The hydraulic valve for variable oil pumps launched back in 2010 is currently being optimized in terms of cost and weight in order to create a new generation, so that it can be used in other applications with up to 4 l/h throughput, such as in coolant circuits.

### »Variable pump technology for the reduction of consumption«

With the continued intensive debate surrounding the reduction of fuel consumption in combustion engines, increasing attention is being paid to the ancillary units of these engines such as the oil pump, water pump and vacuum pump. Even these components can make a substantial contribution to lowering consumption by reducing the required driving power. For example, a variable oil pump, which provides only the amount of oil actually required to lubricate the engine, can be used to reduce pump drive power, thus achieving a reduction in fuel consumption of approximately 1.3%. After Pierburg Pump Technology launched series production of these new generations of oil pumps with a range of automotive manufacturers in 2008, the control systems for the pumps have since been optimized further, meaning that series production of even more efficient oil pumps was able to commence in 2011. These new generations of variable oil pumps enable fuel savings of up to 2.5%, by individually detecting any chosen engine parameters such as the oil temperature or engine load and using these as input parameters for controlling the oil pump.

# Rheinmetall Group business trend
# Research and development

New concepts were also developed in 2011 in the area of electrical oil pumps, which are the preferred choice for installation in automatic transmissions for hybrid vehicles or in dual clutch transmissions. In addition to simplifying the pump structure, development work concentrated in particular on lowering costs by increasing component integration. Since Pierburg Pump Technology launched series production of the world's first electrical coolant pump for cooling gasoline engines in 2004, the third generation has now been delivered in 2011. The core element of this development is the increased power density of the pump, thanks to which it has been possible to double the hydraulic power while retaining the same installation space.

Activities also focused on the development of a new electrical vacuum pump, which was presented to experts at the International Automobile Fair in Frankfurt am Main. The first generation is equipped with a cost-efficient, brushed direct current motor, as it is intended to be used purely as a secondary pump. This electrical vacuum pump achieves the same suction output as a mechanical vacuum pump powered by the combustion engine.

**»Low-friction pistons aimed at reducing $CO_2$«**
Downsizing, charging and direct fuel injection aimed at complying with prescribed exhaust gas limits and reducing fuel consumption and $CO_2$ emissions are still the drivers behind innovation as regards new piston technologies in modern gasoline and diesel engines. Advances in the development of the piston system comprising the pistons, piston rings, piston pins, piston rods and bearings are making a significant contribution to achieving these targets.

For the pistons, this means reduced friction with low weight and high stress. KS Kolbenschmidt has responded to these requirements for gasoline engines with a technology package consisting of the new high-performance alloy KS 309™, the enhanced lightweight concept LITEKS-3® and the shaft coating NANOFRIKS®.

In diesel engines, as well as the high-performance piston cooling systems CONTUREKS® and DYNAMIKS®, targeted materials engineering on the bowl edge is used in combination with thermal protective coatings, through which further potential can be opened up for improvements in performance. As regards the extreme requirements of diesel pistons, where aluminum alloys can no longer be used because of very high thermal and mechanical stress, steel pistons are used both for commercial vehicles and passenger cars. With the patented STEELTEKS™ pistons, a completely new method of constructing and manufacturing monoblock steel pistons has now also become a reality, in addition to established versions. The steel piston, which is manufactured from a single forging, has been especially developed for low compression heights and has now successfully gone into series production for commercial vehicles. Lightweight steel pistons for individual applications for high-performance passenger car diesel engines are at the stage of series development. These allow for a 4% reduction in $CO_2$ emissions.

**»Lightweight aluminum engine blocks and chassis parts«**
Modern, powerful engines are increasingly being replaced with smaller, supercharged engines, with no losses in driving pleasure or engine performance. Legal requirements as regards reducing emissions are also making the already stringent requirements in terms of strength, rigidity and durability of future generations of engines even stricter. This calls for the drive train to be designed even more efficiently and for the consistent use of lightweight materials. Even the latest aluminum casting processes are being continually developed.

This includes, for example, special gating technologies in low pressure chill casting and die casting, and intelligent casting tool cooling during the solidification process in order to increase strength. These casting technologies developed in-house are ideally suited to the production of future engine blocks that can be coated. Friction performance measurements indicate that iron-plated bearing surfaces have a clear advantage over aluminum bearing surfaces. A prototype coating center was commissioned in the fourth quarter of 2011. The first prototypes are undergoing motor testing in order to work with the customer to optimize the tribology system consisting of the piston, piston ring and cylinder working surface, in order to minimize friction and improve resistance to wear and tear. Further vehicle manufacturers have submitted requests to work together on coated cylinder bearing surfaces.

Furthermore, several four-cylinder die-cast crank cases have been developed at the Neckarsulm site, which have gone into series production on behalf of global automotive manufacturers at the Chinese joint venture Kolbenschmidt Pierburg Shanghai Nonferrous Components Co. Ltd. in Shanghai, China.

Development of a gearbox manufactured using low pressure chill casting for heavily loaded trucks has been completed and will go into series production in the first quarter of 2012. Entry onto the commercial vehicle market has therefore been achieved.

### »New materials in response to new requirements«

In 2011, product and process developments in the KS Gleitlager division focused consistently on the major automotive trends of emissions reduction and increasing comfort.

In terms of motor plain bearings, developments in antifriction materials and antifriction layers take account of the use of low-viscosity motor oils and the stronger mixed friction associated with this, as well as the system's increased sensitivity to dirt particles. As such, the lead-free galvanic layer introduced in 2010 is just about to go into series production in further motor projects, while the new polymer antifriction layer is undergoing motor testing in connecting rod bearings. Initial, very promising test results have also been obtained for the completely new steel-aluminum antifriction layer alloy. This composition of materials has been specifically selected, primarily for crankshaft bearing applications, in order to ensure a high level of resistance to wear and tear as well as good flexibility. Preparations for series production start-ups in 2012 have been and will continue to be made by means of validating processes in assembly line production and in the manufacturing of parts.

As regards non-motor plain bearings (Permaglide), the developers concentrated on the development of Permaglide materials with performance characteristics suited to new applications, as well as the technical and commercial optimization of antifriction materials in existing applications. In order to achieve the best possible plain bearing performance, materials, product and process development are closely coordinated.

In the area of common rail pump bearings, which is extremely important to KS Gleitlager in its position as market leader, a new antifriction material with improved properties in biofuel applications is showing initial positive test results. Tests carried out on a new composite material for plain bearings in dual-mass flywheel, belt tensioner and torsional vibration damper applications are also proving positive. Special fillers in the material matrix ensure a high degree of resistance to wear and tear and low-level, constant friction values when subjected to high-frequency vibration stress.

# Rheinmetall Group business trend
# Personnel

**»22,641 employees worldwide committed to the success of Rheinmetall«**

The Defence and Automotive sectors operate in highly competitive markets that are shaped by rapid change and increasing complexity of technologies, processes and products. The employees of the Rheinmetall Group make a significant contribution to attaining corporate goals and securing and expanding the Group's economic success on a sustainable and long-term basis, thanks to their knowledge, skills and dedication. They identify with a distinctive corporate culture that focuses on trust, professional performance, initiative, self-responsibility, shared values and mutual understanding, and work together in partnership across functional, divisional and national boundaries.

As at the 2011 balance sheet date, Rheinmetall employed 22,641 employees, following 21,706 employees on December 31, 2010. Of this total, 19.4% were women (previous year: 19.5%). Of the Group employees, 44.0 % were employed in the Defence sector (previous year: 45.3 %), 55.4 % in the Automotive sector (previous year: 54.0 %) and 0.6 % at Rheinmetall AG and the service companies (previous year: 0.7 %). The percentage of employees working outside Germany rose by 2.1 percentage points to 47.2 % (previous year: 45.1 %), with the Automotive sector expanding its workforce outside Germany by 831 staff. Of the employees based outside Germany, the largest number were in Europe (4,577 employees; previous year: 4,644) (of which non-EU states: 1,596, previous year: 1,638), while 2,327 employees were based in South America (previous year: 2,192) and 1,469 in North America (previous year: 1,325). 1,320 employees (previous year: 1,193) were based in South Africa and 10 in Australia (previous year: 8). In Asia, the number of employees rose to 979 (previous year: 437) following the acquisition of the plain bearing operations of the Indian company Kirloskar Oil Engines Ltd. by KS Gleitlager.

**»Rheinmetall – an attractive employer«**

Thanks to active recruitment marketing, its participation at recruitment fairs and contacts with universities as well as wide-ranging efforts aimed at offering an insight into the working world, Rheinmetall is increasingly positioning itself as an attractive employer for junior staff. The Group-wide consistent presence at university fairs, graduate conferences, recruitment events and online job sites is increasingly bearing fruit. In 2011, the "trendence study" once again looked into the attractiveness of German engineering companies as employers by surveying around 10,000 students at technical schools about to take their final exams. As was the case in 2009 and 2010, Rheinmetall was once again ranked as one of the 100 most attractive employers in Germany in the "Engineering Edition" in the year under review, coming in 78th place following its 82nd place ranking in the previous year. In the past fiscal year, more than 21,000 students from over 100 leading German universities voted in the "Germany's Ideal Employers 2011" survey run by the Agentur Universum. In the first year of the rating, Rheinmetall came in 63rd place of the top 100 employers in the "Engineering" category.

Despite the successes and improvements made to date, efforts will be reinforced further in the area of university marketing, in the online presence and in the use of various social media channels to reach future employees. In particular, it is important to reach Rheinmetall's key target group of young, well-educated engineers to an even better degree and to ensure that these students and young professionals continue to be made aware of the Group as an attractive employer.

In addition to its own junior employees' training, Rheinmetall relies on classic and modern resources for selecting staff and is also in close contact with universities, technical colleges and research institutes in order to get to know suitable graduates from scientific, technical and business courses of study at an early stage. The Group thus creates a platform for presenting its wide range of business activities and the professional opportunities open to its employees. In this context, career orientation placements, integrated management trainee programs and topic suggestions for degree dissertations give an initial insight into the Rheinmetall Group.

**»Future-oriented HR policy supports long-term growth«**

The companies of the Rheinmetall Group are facing increasingly tough competition from other companies for qualified staff. Attracting competent professionals for the companies is therefore one of the key tasks of HR work. In addition to performance-related pay and progressive employee benefits, Rheinmetall focuses in particular on wide-ranging professional prospects in the Defence and Automotive sectors, interdisciplinary career paths, opportunities for employment in the international Group companies and attractive training services, as well as diversity and equal opportunities.

Market, industry and technological trends and their impact on the orientation of the international business activities of the Group companies have been systematically researched, analyzed and assessed for years as part of an integrated approach. In view of demographic factors and the shortage of skilled labor anticipated in a number of locations, the future-oriented development of employees, talented management trainees and experienced specialist and managerial staff that is in line with requirements is an important success factor in the further growth and future viability of the Rheinmetall Group. The high level of qualifications must be secured and expanded continually so that the economic targets of the Group companies can be achieved. Developments in the technologies that are of strategic relevance to Rheinmetall are linked with the planning of staff requirements and staff development and with succession planning, so that the need for technical and managerial staff and specialists to be expected in the companies in the future can be reliably determined.

**»Potential appraisals and succession planning – building blocks for safeguarding the future«**

Future talent is identified and provided with targeted support as part of systematic assessments. On the basis of the transparent Rheinmetall skills model, in which the 17 management skills of relevance to Rheinmetall are incorporated in five skills areas, the current skills profiles of managers and potential management candidates are compared with future requirements as part of a standardized, multi-stage selection and assessment process carried out in all companies of the Rheinmetall Group at regular intervals. The determination of the status quo according to objective criteria allows for open dialog regarding strengths, shortcomings and individual challenges of the employee as well as opportunities for development and promotion based on the employee’s individual assessment of potential.

Career prospects – in the form of a specific position or a career path (management, project and expert career path) – are highlighted in detailed feedback meetings and appropriate measures are agreed in order to further improve the employee’s corporate, technical, methodological, social and management skills. The results and findings of the potential appraisals are also analyzed and summarized and then factored into management and staff development programs that specifically prepare employees for assuming new or extended duties and responsibilities.

The potential appraisal staff development tool facilitates professional, systematic and forward-looking succession planning in the companies. It reliably shows which vacancies are set to arise in the next few years, which of them must be filled as part of strategic HR planning and for which of these posts that must be filled a definite successor has already been found or internal or external recruitment is required. This also ensures that key positions in the Group can be primarily filled with qualified managerial staff from within the Group’s own ranks.

# Rheinmetall Group business trend
# Personnel

### »Training as investment in the future«

A range of training options allow Rheinmetall employees to improve their performance in their area of work and to build on their knowledge of the requirements of their current position. The need for staff development measures is specifically determined at regular intervals on the basis of the Rheinmetall skills model, broken down into salaried employees, managerial staff and exempt employees, either in accordance with the collective training agreement or in the context of management potential appraisals, standard potential appraisals or the Management by Objectives program. As well as the Group-wide and external training and qualification measures bundled in the Rheinmetall Academy, there are also location-specific programs, workshops, training sessions and seminars. For example, new employees get to know their company more quickly through introduction workshops, team leaders are provided with targeted information on how they can successfully motivate and manage their teams, employees of the Rheinmetall holding company attend lectures as part of the open training program and KSPG offers an additional training program in the specialist field of engine technology. The Rheinmetall Group invested around €4.2 million (previous year: €3.4 million) in training programs in Germany alone in 2011. In the year under review, 8,335 employees (previous year: 10,112) benefited from 2,740 qualification measures (previous year: 2,531) over a total of 17,006 days (previous year: 16,951).

### »Rheinmetall academy 2011«

Managerial staff must be adequately prepared for their strategic and operating duties in order to be able to adapt quickly to new challenges and respond to changes on a flexible basis. This not only comes down to specialist suitability, but is also a case of first-rate managerial qualities and skills. In the year under review, the Rheinmetall Academy continued to offer high-quality internal training and qualification events for the fields of strategy, management, leadership, methodological skills, project work and internationalization, in addition to external seminars and events, so that managers and junior staff can adequately prepare for further technical, management and project work. In the year under review, 659 employees attended the 61 (previous year: 37) events held over one or several days, compared to 407 employees in the previous year. The range of topics covered by the Rheinmetall Academy is geared towards current themes, and the range of training courses available is continually expanded to include new programs in accordance with requirements.

The development of managerial and junior staff in the Rheinmetall Group is also promoted by means of special programs, such as the sales development program, the young manager program, the managers' leadership program and the national and international executive development program, which was held for the first time in 2011 and included participants from eight countries. As well as various training modules, networking and therefore “thinking outside the box” of one's own division or area of activity also play a central role in these programs. These training courses and workshops geared towards various hierarchical levels also constitute a platform for employees to exchange overall knowledge, ideas, experience and opinions.

### »Traditionally strong commitment to vocational training«

The operating units primarily require qualified skilled workers in addition to university graduates. In this regard and in the context of social responsibility, the Group continues to attach great importance to qualified, practical, multifaceted and high-quality training, which also includes the option to complete an integrated degree program in a technical or business field. The companies of the Rheinmetall Group continue to take their duty towards training very seriously. The number of training places on offer has remained at a high level for years and they provide training that goes beyond own requirements. Worldwide, 801 young people (previous year: 729) received vocational training, 579 of whom (previous year: 566) were based in Germany.

The diversity of business activities in the companies of the Rheinmetall Group determines the diversity of the range of jobs on offer in the companies requiring training. With over 30 training courses on offer in the field of technology, business and IT, industrial mechanic, mechatronic technician, cutting machine operator and industrial business manager were some of the key job titles at sites in Germany.

The apprenticeship ratio for the German locations was 5.5 % of the workforce, equaling the level of the previous year (5.5 %). The percentage of female apprentices was 18.3 %, following 18.6 % in the previous year. €10.1 million was invested in training in Germany in 2011, following €10.3 million in the previous year. 229 young people (previous year: 159) commenced training at Rheinmetall's German companies in the last fiscal year, while 144 apprentices (previous year: 132) transferred to a permanent or temporary employment contract after successfully completing their training.

### »Fair, performance-related and success-oriented remuneration policy«

Attractive pay arranged on a transparent basis is an important argument in recruitment and in ensuring the retention of dedicated staff at the Company. Rheinmetall offers attractive contract conditions. These are geared towards the scope of the employee's duties, responsibilities and services and are referenced on the market. Here, performance and success-related bonuses and variable salary components are paid in addition to fixed remuneration components.

As regards executives and exempt employees, the Management by Objectives concept is linked with variable salary components. An individual variable proportion of income is determined subject to the attainment of agreed individual targets and the success of the Company. Depending on the extent to which targets are achieved, this ranges between 0 % and 200 % of variable annual target compensation. The fact that these income components are linked to targets provides incentive to act on one's own responsibility and to take on challenges.

Division heads, managers and executives receive a long-term incentive in addition to these short-term components. This is geared towards long-term corporate success and includes payment of 40 % of the long-term incentive amount in Rheinmetall shares, which are subject to a four-year lockup period. The number of shares granted is based on a reference share price which corresponds to the average price on the last five trading days in February of the subsequent fiscal year. 60 % of the long-term incentive is paid in cash and is used to pay tax on the Rheinmetall shares immediately.

The Company's success is reflected in two ways, also for staff covered by collective wage agreements: Firstly, employees receive an annual bonus subject to the performance of their division or sector and, secondly, the increase in the value of the Company achieved is paid out in a success-oriented component in the company pension, thus leading to improved support in old age.

### »Pensions – an important component of HR policy«

The Rheinmetall Group has been supporting its employees for many years with innovative company pension models in order to financially secure their standard of living in retirement. The pension scheme has an identical structure for staff and managers, but higher incomes are reflected in increased benefits. This system, which applies to all sites in Germany, consists of three components: A reliable basic plan, a performance-related intermediate plan linked to the increase in Company value and a supplementary plan financed by the employee, allowing for various forms of compensation such as deferred compensation, direct insurance or a Riester pension.

# Rheinmetall Group business trend
# Personnel

### »Employees take up Rheinmetall shares«

As was the case in previous years, Rheinmetall set up an employee share purchase program in the year under review. In April and November 2011, employees once again had the opportunity to purchase Company shares on preferential terms and thus to participate in the corporate success of their Company as a joint owner. In addition to Rheinmetall Group companies based in Germany, employees of 19 European Group companies were also entitled to subscribe to shares. In the two tranches of 2011, a total of 1,521 employees (previous year: 952) purchased 169,743 Rheinmetall shares (previous year: 100,338), which are subject to a minimum lockup period of two years. Since the share purchase program was introduced in 2008, employees have purchased 680,454 Rheinmetall shares.

### »A reflection of diversity«

People shape and mold the profile, reputation and distinctiveness of a company. 22,641 Rheinmetall employees make up an international community in which a number of cultures, a range of ethnic and social backgrounds and a wide variety of skills, talents and expectations are reflected. With sites in 24 countries spread over five continents, supply relationships in more than 80 countries and 10,682 employees abroad (previous year: 9,799), diversity is already a reality and a factor in the success of global business operations. Daily practice shows that this diversity in languages, education and training, abilities, perspective and ways of thinking and working has a positive impact on cooperation and is an asset to the corporate culture. Openness to foreign cultures and exchange between the sites is also encouraged through secondments. Through assignments outside their home country, employees are able to gain new skills and strengthen their intercultural competence. This also improves the transfer of knowledge across international borders within the Group. In 2011, 62 German employees (previous year: 89) completed a stay abroad, for which they also prepared themselves through seminars dealing with country and culture-specific and intercultural themes.

### »Women at Rheinmetall«

The defence and automotive industries are traditionally dominated by men, who primarily choose technical or scientific subjects during their training or studies. The proportion of female graduates from engineering courses of relevance to Rheinmetall is around 20 %. The ongoing improvement of attractiveness as an employer pursued by Rheinmetall is just beginning to lead towards the desired effect on the employment market – encouraging more young women in technical professions to choose a career in the Rheinmetall Group.

When selecting staff to fill managerial positions, the Executive Board members and managers focus on the specialist and person requirements for the role in question and look for the person that best meets these requirements. If it is a case of choosing from several female or male candidates with the same level of qualification, it is ensured that women are given due consideration when selecting the person to fill the vacancy. In the year under review, the Rheinmetall Group employed 2,052 managers across the first four levels of the Company, of whom 148 were women (7.2 %). Of the senior management staff comprising approximately 270 people, 5 % are women. 8 % of participants in the young manager program are women, and 6 % in the executive development program.

### »Equal opportunities for all«

People with disabilities and employees with health limitations are at Rheinmetall integrated into everyday working life and are able to contribute their skills and ideas in full. The promotion of strengths and potential remains the main focus here. A key prerequisite in order to achieve this is individually adapted workplaces, which offer good opportunities for development and lead to levels of productivity that are in no way inferior to those of colleagues without a disability. In the year under review, 657 severely disabled persons (previous year: 659) were employed in the German companies of the Rheinmetall Group.

### »Improved work-life balance«

Professional success is dependent on factors including contentment in one's private life. The Rheinmetall Group regards the wish of many employees to be able to create more of a balance between their career and their family and private interests through more flexible working hours as an obligation in HR policy. Working hour models with varying weekly working hours and a range of part-time options as well as flexitime on trust allow employees a more flexible timeframe. Rheinmetall also supports mothers and parents with a financial contribution in order for them to find individual childcare solutions for their child or children. The option to obtain parental benefit for a longer period is also utilized in the Rheinmetall companies. In 2011, 108 employees were on parental leave in the German companies (71 female employees, 37 male employees). In the year under review, the Swiss-based Rheinmetall Air Defence AG was chosen by the Canton of Zürich as the winner of the "Trade and Industry" category in the Prix Balance $^{ZH}$ awards for its particularly family-friendly working conditions.

### »Occupational health and safety«

Preventing accidents and safeguarding the health of employees at their place of work are some of the key aims. With regard to health and safety in the workplace and health management, Rheinmetall focuses on identifying and assessing potential risks and on health care in line with requirements, which maintains and supports the personal wellbeing and professional performance of employees. This includes the safety of facilities and production processes, modern equipment, the ergonomic design of work stations and good working conditions, along with company medical services. Employees also benefit from various prevention programs as well as occupational health checks. This ranges from free-of-charge vaccinations and regular check-ups to internal and external sporting activities and consultancy services, right up to medically coordinated rehabilitation following an extended period of illness. In the year under review, KSPG launched a pilot project with the aim of bundling previous measures and services offered in occupational health and safety and establishing a health management system integrated across the sector.

### »Demographic change«

In Germany and other developed countries, companies are being faced with new challenges as a result of the increasing shift in the age structure. The structure of the population is changing in an unprecedented manner due to low birth rates and increasing life expectancy. This trend is also having an impact on the composition of workforces: Competition for suitable junior staff is becoming more intense, the number of employees aged between 40 and 49 is decreasing and the main focus of company workforces is shifting towards the over 50s. Interdisciplinary teams are developing new concepts based on structural analyses and simulation calculations. These are focused on areas including the targeted transfer of knowledge and experience from older colleagues to younger employees, the formation of mixed-age teams, the consistent training of junior employees and changes to the corporate culture. They also include adjustments to working and organizational processes and measures to promote good health. The average age of employees (excluding apprentices and interns) in the Rheinmetall Group in 2011 was 43.5 years (previous year: 43.3 years). The length of service remained the same as the previous year in the year under review at 14.2 years.

### »Further key personnel figures«

Personnel expenses totaled €1,260 million in fiscal 2011, following €1,181 million in the previous year. Wages and salaries accounted for €1,037 million (previous year: €975 million). Social insurance contributions, pension expenses and related employee benefits totaled €223 million (previous year: €206 million). Based on capacity, staff costs per employee amounted to €62,000 (previous year: €59,000). The ratio of personnel expenses to total operating performance dropped from 29 % to 28 %. Sales per employee rose from €199,000 in 2010 to €218,000 in 2011.

# Rheinmetall Aktiengesellschaft

**»Rheinmetall AG fulfills strategic holding functions«**

Under the management of Rheinmetall AG, which is listed on the stock exchange and headquartered in Düsseldorf, the Rheinmetall Group is broken down into two sectors – Defence and Automotive. As the management holding company, Rheinmetall AG is responsible for the consistent management and economic controlling of the Rheinmetall Group. It defines the strategies, framework guidelines and objectives for the Group as a whole. Key administrative functions that are responsible for support and service tasks for the Rheinmetall Group as a whole are combined within Rheinmetall AG. These comprise the overall management of matters concerning strategy, HR policy, legislation and tax, communication with key target groups in the Company environment, particularly the media, the capital market and shareholders, mergers and acquisitions, central finance and liquidity management, Group controlling, Group accounting and the optimization of the investment portfolio. Rheinmetall AG ensures efficient management by means of standardized planning, controlling and management processes that are applied across the Group. It monitors the Group-wide observance of legislation, guidelines and regulations according to standard criteria as part of the compliance system.

Rheinmetall AG holds direct and indirect interests in 157 companies (previous year: 149) belonging to the Rheinmetall Group. 130 companies (previous year: 122) are fully consolidated in the consolidated financial statements. As in the previous year, 27 companies are carried at equity. An overview of these companies is given on pages 147 to 151.

The single-entity financial statements of Rheinmetall AG have been prepared in accordance with the provisions of the German Commercial Code (HGB) and the German Stock Corporation Act (AktG).

**»Earnings situation of Rheinmetall AG«**

In addition to the results of subsidiaries, the earnings situation of Rheinmetall AG is determined to a large extent by expenses and income in central Group financing.

Income statement of Rheinmetall AG in accordance with HGB (summarized version) *€ million*

| | 2010 | 2011 |
|---|---:|---:|
| Investment income | 67 | 179 |
| Net interest | (31) | (32) |
| Other operational income | 62 | 126 |
| Personnel expenses | 28 | 27 |
| Other expenses | 53 | 108 |
| EBT | 17 | 138 |
| Taxes on income and revenue | (2) | (9) |
| Net profit for the year | 15 | 129 |
| Changes in retained earnings | 43 | (60) |
| Net earnings | 58 | 69 |

Net investment income of €179 million was achieved in fiscal 2011, compared with €67 million in the previous year. The Defence sector accounted for €133 million of this (previous year: €59 million) and the Automotive sector for €49 million (previous year: €9 million). Net investment income from the Defence sector in fiscal 2011 includes a dividend of €49 million from Rheinmetall Air Defence AG, Zürich.

Net interest from central financing is around the same level as the previous year at €-32 million. Here, a €6 million increase in interest income from cash pooling and current receivables from affiliated companies is met with an increase in interest expenses for bonds and promissory note loans totaling €4 million. The expenses recognized in fiscal 2011 from the conclusion of the new syndicated loan facility totaled €3 million.

In connection with the performance of the duties of a holding company, other operating income and expenses were incurred amounting to €18 million (previous year: €9 million), along with personnel expenses of €27 million (previous year: €28 million). The year-on-year improvement in these income and expense items, which totaled €10 million, was essentially due to the increased net currency/foreign exchange result.

Earnings before taxes rose by €121 million to €138 million. Tax expenses amounted to €9 million (previous year: €2 million). After deduction of taxes, net income of €129 million remained for fiscal 2011 (previous year: €15 million). After appropriations to retained earnings, net earnings of €69 million were reported.

The Executive and Supervisory Boards of Rheinmetall AG are to propose to the Annual General Meeting on May 15, 2012 that the net earnings be used to pay a dividend of €1.80 per share, whereby the treasury shares held by Rheinmetall AG as treasury stock (as at December 31, 2011: 1,350,842) are not entitled to a dividend.

### »Asset and financial situation of Rheinmetall AG«

The asset situation of Rheinmetall AG is largely shaped by its holding function, i.e. by the management of investments and the financing of Group activities. This is reflected above all in the amount of the investments held and in the receivables due from and payables owed to Group companies.

The total assets of Rheinmetall AG fell by €55 million to €2,036 million. Here, a €118 million decline in cash and cash equivalents is met with a €50 million increase in financial assets.

The financial assets include shares in associated companies in the amount of €1,153 million (previous year: €1,103 million). This represents a share in total assets of 57 % (previous year: 53 %). Receivables from and liabilities to associated companies amounted to €424 million (previous year: €402 million) and to €709 million (previous year: €787 million) respectively. They account, respectively, for 21 % and 35 % of total assets.

Of the total assets of €2,036 million as at December 31, 2011 (previous year: €2,091 million), €581 million (previous year: €510 million) is financed from equity. The equity ratio increased from 24 % to 29 %. The net income led to growth of €129 million, which was offset by a reduction of €58 million owing to the dividend payment for 2010.

# Rheinmetall Aktiengesellschaft

Liabilities fell by €136 million to €1,323 million as at December 31, 2011. Of this decline, €78 million was the result of the reduction in liabilities to subsidiaries and €65 million was due to the early repayment of promissory note loans.

Balance sheet of Rheinmetall AG in accordance with HGB (summarized version) *€ million*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Fixed assets | | |
| Intangible assets, property, plant and equipment | 23 | 22 |
| Financial assets | 1,120 | 1,170 |
| | 1,143 | 1,192 |
| Current assets | | |
| Receivables from affiliated companies | 402 | 424 |
| Other receivables, other assets | 21 | 13 |
| Cash in hand | 525 | 407 |
| | 948 | 844 |
| | | |
| Total assets | 2,091 | 2,036 |

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Equity | 510 | 581 |
| | | |
| Provisions | 122 | 132 |
| | | |
| Liabilities | | |
| Bond, liabilities due to banks | 650 | 586 |
| Liabilities to affiliated companies | 787 | 709 |
| Other liabilities | 22 | 28 |
| | 1,459 | 1,323 |
| | | |
| Total liabilities | 2,091 | 2,036 |

# Corporate responsibility (Sustainability report)

The roots of Rheinmetall date all the way back to 1889. Founded as "Rheinische Metallwaaren- und Maschinenfabrik Aktiengesellschaft", today the Company is one of the hundred largest listed corporations in Germany and enjoys success on the international defence and automotive markets.

The high level of technological expertise of the Rheinmetall Group in its Defence and Automotive sectors, based on more than 100 years' experience, today benefits both people and the environment. The Automotive sector has not only been working on solutions for environmentally friendly automotive technology since the latest debate surrounding climate protection – in times of an increasing number of vehicles around the world and global warming, the KSPG Group, as a long-standing development partner of national and international automotive manufacturers, meets the requirements of manufacturers in the areas of reducing emissions, lowering consumption, reducing weight and optimizing performance with innovative solutions, thus helping to ensure that mobility does not conflict with the protection of the environment. Foreign deployments, peacekeeping missions, rapid deployment forces in crisis regions: With the growth in operations abroad, the armed forces of the 21st century find themselves facing new challenges. Effective protection systems are of central importance in the deployment scenarios of today and the future, in order to offer a maximum level of safety to armed forces. Rheinmetall Defence specializes in the development and production of components and systems for the protection of people, vehicles, aircraft, ships and assets and protects forces involved in foreign operations in its role as equipment supplier to the German armed forces and Nato nations.

The companies of the Rheinmetall Group are involved in the economic, ecological and social conditions of various countries and regions in the context of its international operations and production activities. Rheinmetall is committed to fair competition and to acting in a way that is legal and socially and ethically responsible. Sustainable economic activity is an integral part of business and production processes and also helps to secure the Company's long-term future. In addition to continuity, economic growth and compliance with the principles of good corporate management, the self-image and corporate culture of the Rheinmetall Group also include its responsibility towards shareholders, customers and employees and the respectful handling of natural resources.

The principles of social responsibility are recognized in the Rheinmetall Code of Conduct adopted in 2003. In accordance with this, Rheinmetall will do its utmost to link its economic, environmental and social targets with its medium-term and long-term strategies and planning and with its daily corporate decisions in the context of a corporate development strategy geared towards sustainability. Principles of lawful and responsible actions are specified in the compliance guideline. The aim is to counteract any potential unlawful or unethical conduct at an early stage and prevent misconduct by means of appropriate measures.

The Rheinmetall Group pursues its commitment to society directly on a local basis. Choosing to support projects, initiatives and organizations is largely at the discretion of the divisions, as requirements vary greatly between the various locations where Rheinmetall operates. Rheinmetall is also committed to promoting interest in technology, science and craft in the areas where it is located. Understand technology and try it out for yourself – this is the slogan under which young people are given the opportunity – as part of school partnerships, for example – to get to know technology through hands-on tasks and develop a better understanding of links between technology and commerce by gaining an early insight into the industry.

Since October 2011, Rheinmetall has provided detailed information on sustainability in the Rheinmetall Group on its website at http://csr.rheinmetall.com.

# Board remuneration report

### »Remuneration of the Executive Board«

Rheinmetall AG's pay system is geared towards sustainable corporate development. Using an assessment basis spanning several years, incentives are provided for a sustainable corporate management strategy, in particular as part of the long-term incentive program (LTI). The Supervisory Board of Rheinmetall AG resolves upon and regularly reviews the amount of Executive Board remuneration and any significant employment contract elements following preparation work carried out by the Personnel Committee. The Supervisory Board has performed an extensive review of the remuneration system of the Executive Board on the basis of all relevant information, and has looked in particular at whether the total remuneration of Executive Board members is proportionate to the scope of responsibilities of the Executive Board member in question, his personal performance and the economic situation and success of the Company in comparison with industry peers and ensuring that this remuneration does not exceed standard remuneration unless there are special reasons for this. Remuneration is calculated in such a way as to ensure that it is competitive on a national and international scale, thus offering an incentive for dedicated and successful work. The Supervisory Board most recently reviewed the suitability of current Executive Board remuneration at its meeting on March 22, 2011 and determined that it was appropriate.

Total remuneration is performance-based and is made up of various components. These comprise fixed annual remuneration not linked to performance, performance-related variable remuneration comprising a short-term incentive program (STI) and a long-term incentive program (LTI) as well as fringe benefits and pension commitments. The fixed component makes up 60% and the STI 40% of the annual target salary.

### »Fixed component«

The fixed component is paid out on a monthly basis in twelve equal portions. In addition, Executive Board members receive fringe benefits in the form of non-cash remuneration. This mainly consists of contributions to statutory social pension insurance (or any exempting life insurance in lieu) plus the use of a company car.

### »Performance-related variable remuneration«

Performance-related variable remuneration comprises two elements – the STI and the LTI.

The target value (100 %) for the STI is based on planning for the fiscal year. This is subject to the development of two key figures, EBT and return on capital employed (ROCE), which are each weighted at 50% and used as criteria for determining this figure. The amount paid from the STI ranges between 0% and 200 % of the target amount. 200% of the target amount is paid if the planned value is exceeded by 10%. No payment is made from the STI if target achievement falls 30% below the planned value. In the case of intermediate target achievement values, a corresponding value within the range is paid out. The target parameters are also used, in combination with others, by managerial staff in order to ensure the uniformity and consistency of the target system in the Group as a whole in this respect.

In order to gear the Executive Board remuneration structure more strongly towards sustainable corporate development, measures taken have also included the introduction of a LTI linked to the share price. The LTI provides for a distribution at the end of the fiscal year in question based on the calculation of the average adjusted EBT from the last three fiscal years. This distribution amount is divided into a cash portion and an equity portion.

The number of shares granted is based on a reference share price which corresponds to the average price on the last five trading days in February of the subsequent fiscal year. The shares granted are subject to a four-year lockup period, during which the shares granted are subject to all opportunities and risks inherent in capital market performance. As part of the LTI, the figure to be taken into account when calculating the distribution amount (average adjusted EBT from the last three fiscal years) is limited to a maximum of €300 million. This is therefore a cap intrinsic to the system. As such, the LTI is subject to results achieved in the past and the performance of the share price in the future. The cash portion is mainly used to pay the tax bill incurred upon receipt of the shares and the cash portion.

More than 60 % of total variable remuneration relates to the LTI, on the basis of the planned values for 100 % target achievement. The LTI therefore prevails to a great degree. As such, account is taken of this long-term incentive component.

At the Supervisory Board meeting of March 22, 2011, the LTI was modified with regard to regulations for new Executive Board members. According to this, in the case of future new Executive Board members, who for the purpose of the LTI cannot provide evidence as yet of a past term of service lasting three years, at the end of the first year of appointment, a third of adjusted EBT for that year will be used as the main assessment basis, and at the end of the second year, half of the average adjusted EBT for the past two years will be used as the main assessment basis. In the event of positive Company development, in the third year the new Executive Board member will receive “deferred remuneration” from the first year of his appointment, and “deferred remuneration” in the fourth year from the second year of his appointment. The assessment basis for this “deferred remuneration” of the Executive Board member is two-thirds of the difference between the assessment basis for long-standing Executive Board members and his own assessment basis in the first and second year.

Average adjusted EBT for fiscal 2010 totaled €181 million. On the basis of the reference share price of €58.71 for the end of February 2011, a total of 15,413 shares were transferred to the Executive Board of Rheinmetall AG for fiscal 2011 on April 1, 2011. The CEO, Klaus Eberhardt, received 7,707 shares, while Dr. Gerd Kleinert and Dr. Herbert Müller each received 3,853 shares. The corresponding expenditure is recorded in the remuneration report for the previous year. Average adjusted EBT totaled €210 million for the year under review.

The employment contracts make provision for the ability of the Supervisory Board to grant, in exceptional cases and at its own discretion, a special bonus exclusively for (i) special achievements or specific efforts, (ii) if and to the extent in which the Executive Board member has made a particular difference to the Company through his activities (e.g. restructuring success in a particularly difficult market environment). Executive Board members are not entitled to the granting of this special bonus. No special bonuses were granted in fiscal 2011 or in the previous year.

In addition to salaries, a group accident and invalidity insurance policy and a D&O insurance policy (Directors’ and Officers’ liability insurance) are also in place, whereby a deductible of 10 % of the loss or one and a half times the annual fixed remuneration has been agreed.

The contracts of Executive Board members provide for a compensation payment in the event that the position on the Executive Board is terminated prematurely without cause. This is limited to a maximum of two years’ salary including fringe benefits (compensation cap) and shall not provide any more payment than the remaining term of the employment contract. The members of the Executive Board did not receive any benefits or equivalent entitlements from third parties with regard to their activities as Executive Board members in fiscal 2011 or in the previous year.

# Board remuneration report

### »Pensions«

Executive Board members are entitled to defined benefit pension commitments in the form of pension amounts agreed on the basis of individual contracts, based on an average of 27 % of the annual target salary. The retirement age has been fixed at the age of 63 on average. The Company has set up provisions for future claims.

### »Total remuneration of the Executive Board«

Individual details of the remuneration of the Executive Board in fiscal 2011 and pension commitments attributable to individual members of the Executive Board can be found in the following table, in addition to the respective values for the previous year:

*€ million*

| | Fixed remuneration incl. fringe benefits | Performance based remuneration (STI) | LTI | Total | Annual post-retirement pension | Current service cost-pensions |
|---|---|---|---|---|---|---|
| Klaus Eberhardt | 840 | 972 | 1,155 | 2,967 | 400 | 388 |
| Previous year | 838 | 1,086 | 996 | 2,920 | 400 | 343 |
| Dr. Gerd Kleinert | 546 | 680 | 578 | 1,804 | 203 | - |
| Previous year | 537 | 676 | 498 | 1,711 | 203 | 304 |
| Dr. Herbert Müller | 425 | 518 | 578 | 1,521 | 175 | 131 |
| Previous year | 425 | 560 | 498 | 1,483 | 175 | 113 |
| **Total** | **1,811** | **2,170** | **2,311** | **6,292** | | |
| Previous year | 1,800 | 2,322 | 1,992 | 6,114 | | |

### »Remuneration of the Supervisory Board«

The remuneration of the Supervisory Board of Rheinmetall AG is regulated in Section 13 of the bylaws. According to these, Supervisory Board members receive remuneration comprising a fixed and a variable component, in addition to reimbursement of expenses and meeting attendance fees. The amount of variable remuneration is subject to the dividend distribution. The Supervisory Board Chairman and Vice-Chairman receive double this compensation. The fixed remuneration component is €30,000 and the variable component is €200 for each euro cent of dividend paid out in excess of €0.60. However, this is subject to a cap of €30,000.

Supervisory Board members receive an additional 25 % of their fixed and variable remuneration for any committee membership, subject to a ceiling of 50 % in the case of multiple offices. A committee chairman is paid an additional 50 %, yet this may not exceed 100 % if chairing several committees.

The attendance fee for Supervisory Board meetings is €1,000. When attending committee meetings that are not held on the same day as a Supervisory Board meeting, the attendance fee is €500. Total expenditure for meeting attendance fees in the reporting year totaled €102,000 (previous year: €80,000).

Subject to the resolution of the Annual General Meeting on May 15, 2012 regarding the proposed appropriation of net income for 2011, Supervisory Board members will receive the following remuneration for fiscal 2011.

€

| | Fixed remuneration | Variable remuneration | Fixed committee remuneration | Variable committee remuneration | 2011 remuneration |
|---|---|---|---|---|---|
| Klaus Greinert | 60,000 | 48,000 | 30,000 | 24,000 | 162,000 |
| Previous year | 60,000 | 36,000 | 30,000 | 18,000 | 144,000 |
| Joachim Stöber | 60,000 | 48,000 | 15,000 | 12,000 | 135,000 |
| Previous year | 60,000 | 36,000 | 15,000 | 9,000 | 120,000 |
| Prof. Dr. Andreas Georgi | 30,000 | 24,000 | - | - | 54,000 |
| Previous year | 30,000 | 18,000 | - | - | 48,000 |
| Dr. Siegfried Goll | 30,000 | 24,000 | - | - | 54,000 |
| Previous year | 30,000 | 18,000 | - | - | 48,000 |
| Dr. Peter Mihatsch | 30,000 | 24,000 | 7,500 | 6,000 | 67,500 |
| Previous year | 30,000 | 18,000 | 7,500 | 4,500 | 60,000 |
| DDr. Peter Mitterbauer | 30,000 | 24,000 | - | - | 54,000 |
| Previous year | 30,000 | 18,000 | - | - | 48,000 |
| Detlef Moog | 30,000 | 24,000 | - | - | 54,000 |
| Previous year | 14,417 | 8,650 | - | - | 23,067 |
| Henning von Ondarza | - | - | - | - | - |
| Previous year | 15,000 | 9,000 | - | - | 24,000 |
| Prof. Dr. Frank Richter | 30,000 | 24,000 | 15,000 | 12,000 | 81,000 |
| Previous year | 30,000 | 18,000 | 15,000 | 9,000 | 72,000 |
| Reinhard Sitzmann | - | - | - | - | - |
| Previous year | 24,250 | 14,550 | - | - | 38,800 |
| Toni Wicki | 30,000 | 24,000 | - | - | 54,000 |
| Previous year | 2,083 | 1,250 | - | - | 3,333 |
| Dr. Ludwig Dammer | - | - | - | - | - |
| Previous year | 20,000 | 12,000 | - | - | 32,000 |
| Heinrich Kmett | 30,000 | 24,000 | 7,500 | 6,000 | 67,500 |
| Previous year | 30,000 | 18,000 | 7,500 | 4,500 | 60,000 |
| Dr. Rudolf Luz | 30,000 | 24,000 | - | - | 54,000 |
| Previous year | 30,000 | 18,000 | - | - | 48,000 |
| Dr. Michael Mielke | 30,000 | 24,000 | - | - | 54,000 |
| Previous year | 10,000 | 6,000 | - | - | 16,000 |
| Wolfgang Müller | 30,000 | 24,000 | - | - | 54,000 |
| Previous year | 30,000 | 18,000 | - | - | 48,000 |
| Harald Töpfer | 30,000 | 24,000 | - | - | 54,000 |
| Previous year | 30,000 | 18,000 | - | - | 48,000 |
| Wolfgang Tretbar | 30,000 | 24,000 | 7,500 | 6,000 | 67,500 |
| Previous year | 30,000 | 18,000 | 7,500 | 4,500 | 60,000 |
| Peter Winter | 30,000 | 24,000 | 7,500 | 6,000 | 67,500 |
| Previous year | 30,000 | 18,000 | 7,500 | 4,500 | 60,000 |
| **Total** | **540,000** | **432,000** | **90,000** | **72,000** | 1,134,000 |
| Previous year | 535,750 | 321,450 | 90,000 | 54,000 | 1,001,200 |

In addition, Rheinmetall refunds VAT on Supervisory Board remuneration to the members of the Supervisory Board.

# Declaration of corporate governance

Rheinmetall is traditionally committed to a responsible, fair, reliable and transparent corporate policy geared towards leveraging and developing corporate potential, achieving medium-term financial targets and increasing the value of the Company on a systematic and sustainable basis. Stock corporation law, capital market law, codetermination law, the Company bylaws and the German Corporate Governance Code based on internationally recognized standards form the basis for the organization of management and monitoring in the Company, with the aim of making structures transparent and thus strengthening the confidence held by national and international investors, business partners, analysts, the media and employees in the business policy, management and supervision of Rheinmetall AG and establishing this confidence on a sustainable basis. Effective corporate governance that protects the interests of stakeholders, early reporting, correct accounting and efficient cooperation between the Executive and Supervisory Boards plays a key part at the Rheinmetall Group.

## »Declaration of conformity in accordance with Section 161 of the German Stock Corporation Act (AktG) «

Section 161 of the German Stock Corporation Act (AktG) obliges the Executive and Supervisory Boards of a stock corporation listed in Germany to declare once a year that the recommendations of the Commission of the German Corporate Governance Code published by the Federal Ministry of Justice in the official section of the electronic Federal Gazette have been and are being complied with, or which recommendations have not been or are not being implemented and why not. On December 13, 2011, the Executive Board and Supervisory Board issued the following updated declaration on the recommendations of the German Corporate Governance Code as amended up to May 26, 2010 in accordance with Section 161 AktG:

“The Executive Board and Supervisory Board of Rheinmetall AG hereby declare,

1. that Rheinmetall AG has fully carried out the recommendations of the Commission of the German Corporate Governance Code as amended up to May 26, 2010, officially communicated in the electronic Federal Gazette on July 2, 2010, since it issued its last declaration of conformity dated December 2010.

2. that Rheinmetall AG will in future fully carry out the recommendations of the Commission of the German Corporate Governance Code as amended up to May 26, 2010, officially communicated in the electronic Federal Gazette on July 2, 2010.

Düsseldorf, December 2011
Rheinmetall Aktiengesellschaft
The Supervisory Board      The Executive Board”

The current declaration of conformity, along with the declarations of conformity issued in previous years, has been published on the Company’s website (www.rheinmetall.com) in the section “Group – Corporate Governance”.

## »Shareholders and the Annual General Meeting«

Shareholders of Rheinmetall AG exercise their rights of codetermination and control at the Annual General Meeting, which is convened by the Executive Board or Supervisory Board as prescribed by law, or when it appears necessary in the interest of the Company. Each share grants one vote. This excludes treasury shares held by the Company, which do not entitle the Company to rights. The Annual General Meeting is called at least 38 days prior to the date of the Annual General Meeting, together with a notification of upcoming agenda items and an explanation of the conditions of participation and rights of shareholders.

Every shareholder that registers in due time and submits proof of shareholder status is entitled to participate in the Annual General Meeting, to take the floor on agenda items in these meetings and to ask relevant questions and propose relevant motions. Shareholders who cannot or do not wish to attend in person may appoint a bank, a shareholders' association, a proxy at their discretion or a Rheinmetall-appointed voting proxy to exercise their voting right at the Annual General Meeting, or they may exercise their voting right by means of an absentee ballot.

The Executive Board submits to the Annual General Meeting Rheinmetall's single-entity and consolidated financial statements. Fundamental corporate decisions such as amendments to the bylaws and capital measures, the appropriation of net income for the year, the approval of the activities of the Executive Board and Supervisory Board, the selection of shareholder representatives on the Supervisory Board and the selection of the auditor require the approval of the Annual General Meeting, which can also pass resolutions on the approval of the remuneration system for Executive Board members. Subject to other statutory provisions, the resolutions of the Annual General Meeting are adopted by means of a simple majority of votes cast and, where the law prescribes both a voting and shareholding majority, by means of a simple majority of the common stock represented in the passing of the resolution. All documents and information on the Annual General Meeting are made available to download on the Rheinmetall AG website. The 2011 Annual General Meeting took place in Berlin on May 10, 2011. The Executive Board presentation, the attendance level and the results of the votes were made available on the Internet following the event.

### »Management, control and organization of the Rheinmetall Group«

Rheinmetall AG, a company headquartered in Düsseldorf, manages the Rheinmetall Group with its two sectors, Defence and Automotive, and defines long-term strategies and corporate policies in its role as management holding company. Rheinmetall AG is a listed company under German law and is subject, in particular, to the provisions of the German Stock Corporation Act, capital market regulations and the provisions of the bylaws. A fundamental principle of the German law on stock companies is the dual management principle, which assigns managerial responsibilities to the Executive Board and monitoring and advisory responsibilities to the Supervisory Board. The Executive and Supervisory Boards cooperate constructively in a partnership and in an atmosphere of trust on the basis of sharing tasks and responsibilities, with the aim of ensuring the Company's continued existence as a going concern and a sustainable increase in the value of the Company. Rules of procedure are in place for both boards, containing regulations on the composition, tasks, responsibilities and areas subject to approval.

The Executive Board of Rheinmetall AG ensures that the management of the sectors is focused on the interests of the Group as a whole. The clearly demarcated Defence and Automotive sectors, each assigned all the necessary functions, constitute independent sectors within the strategies, targets and guidelines defined by the Group's Executive Board, with responsibility for global operations and each with its own management hierarchy. This structure ensures high flexibility, rapid market access and distinct customer proximity. The respective divisions of the Defence and Automotive sectors are responsibly managed by the Management Board Defence and the Executive Board of KSPG AG. The division heads report to the members of the Executive Board of the sectors on current business development and discuss strategies, targets and measures during regular review and strategy meetings.

### »Structure and function of the Executive Board«

The Executive Board manages the Company independently and on its own responsibility, in accordance with the law, the bylaws, its rules of procedure and the areas subject to approval by the Supervisory Board and taking into account the resolutions of the Annual General Meeting, with the aim of a sustainable increase in value. It is responsible for the overall management of the Company.

# Declaration of corporate governance

It defines long-term strategies and corporate policy as well as the structure and organization of the Rheinmetall Group and allocates resources. It represents the Company in dealings with third parties. In accordance with Section 6 (1) of the bylaws, the Executive Board of the Company must consist of at least two people. The number of members is determined by the Supervisory Board. The Executive Board currently consists of four members who take overall responsibility for the management of the Company in accordance with uniform objectives. The CEO, Klaus Eberhardt, is the Director of Industrial Relations and up until December 31, 2011 was responsible for the Defence sector, which is now represented in the Executive Board by Armin Papperger who was appointed as a new member of the Executive Board with effect from January 1, 2012. Dr. Gerd Kleinert is responsible for the Automotive sector, while Dr. Herbert Müller undertakes the role of CFO.

Executive Board members bear joint responsibility for company management. They are obliged to act in the best interests of the Company and in due consideration of stakeholder interests. Notwithstanding their overall responsibility, each Executive Board member acts on his own authority in the Executive Board division/corporate sector assigned to him in accordance with the schedule of responsibilities, yet must also ensure that sector and division interests are always subordinate to the overall interests of the Company. In accordance with Section 6 of the Company bylaws, the Executive Board is subject to rules of procedure which govern aspects including cooperation in the Executive Board. The Executive Board as a whole generally makes decisions at meetings which take place at least once a month. The CEO is responsible for coordinating all Executive Board divisions and corporate sectors of the Executive Board. He must work towards ensuring that the management of all Executive Board divisions and corporate sectors is geared consistently towards the targets established by means of Executive Board resolutions.

The specific details of collaboration with the Supervisory Board are based on the bylaws and the rules of procedure for the Supervisory Board of Rheinmetall AG, which govern transactions and measures requiring approval and the information and reporting requirements of the Executive Board. The CEO bears overall responsibility for providing the Supervisory Board and its members with information. He regularly informs the Supervisory Board Chairman of the progress of business activities and the situation of the Company and confers with him on the strategy, business development and risk management of the Company. He informs the Supervisory Board Chairman immediately of important events which are of key significance to the assessment of the situation and development as well as to the management of the Company.

**»Structure and function of the Supervisory Board«**

The Supervisory Board of Rheinmetall AG consists of 16 members in accordance with the German law on codetermination (MitbestG 1976), eight of whom are selected by the shareholders and eight by the employees. The period of office for the Supervisory Board is five years. When carrying out their work, Supervisory Board members are committed to Rheinmetall's best interests, but are not bound by specific orders or instructions. When nominations are made for Supervisory Board elections, consideration is to be given to specialist qualifications and personal competence and to diversity in the composition of the Board and independence as defined by the German Corporate Governance Code. Every Supervisory Board member ensures that he has sufficient time available to carry out his work. During the year under review, the Supervisory Board comprised 16 men. Former Executive Board members of Rheinmetall AG are not represented on the Supervisory Board. With the exception of Dr. Siegfried Goll, Detlef Moog and Toni Wicki, the term of office for the other shareholder and employee representatives terminates at the close of the Annual General Meeting resolving on the approval of Board activities for fiscal 2011. Dr. Siegfried Goll has been elected up to the close of the Annual General Meeting in 2013, while the Supervisory Board seats of Detlef Moog and Toni Wicki expire at the close of the 2016 Annual General Meeting.

The Supervisory Board advises and monitors the Executive Board in its management of the Company and supports it based on its expertise and experience. It is involved in strategies and planning as well as in all issues of key significance to the Company. Significant transactions and important measures, in particular those that will fundamentally alter the assets, financial situation or earnings of the Company, are to be presented to the Supervisory Board in accordance with the catalog of transactions requiring approval which it has issued for the Executive Board.

The Executive Board informs the Supervisory Board regularly and comprehensively about the development of the business, the financial and earnings situation, planning and the achievement of targets and issues relating to compliance, as well as about strategy and existing risks. On the basis of these reports, the Supervisory Board monitors the legality, correctness and economic efficiency of management by the Executive Board. The catalog of transactions requiring approval issued by the Supervisory Board for the Executive Board lists the transactions and activities for which the approval of the Supervisory Board is required. This applies, among other points, to the acquisition and sale of interests in companies, investment planning and taking out bonds and long-term loans.

The Supervisory Board has drawn up its own rules of procedure regarding its work. The main areas covered in the rules of procedure are the composition, duties and responsibilities of the Supervisory Board, the convening, preparation and chairing of meetings, regulations on the committees and the presence of a quorum. The shareholder and employee representatives meet separately where necessary to prepare for meetings. The Chairman of the Supervisory Board coordinates the work of the Supervisory Board, chairs meetings and represents its interests externally. The Supervisory Board Chairman outlines the activities and decisions of the Supervisory Board in the Report of the Supervisory Board published in the annual report and reports on the work of the Board at the Annual General Meeting. He chairs the Annual General Meeting and determines the order in which the agenda items are addressed as well as the form and manner of voting.

Some of the activities of the Supervisory Board are performed by committees of the Supervisory Board. The Supervisory Board has formed four committees from its members. With the exception of the Nomination Committee, which consists of two shareholder representatives, all committees are based on joint representation, with two shareholder representatives and two employee representatives.

Tasks which are the responsibility of the Personnel Committee include selecting suitable candidates to fill Executive Board positions, making preparations for the appointment and withdrawal of Executive Board members and the conclusion, amendment and termination of employment and pension contracts of members of the Executive Board. It is also responsible for appraising the performance of the Executive Board, regularly examining the amount, suitability and customary level of Executive Board remuneration and overseeing the structure of the Executive Board remuneration system. Klaus Greinert (Chairman), Prof. Dr. Frank Richter, Joachim Stöber and Wolfgang Tretbar belong to the Personnel Committee.

It is the job of the Audit Committee to support the Supervisory Board when performing its supervisory functions. It reviews the quarterly accounts and the half-yearly financial report and prepares resolutions of the Supervisory Board for the adoption of the single-entity financial statements and the approval of the consolidated financial statements. The Audit Committee monitors the accounting process and the effectiveness of the internal control system, the risk management system and the internal auditing system. In addition, the Audit Committee deals with compliance issues. In addition to Klaus Greinert as Chairman, the committee includes Prof. Dr. Frank Richter, Joachim Stöber and Heinrich Kmett.

The Mediation Committee formed according to Section 27 (3) MitbestG submits to the Supervisory Board a slate of candidates for Executive Board membership if these have not received the required two-third majority of Supervisory Board member votes in the first ballot. Klaus Greinert (Chairman), Dr. Peter Mihatsch, Joachim Stöber and Peter Winter belong to the Mediation Committee.

# Declaration of corporate governance

The Nomination Committee submits recommendations to the shareholder representatives on the Supervisory Board for the nomination of shareholder representative candidates for election to the Supervisory Board by the Annual General Meeting. Klaus Greinert (Chairman) and Prof. Dr. Frank Richter belong to the Nomination Committee.

The Supervisory Board was regularly and comprehensively informed of the activities of the committees and of the outcome of discussions held in the respective committee meetings in the subsequent plenary meeting.

The Supervisory Board of Rheinmetall AG periodically reviews the efficiency of its activities, as required by Item 5.6 of the German Corporate Governance Code. Here, the organization and function of the Supervisory Board and its committees, the routing of information from the Executive Board to the Supervisory Board and the interaction of the two boards is discussed and evaluated. The plenary assembly discusses possibilities for improvement and decides on appropriate measures where relevant.

The offices held by Executive Board and Supervisory Board members are shown on pages 156 to 158.

### »Remuneration of Board members«

Details on the individual remuneration of Executive Board and Supervisory Board members and the respective remuneration structures are presented in the Board remuneration report within the summarized management report on pages 50 et seq. The Supervisory Board Chairman briefed the Annual General Meeting on May 10, 2011 on the basic components of Executive Board remuneration, which have also been disclosed on the Company's homepage.

### »D&O insurance«

Rheinmetall AG has taken out a D&O policy for its Executive Board and Supervisory Board members. This stipulates a deductible of 10 % of the loss or one and a half times the annual fixed remuneration.

### »Executive Board and Supervisory Board securities transactions subject to reporting requirements«

In accordance with Section 15a of the German Securities Trading Act (WpHG), members of the Executive Board and Supervisory Board and any related parties, as well as employees with managerial responsibilities as defined by WpHG, are obliged to disclose the acquisition or sale of securities or related financial instruments (directors' dealings) both to the Company and to the Federal Financial Supervisory Authority (BaFin), if transactions concluded within the calendar year exceed €5,000. Securities transactions reported since 2005 are permanently available to view on the Internet at www.rheinmetall.com in the Investor Relations section.

### »Shares held by the Executive and Supervisory Boards«

Members of the Supervisory Board and Executive Board and related parties together held 437,853 shares or 1.1 % of the common stock as at December 31, 2011 as was also the case on the 2010 balance sheet date. The Executive Board holds 89,313 shares or 0.2 %, the Supervisory Board 348,440 shares or 0.9 %.

### »Compliance«

In the interest of its customers, shareholders and employees, over time the Company has established a comprehensive compliance organization, with the aim of identifying legal risks and avoiding the consequences of these, preventing employees from breaching laws and corporate guidelines and supporting them in the correct and appropriate application of laws and corporate guidelines.

Compliance includes all instruments, guidelines and measures which ensure that procedures in the companies of the Rheinmetall Group comply with country-specific legislation, general legal conditions, regulatory provisions and the Company's own guidelines and that law-abiding conduct is assured. Compliance has always been an integral part of the corporate culture of the Rheinmetall Group. The Company operates in countries with differing political systems, legal and social conditions, standards and values.

The compliance principles applicable across the Group include regulations on issues relating to placing orders, the receipt and granting of gifts, competition and cartel law, the prevention of corruption, the prevention of insider violations, industrial and corporate safety and IT security. Every employee is obliged to observe the multilingual compliance guideline provided on the Company Intranet, and is asked to actively cooperate in the implementation and observance of the compliance program in his area of responsibility. In order to make employees aware of compliance risks, numerous seminars and workshops are held where legislation and provisions are explained and based on case studies, practical advice is given on correct conduct in specific situations during everyday business activities. These classroom training sessions, which also serve as a practical forum for discussions, are accompanied by online programs. In the year under review, over 900 employees were trained not only in general compliance-related topics, but also in issues surrounding export controls in particular.

The central body of the compliance organization is the Compliance team, which is headed by the Chief Compliance Officer who reports directly to the CEO of Rheinmetall AG. Experienced managers from the Group's divisions and the holding company's main departments are represented in this network. Compliance officers are appointed in the Group companies, meaning that employees have a point of contact regarding this issue in their immediate work environment and are able to seek help and guidance. If an employee has information on questionable activities or potential issues, or suspected or actual misconduct, he or she can approach these officers or other contacts within the Company on a strictly confidential basis. These officers are also there to advise preventatively on specific questions. The Executive Board follows a zero-tolerance policy. The discovery of misconduct is sanctioned and entails organizational measures and work-related consequences for the individual concerned.

The compliance program, which is supplemented by policies including the Code of Conduct, various Group-wide guidelines and numerous organizational specifications, is periodically reviewed and updated where necessary by the Compliance team. The Executive Board and the Supervisory Board's Audit Committee are regularly informed of current developments. In serious cases, the committees are informed immediately.

### »Risk management system«

The Group-wide reporting and control system is designed to detect, record, analyze and control business and financial risks to which the Company is exposed in the context of its international activities. This is intended to ensure that corporate decisions and ongoing business activities are kept within defined risk limits and comply with legal requirements.

# Declaration of corporate governance

The individual elements of the monitoring system provide reliable information on the current risk situation. They ensure that goals are met and that costs arising from the risks detected are kept to a minimum. The risk policy is geared in particular towards business risks, financial risks and specific division risks. The Executive Board determines the Group's risk strategy and defines accountabilities, reporting structures, documentation and management of identified risks, and thresholds. The Executive Board regularly informs the Supervisory Board and Audit Committee of existing risks and their development. The Company updates the monitoring system on an ongoing basis and adapts it to changing general corporate conditions. Details of risk management at Rheinmetall AG are presented in the risk report on pages 64 to 74. This includes the report on the accounting-related internal control and risk management system required in accordance with the German Accounting Law Modernization Act (BilMoG). The auditor examines whether the Executive Board has taken the necessary action to set up a suitable early risk identification system as required by Section 91 (2) AktG and ensures that this is able to identify in good time any developments that may jeopardize the Company's continued existence as a going concern.

### »Annual financial statements«

Rheinmetall AG prepares the consolidated financial statements and interim reports in accordance with the International Financial Reporting Standards (IFRS) as required in the European Union. The single-entity financial statements of Rheinmetall AG, required by law and decisive for the dividend distribution, are prepared according to the provisions of German law, particularly the German Commercial Code (HGB). PricewaterhouseCoopers AG Wirtschaftsprüfungsgesellschaft, Frankfurt am Main, Düsseldorf branch, performed the statutory audits for 2011. The audit assignment was awarded by the Supervisory Board based on the proposals of the Audit Committee. The Supervisory Board ensures that no conflicts of interest adversely affect the auditor's work and commits the auditor to promptly disclose any incompatibility with the assignment (e.g. non-eligibility or bias). Moreover, the statutory auditor reports on any material findings and events that contradict the declaration of conformity of the Executive Board and Supervisory Board under the terms of Section 161 AktG. The 2011 audit of financial statements has not indicated any such reportable facts.

### »Communication with stakeholders«

Up-to-date, transparent and objective communication is considered a matter of course in the Rheinmetall Group. This is geared towards the rights and interests of the shareholders, the media and the general public. According to the principle of fair disclosure, relevant target groups are provided with information at the same time. The Company reports extensively on the business and financial situation and significant events and changes within the Group. Quarterly and annual reports, press releases and other key information regarding current developments and changes are made available on the website in English and German. Links to the Defence and Automotive sectors allow website users to access comprehensive information on their business activities. Since October 2011, Rheinmetall has also reported on corporate social responsibility in the Group at http://csr.rheinmetall.com. Facts and circumstances that may affect the share price on the stock exchange are immediately published in an ad hoc notification in accordance with statutory provisions. Securities transactions subject to reporting requirements are published by Rheinmetall in media prescribed by law and on its website. As well as regularly attending conferences and investor meetings, road shows for institutional investors and analysts also ensure the continual exchange of information with the capital markets. Corporate Treasury is in direct contact with the financing banks. Throughout the year, Corporate Communications maintains dialog with representatives from the national and international specialist press and economic publications. Rheinmetall also stays in contact with its customers by attending a large number of trade fairs. The Annual General Meeting provides the opportunity to discuss matters with private investors, who are also able to approach the Investor Relations department with questions by telephone, in writing or by e-mail.

# Statutory disclosures in accordance with Sections 289 (4) and 315 (4) HGB and explanatory report

### »Composition of the subscribed capital«

The subscribed capital (common stock) of Rheinmetall AG remained unchanged from the previous year at the 2011 balance sheet date at €101,373,440 and was divided into 39,599,000 ordinary bearer shares with no nominal value (no-par value shares), each of which represented €2.56 of the common stock. The shares are fully paid. Different classes of shares are not in place. According to Section 5 (2) of the bylaws, no shareholder is entitled to a physical share certificate. The Company is authorized to issue bearer share certificates that document several shares.

### »Shareholder rights and obligations«

The same rights and obligations are attached to all shares, as set out in the German Stock Corporation Act (AktG), in particular Sections 12, 53a et seq, 118 et seq, and 186 AktG. The shareholder is entitled to asset-related and administrative rights. Asset-related rights primarily include the right to a share in the profits under the terms of Section 58 (4) AktG, the right to net liquidation assets following the dissolution of the Company in accordance with Section 271 AktG and share subscription rights in the event of capital increases according to Section 186 (1) AktG. Administrative rights comprise the right to attend the Annual General Meeting and the right to speak there, ask questions, submit motions and exercise voting rights. Any shareholder may enforce such rights, in particular through actions for information, avoidance or rescission.

Each share in Rheinmetall AG grants one vote at the Annual General Meeting. In accordance with Section 71 b AktG, this excludes treasury shares held by the Company, which do not entitle the Company to rights. The Annual General Meeting selects shareholder representatives on the Supervisory Board as well as the auditor. It decides in particular on the appropriation of net income and approval of the activities of the members of the Executive Board and Supervisory Board. The Annual General Meeting passes resolutions on the bylaws and the objective of the Company, amendments to the bylaws and key corporate measures such as affiliation agreements and conversions, the issuing of new shares, convertible bonds and bonds with warrants and authorization to acquire treasury shares, as well as the performance of a special audit, the early removal of Supervisory Board members and the dissolution of the Company. Subject to other overriding legal provisions, the Annual General Meeting adopts its resolutions by means of a simple majority of votes cast and, where the law prescribes both a voting and shareholding majority, by means of a simple majority of the common stock represented in the passing of the resolution.

### »Restrictions on voting rights and share transfer«

As of the 2011 balance sheet date, the shares of Rheinmetall AG were not subject to any voting restrictions under the bylaws or legislation. To the extent that Rheinmetall AG issues shares under its long-term incentive program to Executive Board members and other senior management staff, these shares have been subject to a four-year lockup period since 2010. These beneficiaries cannot sell shares transferred this way before the end of the lockup period. Eligible staff of the Rheinmetall Group in Germany, and in other European countries, may purchase Rheinmetall AG shares on preferential terms as part of the employee share purchase program. There is a lockup period of two years for these shares.

### »Type of voting control if employees have shareholdings and do not exercise their rights of control directly«

To the extent that Rheinmetall AG issues shares under its long-term incentive program and employee share purchase program, these shares are directly transferred to these individuals subject to a resale lockup period. As with other shareholders, these beneficiaries are also able to directly exercise the rights of control to which they are entitled based on the transferred shares, subject to the provisions of the law and bylaws.

# Statutory disclosures in accordance with Sections 289 (4) and 315 (4) HGB and explanatory report

### »Shareholdings exceeding 10% of voting rights«

On November 3, 2011, Harris Associates L.P., Chicago, USA, informed Rheinmetall AG in accordance with Section 21 of the German Securities Trading Act (WpHG) that it had held 10.46 % of shares in the Company since November 2, 2011. Rheinmetall AG is not aware of any indirect shareholdings as defined by Section 22 of the German Securities Trading Act (WpHG) that exceed 10% of the voting rights.

### »Shares with special rights conferring controlling privileges«

None of the shares issued by Rheinmetall AG vest rights which confer special control privileges on their holders.

### »Provisions on the appointment and removal of Executive Board members and amendments to the bylaws«

The appointment and removal of the members of the Executive Board of Rheinmetall AG is based on Sections 84 and 85 AktG and Section 31 MitbestG in conjunction with Section 6 of the bylaws. Executive Board members are appointed by the Supervisory Board for a maximum of five years and may be reappointed or their term of office renewed, for a maximum period of five years in each case. The provisions of Sections 179 et seq. AktG apply to any amendment of the bylaws of Rheinmetall AG. In accordance with Section 4 of the bylaws, amendments that affect only the version or wording of the bylaws with regard to the balance and utilization of authorized capital can be carried out by the Supervisory Board without the passing of a resolution by the Annual General Meeting.

### »Executive Board powers to issue new shares and repurchase treasury shares«

According to Section 202 AktG, the Annual General Meeting may authorize the Executive Board for a maximum period of five years to increase the common stock by issuing new shares in return for capital contributions. The Annual General Meeting of May 11, 2010 authorized the Executive Board, with the approval of the Supervisory Board, to increase the common stock of the Company through the issue of new no-par shares in return for contributions in cash and/or in kind on one or several occasions up to May 10, 2015, up to an aggregate €50,000,000.00 (authorized capital). The new shares may also be issued to employees of Rheinmetall AG or any subsidiary it controls. The exclusion of subscription rights upon which the Executive Board may resolve with the approval of the Supervisory Board is governed by Section 4 (3) of the bylaws of Rheinmetall AG.

In accordance with a resolution of the Annual General Meeting on May 11, 2010, a contingent capital increase of up to €20,000,000.00 has been approved for the Company's common stock (contingent capital). The contingent capital increase is to be carried out through the issue of up to 7,812,500 bearer shares or – if the Company's bylaws at the time of issuing the bond also permit the issue of registered shares – new registered shares in accordance with Section 4 (4) of the bylaws of Rheinmetall AG.

The purchase of treasury stock is governed by Section 71 AktG. According to the resolution by the Annual General Meeting of May 11, 2010, the Executive Board of Rheinmetall AG is authorized pursuant to Section 71 (1) No. 8 AktG to repurchase treasury bearer shares of Rheinmetall AG not to exceed 10% of the current common stock of €101,373,440.00. Such treasury shares may be acquired via the stock exchange or by public bid directed at all shareholders or by public invitation to submit a purchase bid. This authorization is valid up to May 10, 2015, unless otherwise resolved by the Annual General Meeting before this date.

The proportion of own shares held as treasury stock was 3.4 % (1,350,842 shares) at the end of the 2011 fiscal year, compared to 3.3 % or 1,293,198 shares on the previous year's balance sheet date. On February 9, 2012, Rheinmetall AG held 1,547,842 shares or 3.9 %.

### »Major agreements terminable upon a change of control«

In December 2011, a banking consortium granted Rheinmetall AG a syndicated credit facility of €500 million with a duration of five years. If half of the Rheinmetall AG shares are held directly or indirectly by one or several persons (acting either jointly or severally), the agreement's terms and conditions must be terminated or renegotiated.

In September 2010, Rheinmetall AG issued a €500 million bond maturing in June 2017. Upon a change of control, bond holders may call in the bonds with between 40 and 60 days' notice as from the publication date of the change of control and request redemption of the bond principal plus interest.

As at December 31, 2011, Rheinmetall AG reported promissory note loans of €85 million which were issued in May 2009 with a duration of four or five years. In the event of a change of control, the promissory note holders also have an extraordinary right to terminate along the lines of the aforementioned agreements.

The agreement of these types of rights of termination is standard practice, particularly when granting longer-term loans.

No preventive precautions have been taken against a public takeover bid, the successive acquisition of a controlling stake via share purchases on the stock markets, or control being gained by buying blocks of shares. In the case of acquisition of a defence technology company in Germany, Sections 52 et seq. of the German Foreign Trade & Payments Regulation (AWV) require that the Federal Government give its prior approval before any non-resident party can purchase 25 % of the shares. This Regulation aims to safeguard material security interests of the Federal Republic of Germany.

### »Compensation arrangements between the Company and Executive Board members and employees in the event of a takeover bid«

No compensation arrangements have been made with members of the Executive Board and employees.

# Risk report and report in accordance with Sections 289 (5) and 315 (2) No. 5 HGB

### »Using opportunities – Limiting risks«

In view of more rapid market changes, growing uncertainty, increasing complexity of general conditions that vary widely around the world and major technological progress, corporate decisions are evermore dependent on the reliable assessment of potential risks. As a technology group with global operations and a varied product portfolio in its Defence and Automotive sectors, Rheinmetall is exposed to a wide range of risks of varying severity depending on the division, the industry and the region. From this arises the need to identify and limit potential risks systematically at an early stage to prevent the Company being jeopardized. Corporate policy is geared towards generating appropriate yields on a sustainable basis, taking and optimizing any opportunities that present themselves, making use of and expanding success potential, yet at the same time avoiding, minimizing or offsetting associated risks as far as possible. The aim is to maintain entrepreneurial flexibility and financial stability, to increase systematically the value of the Company on a sustainable basis and thus to ensure the continued existence of the Rheinmetall Group in the long term.

### »Risk management system increases transparency«

The standardized Group-wide risk management system aimed at identifying material developments jeopardizing the continued existence of the Company at an early stage is characterized by the principle of caution. The Executive Board determines the Group's risk strategy and defines accountabilities, management and documentation of identified risks, and thresholds. Risk management, which is geared towards financial resources as well as strategic and operational planning, is considered a primary responsibility of the heads of the divisions and central departments as well as process and project managers. This professional risk management system ensures that corporate decisions and ongoing business activities are kept within the risk limits defined in the guidelines and comply with legal requirements. It supplements the existing planning, management and controlling instruments and is rooted in the organizational structure of the Rheinmetall Group based on fully-defined responsibilities.

Risk is defined as the possibility of unfavorable future developments with regard to adopted corporate targets. In order to identify and analyze potential risks, a risk inventory is prepared once a year by the management of the operating units during corporate planning, which contains all material risks affecting corporate targets and sub-targets, early warning indicators, responsibilities and suitable countermeasures. On this basis, the operating units and central divisions record, manage and report risks associated with the current business situation and future development, along with the probability of their occurrence and the impact on earnings, on a monthly basis in accordance with prescribed standardized parameters.

As part of monthly reporting, risk reports from the subsidiaries and central departments of Rheinmetall AG systematically record current business risks and give a structured assessment of these risks according to their probability of occurrence and the level of damage to be expected. These individual risk reports are summarized in the context of risk aggregation and the overall risk situation of the Company is defined. Appropriate preventative, safeguarding and corrective measures reduce the probability of occurrence of risks or restrict their potential level of damage. The measures introduced to manage risk are closely monitored on an ongoing basis and adjusted to a new risk assessment where necessary. If necessary, additional measures are taken in order to further limit and reduce identified potential risks. Group Controlling regularly informs the Executive Board and managers of the development of the risk situation, the status of, and significant changes to, important ventures that are subject to reporting requirements and the status of countermeasures that have already been introduced. The Executive Board is immediately informed of any unforeseen significant changes to the risk situation.

### »Market risks«

In times of advancing globalization and growing competition and market transparency, market risks are becoming more prevalent. The outcome: Possible fluctuations in prices, volumes and margins. Focusing on high-end market segments, product innovations, process improvements, production and capacity adjustments and strict cost management all contribute to strengthening competitiveness in each of the Company’s industries and securing and building on the profitability of the Rheinmetall Group.

It is not possible to avoid fully risks that arise due to economic and market cycles, rapid technological change, capex cycles becoming increasingly short and intensifying competition. A deterioration in general economic conditions or a change in political conditions in the sales regions can negatively impact the sales and earnings situation of the Rheinmetall Group. Thanks to the Company’s presence on international markets, the diversified product portfolio of the divisions and the continued efforts to internationalize the Defence and Automotive sectors, temporary economic fluctuations and market cycles running counter to the general trend in regions, countries and industries can be offset in part by more favorable trends in other regions and markets. Furthermore, the risk profile of Rheinmetall can also be affected by structural market risks, such as the presence of new suppliers, product substitution or trends towards consolidation on sales markets.

### »Technology and development risks«

The market presence and customer proximity associated with international distribution structures make it possible to obtain first-hand information at an early stage, to respond to trends and to gear product strategies consistently towards the relevant requirements. Technological and product-related new and optimized developments geared towards requirements are systematically pursued on the basis of high technical competitiveness, allowing the Rheinmetall Group to remain economically successful in the long term. The involvement of customers at early stages in the definition, design, development and testing of new products, thorough preliminary research in the form of market and competition analyses, feasibility studies and profitability analyses, modern project management aimed at reviewing the criteria for technical and economic success and securing the technological position through patents reduces potential R&D-related risks such as misdevelopments or budget overruns. Despite compliance with the processes described and the use of modern project management, monitoring and controlling measures, the development of new products and launching these onto the market, as well as improving the existing product portfolio, harbor cost risks. These exist in the actual design and development stage, but also following market launch due to the potential need for technical improvements which will only come to light following use in real-life situations or through continuous operation.

### »Production risks«

Production can be compromised by unforeseen events at production sites, unexpected technical disruptions, fire, accidents and human error, even if high technical and safety standards apply. The availability of industrial premises and production plants is ensured through preventative maintenance with ongoing checks, regular inspections and maintenance work, constant modernization and targeted investment. Occupational health and safety and environmental protection as well as contingency and hazard prevention plans should reduce accident hazards and health risks to a minimum for employees and third parties or prevent them completely if possible. Problems encountered by partner companies or subcontractors can lead to disruptions, e.g. in logistics. For potential damage and associated disruptions to operations or longer production downtimes and for other conceivable loss occurrences and liability risks, reasonable insurance cover has been taken out, where available, as is usual in the industry to ensure that the financial consequences of potential risks are contained or completely offset. The extent of insurance cover is regularly reviewed and adjusted where necessary.

# Risk report and report in accordance with Sections 289 (5) and 315 (2) No. 5 HGB

**»Procurement risks«**
Procurement risks may arise due to the raw materials, parts and components required to manufacture products not being available or not in a sufficient quantity, or due to it not being possible to purchase these in good time and without problems, or at prices that are in line with the market. In order to prevent potential procurement bottlenecks and to ensure the security of supply, the procurement markets are subject to ongoing monitoring in order to be able to react to changes promptly. A significant proportion of the supply of raw materials is covered by long-term supply contracts and issued with cost escalation clauses where possible in contracts with customers. International purchasing activities, careful selection of suppliers, annual supplier reviews, quality and reliability checks on suppliers, alternative suppliers, adequate reserve stocks and efficient contract management also reduce potential risks. An inadequate energy supply for companies of the Rheinmetall Group under cost-efficient conditions constitutes a risk for maintaining competitive production at the sites. It is not possible to ensure complete hedging of fluctuations in the price of energy sources or to guarantee that increases in energy prices will be passed onto customers. Rising energy costs are addressed by bundling procurement volumes and through invitations to tender, long contract durations and optimizing the electricity price via the European Energy Exchange (EEX) in Leipzig.

**»Acquisition and integration risks«**
The companies of the Rheinmetall Group regularly review the possibility of acquisitions or strategic partnerships. These are a key component of the growth and internationalization strategy, in order to, for example, improve market position, expand the product portfolio, open up further markets with growth potential and gain additional technologies. The companies identified by means of observation and analysis of the market are examined with regard to their strategic relevance, earnings potential and future prospects, are subjected to an analysis of opportunities and risks and are assessed on the basis of yield/risk considerations. Qualified experts examine areas including operational, legal and financial themes by means of systematic due diligence procedures. Following approval proceedings carried out over several stages, the Executive Board, and if the defined value limits are exceeded the Supervisory Board, of Rheinmetall AG decides on whether to implement the plans. Once the transaction has been approved, the companies are integrated into the relevant division on the basis of structured processes, which are also subject to schedules and milestone planning. However, the integration of employees, processes, technologies and products into the Rheinmetall Group may prove to be more difficult or more intensive in terms of time or costs than expected. It is also possible that the objectives and potential synergies targeted with the transaction may not be achieved or that they may not be achieved to the planned extent. Risks may also arise in connection with the activities of the newly acquired company that were not previously known or that were considered insignificant.

**»Financial risks«**
The key tasks of Rheinmetall AG include ensuring that financial requirements are hedged for both operating activities and capital expenditure. In addition to the optimization of Group financing, the focus here is on limiting financial risks. The liquidity risks of the Rheinmetall Group are hedged on the basis of short-, medium- and long-term liquidity forecasts, by ensuring that the total volume of highly diversified credit facilities available definitely exceeds the Group's foreseeable requirements. Money and capital market products and bilateral and syndicated loans are used as financial instruments. Interest rate risks arise through changes in market interest rates. Interest caps and swaps are used to control these risks. Currency risks, which result from a large number of payment flows in different currencies, are hedged no later than the time that they arise. Currency forwards and currency swaps are used here. The use of derivative financial instruments purely for speculation purposes is prohibited. Counterparty risks upon conclusion of financial transactions are limited through a creditworthiness-dependent, limit-controlled spread.

Sufficient balance sheet provisions have been recognized for potential losses on long-term contracts or from supply or sourcing agreements, as well as other risks from warranty claims, for example. Given Rheinmetall's customer mix, credit risks are negligible. The Rheinmetall Group is not dependent on any customers or countries which could jeopardize the Group's continued existence as a going concern in the event of negative development.

### »IT risks«

The world of IT is changing more rapidly than ever before. Information is increasingly becoming a resource that is crucial to success. Ever larger data volumes, short access times and structured provision of information require state-of-the-art infrastructure and highly-available, failsafe IT systems with a redundant design. Group-wide frameworks and defined routines increase performance and reduce the need for coordination. Capacity that is systematically geared towards market opportunities, the bundling of resources, close interaction in user support and synergies in procurement and service all contribute to improving the cost efficiency of existing infrastructure and boosting their performance.

Information and data are exposed to various, and in some cases growing, threats with regard to availability, confidentiality and integrity. Significant disruptions to application-critical IT systems, applications and infrastructure components can seriously compromise the management of business and production processes and lead to business activities being severely hindered. Networks can fail, and programming and operating errors, tampering and external factors can lead to the corruption or deletion of data. As well as high security standards and Group-wide procedural and security guidelines, technical and organizational emergency measures, safeguards and precautions, such as detailed back-up and recovery procedures, uninterruptible power supply, secure access procedures and daily data reflection and archiving, limit serious disruptions and breakdowns. In order to protect against external attacks, the Rheinmetall Group uses systems including firewalls and virus scanners. By continually monitoring the software used, functions and applications are expanded, any security vulnerabilities identified are closed up and any errors that occur are rectified. This ensures the ongoing, secure coordination of IT-based business processes. The installed software and hardware are kept state-of-the-art thanks to regular capital expenditure. Together with specialist service providers certified according to ISO 27001, the technical configuration, functional security structures and efficient operation of the IT systems are periodically reviewed and continuously improved.

### »Personnel risks«

The achievement of ambitious corporate targets and the sustainable economic success of the Rheinmetall Group depend to a great degree on the qualifications, expertise and knowledge of employees. Fluctuations in staff holding key positions and problems with not being able finding suitable specialist staff, managers and junior staff with the desired commercial, technical or industry-specific skills for job vacancies, or not being able to find these staff quickly enough, could have just as much of an adverse impact on the Company as insufficient qualifications or a lack of motivation. These risks are countered by means of numerous measures ensuring performance-related remuneration that is in line with the market, qualified staff development and modern staff recruitment, as well as forward-looking succession planning.

Rheinmetall facilitates the recruitment, promotion and long-term retention of employees at the Company with a corporate culture that focuses on professional performance, initiative, self-responsibility, integrity, shared values and mutual understanding, and with performance-related remuneration, comprehensive fringe benefits and pension schemes, a range of career prospects and interesting opportunities for promotion.

# Risk report and report in accordance with Sections 289 (5) and 315 (2) No. 5 HGB

As well as the traditional means of recruiting staff, the Company's participation in numerous recruitment marketing events, its close contact with selected universities, its attendance at university fairs and recruitment fairs, its offering work placements for students and graduates and its presence on online job sites ensure the recruitment of competent staff with good qualifications. Rheinmetall is also recognized as an attractive employer in the defence and automotive industries thanks to its excellent international reputation, its membership of MDAX, its size and its technologically sophisticated products. The range of opportunities for professional development offered in the companies of the Defence and Automotive sectors also set Rheinmetall apart from other employers.

The future-oriented development of employees, talented management trainees and experienced specialist and managerial staff that is in line with requirements is a key factor in the further growth of the Group. Based on systematic selection and assessment procedures, the development of selected top performers is promoted by means of multi-stage seminar programs and individual training measures. A range of training programs allow Rheinmetall employees to continually improve the skills, competencies and knowledge required to ensure success in their professional life and to obtain new qualifications.

### »Compliance risks«

The compliance organization is designed to ensure proper modes of conduct and behavior on the part of a company and its employees. This is built on proven principles which have governed entrepreneurial activities within the Rheinmetall Group since its formation, and is designed to prevent any liability risks, risks of incurring a penalty or a fine, and reputational risks, as well as other financial disadvantages, loss or damage that the Company may incur as a result of misconduct or violations of the law.

For many years now, Rheinmetall has had a comprehensive set of corporate policies in the form of guidelines and organizational and operating instructions, which ensure compliance with legal guidelines at all times and prevent infringements of the applicable laws, in addition to ensuring appropriate actions that are in accordance with respective duties during day-to-day business activities. However, despite multi-level inspection and control mechanisms, the possibility of risks arising from unlawful activities of individual parties cannot be ruled out.

Subject to their respective areas of responsibility, employees in Germany and abroad are periodically informed of the relevant rules and regulations and any amendments to these as well as rules of conduct for everyday business activities by means of seminars, workshops, interactive e-learning courses and other communication measures. The Chief Compliance Officer regularly reports to the Executive Board and the Supervisory Board's Audit Committee on current developments as regards compliance.

Persons with insider knowledge as defined by stock corporation legislation are listed in an insider directory and undertake to comply with the associated provisions.

### »Legal risks«

Legal risks can arise through legal disputes with competitors, business partners, customers or other external third parties and through changes to the legal framework in the relevant markets. Legal risks include in particular risks arising from product liability, competition and cartel law, patent law and tax law. In such decisions and in the organization of business processes, the Group is not only supported by detailed advice from its own specialists but, in certain cases, also calls in renowned outside experts and specialists. Potential loss, damage and liability resulting from ordinary operations are appropriately covered by insurance policies or accounting provisions.

Following restructuring measures under company law, two legal proceedings have been initiated by external shareholders with a view to reviewing the suitability of the amount of cash compensation offered. In the legal proceedings initiated by external shareholders in 1998 in connection with the merger of Kolbenschmidt AG and Pierburg GmbH, the senate of Stuttgart Higher Regional Court presented a proposal for the amicable termination of proceedings to the parties to the proceedings at a hearing on January 19, 2011, which was accepted by the parties. The proceedings instituted in 2007 to squeeze out Kolbenschmidt Pierburg shareholders came to an end on July 5, 2011. The Stuttgart Higher Regional Court dismissed the challenges of the violation of the right to a hearing in court of the claimants who had immediately lodged appeals against the decision of the Stuttgart Regional Court given on September 1, 2008. The duration and outcome of the other proceedings opened in 2003 in connection with the squeeze-out of Aditron AG are still unknown.

The apartheid legal proceedings brought against Rheinmetall in 2009 are currently suspended due to one ongoing parallel proceedings brought against other companies affected by the apartheid lawsuit. Rheinmetall regards the action as inadmissible and does not regard the US court as having jurisdiction. The claimants are not US citizens, the event did not take place on US territory and prosecutions have already been carried out in Germany for the legal violations upon which the action is based.

Appropriate provisions have been established based on the known facts for the risks arising from the legal proceedings described above and other proceedings as far as is considered necessary. It is very difficult to determine or predict the outcome of pending proceedings or of the threat of proceedings. Costs can arise on the basis of court or official decisions or the agreement of settlements that are not covered or not fully covered by provisions or insurance policies and can thus have an impact on the business and its results.

**»Tax risks«**

The results of internal tax audits may lead to charges based on audit findings together with interest and tax payments in arrears derived from these. There is also the risk that the tax burden for the Rheinmetall Group may increase as a result of changes to tax legislation or court decisions.

**»Environmental risks«**

A large amount of land owned by the Rheinmetall Group has for decades been subject to industrial usage. The possibility cannot be ruled out that pollution has also been generated during this time as a result of production that Rheinmetall is not yet aware of. Rheinmetall operates an active environmental management system. Environmental Officers monitor compliance with statutory requirements at the production locations. The risk potential arising from production processes and environmental protection risks is effectively reduced by means of modern and secure facilities, strict compliance with relevant laws, requirements and regulations, extensive guidelines on quality assurance and stringent quality controls. This includes certification in accordance with international standards for quality (DIN 9001 and TS 16949) and environmental protection (ISO 14001). Regular reviews of these certifications confirm these high standards on an objective basis. Sufficient provisions have been recognized for necessary measures to safeguard against or clean up identified pollution.

It is possible that the relevant authorities may issue regulations that require costly clean up measures. The tightening of safety, quality and environmental protection provisions and standards may lead to additional costs and liability risks over which Rheinmetall would have no influence. In this context, reference is made to the implementation of the EU Regulation on the Registration, Evaluation, Authorization and Restriction of Chemicals (REACH). In addition to direct costs that may arise owing to additional measures for the fulfillment of these standards, market structures may change to the disadvantage of Rheinmetall.

# Risk report and report in accordance with Sections 289 (5) and 315 (2) No. 5 HGB

**»Opportunities and risks in the Defence sector«**

Foreign deployments of UN and Nato troops, crisis intervention, peace keeping missions – due to constant changes in national and international security and defence policy, brought about, for example, by geopolitical realignment, political upheaval and new conflict situations, the armed forces of the 21st century are being faced with new challenges in military deployments. Huge threats to external and internal security arise from unstable nations and dictatorial regimes as well as terrorists and radical activists. Rheinmetall Defence is one of the leading European suppliers of defence technology and specializes in arming land forces with armored military vehicles, weapons and munitions as well as electronic equipment and state-of-the-art air defence systems. In the protection of armed forces in particular, Rheinmetall has been treading new paths for years. Effective protection systems are of central importance in the deployment scenarios of today and the future, in order to offer a maximum level of safety to soldiers. The companies in this corporate sector specialize in the development and production of components and systems for the protection of people, vehicles, aircraft, ships and assets. They are a strong partner to the German armed forces, its allies and friendly armies, along with civil national security forces, and protect the forces involved in foreign operations.

A substantial proportion of the market potential for Rheinmetall Defence comes from the defence budgets of customer nations. Opportunities for its divisions are tied to the changing military requirements of the German armed forces and other armed forces from around the world. The range of products and capabilities of Rheinmetall Defence is tailored to central defence technology requirements resulting internationally from the ongoing need for substantial modernization of armed forces and new military deployment scenarios. The Defence sector may also benefit from ad hoc procurement needs triggered by the deployment of forces in crisis regions. Despite pressure on governments to consolidate budgets and carry out spending cuts, defence still remains a growth market – even though it has lost some momentum compared to previous years. Industry experts expect the procurement budgets of the 65 countries with the largest defence budgets to rise by around 12 % by 2015 compared to 2010. Reference projects commissioned by the German armed forces, such as the series contract for the Puma infantry fighting vehicle, the Future Soldier program and the MANTIS® close-range protection system, are just as critical to winning orders abroad as an innovative product range geared towards the new needs of the armed forces and on a par with international competitors. Other growth opportunities may arise for Rheinmetall Defence as a result of the expected ongoing consolidation process in the European defence market.

Defence's business areas are not directly dependent on the state of the economy. However, risks lie in dependence on spending patterns for public budgets in Germany and foreign customer nations. In the wake of the government debt crisis and euro crisis, this will lead to shifts and cuts in state budgets, which will also affect defence. Political influences and changes in the defence technology requirements of customer nations, along with budget restrictions or general financing problems on the part of customers, could result in risks in the form of delays in awarding contracts, time extensions or even the cancellation of orders. Risks also arise from increasing transatlantic competition. Those export markets which are accessible are exposed to fierce international competition.

Higher prefinancing due to worsened downpayment conditions and possible financial interests in projects constitute further risks. Additionally, unforeseeable difficulties in project processing may lead to unforeseen burdens. As well as uncertainty in calculations, these also include altered economic and technical terms and conditions following the conclusion of a contract, unexpected technical difficulties or faults, problems with business partners or suppliers and deferred dates of acceptance and settlement. By means of professional project management and comprehensive quality management measures, as well as the appropriate formulation of contracts, it is possible to limit these risks, but not to exclude them altogether.

The expansion of international business activities harbors the risk that, in some regions of the world, due to the industry-specific practices in place in the countries in question, delays may arise in order processing or risks arising from the payment practices of customers or business partners that are customary in these regions may increase. As a matter of principle, Rheinmetall Defence works with contractual parties with good creditworthiness. Risks are limited as far as possible by means of professional project management, comprehensive project controlling and appropriate formulation of contracts. However, despite ongoing monitoring, delayed payments or defaults on the part of contractual parties may unexpectedly arise.

**»Opportunities and risks in the Automotive sector«**

The world economy is appearing increasingly volatile. Brief phases of recovery follow serious crises, such as the previous global economic crisis in 2008/2009, which are then followed by new crises such as the current euro crisis, which is having a growing impact on the automotive markets in Europe. As such, the Automotive sector is confronted with a volatile market environment of varying severity in different regions, which is characterized by both opportunities and risks.

In addition to market development, opportunities arise in particular in planned product innovations up to the start of series production. Moreover, streamlining measures, improvements in quality and the reduction of the reject rate opens up additional opportunities.

Increasing global awareness of markets in terms of ecology with corresponding demands for drive concepts which are energy-efficient and reduce $CO_2$ output, as well as emission legislation that will become even more restrictive in the future, both in core markets and in the emerging markets, offer KSPG the opportunity to increase sales and market share on the basis of existing products and processes and those being developed. Whereas in previous years, growth was mainly determined by emissions-driven technologies for combustion engines, particularly for diesel engine drive systems, the main focus in the future will be on making technological changes to conserve resources and reduce fuel consumption and thus $CO_2$ emissions.

The generally recognized trend towards low-consumption and thus smaller engine sizes will be stepped up through the gradual coming into force of legislation limiting $CO_2$ emissions. As well as the potential offered by the further development of diesel engine drive systems, which already offer low fuel consumption as it is, new concepts for gasoline engines will make a significant contribution to observing legally prescribed limits. Technologies such as charging and downsizing offer the Automotive sector opportunities to place competitive, innovative products. In addition to these technological fields that have already been established, KSPG is developing a variable valve control system in order to supply the key market for gasoline engine drive systems in particular with a technology aimed at optimizing gas exchange and thus improving operating performance and, in particular, aimed at reducing fuel consumption.

The Automotive sector will benefit from the European trend towards low-consumption engines, which is also increasingly making its way into the USA. As well as downsizing and measures aimed at mixture control and gas exchange, the main technologies in demand for all drive concepts with combustion engines are developments to minimize friction losses and to utilize auxiliary units according to individual needs. KSPG already offers customized product solutions in these areas, thus partaking in the growth of the core markets of Europe and the USA. This applies both to passenger car markets and commercial vehicle markets.

# Risk report and report in accordance with Sections 289 (5) and 315 (2) No. 5 HGB

In addition to the above measures relating to the drive train, lightweight construction is a primary aim of future vehicle development, owing to the need to save fuel. This applies in particular to vehicles with a battery-electric drive. Thanks to its expertise in the fields of aluminum and magnesium technology, KSPG has opportunities here in completely new applications.

In times of fiercer competition as a result of overcapacity in the triad markets, unexpected changes in regular order placement, shifts in the product range, tighter competition and increasing price pressure are all possibilities. The outcome: Possible fluctuations in prices, volumes and margins. In parallel to the shorter product life cycles, vehicle manufacturers find themselves exposed to tight competitive, innovative and cost reduction constraints which they then pass on to their suppliers. The Automotive sector is limiting the impact of these trends by investing in new products, deploying modern manufacturing processes, cost-saving technologies and new materials and realizing potential savings in corporate functions.

Potential declines in automotive demand in certain countries are countered by the expansion of international presence and marketing products outside the automotive industry. Advantageous economic parameters for new locations and expanding existing production capacities are exploited. Additionally, the diversified customer structure allows fluctuations in the production figures of individual automotive manufacturers to be balanced out. Thanks to the broad product range and low reliance on individual customers, it is possible to absorb price risks, weak demand and insolvency risks to a certain degree.

Among the cost risks are extremely fluctuating commodity and energy prices. Such risks are contained by cost escalation clauses in corresponding contracts – especially for aluminum, copper and nickel. Energy for the Rheinmetall Group’s sites in Germany is jointly procured via the Leipzig-based European Energy Exchange (EEX). Procurement timing and volumes are also controlled and optimized, in addition to relevant hedging tools, by the central Commodities Office. Further procurement risks arise from the potential insolvency of subcontractors. These risks are countered by carefully selecting subcontractors, spreading the risk by distributing the purchase volume across further suppliers and supporting suppliers in emergency situations if necessary.

Appropriate insurance cover is in place for warranty, product liability and recall risks, which is reviewed periodically and adjusted where necessary.

Risks also arise from acquisitions carried out. These risks may come into being, for example, in the form of delayed integration of the companies acquired or even in an unforeseen reaction on the part of the competition or suppliers. KSPG takes all possible measures to minimize these types of risk both during the acquisition process and in the subsequent integration phase.

The automotive industry continued on its strong growth path in fiscal 2011. Industry experts expect growth overall in the triad markets in 2012 compared to 2011. However, development in the core markets will vary. While declining production figures are forecast for Western Europe, significant growth is expected for Japan in particular – thanks to its recovery following the earthquake and tsunami disaster – and for North America. Further growth is also set to emerge from the Asian markets. However, these forecasts are characterized by much greater uncertainty due to the as yet unresolved euro crisis. Forecasts and assessments of economic, market and industry developments were revised downwards at increasingly short intervals in the year under review. There is a latent risk of declining sales. Any change with regard to customers, e.g. relocation of production sites, loss of customers, sale of companies, insolvencies, declines in demand and changes in customer requirements, can lead to a decline in operating activities and/or reduce the value of investments.

### »Internal accounting-related control and risk management system (disclosures in accordance with Sections 289 (5) and 315 (2) No. 5 HGB) «

The internal control and risk management system (ICS) related to the accounting process at the Rheinmetall Group includes all principles, procedures and measures which ensure, by both organizational and technical means, that all business processes and transactions are recorded in the accounting system promptly, accurately and consistently in accordance with relevant legal requirements, other accounting principles and internal Group guidelines. The ICS also ensures that changes in the economic and legal environment of the Rheinmetall Group and new or amended legal provisions are recognized. These changes are analyzed in order to determine whether adjustments to internal Group organizational, control and monitoring structures or guidelines and systems are necessary. In addition to defined control mechanisms, e.g. manual coordination processes and technical coordination processes for systems, the ICS is based on the separation of administrative, executive, settlement and approval functions and compliance with guidelines and operating instructions. The main Accounting department of Rheinmetall AG is responsible for central management of the (Group) accounting process.

The single-entity financial statements of Rheinmetall AG and of the companies included in consolidation are prepared in accordance with the respective national accounting principles and then transferred to financial statements in accordance with IFRS. Here, the central IFRS accounting guidelines prescribed by Rheinmetall AG are to be strictly observed. These ensure standardized accounting, measurement, calculation of results and reporting obligations for the companies included in the consolidated financial statements of the Rheinmetall Group. A check is carried out every quarter to ensure the completeness of the scope of consolidation. The management of each Group company must monitor compliance with IFRS-compliant accounting guidelines and confirm the correctness of the financial statements in a corresponding declaration. The IFRS accounting guidelines cover all IFRS regulations that are of relevance to Rheinmetall AG. The content of the guidelines is the responsibility of the main Accounting department of Rheinmetall AG. The IFRS accounting guidelines are continually adapted to changes in IFRS and are made available to all companies included in the consolidated financial statements after being reviewed by the auditor.

It is the responsibility of the management of the respective companies to ensure the correctness of the financial statements prepared in accordance with national and international accounting principles. This also includes compliance with Group-wide guidelines and procedural regulations, including compliance with the regulations on the timely execution of accounting-related processes and systems. In principle, the single-entity financial statements of the companies included in consolidation in accordance with IFRS are drawn up in SAP-based accounting systems (SAP-FI). Procedures are implemented in the accounting process to ensure the correctness of the financial statements.

The consolidated financial statements of Rheinmetall AG are drawn up by means of a structured process, with the aid of the consolidation software SAP SEM-BCS. A standardized, binding chart of accounts and standardized consolidation forms are incorporated into this system, which must be completed by all companies included in the consolidated financial statements, taking into account the Group-wide IFRS accounting guidelines, and are summarized in a stringent Group report package. Rheinmetall AG stipulates the schedule for the consolidated financial statements centrally and monitors compliance with deadlines. After the data from the single-entity financial statements in accordance with IFRS have been entered into the SAP consolidation module SAP SEM-BCS, the data are subjected there to automatic plausibility checks and system-based validation. If error or warning messages are displayed during this process, these are to be analyzed and dealt with by the person responsible for the single-entity financial statements before the data are forwarded to the consolidation center. Further technical system checks are monitored centrally by employees in the consolidation department of Rheinmetall AG and supplemented with manual checks. Approval processes are performed throughout the entire accounting process. Generally, the dual control principle applies at every level. Throughout the entire accounting process, the subsidiaries are supported by central contacts.

# Risk report and report in accordance with Sections 289 (5) and 315 (2) No. 5 HGB

As a process-independent authority, Internal Auditing examines workflows, structures and procedures for their suitability, effectiveness, safety and correctness as part of the internal control system on the basis of an audit and project plan coordinated with the Group companies and adopted by the Executive Board. In the year under review, risk-oriented audit activities focused on the capital expenditure, the performance of efficiency, system and regularity audits and compliance with statutory and Group-internal specifications. Risks identified and weaknesses discovered during these audits are promptly eliminated in collaboration with the management responsible. The Executive Board and Audit Committee of the Supervisory Board are informed of the implementation status of the established improvement measures in a review. The Internal Auditing department of the Rheinmetall Group carried out a quality assessment in the year under review. The external auditors accredited by Deutsches Institut für Interne Revision e.V. (DIIR – German Institute for Internal Auditing) confirmed that internal auditing in the Rheinmetall Group meets the requirements of the DIIR with regard to “Quality management in internal auditing”, as set out in audit standard no. 3 and in the “Guidelines for carrying out a quality assessment”, and that internal auditing at Rheinmetall AG is appropriate and effective overall. Some potential for improvement was identified.

At its meetings, the Audit Committee of Rheinmetall AG deals regularly with the accounting process and the effectiveness of the internal control system, the risk management system and the internal auditing system on the basis of Section 107 (3) AktG. In addition to the suitability, effectiveness, monitoring and management of the processes implemented, potential risks of incorrect statements in financial reporting are discussed.

As part of their audit of the annual financial statements, the auditors of companies included in the consolidated financial statements confirm that the IFRS accounting guidelines have been applied correctly and in full. Moreover, both the single-entity financial statements drawn up by the Group companies and the single-entity and consolidated financial statements of Rheinmetall AG are checked by the respective auditor to ensure compliance with the applicable accounting principles. The audit also includes an assessment of the effectiveness of the accounting-related ICS based on spot checks in sub-divisions.

### »General risk situation«

Potential risks for companies in the Rheinmetall Group include on the one hand factors that cannot be influenced, such as the national and international economy and the general economic situation, and on the other hand risks that can be influenced directly, which are generally operational risks. These are analyzed through the established risk management system at an early stage and countermeasures are initiated if necessary.

The aforementioned risks are not necessarily the only risks to which the Rheinmetall Group is exposed. Risks which have not yet been identified or which are still assessed as insignificant may materialize under altered circumstances, hinder business activities and adversely impact the assets, financial situation and earnings of the Group. The auditor of the financial statements, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, examined the early risk identification system of the Rheinmetall Group to ensure that it complies with the provisions of the Stock Corporation Act as part of its audit of the consolidated annual financial statements and confirmed that it fulfills all legal requirements in accordance with Section 91 (2) AktG and is suitable for identifying developments that could jeopardize the continued existence of the Group at an early stage.

In accordance with the basis outlined for the assessment of risk factors and taking into account the overall risk situation, major asset, financial and earnings risks jeopardizing the Rheinmetall Group on a long-term basis were not identifiable during the past fiscal year. From today’s perspective and in terms of assets and liquidity, no risks exist on an individual basis, in combination with other risks or as a collectivity that may significantly jeopardize the continued existence of Rheinmetall AG and its subsidiaries as a going concern in the foreseeable future.

# Prospects

**»Slowdown in the global economy – growing uncertainty in forecasting«**

The resolutions made at the EU summit held at the start of December 2011 on tackling the debt crisis did not initially lead to the hoped-for stabilization of the markets. The major rating agencies Standard & Poor's, Moody's and Fitch appeared dissatisfied with the outcome of the summit and announced that they would be monitoring the creditworthiness of all EU nations even more closely. In January 2012, Standard & Poor's followed up its announcement with action, downgrading the ratings of both the European bailout fund and nine EU countries, including France and Austria.

In mid-December 2011, the head of the IMF, Christine Lagarde, also made an urgent appeal, stating that the global economy was threatening to escalate out of control and that the outlook for the world economy was "quite gloomy". Lagarde called for collective action on the part of the international community in order to counter the risk of a global economic crisis.

Previously, the Organization for Economic Cooperation and Development (OECD) had identified the euro crisis as the biggest threat to the global economy, stating that if market concerns were not addressed, there would be the risk of huge economic disruption and a new credit crunch. "Prospects only improve if decisive action is taken quickly," explained OECD Chief Economist Pier Carlo Padoan. The OECD sees the situation in the USA as a further risk factor: According to the OECD Economic Outlook from November 2011, if no way is found to attenuate the austerity measures set to come into law from 2013, this could tip the economy into a recession that monetary policy can do little to prevent.

Uncertainty in forecasting has increased further against this backdrop. Like most economic researchers, the economic experts at the OECD revised their forecast for 2012 downward. The experts still only expected growth of 1.6 % for the 34 OECD member states in 2012, and of just 0.2 % for the euro zone. However, gross domestic product in the USA is still expected to rise by 2.0%.

Leading economic research institutes anticipate that the weakening global economy in 2012 will also cast a shadow over the German economy. However, according to the Ifo Economic Forecast, a recession could be avoided if the euro crisis does not intensify any further. Under these conditions, the ifo economic researchers expect a slight increase in German gross domestic product of 0.4 % in 2012. The OECD is only faintly more optimistic and forecasts growth in annual economic output for Germany of 0.6%. In January 2012, the German government lowered its growth forecast for the year as a whole from its initial 1.0% to 0.7%.

Surprisingly positive news came out of Italy and Spain at the start of 2012: Successful auctions of Italian and Spanish government bonds led, at least temporarily, to a calming of the markets and were regarded by some observers as an important indicator of a gradual easing of the debt crisis.

Emerging countries, especially those in Asia, will continue to dictate the rhythm of global economic growth in 2012. However, the impetus for growth arising from emerging countries such as China and India is expected to weaken in 2012. OECD experts forecast growth of 8.5 % for China in 2012, following 9.3 % in the previous year. For India, a slowdown in growth momentum from 7.7 % in 2011 to 7.2 % in 2012 is expected.

# Prospects

Despite the unfavorable global economic outlook, China still believes it is on a stable growth path. At China's Central Economic Work Conference, held in Beijing in mid-December 2011, it was stated that stability would be maintained by controlling the overheated real estate market, combating inflation and promoting domestic demand. In Japan, the after-effects of the earthquake and tsunami disaster of March 2011 were offset more quickly than expected. Following a drop in economic output of 0.3 % in 2011 compared to 2010, the OECD is already forecasting a return to growth of 2.0% in 2012.

The forecasts for 2013 are more optimistic overall. The OECD predicts growth of 2.3% for its 34 member states. An increase in economic output of 9.5 % is anticipated in China, while India's gross domestic product is expected to rise by 8.2 %. For the USA, the OECD experts anticipate growth of 2.5 %. The forecast for Germany is somewhat lower, where economic growth of 1.9 % is expected in 2013. Nevertheless, the German economy is anticipated to enjoy once again more positive development than all of the other EU nations. However, the OECD expects the euro zone to have also once again bottomed out: In 2013, its member states are expected to grow by 1.4%.

**»Defence technology remains a growth market – global defence expenditure increases«**

Irrespective of the budgetary constraints in a number of countries, defence technology remains a growth market. However, this growth momentum is set to decline considerably, especially as a result of the austerity measures in the USA and numerous European countries. According to the calculations of defence analysts at IHS Jane's, global defence expenditure in the 65 countries with the largest defence budgets will increase by approximately 7% by 2015. For procurement budgets, this increase is expected to be as high as around 12%. The main drivers behind this growth will be emerging countries such as China, Russia, India and Brazil, but Australia, South Africa and countries in the Middle East and Far East will also provide impetus for growth.

However, in the USA, the first appreciable austerity measures have been adopted in the defence budget. While in 2011 the defence budget still stood at around USD 711 billion, in 2012 it is expected to drop to USD 656 billion in accordance with the Department of Defence's planning. The trend towards budget cuts will nevertheless continue: IHS Jane's forecasts – not least due to the cuts in spending already agreed and the austerity measures still to be expected – that US armaments expenditure in 2015 will be around 14% lower than the level seen in 2011. Despite these huge cost-cutting measures, the USA will remain number one in terms of defence expenditure. In 2015, its share of global armaments expenditure will still be 40%.

A varied picture is emerging for Europe. Although IHS Jane's expects a reduction in spending of around 8% by 2015 for the five European countries with the highest defence expenditure, reduced budgets in the United Kingdom, Italy, Spain and Greece will be seen alongside some significant increases in other countries, including Turkey and Norway.

From today's perspective, the pressure placed on the German armed forces to cut costs will be lower than originally intended. So as not to jeopardize the performance and operational capability of the German armed forces, the budget will now only be reduced to €30.4 billion up to 2015 according to the latest medium-term financial planning. In the budget for 2012, defence expenditure totaling approximately €31.9 billion is planned. This is an overall increase of around €320 million compared to 2011, despite reductions in personnel expenditure and increased operating expenditure. Deployment expenditure will increase by €250 million compared to 2011. An additional €190 million is planned for the procurement of military equipment.

With its expertise in the protection and engagement of land forces, Rheinmetall Defence believes it is well prepared for a modernization of the German armed forces that is in line with requirements and at the same time cost-efficient. Furthermore, thanks to its increased international focus – the proportion of sales achieved abroad by Rheinmetall Defence is 63 % – the Company has laid the best possible foundations for further benefiting from the modernization projects of Germany's friendly nations.

### »European automotive industry loses momentum – Asia remains the growth driver«

Following a strong automotive year in 2011, the German automotive industry is expecting much more muted development in 2012. The industry is anticipating "more headwinds – 2012 will be a hard year," explained the President of the Association of the German Automotive Industry (VDA), Matthias Wissmann, at the annual VDA press conference at the start of December 2011. However, Wissmann appeared confident about 2012 overall, as long as the financial markets are successfully stabilized.

According to the VDA, the automotive industry will remain a growth industry in the long term. The German automotive industry will have good opportunities to play a major role in this dynamic growth.

Analysts from IHS Automotive expect global production of passenger cars and light commercial vehicles up to 3.5t to increase by 6.0 % in 2012. According to the IHS forecast, production figures in the NAFTA region are set to rise by 5.9 % in 2012. At the end of the year, Japan will significantly exceed the production volumes seen prior to the earthquake and tsunami disaster: The analysts anticipate an increase of 18.6 % in 2012, following a 14.2 % decline in 2011 as a result of the disaster. Other Asian nations will also provide the automotive market with clear impetus for growth. For example, production in China is set to increase by 8.8 % and in India by 9.1 %. An overall increase of 11.4 % is expected for Asia in the production of passenger cars and light commercial vehicles up to 3.5t.

Forecasts for the Western European automotive market are considerably weaker, where IHS Automotive is expecting a decline in automotive production of 5.4%, while a drop of 4.5% is anticipated for Germany in 2012, following a record year in 2011.

Product trends will continue to be dominated by technologies aimed at reducing consumption and lowering pollution. Here, the Automotive sector believes that the KSPG's decision to position itself at an early stage as a development partner of internationally successful vehicle manufacturers with a range of products that make a significant contribution to improving engine and drive train technology was a worthwhile one.

### »Continuation of corporate growth«

Rheinmetall anticipates further growth in the Group: For fiscal 2012, Rheinmetall expects consolidated sales of approximately €4.9 billion, following €4.5 billion in the past fiscal year.

Sales development in the Automotive sector will continue to be largely determined by the global automotive industry in the current fiscal year. Here, growth expectations for automotive production in North and South America and in Asia – according to current expert forecasts – will be accompanied by an anticipated decline in production volumes in Western Europe. Against this backdrop, Rheinmetall is currently expecting the Automotive sector to achieve sales growth of around 5 % to slightly over €2.4 billion in 2012. Here, it must be taken into consideration that sales from the joint venture in China are not consolidated and therefore cannot make a recognized contribution to growth, even though sales here are expected to be in the region of €300 million.

# Prospects

With lower defence expenditure in some European countries and the USA in 2012, the Defence sector is expecting sales slightly down on the previous year's level based on the current scope of consolidation. Based on the addition of logistical vehicle sales in the Rheinmetall MAN Military Vehicles (RMMV) joint venture, which is to be fully included in corporate accounting for the first time from the start of fiscal 2012, Rheinmetall is anticipating sales of approximately €2.5 billion for the Defence sector in 2012, following €2.1 billion in 2011.

**»2012 earnings at previous year's level«**

For the current 2012 fiscal year, Rheinmetall anticipates consolidated earnings before interest and taxes (EBIT) around the same level as the previous year, when the best result in the history of the Company was achieved with €354 million. A somewhat weaker earnings development in the Defence sector forms the basis of this expectation. However, a slight improvement in earnings is anticipated for the Automotive sector.

Rheinmetall expects growth in sales and earnings in fiscal 2013. This requires the continued positive development of the global automotive industry and the implementation of large projects in the Defence sector as planned.

Ongoing satisfactory net investment income and net income is expected for the Rheinmetall AG management holding company in 2012 and 2013.

# Report on post-balance sheet date events

**»Events after the balance sheet date«**

Armin Papperger, who has up to now been a member of the Management Board Defence, has been appointed as a member of the Executive Board of Rheinmetall AG for five years with effect from January 1, 2012. As the new Chairman of the Management Board Defence, he will be the Executive Board member responsible for the Defence sector, which up to December 31, 2011 was managed by Klaus Eberhardt, CEO of Rheinmetall AG.

In January 2012, Rheinmetall Defence and Cassidian, a division of EADS Deutschland GmbH, announced that they would be pooling their unmanned aerial systems activities (UAS) and working together in the future in the areas of UAS and cargo loading systems as part of a joint venture to be established. This step will significantly improve the future opportunities for development of the Rheinmetall Defence airborne systems product group. This joint venture will give the product group access to broader development resources and international market access opportunities that have not so far existed to any comparable extent. Once all the necessary authorizations and antitrust approvals have been granted, Cassidian will hold 51 % of the shares in the joint venture, while Rheinmetall Defence will hold 49 %. For Rheinmetall Defence, its primary goal was to establish future prospects for the airborne systems product group that are sustainable in the long term, to strengthen its competitive position on a sustainable basis and to secure jobs at the Bremen site. For Cassidian, the integration of this product group from Rheinmetall Defence is a perfect addition to its existing unmanned aerial systems product range.

As of February 1, 2012, Rheinmetall Defence has responded to the ongoing growth and increasing internationalization of its business. The Combat Systems, Electronic Solutions and Wheeled Vehicles divisions will represent the core of the new management and organizational structure of Rheinmetall Defence. Up to now, six divisions and the wheeled vehicle joint venture have been combined in these three divisions, in a new form in some cases.

On February 2, 2012, Rheinmetall Waffe Munition GmbH, Unterlüß, sold its 40 % stake in Burkan Munitions Systems L.L.C., Abu Dhabi, United Arab Emirates, to Tawazun Holding Company L.L.C., Abu Dhabi, United Arab Emirates, following the successful completion of the establishment of the ammunition factory.

Düsseldorf, March 15, 2012

Rheinmetall Aktiengesellschaft
The Executive Board

Klaus Eberhardt    Dr. Gerd Kleinert    Dr. Herbert Müller    Armin Papperger

# Consolidated financial statements 2011 of Rheinmetall AG

# Rheinmetall Group
# Consolidated balance sheet as of December 31, 2011

Assets *€ million*

| | Note | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|---|
| Intangible assets | (7) | 694 | 902 |
| Property, plant and equipment | (8) | 1,104 | 1,135 |
| Investment property | (9) | 21 | 20 |
| Investments accounted for using the equity method | (10) | 106 | 111 |
| Other noncurrent financial assets | (13) | 33 | 11 |
| Other noncurrent assets | (14) | 8 | 7 |
| Deferred taxes | (30) | 71 | 85 |
| **Noncurrent assets** | | **2,037** | **2,271** |
| | | | |
| Inventories | (11) | 739 | 813 |
| ./. Prepayments received | | (31) | (28) |
| | | 708 | 785 |
| | | | |
| Trade receivables | (12) | 909 | 1,027 |
| Other current financial assets | (13) | 58 | 38 |
| Other current receivables and assets | (14) | 94 | 131 |
| Income tax receivables | | 25 | 16 |
| Cash and cash equivalents | (15) | 629 | 535 |
| Disposal group held for sale | (3) | - | 29 |
| **Current assets** | | **2,423** | **2,561** |
| | | | |
| **Total assets** | | **4,460** | **4,832** |

Equity and liabilities *€ million*

| | Note | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|---|
| Share capital | | 101 | 101 |
| Additional paid-in capital | | 304 | 307 |
| Other reserves | | 751 | 843 |
| Net income of Rheinmetall AG shareholders | | 162 | 213 |
| Treasury shares | | (52) | (55) |
| **Rheinmetall AG shareholders' equity** | | **1,266** | **1,409** |
| Minority interests | | 89 | 137 |
| **Equity** | (16) | **1,355** | **1,546** |
| | | | |
| Provisions for pensions and similar obligations | (17) | 677 | 729 |
| Other noncurrent provisions | (18) | 112 | 93 |
| Noncurrent financial debts | (19) | 671 | 620 |
| Other noncurrent liabilities | (21) | 37 | 34 |
| Deferred taxes | (30) | 50 | 81 |
| **Noncurrent liabilities** | | **1,547** | **1,557** |
| | | | |
| Current provisions | (18) | 395 | 371 |
| Current financial debts | (19) | 34 | 45 |
| Trade liabilities | (20) | 593 | 667 |
| Other current liabilities | (21) | 472 | 578 |
| Income tax liabilities | | 64 | 46 |
| Liabilities in connection with disposal groups | (3) | - | 22 |
| **Current liabilities** | | **1,558** | **1,729** |
| | | | |
| **Total liabilities** | | **4,460** | **4,832** |

# Rheinmetall Group
# Consolidated income statement for fiscal 2011

*€ million*

| | Note | 2010 | 2011 |
|---|---|---|---|
| **Sales** | | **3,989** | **4,454** |
| Changes in inventories and work performed by the enterprise and capitalised | | 69 | 51 |
| **Total operating performance** | (22) | **4,058** | **4,505** |
| | | | |
| Other operating income | (23) | 136 | 151 |
| Cost of materials | (24) | 1,989 | 2,291 |
| Personnel expenses | (25) | 1,181 | 1,260 |
| Amortization, depreciation and impairment | (26) | 167 | 184 |
| Other operating expenses | (27) | 579 | 585 |
| **Net operating income** | | **278** | **336** |
| | | | |
| Net interest [1] | (28) | (68) | (59) |
| Net investment income and other net financial income [2] | (29) | 19 | 18 |
| **Net financial income** | | **(49)** | **(41)** |
| | | | |
| **Earnings before taxes (EBT)** | | **229** | **295** |
| Income taxes | (30) | (55) | (70) |
| **Net income** | | **174** | **225** |
| Of which: | | | |
| *Minority interests* | (31) | *12* | *12* |
| *Rheinmetall AG shareholders* | | *162* | *213* |
| | | | |
| Earnings per share | (32) | € 4.23 | € 5.55 |
| | | | |
| EBITDA | | 464 | 538 |
| EBIT | | 297 | 354 |

1) *Of which interest expense: €65 million (previous year: €72 million)*
2) *Of which income from investments carried at equity: €18 million (previous year: €22 million)*

# Comprehensive income 2011

*€ million*

| | 2010 | 2011 |
|---|---|---|
| **Net income** | **174** | **225** |
| Actuarial gains and losses from pension provisions | (54) | (45) |
| Currency conversion difference | 89 | (10) |
| Change in value of derivative financial instruments (cash flow hedge) | 13 | (28) |
| Income/expenses from investments accounted for using the equtiy method | (7) | (1) |
| **Other comprehensive income (after taxes)** | **41** | **(84)** |
| | | |
| **Comprehensive income** | **215** | **141** |
| Of which: | | |
| *Minority interests* | *21* | *0* |
| *Rheinmetall AG shareholders* | *194* | *141* |

# Rheinmetall Group
# Consolidated statement of cash flows for fiscal 2011

*€ million*

| | 2010 | 2011 |
|---|---|---|
| **Financial resources January 1** | **577** | **629** |
| | | |
| Net income | 174 | 225 |
| Amortization, depreciation and impairments | 167 | 184 |
| Changes in pension provisions | 3 | (7) |
| | | |
| **Gross cash flows** | **344** | **402** |
| | | |
| Income from disposition of non-current assets | (2) | (7) |
| Changes in other provisions | 1 | (51) |
| Changes in inventories | (84) | (39) |
| Changes in receivables, liabilities without financial debts and prepaid & deferred items | (104) | 17 |
| Other non-cash expenses and income | (8) | (32) |
| | | |
| **Cash flows from operating activities** [1] | **147** | **290** |
| | | |
| Investments in property, plant and equipment, intangible assets and investment property | (186) | (197) |
| Cash receipts from the disposal of property, plant and equipment, intangible assets and investment property | 12 | 14 |
| Investments in consolidated companies and financial assets | (103) | (71) |
| Divestments of consolidated companies and financial assets | 19 | 3 |
| | | |
| **Cash flows from investing activities** | **(258)** | **(251)** |
| | | |
| Capital contributions by third parties | 2 | 2 |
| Rheinmetall AG capital increase | (11) | (58) |
| Dividends paid out by Rheinmetall AG | (4) | (4) |
| Other profit distributions | - | (15) |
| Sale of treasury shares | 4 | 6 |
| Borrowing of financial debts | 504 | 21 |
| Repayment of financial debts | (339) | (83) |
| | | |
| **Cash flows from financing activities** | **156** | **(131)** |
| | | |
| **Changes in financial resources** | 45 | (92) |
| Changes in cash and cash equivalents due to exchange rates | 7 | (2) |
| | | |
| **Total change in financial resources** | **52** | **(94)** |
| **Financial resources December 31** | **629** | **535** |

*For comments on the cash flow statement, see Note (34).*

1) *including:*

*Net interest of €-15 million (previous year: €-42 million)*

*Net income taxes of €-32 million (previous year: €-39 million)*

# Rheinmetall Group
# Statement of changes in equity

*€ million*

| | Share capital | Additional paid-in capital | Retained earnings | Difference of currency conversion | Statement of fair value and other valuations | Total of fair value changes | Group net income/loss allocated to shareholders of Rheinmetall AG | Treasury shares | Rheinmetall AG shareholders equity | Minority interests | Equity |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Balance as at December 31, 2009 / as at January 1, 2010** | **101** | **303** | **711** | *(20)* | *90* | **70** | **(58)** | **(57)** | **1,070** | **64** | **1,134** |
| Net income | - | - | - | - | - | - | 162 | - | 162 | 12 | 174 |
| Other comprehensive income | - | - | (57) | *80* | *9* | 89 | - | - | 32 | 9 | 41 |
| **Comprehensive income** | **-** | **-** | **(57)** | **80** | **9** | **89** | **162** | **-** | **194** | **21** | **215** |
| Dividends payout | - | - | (11) | - | - | - | - | - | (11) | (4) | -15 |
| Changes in scope of consolidation | - | - | (1) | - | - | - | - | - | (1) | 4 | 3 |
| Transfer to/from reserves | - | - | (58) | - | - | - | 58 | - | - | - | - |
| Other changes | - | 1 | 8 | - | - | - | - | 5 | 14 | 4 | 18 |
| **Balance as at December 31, 2010/ as at January 1, 2011** | **101** | **304** | **592** | *60* | *99* | **159** | **162** | **(52)** | **1,266** | **89** | **1,355** |
| Net income | - | - | - | - | - | - | 213 | - | 213 | 12 | 225 |
| Other comprehensive income | - | - | (46) | *(4)* | *(22)* | (26) | - | - | (72) | (12) | (84) |
| **Comprehensive income** | **-** | **-** | **(46)** | **(4)** | **(22)** | **(26)** | **213** | **-** | **141** | **0** | **141** |
| Dividends payout | - | - | (58) | - | - | - | - | - | (58) | (4) | (62) |
| Changes in scope of consolidation | - | - | 60 | - | - | - | - | - | 60 | 52 | 112 |
| Transfer to/from reserves | - | - | 162 | - | - | - | (162) | - | - | - | - |
| Other changes | - | 3 | - | - | - | - | - | (3) | - | - | - |
| **Balance as at December 31, 2011** | **101** | **307** | **710** | *56* | *77* | **133** | **213** | **(55)** | **1,409** | **137** | **1,546** |

*For comments on equity, see Note (16).*

# Notes to the consolidated financial statements
# Segment reporting

*€ million*

| Corporate sectors | | Defence | | Automotive | | Others / Consolidation | | Group | |
|---|---|---|---|---|---|---|---|---|---|
| | | **2010** | **2011** | **2010** | **2011** | **2010** | **2011** | **2010** | **2011** |
| **Balance sheet (December 31)** | | | | | | | | | |
| Equity | (1) | 971 | 1,046 | 687 | 690 | (303) | (190) | 1,355 | 1,546 |
| Pension provisions | (2) | 354 | 396 | 281 | 290 | 42 | 43 | 677 | 729 |
| Net financial debts | (3) | (178) | (120) | (209) | (161) | 463 | 411 | 76 | 130 |
| Capital employed | (1)+(2)+(3) | 1,147 | 1,322 | 759 | 819 | 202 | 264 | 2,108 | 2,405 |
| Additions to capital employed | | 77 | 77 | 169 | 169 | (122) | (122) | 124 | 124 |
| Capital employed December 31 | | 1,224 | 1,399 | 928 | 988 | 80 | 142 | 2,232 | 2,529 |
| Average capital employed | (4) | 1,092 | 1,312 | 895 | 958 | 41 | 111 | 2,028 | 2,381 |
| | | | | | | | | | |
| **Income statement** | | | | | | | | | |
| External sales | | 2,007 | 2,141 | 1,982 | 2,313 | - | - | 3,989 | 4,454 |
| *Of which domestic (in %)* | | *33.7* | *36.8* | *27.9* | *23.6* | - | - | *30.8* | *29.9* |
| *Of which foreign (in %)* | | *66.3* | *63.2* | *72.1* | *76.4* | - | - | *69.2* | *70.1* |
| Equity income | | 12 | 7 | 9 | 11 | 1 | 0 | 22 | 18 |
| EBITDA | | 297 | 303 | 183 | 254 | (16) | (19) | 464 | 538 |
| Amortization, depreciation and impairment | | (63) | (80) | (102) | (103) | (2) | (1) | (167) | (184) |
| *Of which impairment* | | *0* | *(3)* | *(6)* | *(5)* | *(2)* | 0 | *(8)* | *(8)* |
| EBIT | (5) | 234 | 223 | 81 | 151 | (18) | (20) | 297 | 354 |
| Interest income | | 5 | 8 | 4 | 5 | (5) | (7) | 4 | 6 |
| Interest expenses | | (32) | (24) | (22) | (21) | (18) | (20) | (72) | (65) |
| Net interest | | (27) | (16) | (18) | (16) | (23) | (27) | (68) | (59) |
| EBT | | 207 | 207 | 63 | 135 | (41) | (47) | 229 | 295 |
| Income taxes | | (41) | (46) | (25) | (30) | 11 | 6 | (55) | (70) |
| Net income | | 166 | 161 | 38 | 105 | (30) | (41) | 174 | 225 |
| EBIT rate of return (in %) | | 11.6 | 10.4 | 4.1 | 6.5 | - | - | 7.4 | 7.9 |
| | | | | | | | | | |
| **Other data** | | | | | | | | | |
| ROCE (in %) | (5) / (4) | 21.4 | 17.0 | 9.1 | 15.8 | - | - | 14.6 | 14.9 |
| Capital expenditures | | 93 | 102 | 96 | 104 | 0 | 1 | 189 | 207 |
| R&D expenditures | | 88 | 82 | 120 | 130 | - | - | 208 | 212 |
| Order intake | | 1,977 | 1,831 | 1,997 | 2,358 | - | - | 3,974 | 4,189 |
| Order backlog December 31 | | 4,772 | 4,541 | 364 | 409 | - | - | 5,136 | 4,950 |
| Prepayments received | | 584 | 699 | 8 | 9 | - | - | 592 | 708 |
| Employees as at December 31 (capacities) | | 9,037 | 9,833 | 10,816 | 11,548 | 126 | 135 | 19,979 | 21,516 |

*€ million*

| Regions | Germany | | Rest of Europe | | North America | | Asia | | Other regions / Consolidation | | **Group** | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **2010** | **2011** | **2010** | **2011** | **2010** | **2011** | **2010** | **2011** | **2010** | **2011** | **2010** | **2011** |
| External sales Defence | 677 | 788 | 598 | 612 | 219 | 242 | 392 | 388 | 121 | 111 | 2,007 | 2,141 |
| External sales Automotive | 552 | 545 | 934 | 1,184 | 211 | 241 | 117 | 152 | 168 | 191 | 1,982 | 2,313 |
| External sales Total | 1,229 | 1,333 | 1,532 | 1,796 | 430 | 483 | 509 | 540 | 289 | 302 | 3,989 | 4,454 |
| in % of Group sales | 31 | 30 | 38 | 40 | 11 | 11 | 13 | 12 | 7 | 7 | - | - |
| Assets | 1,029 | 1,175 | 539 | 609 | 111 | 122 | 46 | 60 | 94 | 91 | 1,819 | 2,057 |

*For comments on the segment reports, see Note (35).*

# Notes to the consolidated financial statements
# Fixed-asset analysis

*€ million*

| | Gross values | | | | | |
|---|---|---|---|---|---|---|
| **2010** | Jan.1, 2010 | Additions | Disposals | Book transfers/ step-up | Adjustment scope of consolidation | Currency differences |
| **Intangible assets** | | | | | | |
| Development costs | 135 | 38 | 4 | - | - | 4 |
| Concessions, industrial property rights and licenses | 103 | 8 | 3 | 6 | 5 | 1 |
| Other intangible assets | 38 | 9 | 0 | 1 | 77 | 2 |
| Goodwill | 422 | - | 0 | - | 25 | 1 |
| Prepayments made | 2 | 1 | 0 | (2) | - | 0 |
| | **700** | **56** | **7** | **5** | **107** | **8** |
| **Property, plant and equipment** | | | | | | |
| Land, equivalent titles, and buildings (incl. buildings on leased land) | 959 | 6 | 2 | 1 | 2 | 56 |
| Production plant and machinery | 1,735 | 42 | 81 | 40 | 11 | 75 |
| Other plant, factory and office equipment | 506 | 26 | 34 | 11 | 2 | 15 |
| Prepayments made and construction in progress | 58 | 59 | 1 | (53) | 1 | 3 |
| | **3,258** | **133** | **118** | **(1)** | **16** | **149** |
| | | | | | | |
| **Investment Property** | **42** | **0** | **0** | **0** | **-** | **0** |
| | | | | | | |
| **Total** | **4,000** | **189** | **125** | **4** | **123** | **157** |

| **2011** | Jan.1, 2011 | Additions | Disposals | Book transfers | Adjustment scope of consolidation | Currency differences |
|---|---|---|---|---|---|---|
| **Intangible assets** | | | | | | |
| Development costs | 173 | 35 | 3 | - | - | 1 |
| Concessions, industrial property rights and licenses | 120 | 11 | 2 | 10 | 2 | (1) |
| Other intangible assets | 127 | 1 | - | (10) | 101 | 0 |
| Goodwill | 448 | - | - | - | 105 | 0 |
| Prepayments made | 1 | 1 | - | (1) | 0 | 0 |
| | **869** | **48** | **5** | **(1)** | **208** | **0** |
| **Property, plant and equipment** | | | | | | |
| Land, equivalent titles, and buildings (incl. buildings on leased land) | 1,022 | 12 | 7 | 4 | 1 | 5 |
| Production plant and machinery | 1,822 | 47 | 85 | 36 | 39 | 6 |
| Other plant, factory and office equipment | 526 | 17 | 39 | 7 | 15 | (3) |
| Prepayments made and construction in progress | 67 | 83 | 1 | (53) | 0 | (2) |
| | **3,437** | **159** | **132** | **(6)** | **55** | **6** |
| | | | | | | |
| **Investment Property** | **42** | **-** | **6** | **0** | **-** | **0** |
| | | | | | | |
| **Total** | **4,348** | **207** | **143** | **(7)** | **263** | **6** |

| | Amortization, depreciation and impairment | | | | | | | | Net value |
|---|---|---|---|---|---|---|---|---|---|
| **Dec. 31, 2010** | Jan.1, 2010 | Additions | Disposals | Book transfers | Write-ups | Adjustment scope of consolidation | Currency differences | **Dec. 31, 2010** | **Dec. 31, 2010** |
| | | | | | | | | | |
| 173 | 52 | 12 | - | - | - | - | 1 | 65 | 108 |
| 120 | 83 | 9 | 3 | 1 | - | - | 2 | 92 | 28 |
| 127 | 10 | 9 | - | - | - | 0 | (1) | 18 | 109 |
| 448 | 0 | - | - | - | - | - | - | - | 448 |
| 1 | - | - | - | - | - | - | - | - | 1 |
| **869** | **145** | **30** | **3** | **1** | **-** | **0** | **2** | **175** | **694** |
| | | | | | | | | | |
| 1,022 | 467 | 25 | 1 | (2) | - | (1) | 35 | 523 | 499 |
| 1,822 | 1,341 | 75 | 78 | (1) | - | 0 | 54 | 1,391 | 431 |
| 526 | 406 | 34 | 31 | 0 | - | (3) | 12 | 418 | 108 |
| 67 | - | 1 | - | - | - | - | - | 1 | 66 |
| **3,437** | **2,214** | **135** | **110** | **(3)** | **-** | **(4)** | **101** | **2,333** | **1,104** |
| | | | | | | | | | |
| **42** | **19** | **2** | **0** | **0** | **-** | **-** | **0** | **21** | **21** |
| | | | | | | | | | |
| **4,348** | **2,378** | **167** | **113** | **(2)** | **-** | **(4)** | **103** | **2,529** | **1,819** |

| **Dec. 31, 2011** | Jan.1, 2011 | Additions | Disposals | Book transfers | Write-ups | Adjustment scope of consolidation | Currency differences | **Dec. 31, 2011** | **Dec. 31, 2011** |
|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | | |
| 206 | 65 | 14 | - | - | - | 0 | 0 | 79 | 127 |
| 140 | 92 | 13 | 1 | 0 | - | 0 | (1) | 103 | 37 |
| 219 | 18 | 17 | - | (1) | - | - | 1 | 35 | 184 |
| 553 | - | - | - | - | - | - | - | - | 553 |
| 1 | - | - | - | - | - | - | - | - | 1 |
| **1,119** | **175** | **44** | **1** | **(1)** | **-** | **0** | **0** | **217** | **902** |
| | | | | | | | | | |
| 1,037 | 523 | 23 | 6 | (2) | 0 | 0 | 7 | 545 | 492 |
| 1,865 | 1,391 | 81 | 82 | 0 | (1) | 22 | 6 | 1,417 | 448 |
| 523 | 418 | 36 | 38 | (2) | 0 | 12 | (4) | 422 | 101 |
| 94 | 1 | - | - | (1) | - | - | 0 | 0 | 94 |
| **3,519** | **2,333** | **140** | **126** | **(5)** | **(1)** | **34** | **9** | **2,384** | **1,135** |
| | | | | | | | | | |
| **36** | **21** | **0** | **6** | **0** | **-** | **-** | **1** | **16** | **20** |
| | | | | | | | | | |
| **4,674** | **2,529** | **184** | **133** | **(6)** | **(1)** | **34** | **10** | **2,617** | **2,057** |

# Notes to the consolidated financial statements
# Accounting principles

**(1) »General information«**
The consolidated financial statements of Rheinmetall AG have been prepared in accordance with the regulations of Section 315a (1) German Commercial Code (“HGB”) and hence with the International Financial Reporting Standards (IFRS) as adopted by the European Union (EU). A Group-wide accounting guideline binding on all companies included in the consolidated financial statements ensures that all current rules and principles are consistently applied and interpreted. The consolidated financial statements and the Group management report, which is consolidated with the management report of Rheinmetall AG, are to be submitted to the operator of the electronic Federal Gazette and published in the electronic Federal Gazette.

The following standards, interpretations and amendments to existing standards were used on an obligatory basis for the first time in fiscal 2011.

| | |
|---|---|
| IFRS improvements | Collective standard published 2010 |
| IFRIC 19 | “Extinguishing Financial Liabilities with Equity Instruments” |

As part of its annual updating process, the IASB published the collective standard Improvements to IFRS in May 2010, through which smaller amendments are to be made to six IFRS standards and one interpretation. Application of the amendments is mandatory as of January 1, 2011. The amendments did not have a significant impact on Rheinmetall’s consolidated financial statements.

IFRIC Interpretation 19 “Extinguishing Financial Liabilities with Equity Instruments”, published in November 2009, clarifies, with regard to accounting for financial liabilities, the way in which partial or full repayment with equity instruments agreed subsequently between the creditor and debtor is to be recognized in the balance sheet. Application of this interpretation is mandatory for fiscal years from July 1, 2010. There were no significant effects on the Rheinmetall consolidated financial statements from this first-time application.

The transitional provisions have been duly complied with.

In the case of the following new or amended standards and interpretations, published by the IASB, adoption is not mandatory and, with the exception of one amendment to IFRS 7, adoption into the EU Community Law has not yet taken place.

| | |
|---|---|
| Amendment to IAS 1 | “Presentation of Financial Statements” |
| Amendment to IAS 12 | “Income Taxes” |
| Amendment to IAS 19 | “Employee Benefits” |
| Amendment to IAS 27 | “Consolidated and Separate Financial Statements” |
| Amendment to IAS 28 | “Investments in Associates” |
| Amendment to IAS 32 | “Financial Instruments: Presentation” |
| Amendment to IFRS 7 | “Financial Instruments: Disclosures” |
| Amendment to IFRS 9 | “Financial Instruments” |
| IFRS 9 | “Financial Instruments” |
| IFRS 10 | “Consolidated Financial Statements” |
| IFRS 11 | “Joint Arrangements” |
| IFRS 12 | “Disclosure of Interests in Other Entities” |
| IFRS 13 | “Fair Value Measurement” |
| IFRIC 20 | “Stripping Costs in the Production Phase of Surface Mine” |

The amendments to IAS 1 “Presentation of Financial Statements” relate to the presentation of amounts recognized directly in equity which constitute components of comprehensive income. In future, items are to be allocated according to whether or not they are to be subsequently reclassified to the income statement. Application of this amendment is mandatory for fiscal years from January 1, 2012 onwards and will affect the disclosure of other comprehensive income.

The amendment to IAS 12 “Income Taxes” relates to the measurement of deferred taxes for properties held for investment, which are measured at fair value, and for intangible assets and property, plant and equipment, which are measured in accordance with the revaluation model. Until now, the measurement of deferred taxes for these assets has depended on whether the company intends to realize the carrying amount through use or through a sale. The new regulation implies a refutable assumption of realization through the sale of the asset. Application of the amendment is mandatory as of January 1, 2012. This amendment will have no impact on the assets and earnings situation of the Rheinmetall Group.

The amendments to IAS 19 “Employee Benefits” mainly involve the abolition of the postponed recognition of actuarial gains and losses as part of the corridor method, the re-structuring of the pension expense and expanded Notes for defined benefit plans. When the pension expense is being calculated, the new regulations specify that a past service cost is to be recognized in full immediately in the period of the planned amendment, and that the interest rate which is decisive for discounting the fund assets is also to be used as the expected return on the plan assets. The discontinuation of the corridor method has no effect on the Rheinmetall Group as actuarial gains and losses are already fully recognized directly in other income in the year in which they arise. The other amendments will influence the consolidated financial statements and the Notes in particular, although the evaluation of the effects has not yet been carried out. Application of the revised standard is mandatory for fiscal years from January 1, 2013 onwards.

The amendments to IAS 32 “Financial Instruments: Presentation” and IFRS 7 “Financial Instruments: Disclosures” published in 2011 provide clarification as regards the offsetting of financial receivables and financial liabilities and the expanded Notes regarding this. This amendment does not intend to alter recognition in the balance sheet. Application of the amendments to the Notes is mandatory for fiscal years from January 1, 2013 onwards and the clarification regarding offsetting from January 1, 2014 onwards. Changes to the assets and earnings in the Rheinmetall consolidated financial statements are not expected.

An amendment to IFRS 7 “Financial Instruments: Disclosures” was published in the previous year, relating to extended disclosures in the Notes in the event of the transfer of financial assets with regard to corresponding financial liabilities and the risks of a remaining exposure. In addition, disclosures are required for substantial transfers around the end of a reporting period. Application is to become compulsory for the first time for fiscal years beginning on or after July 1, 2011. This amendment will not have a significant impact on the Notes to Rheinmetall’s consolidated financial statements.

IFRS 9 “Financial Instruments” replaces IAS 39 “Financial Instruments: Recognition and Measurement” for the classification and measurement of financial assets and liabilities. With the amendments published in 2011, the date from which the first-time application of this standard published in 2010 is to become compulsory has been shifted from 2013 as originally planned to fiscal years from January 1, 2015 onwards. The resulting effects on Rheinmetall’s consolidated financial statements are currently deemed to be not significant.

# Notes to the consolidated financial statements
## Accounting principles

A new concept for determining subsidiaries subject to consolidation has been introduced into IFRS 10 "Consolidated Financial Statements" in the form of an amended definition of the concept of control. In addition to the voting rights, other contractual agreements or constructive patterns can lead to control if the parent companies can determine the financial and business activities of another company, achieve variable returns from this and influence the level of the returns. The new control concept may lead to changes in the manner in which the entities to be included in the scope of consolidation are determined. In addition, the consolidation guidelines which were formerly contained in IAS 27 have been integrated into the new standard. No amendments have been made to their content. This means that IAS 27 is only relevant for separate financial statements and contains the designation "Separate Financial Statements". Application of the new IFRS 10 and the amended IAS 27 is mandatory for fiscal years from January 1, 2013 onwards.

IFRS 11 "Joint Arrangements" contains the regulations for recognition in the balance sheet of joint arrangements with one or more companies, and thus replaces IAS 31 "Interests in Joint Ventures". The main amendments relate to the abolition of the voting right of the proportionate consolidation of joint ventures, the terminology used and the categorization of joint arrangements, which distinguishes between joint activities and joint ventures. The discontinuation of proportionate consolidation has no effects on the Rheinmetall Group as joint ventures are already included in the consolidated financial statements in accordance with the equity method. In the future, only this method will be permissible. The investigation as to whether joint arrangements based on the new standard will lead to a different evaluation than at present, and hence to amended accounting, has not yet been carried out. Application of the new standard is mandatory for fiscal years from January 1, 2013 onwards.

In IFRS 12 "Disclosure of Interests in Other Entities", all Notes about companies which are under joint control, joint management or considerable influence of the reporting company are combined together in a standard. This means that the disclosure requirements formerly contained in standards IAS 27, IAS 28 and IAS 31 are replaced. The scope of the necessary disclosure requirements has been expanded compared to the existing regulations as information about judgments when evaluating whether a controlling influence is being exerted as well as information about non-consolidated structured companies must be disclosed. The application of the new standard will affect the Notes to the consolidated financial statements. Application of IFRS 12 is mandatory for fiscal years from January 1, 2013 onwards.

In IFRS 13 "Fair Value Measurement", all fair value measurement regulations formerly contained in different standards are combined together and standardized. This standard regulates how the fair value measurement is to be performed if this measurement is prescribed or permitted in a different standard. The new standard is not currently expected to have a material impact on Rheinmetall Group's assets, financial situation and earnings. Application of this standard is mandatory for fiscal years from January 1, 2013 onwards.

IFRIC 20 governs accounting for stripping costs in the production phase of a surface mine and is not relevant to the Rheinmetall consolidated financial statements.

The consolidated financial statements are presented in euro (€). Unless otherwise stated, amounts are indicated throughout in € million (including prior-year comparatives). Non-rounded amounts may differ. The consolidated income statement has been presented in the total-cost format.

The fiscal year of Rheinmetall AG and its consolidated subsidiaries corresponds to the calendar year. Rheinmetall AG (Local Court of Registration: Düsseldorf, Commercial Register No. HRB 39401) has its registered office in Düsseldorf at Rheinmetall Platz 1.

Based on the provisions of Section 264 (3) HGB governing companies, the following German enterprises have elected not to disclose their 2011 financial statements:

Rheinmetall Berlin Verwaltungsgesellschaft mbH
Rheinmetall Verwaltungsgesellschaft mbH
Rheinmetall Industrietechnik GmbH
MEG Marine Electronics Holding GmbH
Rheinmetall Insurance Services GmbH
Rheinmetall Immobilien GmbH
Rheinmetall Maschinenbau GmbH
Rheinmetall Bürosysteme GmbH
EMG EuroMarine Electronics GmbH
SUPRENUM Gesellschaft für numerische Superrechner mbH
Rheinmetall Waffe Munition GmbH
Rheinmetall Defence Electronics GmbH
Rheinmetall Dienstleistungszentrum Altmark GmbH
Rheinmetall Technical Publications GmbH
Rheinmetall Landsysteme GmbH
Rheinmetall Verseidag Ballistic Protection GmbH
Rheinmetall Soldier Electronics GmbH

# Notes to the consolidated financial statements
# Accounting principles

### (2) »Scope of consolidation«

Besides Rheinmetall AG, the consolidated financial statements include all German and foreign subsidiaries in which Rheinmetall AG holds the majority of voting rights (whether directly or indirectly) or whose financial and business policies are otherwise controlled by the Group. Generally, companies are newly consolidated or derecognized when control is transferred. Companies over which Rheinmetall has a controlling influence, which is generally assumed if there is a stake of between 20% and 49% (associated companies) are carried at equity. Companies that are jointly managed (joint ventures) are also carried at equity.

Scope of consolidation – Companies included

| | **Dec. 31, 2010** | Additions | Disposals | **Dec. 31, 2011** |
|---|---|---|---|---|
| | | | | |
| Fully consolidated subsidiaries | | | | |
| Domestic | 48 | 4 | 5 | 47 |
| Foreign | 74 | 12 | 3 | 83 |
| | **122** | **16** | **8** | **130** |
| | | | | |
| Investments accounted for using the equity method | | | | |
| Domestic | 17 | 1 | 1 | 17 |
| Foreign | 10 | - | - | 10 |
| | **27** | **1** | **1** | **27** |

Changes to the scope of consolidation in terms of the fully consolidated companies of the Rheinmetall Group involved the formation of eleven companies, nine of which were abroad, and five acquisitions, three of which were abroad. The acquisitions also included an increase in the stake held in a previously associated company, leading to majority ownership and therefore full consolidation. The disposals of fully consolidated companies are mainly the result of internal Group restructuring in the form of mergers with other subsidiaries and the relinquishment of control over a company.

With effect from January 4, 2011, Rheinmetall has taken over the assets and liabilities of the Laingsdale Engineering division of the South African company Tellumat (Pty) Ltd., Cape Town, as part of an asset deal. The assets and liabilities have been acquired by Rheinmetall Laingsdale (Pty) Ltd. (Laingsdale), headquartered in Cape Town, South Africa (which is fully consolidated in the Rheinmetall Group), after Rheinmetall Waffe Munition GmbH, Unterlüß, previously acquired 51% of the company and Rheinmetall Denel Munition (Pty) Ltd., Somerset West, South Africa, 49% of the company at the beginning of fiscal 2011 and then carried out a capital increase. Since shareholders are also involved in Rheinmetall Denel Munition (Pty) Ltd. who do not exercise a controlling influence, Rheinmetall's share in the new South African company Rheinmetall Laingsdale (Pty) Ltd. totals 76%. The activities of Tellumat (Pty) Ltd. acquired encompass the development and production of precision components for fuses and will thus supplement Rheinmetall's technological portfolio in the field of ammunition. Moreover, the acquisition serves to further expand distribution activities in South Africa and other customer nations. The translated purchase price was €13 million and was paid entirely in cash.

As at February 1, 2011, Rheinmetall also increased its share of the capital and voting rights of ADS Gesellschaft für aktive Schutzsysteme mbH, Lohmar (ADS) by 49% to 74%. The purchase price for this increase in shares was €40 million and was settled in cash. ADS is involved in the development of standoff protection technologies for military vehicles. With the acquisition of the majority of voting rights in the company, Rheinmetall has further expanded its expertise and its position on the market for protection technologies. The current 25% stake in ADS was carried at equity.

The revaluation of this current investment, performed as part of the acquisition of additional shares on the basis of the purchase price for the acquisition, produced a value of €20 million for the stake held up to then. When the number of shares was increased, ADS was incorporated into the Rheinmetall Group as a fully consolidated subsidiary. The earnings of €11 million gained from the transition of the equity carrying amount for full consolidation were reported in other operating income. At the time of acquisition, the non-controlling interests in ADS (26%) were measured in terms of the prorated remeasured net assets of the company of €8 million, without taking into account the prorated goodwill. The valuation of the non-controlling interests is based on the assumption that the purchase price is proportional to the investment.

Two further acquisitions were made in the Defence sector of the Rheinmetall Group through the subsidiary Rheinmetall Defence Electronics GmbH as of October 1, 2011. Within Germany, there was the purchase of 49% of shares in MarineSoft Entwicklungs- und Logistikgesellschaft mbH in Rostock. The company's operations in the field of marine simulation supplement Rheinmetall's expertise in the area of simulation and training. In addition, there was the purchase of 100% of shares in the Switzerland-based Swiss SIMTEC AG, Thun, which is involved in the manufacture and development of components and concepts for simulation and training. The purchase prices for both of these acquisitions amounted to approximately €2 million in total and were paid almost entirely in cash.

KSPG Automotive India Private Ltd., Mumbai Maharashtra, India, which belongs to the Rheinmetall Group, acquired the plain bearing operations of Kirloskar Oil Engines Ltd. (KOEL), Pune, India, as part of an asset deal at a translated purchase price of approximately €13 million as of October 1, 2011. The purchase price was paid entirely in cash. As India's largest manufacturer of plain bearings, KOEL sells chiefly to the domestic market. With this acquisition, the Rheinmetall Group is further expanding its current operations in the Indian automotive industry.

The merging of the joint activities of Rheinmetall AG and MAN Truck & Bus AG (MAN) in the area of wheeled military vehicles from 2010 was implemented as of December 31, 2011. The starting point for this was the sale of 49% of shares held in Rheinmetall MAN Military Vehicles GmbH, Munich (RMMV) (which was newly formed by Rheinmetall), to MAN in 2010, meaning that Rheinmetall subsequently held a 51% stake and MAN a 49% stake in the company. The development and distribution activities of the two companies in the area of wheeled military vehicles were merged in RMMV by means of a spin-off in exchange for a capital increase and through a sale. In the year under review, the two shareholders in RMMV have now each merged their production activities and all other activities with regard to wheeled military vehicles in the company. In the wake of this, Rheinmetall merged Rheinmetall Radfahrzeuge GmbH, Munich, with RMMV as of December 31, 2011. In return, MAN split off and transferred the Vienna production site to Rheinmetall MAN Military Vehicles Österreich GesmbH. The shares held by MAN in the parent company of Rheinmetall MAN Military Vehicles Österreich GesmbH were then also integrated into RMMV as at December 31, 2011. The provisional purchase price for the acquisition of the wheeled military vehicles division of MAN is €103 million and is composed of the prorated fair value of Rheinmetall Radfahrzeuge GmbH which has been merged, in which MAN holds 49% of shares via the stake held in RMMV as the absorbing company, plus the €37 million paid in cash at the start of fiscal 2012. The valuation of the non-controlling interests is based on the assumption that the purchase price is proportional to the investment.

# Notes to the consolidated financial statements
## Accounting principles

The assets and liabilities taken over from the acquisitions in 2011 were entered into the consolidated financial statements at their fair value at the time of the acquisition. Based on the carrying amounts before the acquisition, which had to be adjusted for hidden reserves and charges taking into account deferred taxes, the following fair values were calculated, whereby measurements and investigations have only been completed as yet for the ADS and Laingsdale acquisitions. Provisional fair values are given for all other acquisitions described above, as not all accounting-related analyses, measurements and calculated have been conclusively carried out as yet.

*€ million*

| | Pre-acquisition book values | Adjustments | Fair values |
|---|---|---|---|
| Other intangible assets | - | 103 | 103 |
| Property, plant and equipment | 21 | - | 21 |
| Other noncurrent assets | 2 | 4 | 6 |
| Inventories | 39 | - | 39 |
| Receivables | 61 | - | 61 |
| Cash and cash equivalents/Other current assets | 16 | - | 16 |
| Current liabilities | 58 | - | 58 |
| Noncurrent liabilities | 27 | 28 | 55 |
| Net assets acquired | 54 | 79 | 133 |
| Goodwill | - | 105 | 105 |
| Total | 54 | 184 | 238 |

The allocation of the fair values of the assets and liabilities acquired from the acquisitions are shown in the list below.

*€ million*

| | ADS | RMMV | Others Defence | KOEL | Total |
|---|---|---|---|---|---|
| Other intangible assets | 43 | 56 | 2 | 2 | 103 |
| Property, plant and equipment | 1 | 8 | 6 | 6 | 21 |
| Other noncurrent assets | 2 | 4 | 0 | - | 6 |
| Inventories | 2 | 33 | 1 | 3 | 39 |
| Receivables | 0 | 57 | 1 | 3 | 61 |
| Cash and cash equivalents/ Other current assets | 0 | 12 | 3 | 1 | 16 |
| Current liabilities | 1 | 54 | 1 | 2 | 58 |
| Noncurrent liabilities | 14 | 38 | 1 | 2 | 55 |
| Net assets acquired | 33 | 78 | 11 | 11 | 133 |
| Goodwill | 35 | 63 | 5 | 2 | 105 |
| Total | 68 | 141 | 16 | 13 | 238 |
| Fair value of non-controlling interests | (8) | (38) | - | - | (46) |
| Fair value of controlling interests | 60 | 103 | 16 | 13 | 192 |
| Fair value of shares already held | (20) | - | 0 | - | (20) |
| Income from recognition of badwill | - | - | (1) | - | (1) |
| Purchase prices paid for acquisitions | 40 | 103 | 15 | 13 | 171 |
| of which paid in 2011 | 40 | - | 15 | 13 | 68 |

During the purchase price allocations, intangible assets were identified totaling €103 million, the majority of which were attributable to existing technologies and licenses (€85 million) and customer relations (€16 million). Total goodwill of €105 million resulted from the business combinations. This represents anticipated synergy effects, non-separable workforce expertise and access to future market developments. The fair values of the receivables mainly correspond to the contractually agreed gross amounts.

The companies included in the consolidated financial statements for the first time impacted the earnings of the relevant sectors and of the Rheinmetall Group in 2011 as shown in the following. This also includes the expense from the depreciation of intangible assets identified through the purchase price allocation of €3 million.

*€ million*

| | Sector Defence | Sector Automotive | Total |
|---|---|---|---|
| Sales | 9 | 4 | **13** |
| EBIT | (4) | (4) | **(8)** |

If the acquisitions had taken place on January 1, 2011, the Rheinmetall Group would have achieved additional sales of around €5 million, while the EBIT would have been €0 million higher. This observation does not take into account the acquisition of the plain bearing operations of Kirsloskar Oil Engines Ltd., as the necessary data for the operations acquired, which only constitute a sub-area of the business operations of the vendor, are not available. RMMV's acquisition was also not included, as the overall result of the wheeled military vehicles division of MAN for fiscal 2011 as a whole is still to be attributed to MAN.

The provisional purchase price allocation for the acquisition of the defence operations of SEI S.p.A., Italy through RWM Italia S.p.A. (formerly RWM Italia Munitions S.r.l.) as at December 1, 2010 was finalized in the third quarter of 2011. In comparison to the provisional figures processed in the 2010 annual financial statements and presented in the 2010 Annual Report there were the following changes:

*€ million*

| | RWM Italia provisional | RWM Italia change | RWM Italia final |
|---|---|---|---|
| Other intangible assets | 13 | 1 | 14 |
| Property, plant and equipment | 12 | 0 | 12 |
| Other noncurrent assets | - | 0 | 0 |
| Inventories | 11 | (1) | 10 |
| Receivables | 0 | 0 | 0 |
| Cash and cash equivalents/Other current assets | 1 | 0 | 1 |
| Current liabilities | 6 | 1 | 7 |
| Noncurrent liabilities | 6 | 0 | 6 |
| Net assets acquired | 25 | (1) | 24 |
| Income from recognition of badwill | (8) | - | (8) |
| Purchase price paid | 17 | (1) | 16 |

# Notes to the consolidated financial statements
# Accounting principles

### (3) »Assets and associated liabilities held for sale«

With the contract dated December 22, 2011, it was agreed between EADS Deutschland GmbH and Rheinmetall that the current activities of Rheinmetall in the area of unmanned aerial systems would in future be pursued at the Bremen site in collaboration with Cassidian, a division of the EADS Group. For this purpose, Rheinmetall's unmanned aerial systems activities, which are allocated to the Defence sector, are to be moved to Rheinmetall Airborne Systems GmbH, Bremen, which was newly formed in December 2011. A majority stake in Rheinmetall Airborne Systems is then to be sold, so that Cassidian will in future hold 51% of shares and Rheinmetall 49% of shares in the company. The planned transactions are set to take place once all the necessary authorizations and antitrust approvals have been granted and are to be completed by mid-2012.

The relevant assets are reported in the consolidated balance sheet as at December 31, 2011 as a disposal group held for sale totaling €29 million, while the associated liabilities are reported at €22 million. The composition of the items can be seen in the following overview:

*€ million*

| | |
|---|---|
| **Disposal group held for sale** | |
| Property, plant and equipment | 2 |
| Noncurrent financial assets | 2 |
| Inventories | 7 |
| Trade receivables | 16 |
| Current financial assets | 2 |
| **Total** | **29** |
| | |
| **Liabilities in connection with disposal groups** | |
| Pension provisions | 5 |
| Other noncurrent provisions | 2 |
| Other noncurrent liabilities | 1 |
| Current provisions | 2 |
| Trade liabilities | 11 |
| Other current liabilities | 1 |
| **Total** | **22** |

The carrying amount of property, plant and equipment of €2 million primarily includes developed land, factory and office equipment and production plants and machinery and is divided into €7 million in historical cost and €5 million in cumulative depreciation. The non-current financial assets primarily comprise receivables from currency hedges. Inventories relate in particular to raw materials and supplies of €2 million and work in progress of €4 million. Trade receivables are composed of €6 million in customer receivables and €10 million in receivables on construction contracts. Receivables on construction contracts arise from production costs incurred of €58 million plus a markup of €6 million and less progress billings of €54 million.

Pension provisions consist of defined benefit commitments. The measurement of the present value of the DBO of €5 million was based on a discount rate of 5.25% and the actuarial parameters given in Note (17). Other provisions provide mainly for staff costs, contract-related costs, sales fees and warranty obligations.

The first-time classification of assets and associated liabilities held for sale as a disposal group took place at the end of the year under review. Up to their classification as a disposal group, the accounting principles described in Note (4) were applied accordingly to the assets and liabilities in question. The classification itself did not result in impairment.

### (4) »Consolidation principles«

The financial statements of consolidated German and foreign companies are prepared in accordance with Group-wide uniform accounting and valuation methods.

Subsidiaries included for the first time are consolidated according to the acquisition method (involving full revaluation) by contrasting the cost of shares acquired against the subsidiaries' prorated equity revalued as of the date of change of control. Cost equals the fair values of the assets given, liabilities assumed, and equity instruments issued by the acquirer, in exchange for the acquisition. Any acquisition-related costs incurred are recognized in expenses.

Goodwill to be recognized at the time of acquisition is calculated from the cost of the subsidiary acquired, the fair value of the prorated net assets attributable to minority interests and the fair value of shares held in the subsidiary prior to the acquisition, minus the revalued net assets acquired.

Any resulting positive difference is capitalized as goodwill within intangible assets. Any residual badwill is reported in other operating income.

The hidden reserves and charges identified in the revaluation of the net assets acquired that relate to non-controlling interests are assigned to the adjustment item for minority interests in capital subject to consolidation. When additional shares in already fully consolidated subsidiaries are acquired, the difference between the cost and minority interests is reported as an equity measure.

Receivables and payables, expenses and income and intercompany profits/losses among fully consolidated companies are eliminated. Unless allocable to goodwill, taxes are deferred for all temporary differences from the consolidation of receivables/payables, income/expenses, and the elimination of intercompany profits/losses.

Shares in associated affiliates and joint ventures are stated at equity. Taking the historical cost of the shares as of the date of their acquisition, the investment book value is increased or decreased to reflect such changes in the equity of these associated affiliates/joint ventures as are allocable to the Rheinmetall Group. To determine the goodwill (if any) of investees, principles analogous to full consolidation are adopted, capitalized goodwill being mirrored in the investment book value. Consolidation transactions comply with the principles for fully consolidated subsidiaries.

# Notes to the consolidated financial statements
# Accounting principles

In the case of the gradual acquisition of a company, the difference between the carrying amount of the shares up to now and their fair value is recognized in income when the company is fully consolidated for the first time. In the case of the incomplete disposal of a subsidiary, the result arising from the sale price and the fair value of the remaining shares, less the Group carrying amounts for the subsidiary, is to be recognized in income.

### (5) »Currency translation«

In the separate financial statements of consolidated companies, each foreign currency transaction is recognized at the historical rate. Monetary assets and liabilities originally denominated in a foreign currency are translated at the rate on the reporting date. If carried at cost, other assets and liabilities are translated using the historical cost rate and, if carried at fair value, at the rate at the date of measuring the fair value. Any currency translation differences that arise are duly recognized in the net financial result.

The single-entity financial statements of foreign Group companies whose functional currency is not the euro are translated into euro as the Group currency in accordance with the functional currency concept. As a rule, their functional currency corresponds to the local currency as the currency of the primary business environment in which such companies operate. Translation is carried out using the rate on the reporting date, whereby assets and liabilities are translated at the average spot exchange rate as at the reporting date and the income statement at the average annual rate. The translation differences resulting from this are recognized in, and only in, equity as other comprehensive income (OCI).

### (6) »Accounting policies«

The key accounting and valuation methods applied on the basis of the Group-wide uniform accounting guideline to Rheinmetall AG's consolidated financial statements are described below.

### »Cost«

Purchase cost includes the purchase price and, with the exception of acquisitions, all incidental costs that can be directly attributed to the purchase. Where applicable, cost equals the fair value of the asset given in an exchange of assets transaction as at the date of the exchange. Any cash compensation is accounted for accordingly.

The production cost of internally generated assets from which future economic benefits are likely to flow to the Group and whose value can be reliably determined includes the costs directly allocable to the production or conversion process, as well as reasonable portions of production-related overheads, the latter also comprising indirect materials and indirect labor, as well as production-related depreciation and social security expenses, all based on normal workloads. Financing costs are capitalized as costs if they relate to assets which are produced or purchased over a period exceeding one year.

### »Subsidies and grants«

Public subsidies and customer grants or allowances which by their nature are considered investment grants are directly offset against the capital expenditures, whereas any grants or allowances for expenses for purposes other than investing activities are deferred as income and amortized to the income statement when the related expenses are incurred. Where the effect of interest from discounting is material, long-term deferred income is carried at the settlement amount discounted as of the balance sheet date.

### »Impairment«

If there is an indication that the value of an intangible or tangible asset may be impaired, and if the recoverable amount is below amortized or depreciated cost, a write-down is charged. When the reasons for write-down have ceased to exist, the asset is written up to an amount not exceeding its amortized or depreciated cost excluding write-down.

Within the Rheinmetall Group, goodwill is allocated to the relevant sectors according to its potential benefit. The value of goodwill is tested once annually for impairment, and during the year if impairment is indicated. There was no impairment during the year under review. In the impairment test, the carrying amount is compared with the recoverable amount. The value in use is generally used as a recoverable amount. If this value is below the carrying amount, a check is made as to whether the net fair value (NFV: fair value less costs to sell) is higher. If the carrying amount exceeds the recoverable amount, an impairment loss is then charged on the difference. A cash-generating unit's value in use is calculated according to the DCF method, discounting future cash flows over a three-year corporate planning period. For periods after the detailed planning period, cash flows are extrapolated from the last planning period, taking into account growth allowances.

In the Rheinmetall Group, the corporate plan is prepared on the basis of empirical and current forecast data. Within the Defence sector, planning is substantially predicated – besides on projects and inquiries already included in its order backlog – on national defence budgets of EU nations and NATO, duly allowing for new-market access and cost-paring programs.

# Notes to the consolidated financial statements
# Accounting principles

Key planning assumptions by Automotive are based on the sector forecasts underlying sales plans and covering the worldwide automotive market trend, the planned engine programs of carmakers, specific customer commitments to individual projects, as well as on Automotive-specific adjustments to allow for planned product innovations and cost savings.

Rheinmetall's WACC (before tax) was used as the discount rate:

| | | |
|---|---|---|
| Defence sector | 8.2% | (previous year: 8.9%) |
| Automotive sector | 10.9% | (previous year: 9.7%) |

For the period after the last planning year, the following growth allowance is deducted from the risk-specific pretax discount rate:

| | | |
|---|---|---|
| Defence sector | 1.0% | (previous year: 1.0%) |
| Automotive sector | 1.0% | (previous year: 1.0%) |

Neither the discount rate increase by 0.5 percentage points, nor the growth allowance decrease by 0.5 percentage points impair goodwill. Goodwill impairment losses are immediately recognized as write-downs in the corresponding income statement line. However, any subsequent reversal is prohibited.

### »Intangible assets«

Intangible assets are capitalized at cost. Research costs are always expensed. Development costs are not capitalized unless and until a newly developed product or process can be clearly defined and technologically realized and either it is to be used internally or marketing is planned, and if its costs can be reliably measured and there is reasonable assurance that its costs will be recovered by future cash inflows. Any other development costs are immediately expensed.

Finite-lived intangible assets are amortized by straight-line charges from the date of first use over the economic lives.

The measurement is subject to the following useful lives:

| | Years |
|---|---|
| Concessions and industrial property rights | 3-15 |
| Development costs | 5-7 |
| Customer relations | 5-15 |
| Technology | 5-15 |

Goodwill is not amortized, but its value is tested for impairment once a year, or whenever deemed appropriate.

### »Property, plant and equipment«

Property, plant and equipment is carried at depreciated cost less depreciation and impairment. Property, plant and equipment (if finite-lived) are depreciated on a straight-line basis over their estimated useful lives unless in exceptional cases another method better reflects the pattern of consumption.

Property, plant and equipment are depreciated over the following period of economic life:

| | Years |
|---|---|
| Buildings | 20-50 |
| Other structures | 8-30 |
| Equivalent titles | 5-15 |
| Production plant and machinery | 3-20 |
| Other plant, factory and office equipment | 3-15 |

Essential plots of land owned for business purposes are carried according to the revaluation method at fair value, which generally equals market value. Generally accepted valuation techniques are used to determine fair market values, which are in most cases based on the expert reports of an independent appraiser. External appraisal reports are obtained at regular intervals, the latest being the valuation as of December 31, 2008.

### »Leasing«

Agreements which transfer the right to use assets for a specified period of time in return for payment or a series of payments are qualified as leases.

If leasing transactions result in the transfer of virtually all opportunities and risks associated with ownership of an asset to the lessee, these are to be qualified as finance leases. All other leasing transactions are to be reported as operating leases.

Property, plant and equipment used under a finance lease are capitalized at the lower of their fair value or the present value of minimum lease payments and depreciated on a straight-line basis over the shorter of their estimated useful lives or underlying lease terms. At the same time, a financial liability is recognized in the corresponding amount and written down over the term of the lease using the effective interest method. For usage involving operating leases, rent and lease payments are recognized in expenses.

### »Investment property«

These are properties held for investment, i.e. to earn rental income or benefit from long-term capital appreciation, and not for use in production or administration.

Investment properties (unless land) are carried at depreciated cost less any impairment. Depreciation is recognized on a straight-line basis over useful lives of 20 to 50 years. The market value of investment property is stated under Note (9). Generally accepted valuation techniques are used to determine fair market values, in most cases based on regular expert reports by an independent appraiser (updated as of December 31, 2008).

# Notes to the consolidated financial statements
## Accounting principles

### »Financial instruments«

A financial instrument is based on a contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. Key financial assets in the Rheinmetall Group are cash and cash equivalents, trade receivables, loans, securities and derivatives with a positive fair value. Key financial liabilities relate to a bond, promissory note loans, liabilities to banks from leases, trade payables as well as derivatives with negative market values.

In the Rheinmetall Group, financial instruments are broken down into those measured at market value and those measured at amortized cost.

Financial instruments are generally recognized at the settlement date. The settlement date is the value date when the financial instrument is supplied or the payment is made. Notwithstanding this, derivatives are recognized as of the trading date, i.e. the date when the contract is concluded. The first-time measurement of financial instruments occurs at fair value. Acquisition-related costs are recognized in expenses for financial instruments measured at fair value in subsequent periods. For all other financial instruments, acquisition-related costs are to be included in the first-time measurement.

### »Cash and cash equivalents«

Cash equivalents comprise any liquid assets with a remaining term of less than three months at the date of their purchase or investment. Cash and cash equivalents are carried at amortized cost.

### »Available-for-sale financial assets«

Securities are assigned to the “available for sale” measurement category. Measurement is generally at market value. Where such fair market value is not reliably determinable, the assets are carried at amortized cost. Unrealized gains and losses are shown as other comprehensive income and recognized in the surplus from statement at fair value and other remeasurement. If there are substantial indications of impairment before or when selling securities, the cumulated amount recognized in equity is reclassified to the income statement at the level of impairment or the disposal value.

### »Trade receivables and other financial assets«

Receivables are measured at amortized cost. Account is taken of the default risk with appropriate valuation allowances. Receivables sold under an ABS program are offset against customer receivables received within trade receivables and, at the amount of the continuing involvement (i.e., the risk retained), shown as both other current receivables and other current liabilities.

Loans bearing normal market interest are recognized at amortized cost. Loans at nil or no interest rates are carried to the net present value.

**»Liabilities«**
Financial liabilities are measured at amortized cost as at the reporting date, using the effective interest method.

Liabilities resulting from finance leases are recognized at the present value of future minimum lease payments.

All other liabilities are measured at amortized cost, which as a rule equals the settlement or repayment amount.

**»Derivative financial instruments«**
In the Rheinmetall Group, derivatives are used exclusively to hedge against currency, interest rate, commodity price and electricity price risks. Future cash flows from current underlyings or planned transactions are hedged.

Derivatives are measured at fair value. The fair value is determined on the basis of input factors observed directly or indirectly on the market and thus corresponds to level 2 of the designations provided by IFRS 7. In the Rheinmetall Group, the foreign exchange rates applicable on the balance sheet date and yield curves are key input factors in calculating the fair value of derivatives for currency and interest rate hedges. In the case of interest caps, the market value is calculated on the basis of the Black/Scholes model, taking into consideration volatilities. The discounted cash flow method is used for interest rate swaps, currency swaps and currency forwards. The euro yield curve used to measure the interest rate derivatives takes into account basis spreads. The fair value of the commodity futures is derived from the value of all contracts at market as of the valuation date. The forward rates applicable on the balance sheet date (released by the EEX European Energy Exchange) are used to determine the market value of electricity derivatives.

Derivatives with a positive fair value are reported under other financial assets and derivatives with a negative fair value are recorded in other liabilities.

If the conditions for an effective hedge in line with IAS 39 are met (Cash Flow Hedge Accounting), the effective portion of the changes in the fair value of the designated derivative is recorded directly in equity in the surplus from statement at fair value and other remeasurement. If the hedged item is recognized in profit or loss, the cumulated gains or losses previously recognized in equity are recognized in the income statement. Any ineffective portion of changes in the fair value of the hedge is always immediately recognized in the income statement.

The changes in the fair value of derivatives used for hedging purposes, but which are not recorded in hedge accounting in line with IAS 39, are immediately recognized in the income statement. These derivatives are allocated to the held for trading measurement category.

# Notes to the consolidated financial statements
# Accounting principles

**»Inventories and prepayments received«**

Inventories are recognized at cost. As a rule, this equals average values. Risks inherent in inventories due to reduced utility or to obsolescence are adequately allowed for. If the net realizable value (NRV) of any inventories at the balance sheet date is below their carrying amount, such inventories are written down to net realizable value. The write-down either raises the cost of materials (raw materials and supplies) or reduces the net inventory level of finished products and work in progress. If the net realizable value of inventories previously written down increases, the ensuing reversal is routinely offset against cost of materials (raw materials and supplies) or shown as an increase in inventories of finished products and work in progress.

Prepayments received from customers for contracts which are not manufacturing or construction contracts under the terms of IAS 11 are, if production cost has already been incurred for the respective contract, openly deducted directly from inventories, any other prepayments being recognized as liabilities.

**»Construction contracts«**

Where the criteria and requirements of IAS 11 are met, manufacturing orders or construction contracts from customers are recognized in accordance with their percentage of completion. This method records the production cost incurred, plus a markup in line with the percentage of completion, as receivables from contract manufacturing and as revenue. As a rule, the percentage of completion is determined on a cost-to-cost basis, i.e., at the ratio the expenses incurred bear to anticipated total expenses. If the construction contracts require more than one year for settlement, contract costs also include allocable borrowing costs. If the net result from a percentage of completion contract cannot be reliably estimated, sales are recognized only at the level of costs actually incurred. Expected losses on manufacturing contracts (so-called onerous contracts) are either covered by an appropriate write-down or else covered by a provision, taking account of all foreseeable risks. Receivables on construction contracts are deducted directly from advance payments of payments resulting from part settlements up to a maximum of the performance already provided. Additional payments are reported under payments received.

**»Deferred taxes«**

Taxes are deferred for temporary differences between the values of assets and liabilities in the IFRS-based balance sheet and those in the individual companies' tax accounts. Deferred tax assets also include the tax assets receivable from the expected future utilization of tax loss carryovers (if their realization is reasonably certain). Deferred taxes are determined by applying the local tax rates current or announced in each country at the balance sheet date.

For domestic taxes, a tax rate of 30% is used, as was done in the previous year. This rate covers corporate income tax, the solidarity surtax thereon, and municipal trade tax. Taxation rates outside Germany range between 16% and 38% (previous year: 16% to 41%).

No deferred tax liabilities for temporary differences of shares in subsidiaries and associated affiliates were recognized, since Rheinmetall can control the reversal of such differences and the reversal is not probable in the foreseeable future.

### »Provisions«

Provisions for pensions and similar obligations are calculated using the projected unit credit method for defined benefit plans. The calculation of the extent of the obligations is predicated on assumptions such as mortality, expected future pay and pension increases, plan participant turnover rates, interest rate variations, as well as other actuarial parameters. The DBO volume of any existing pension plan assets is deducted from pension accruals. Any excess of plan assets over the DBO volume (a so-called defined benefit asset) is not recognized unless Rheinmetall can actually utilize or realize it. If there are deviations between the actuarial assumptions and the actual development of the underlying parameters to calculate the projected unit credits and the market value of the pension funds, actuarial losses or gains result. These actuarial gains and losses and the effects from the asset cap are recognized immediately in retained earnings in the year they occur.

Payments to defined contribution plans (DCP), under which the company incurs no obligations other than to pay the contributions to earmarked post-employment benefit plans, are recognized in net income in the year they are incurred. In addition, the Rheinmetall Group participates to a minor extent in some multi-employer plans which, although generally based on defined benefit obligations, are accounted for as defined contribution plans under the terms of IAS 19.30 if no information is available that would suffice for defined benefit plan accounting. With one Dutch subsidiary, the defined benefit pension plan is treated as a defined contribution plan as it is not possible to make an exact allocation of the assets of the post-employment benefit fund to the companies involved.

The remaining provisions take into account all identifiable commitments and obligations to third parties if based on past transactions or events and if it is probable that an outflow of resources (which can be reliably estimated) embodying economic benefits results. Non-current provisions are shown, if the effect of discounting is significant, at the settlement amount discounted as of the balance sheet date. The settlement amount also accounts for identifiable future cost increases.

### »Recognition of sales«

Sales result primarily from the sale of goods. In addition, sales are generated from services in the context of service and maintenance activities and contracted development work. Sales are measured at the fair value of the consideration received or to be received minus discounts, reductions or other deductions. Sales from supply agreements are realized with the passage of risk to the customer if the sales amount can be reliably estimated and a flow of benefits is probable. Under (longer-term) manufacturing contracts with customers, sales are prorated according to the percentage of completion. The stage of completion is measured in accordance with the ratio of contract costs incurred so far to the estimated total contract costs. Sales from service contracts and, as a rule, sales from contracted development work are recognized in accordance with the stage of completion, if the result can be reliably estimated.

# Notes to the consolidated financial statements
# Accounting principles

### »Other operating income«

Other operating income is recognized upon performance of the contract for goods/services or upon passage of risk to the customer.

### »Expenses«

Operating expenses are recognized when caused or when the underlying service, etc. is used.

### »Interest and dividends«

Interest income and expense are recognized on an accrual basis. Dividends are recognized in income when the legal claim to payment is established.

### »Estimates«

Preparing the consolidated financial statements requires certain assumptions and estimates which impact on the application of accounting principles within the Group and the disclosure of assets and liabilities, income and expenses.

When examining the recognition of goodwill, assumptions and estimates on forecasts and discounting future cash flows are made to determine the recoverable amount of the relevant cash-generating units. Details of the parameters used are described in the comments on impairment.

On an annual basis and on other occasions if appropriate, an assessment is made as to whether there are indications of a possible impairment and whether the fair value of intangible assets, property, plant and equipment or properties held for investment is lower than their carrying amount. When calculating the fair value, assumptions and estimates are made on the cash flows from realizable sales prices, costs and the discount rates. The yield curves used in the measurement of derivatives include assumptions about the expected future development of interest rates, taking into account estimated liquidity risks dependent on terms. Moreover, the measurement models used also incorporate parameters that are based on assumptions about volatilities and discount rates.

The measurement of pension provisions and other obligations is based on actuarial parameters such as the discount rate, salary increases, the expected income from fund assets, the mortality rate and the development of health care costs. A change in the discount rate of +/-0.25 percentage points compared to the 5.25% rate as of the balance sheet date for defined benefit pension plans in Germany would lead to a 3% reduction or increase in the present value of the DBO of €593 million. Defined benefit pension plans outside Germany relate primarily to subsidiaries based in Switzerland. In the event of a +/–0.25 percentage point variation in the discount rate for the main Swiss pension plans compared to the 2.25% rate as of the balance sheet date, the present value of the DBO with regard to these pension plans of €1,001 million would also decrease or increase by 3% and the associated fund assets of €920 million would decrease or increase by 0%. Any discrepancy between the parameters assumed and the actual conditions on the balance sheet date has no impact on net income, as actuarial gains and losses resulting from the discrepancy are recognized directly in equity.

Sales realization for construction orders is based on estimates for the level of completion which results from comparing the actual contract costs with the expected total costs calculated in the context of a project calculation. Pro rata sales for the period are worked out on the basis of the calculated level of completion and the estimated total revenue.

The determination of future tax advantages which reflect the recognition of deferred tax assets is based on assumptions and estimates on the development of tax income and the tax legislation in the countries of the Group companies working there.

In the context of business combinations, the fair values of the identifiable assets, liabilities and contingent liabilities may be based on estimates at the time of acquisition. To determine fair values, independent valuation appraisals or internal calculations are implemented on the basis of recognized measurement procedures, generally on the basis of forecast cash flows. In particular, when measuring intangible assets, assumptions and estimates on expected development, the expected economic lives and the discount rates are to be made.

When assessing and accounting for legal risks, estimates on the possible occurrence and the level of the expected obligations are made. In the process, the management deploys internal legal advice as well as that of external attorneys.

The respective assumptions and estimates are based on premises which represent the most recent knowledge. The estimates and the underlying assumptions are examined on an ongoing basis. Actual developments may result in amounts differing from these estimates. Such differences, if impacting on the accounting, are recognized in the period of change where the change affects this period only. If changes in estimates affect both the current period and future periods, these are recognized accordingly in the periods in question.

# Notes to the consolidated financial statements
# Notes on the balance sheet

### (7) »Intangible assets«

Research and development costs of €212 million were incurred in the fiscal year. The previous year's figure of €208 million was adjusted by €-6 million compared to the figure disclosed in the previous year. This adjustment relates to the Automotive sector. Of the total research and development costs incurred, development costs of €35 million (previous year: €38 million) met the capitalization criteria according to IFRS.

Breakdown of capitalized goodwill:

*€ million*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Defence sector | 279 | 382 |
| Automotive sector | 169 | 171 |
| | **448** | **553** |

Impairment of €4 million were carried out on intangible assets in the fiscal year (previous year: €0 million). €3 million of these impairment related to concessions, industrial property rights and licenses and €1 million to development costs.

### (8) »Property, plant and equipment«

Total impairment taken in 2011 was €4 million (previous year: €6 million), including €3 million charged to technical equipment and machinery (previous year: €1 million) and €1 million to other plant, factory and office equipment (previous year: €1 million). In the previous year, impairment was also carried out on land, land rights and buildings (€3 million) and construction in progress (€1 million).

In accordance with the revaluation method, essential plots of land are stated at fair value, which generally equals their market values. The fair value was €211 million (previous year: €210 million), which includes a step-up of €110 million (previous year: €111 million). Regarding the movement of the revaluation reserve, see the comments on total equity in Note (16).

€55 million of property, plant and equipment (previous year: €57 million) is subject to restrictions on disposal in the form of land charges.

On the basis of leases, €12 million in technical equipment and machinery are capitalized (previous year: €3 million). Here, normal restrictions on disposal apply. This increase is the result of a contract concluded in 2011 between a Group company and an external energy provider regarding the construction and operation of a heating system. The contract recognized as a capital lease has a remaining term up to 2026 and does not include a purchase option. An incremental borrowing rate of interest of 2.4% is used as the discount rate.

As a rule, other leases include a purchase option. These contracts have a remaining term of 1 year (previous year: between 1 and 3 years). The contractually agreed interest rate is 6.5% (previous year: between 4.7% and 6.5%).

The future lease payments under capital leases, the interest portions included therein, and the present values of future lease payments, which are recognized as financial debts, are shown in the table below:

Capital leases *€ million*

| | **2010** | | | | **2011** | | | |
|---|---|---|---|---|---|---|---|---|
| | 2011 | 2012-2015 | from 2016 | Total | 2012 | 2013-2016 | from 2017 | Total |
| Lease payments | 0 | 1 | - | 1 | 1 | 4 | 7 | 12 |
| Discounts | 0 | 0 | - | 0 | 0 | (1) | (1) | (2) |
| **Present values** | **0** | **1** | **-** | **1** | **1** | **3** | **6** | **10** |

The purchasing obligation from firm capital expenditure contracts totals €30 million (up from €27 million).

### (9) »Investment property«

The investment properties have a total fair value of €28 million (previous year: €33 million), largely determined on the basis of external appraisal reports as of December 31, 2008. In the year under review, rental income of €2 million (previous year: €1 million) was earned, contrasting with direct operating expenses of €2 million (previous year: €2 million). Impairment of €0 million was taken (previous year: €2 million).

# Notes to the consolidated financial statements
# Notes on the balance sheet

### (10) »Investments«

The pro-ratable assets, liabilities, income and expenses of joint ventures and associated affiliates break down as follows:

Joint ventures *€ million*

| | | 2010 | 2011 |
|---|---|---|---|
| Assets | (Dec. 31) | 324 | 348 |
| *Of which noncurrent* | | *115* | *126* |
| Equity | (Dec. 31) | 63 | 73 |
| Debt | (Dec. 31) | 261 | 275 |
| *Of which noncurrent* | | *16* | *13* |
| Income | | 364 | 469 |
| Expenses | | 348 | 456 |
| Annual income | | 16 | 13 |

Associated companies *€ million*

| | | 2010 | 2011 |
|---|---|---|---|
| Assets | (Dec. 31) | 85 | 85 |
| Equity | (Dec. 31) | 24 | 22 |
| Debt | (Dec. 31) | 61 | 63 |
| Sales | | 70 | 69 |
| Annual income | | 6 | 5 |

Development of investments *€ million*

| **2010** | **Book value Jan. 1, 2010** | Addition | Change not affecting Income Statement | Prorated net profit | Dividend payout | **Book value Dec. 31, 2010** |
|---|---|---|---|---|---|---|
| Joint ventures | 48 | 5 | (7) | 16 | (6) | **56** |
| Associated companies | 49 | - | - | 6 | (5) | **50** |
| | **97** | **5** | **(7)** | **22** | **(11)** | **106** |

| **2011** | **Book value Jan. 1, 2011** | Addition/ Disposal | Change not affecting Income Statement | Prorated net profit | Dividend payout | **Book value Dec. 31, 2011** |
|---|---|---|---|---|---|---|
| Joint ventures | 56 | 3 | (1) | 13 | (2) | **69** |
| Associated companies | 50 | (10) | 0 | 5 | (3) | **42** |
| | **106** | **(7)** | **(1)** | **18** | **(5)** | **111** |

Defence's key joint ventures include PSM Projekt System & Management GmbH and ARTEC GmbH (two project management companies for the PUMA and Boxer contracts), as well as HIL Industrie-Holding GmbH as a public-private partnership (PPP) model for repair logistics for the army. The joint venture HFTS Helicopter Flight Training Services GmbH for the provision and maintenance of flight simulators and an interest in the associated affiliate AIM Infrarot-Module GmbH, a specialist in the development and manufacture of electronic components equipped with infrared technology, also belong to the Defence sector. The joint venture Contraves Advanced Devices Sdn Bhd in Malaysia is opening up access to the markets for product technology for the land, naval and air forces of Malaysia and partner countries in the region.

The Automotive sector is stepping up its presence on the Asian market for pistons and other engine parts through the joint ventures Kolbenschmidt Shanghai Piston Co. Ltd. and Kolbenschmidt Pierburg Shanghai Nonferrous Components Co. Ltd. in China and the associated company Shriram Pistons & Rings Ltd. in India.

### (11) »Inventories«

*€ million*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Raw materials and supplies | 253 | 292 |
| Work in process | 293 | 294 |
| Finished products | 77 | 90 |
| Merchandise | 71 | 78 |
| Prepayments made | 45 | 59 |
| | **739** | **813** |
| ./. Prepayments received | (31) | (28) |
| | **708** | **785** |

Additions to write-downs totaled €20 million as in the previous year. In the year under review, inventories previously written down were written up by €13 million (previous year: €2 million). As in the previous year, inventories do not collateralize any liabilities.

### (12) »Trade receivables«

*€ million*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Customer receivables | 507 | 588 |
| *Of which with remaining term of more than 1 year* | *1* | *8* |
| *Of which from joint ventures and associated companies* | *41* | *56* |
| Receivables from construction contracts | 402 | 439 |
| | **909** | **1,027** |

# Notes to the consolidated financial statements
# Notes on the balance sheet

Breakdown of construction contract receivables

*€ million*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Production costs incurred | 2,565 | 2,861 |
| Plus margins (less losses) | 453 | 463 |
| | **3,018** | **3,324** |
| Progress billings | (2,616) | (2,885) |
| **Receivables from construction contracts** | **402** | **439** |

Obligations from construction contracts are included in the sundry other liabilities and break down as follows:

*€ million*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Production costs incurred | 10 | 13 |
| Losses incurred by stage of completion | 0 | 0 |
| Anticipated losses | 0 | 0 |
| | **10** | **13** |
| Progress billings | (10) | (13) |
| **Payables from construction contracts** | **0** | **0** |

Sales from construction contracts total €921 million in the fiscal year (previous year: €831 million).

### (13) »Other financial assets«

*€ million*

| | Dec. 31, 2010 | of which current | of which noncurrent | Dec. 31, 2011 | of which current | of which noncurrent |
|---|---|---|---|---|---|---|
| Derivatives in cash flow hedge | 56 | 34 | 22 | 21 | 18 | 3 |
| Loans | 8 | 1 | 7 | 10 | 4 | 6 |
| Derivatives without hedge accounting | 19 | 17 | 2 | 9 | 8 | 1 |
| Securities | 3 | 3 | - | 3 | 3 | 0 |
| Other | 5 | 3 | 2 | 6 | 5 | 1 |
| | **91** | **58** | **33** | **49** | **38** | **11** |

Loans of €10 million (previous year: €8 million) and securities of €3 million (previous year: €3 million) are recognized at amortized cost.

## (14) »Other receivables and assets«

Other receivables and assets are as follows:

*€ million*

| | Dec. 31, 2010 | Of which current | Of which noncurrent | Dec. 31, 2011 | Of which current | Of which noncurrent |
|---|---|---|---|---|---|---|
| Other taxes | 33 | 33 | 0 | 55 | 55 | 0 |
| Subsidies/grants receivable | 35 | 35 | - | 33 | 33 | - |
| Deferred income | 8 | 7 | 1 | 11 | 10 | 1 |
| Prepayments made | 3 | 3 | 0 | 7 | 7 | 0 |
| Compensation claims | 6 | - | 6 | 6 | 1 | 5 |
| Subsidies | 3 | 3 | - | 6 | 5 | 1 |
| Other | 14 | 13 | 1 | 20 | 20 | 0 |
| | **102** | **94** | **8** | **138** | **131** | **7** |

## (15) »Cash and cash equivalents«

*€ million*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Bank balances in credit institutions, checks, cash in hand | 629 | 535 |

Cash and cash equivalents for the year under review are not subject to any restrictions on disposal (previous year: disposal of €13K restricted). They correspond to the cash and cash equivalents in the cash flow statements for the respective balance sheet dates of the year under review and the previous year.

# Notes to the consolidated financial statements
# Notes on the balance sheet

**(16) »Equity«**

The subscribed capital of Rheinmetall AG amounts to €101,373,440.00 (unchanged) and is divided into 39,599,000 shares (with no nominal value).

The Annual General Meeting on May 11, 2010 authorized the Executive Board to acquire treasury shares equivalent to a maximum of 10% of the share capital of €101,373,000 up to May 10, 2015.

By resolution of the Annual General Meeting on May 11, 2010, the Executive Board of the Company was authorized, with the approval of the Supervisory Board, to increase the share capital of the Company up to May 10, 2015 by issuing once or several times new no-par shares in return for contributions in cash and/or in kind, up to a total of €50,000,000.00 (authorized capital). The new shares may also be issued to employees of Rheinmetall AG or any subsidiary it controls. By resolution of the Annual General Meeting on May 11, 2010, the Executive Board was authorized to decide on the further details of the issuing of shares as part of authorized capital, with the approval of the Supervisory Board. The Supervisory Board was authorized to amend the Company bylaws in accordance with the respective holdings and the respective utilization of the authorized capital.

Furthermore, the Executive Board of the Company was authorized by resolution of the Annual General Meeting of May 11, 2010 to issue interest-bearing bearer bonds with warrants and/or convertible bonds up to a total nominal value of €750,000,000.00 with a term of up to 20 years on one or several occasions, with the approval of the Supervisory Board, up to May 10, 2015, and to grant the holders of the respective bonds, which carry the same rights, options and conversion rights on new shares of the Company up to a total of 7,812,500 shares, in accordance with the more detailed provisions of the conditions for bonds with warrants and/or convertible bonds. The bonds with warrants and/or convertible bonds can also bear variable interest, whereby the interest rate can be wholly or partly dependent on the amount of the Company's dividend, as with an income bond.

In connection with the above bonds with warrants and/or convertible bonds, the Annual General Meeting resolved on May 11, 2010 to carry out a contingent increase of the Company's common stock by up to €20,000,000.00 through the issue of up to 7,812,500 bearer shares or – if the Company's bylaws at the time of issuing the bond also permit the issue of registered shares – new registered shares (contingent capital). The contingent capital increase is to serve shares granted when options and/or conversion rights are exercised and when option and/or conversion obligations are fulfilled for the holders of bonds with warrants and/or convertible bonds issued on the basis of the authorization granted by the Annual General Meeting on May 11, 2010. The Executive Board was authorized by resolution of the Annual General Meeting of May 11, 2010 to stipulate further details of the implementation of the contingent capital increase, with the approval of the Supervisory Board. The Supervisory Board was authorized to amend Section 4 of the Company bylaws in accordance with the respective utilization of the contingent capital and after the expiry of all option periods and/or conversion periods.

The increase in the additional paid-in capital is linked to the sale of treasury shares. The sales proceeds from the disposal of treasury shares were recognized in the retained earnings up to the amount of the respective costs on acquisition; the surplus amount (in 2011: €3 million; previous year: €1 million) was assigned to the additional paid-in capital.

A breakdown and analysis of OCI from the statement at fair value and other remeasurement are shown below:

*€ million*

| | Reserve for revaluation of properties | Reserve for hedging transaction | Reserve from fair value and other valuations |
|---|---|---|---|
| **January 1, 2010** | **78** | **12** | **90** |
| Change in fair value | - | 21 | 21 |
| Disposals / book transfers | 0 | (12) | (12) |
| **December 31, 2010/ January 1, 2011** | **78** | **21** | **99** |
| Change in fair value | - | (15) | (15) |
| Disposals / book transfers | (1) | (6) | (7) |
| **December 31, 2011** | **77** | **0** | **77** |

Breakdown of the land revaluation reserve (recognized for essential land capitalized within tangible assets):

*€ million*

| | **Dec. 31, 2010** | **Dec. 31, 2011** |
|---|---|---|
| Gains in property | 111 | 110 |
| Deferred taxes | (33) | (33) |
| | **78** | **77** |

In fiscal 2011, Rheinmetall AG paid a dividend of €58 million or €1.50 per share (previous year: €11 million or €0.30 per share) to its shareholders.

Minority interests refer to the Defence sector at €135 million (previous year: €89 million), and to Automotive at €2 million (previous year: €0 million).

**»Capital management«**

Rheinmetall's capital management aims at establishing the best possible equity-debt ratio.

In line with the IFRS definition, Rheinmetall's total equity includes minority interests, since these are at the Group's disposal.

For more details, see our statements on the financing strategy as well as on the asset and capital structure in our group management report.

# Notes to the consolidated financial statements
# Notes on the balance sheet

### (17) »Provisions for pensions and similar obligations«

The company pension systems consist of both defined contribution and defined benefit plans. Under the DCPs, Rheinmetall incurs no obligation other than the payment of contributions to earmarked pension funds. These pension expenses are shown within personnel expenses and need not be provisioned. In the year under review, a total of €70 million (previous year: €68 million) was paid to DCPs, specifically the Statutory Social Security Insurance in Germany.

Under its defined benefit plans, Rheinmetall is obligated to meet its confirmed benefit obligations to active and former employees. Pension accruals provide for obligations under vested rights and current pensions payable to eligible active and former employees, retirees and surviving dependents. Such obligations primarily encompass pensions, both basic and supplementary. The individual, confirmed, pension obligations entitle employees to benefits that vary according to country and company and, as a rule, are measured according to service years and pensionable pay. Moreover, at the German subsidiaries, a performance-related pension obligation has been incurred whose amount hinges on the achievement of certain benchmarks for the ROCE formula. Being a noncurrent provision for the accumulated postretirement benefit obligation, the accrued health care obligations to the retirees of some US subsidiaries are also included in the pension accruals recognized hereunder.

Movement analysis of the present value of the DBO and the plan assets (as time series):

*€ million*

| | Dec. 31, 2007 | Dec. 31, 2008 | Dec. 31, 2009 | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|---|---|---|
| Present value of DBO | 1,344 | 1,405 | 1,474 | 1,741 | 1,778 |
| Fund assets | 878 | 828 | 864 | 1,064 | 1,046 |
| **Pension obligations not covered by fund assets** | **466** | **577** | **610** | **677** | **732** |

The following actuarial parameters have been used:

Parameters *in %*

| | Dec. 31, 2010 | | | Dec. 31, 2011 | | |
|---|---|---|---|---|---|---|
| | Domestic | USA | Switzerland | Domestic | USA | Switzerland |
| Discount rate | 5.25 | 5.07 | 2.50 | 5.25 | 4.35 | 2,25-2,30 |
| Salary growth (general) | 2.75 | 0.00 | 1.50 | 2.75 | 0.00 | 1.50 |
| Salary growth (fixed sums) | 1.25 | - | - | 1.25 | - | - |
| Pension growth | 1.75 | - | - | 1.75 | - | - |
| Expected return on fund assets | - | 8.50 | 4.00 | - | 8.50 | 3.50-4.00 |
| Health care expense rise | - | 5.2-8.2 | - | - | 5.2-7.8 | - |

The non-German DBO primarily refer to benefit obligations incurred by Swiss and US subsidiaries, most of which are plan-funded. The plan assets of the Swiss subsidiaries have been transferred to independent pension funds and benefit exclusively the beneficiaries. Any return of income and assets to the contributing companies is excluded.

Pension provisions *€ million*

| | 2010 | | | 2011 | | |
|---|---|---|---|---|---|---|
| | Domestic | Foreign | Total | Domestic | Foreign | Total |
| **Development of present value of DBO** | | | | | | |
| Present value of DBO as at Jan. 1 | 544 | 930 | **1,474** | 587 | 1,154 | **1,741** |
| Currency differences | - | 168 | **168** | - | 33 | **33** |
| Current service cost | 12 | 9 | **21** | 12 | 12 | **24** |
| Past service cost | 1 | - | **1** | - | 3 | **3** |
| Interest cost | 29 | 33 | **62** | 30 | 29 | **59** |
| Employee contributions | - | 7 | **7** | 1 | 9 | **10** |
| Entry payments | - | 6 | **6** | - | 9 | **9** |
| Pension payments | (31) | (70) | **(101)** | (33) | (81) | **(114)** |
| Curtailments / settlements | - | (13) | **(13)** | - | (57) | **(57)** |
| Reclassification in accordance with IFRS 5 | - | - | **-** | (5) | - | **(5)** |
| Actuarial gains and losses | 15 | 81 | **96** | 1 | 58 | **59** |
| First-time inclusion of pension obligations | 17 | 3 | **20** | - | 16 | **16** |
| **Present value of DBO at Dec. 31** | **587** | **1,154** | **1,741** | **593** | **1,185** | **1,778** |
| | | | | | | |
| *Of which funds financed* | *8* | *1,129* | ***1,137*** | *10* | *1,144* | ***1,154*** |
| *Of which internally funded* | *579* | *25* | ***604*** | *583* | *41* | ***624*** |
| | | | | | | |
| **Development of fund assets** | | | | | | |
| Fair value of fund asset at Jan. 1 | - | 864 | **864** | 8 | 1,056 | **1,064** |
| Currency differences | - | 159 | **159** | - | 30 | **30** |
| Expected return on fund assets | - | 38 | **38** | 1 | 43 | **44** |
| Employer contributions | - | 17 | **17** | - | 15 | **15** |
| Employee contributions | - | 7 | **7** | 1 | 9 | **10** |
| Entry payments | - | 6 | **6** | - | 9 | **9** |
| Pensions paid by funds | - | (66) | **(66)** | - | (79) | **(79)** |
| Curtailments / settlements | - | (8) | **(8)** | - | (51) | **(51)** |
| Actuarial gains and losses | - | 27 | **27** | - | 4 | **4** |
| First-time inclusion of fund assets | 8 | 12 | **20** | - | - | **-** |
| **Fair value of fund assets at Dec. 31** | **8** | **1,056** | **1,064** | **10** | **1,036** | **1,046** |
| **Pension obligations not covered by fund assets as at Dec. 31** | **579** | **98** | **677** | **583** | **149** | **732** |
| Service costs and income not yet taken into account | 0 | 0 | 0 | 0 | (3) | **(3)** |
| **Pension provisions as at Dec. 31** | **579** | **98** | **677** | **583** | **146** | **729** |

# Notes to the consolidated financial statements
## Notes on the balance sheet

In the year under review, the plan assets returned a profit of €48 million (previous year: €65 million) before the net currency result recognized in equity. The contributions expected for the following fiscal year will be the same as in the reporting year.

Net cumulative actuarial gains and losses in equity (before taxes) totaled €229 million on December 31, 2011 (previous year: €174 million). Those of the current year total €55 million (previous year: €69 million).

Plan asset structure:

*in %*

| | 2010 | 2011 |
|---|---|---|
| Real estate and property investment funds | 43 | 42 |
| Equities | 27 | 23 |
| Treasuries and corporates/securities | 16 | 15 |
| Other | 14 | 20 |
| **Summe** | **100** | **100** |

Development of empirical adjustments *in %*

| | Dec. 31, 2007 | Dec. 31, 2008 | Dec. 31, 2009 | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|---|---|---|
| Present value of DBO | 0.4 | 1.2 | (1.1) | (0.8) | (0.5) |
| Fund assets | 0.6 | (16.3) | 1.2 | 2.8 | 0.0 |

The long-term return on fund assets is determined by the investment strategy defined for each asset class.

Breakdown of pension expense:

*€ million*

| | 2010 | | | 2011 | | |
|---|---|---|---|---|---|---|
| | Domestic | Foreign | Total | Domestic | Foreign | Total |
| Service cost | 12 | 9 | **21** | 12 | 12 | **24** |
| Past service cost | 1 | - | **1** | - | - | **-** |
| Accrual of expected pension obligations | 29 | 33 | **62** | 30 | 29 | **59** |
| Curtailments/settlements | - | (5) | **(5)** | - | (6) | **(6)** |
| Expected return on fund assets | - | (38) | **(38)** | (1) | (43) | **(44)** |
| **Total** | **42** | **(1)** | **41** | **41** | **(8)** | **33** |

The service cost and the result from curtailments/settlements are reported under personnel expenses. The accrual of expected pension obligations and the expected return on fund assets are contained in interest expenses on a netted basis.

## (18) »Other provisions«

Statement of changes in provisions *€ million*

| 2010 | Personnel | Structural measures | Guarantees | Noticeable losses | Contract-related costs | Other provisions | Total |
|---|---|---|---|---|---|---|---|
| **As at January 1, 2010** | **145** | **121** | **54** | **34** | **73** | **75** | **502** |
| Utilization | 112 | 48 | 14 | 11 | 21 | 25 | 231 |
| Reversal | 2 | 13 | 9 | 4 | 7 | 8 | 43 |
| Added / provided for | 124 | 16 | 26 | 9 | 39 | 41 | 255 |
| Accrual | 1 | 1 | 0 | 1 | 0 | 0 | 3 |
| Changes in scope of consolidation | 2 | 0 | 0 | - | 0 | 2 | 4 |
| Currency differences / Other | 6 | 1 | 2 | 1 | 5 | 2 | 17 |
| **As at December 31, 2010** | **164** | **78** | **59** | **30** | **89** | **87** | **507** |
| | | | | | | | |
| **Cash outflows** | | | | | | | |
| **Short term (‹ 1 year)** | **133** | **43** | **45** | **20** | **83** | **71** | **395** |
| | | | | | | | |
| **Long term** | **31** | **35** | **14** | **10** | **6** | **16** | **112** |
| *Of which 1 - 5 years* | *27* | *34* | *13* | *10* | *5* | *15* | *104* |
| *Of which › 5 years* | *4* | *1* | *1* | - | *1* | *1* | *8* |

| 2011 | Personnel | Structural measures | Guarantees | Noticeable losses | Contract-related costs | Other provisions | Total |
|---|---|---|---|---|---|---|---|
| **As at January 1, 2011** | **164** | **78** | **59** | **30** | **89** | **87** | **507** |
| Utilization | 130 | 17 | 17 | 11 | 50 | 35 | 260 |
| Reversal | 3 | 11 | 13 | 4 | 12 | 12 | 55 |
| Added / provided for | 140 | 8 | 22 | 7 | 41 | 44 | 262 |
| Accrual | 1 | 1 | 0 | 1 | 0 | 1 | 4 |
| Changes in scope of consolidation | 8 | 1 | 1 | 0 | 2 | 0 | 12 |
| Currency differences / Other | (8) | 4 | 1 | (1) | (1) | (1) | (6) |
| **As at December 31, 2011** | **172** | **64** | **53** | **22** | **69** | **84** | **464** |
| | | | | | | | |
| **Cash outflows** | | | | | | | |
| **Short term (‹ 1 year)** | **148** | **28** | **44** | **16** | **65** | **70** | **371** |
| | | | | | | | |
| **Long term** | **24** | **36** | **9** | **6** | **4** | **14** | **93** |
| *Of which 1 - 5 years* | *18* | *36* | *8* | *6* | *4* | *13* | *85* |
| *Of which › 5 years* | *6* | *0* | *1* | - | *0* | *1* | *8* |

Provisions for restructuring mainly cover the reduction in the workforce that is planned in order to adjust capacity (including termination settlements and pre-retirement part-time work). Other provisions relate primarily to €7 million of legal, consulting and audit fees (previous year: €7 million), €12 million of discounts and bonuses (previous year: €11 million), and €5 million for environmental risks (previous year: €5 million).

# Notes to the consolidated financial statements
# Notes on the balance sheet

### (19) »Financial debts«

*€ million*

| | **Dec. 31, 2010** | Of which current | Of which noncurrent | **Dec. 31, 2011** | Of which current | Of which noncurrent |
|---|---|---|---|---|---|---|
| Bond | 493 | - | 493 | 494 | - | 494 |
| Promissory notes | 149 | - | 149 | 85 | - | 85 |
| Bank liabilities | 49 | 23 | 26 | 54 | 26 | 28 |
| Leasing | 1 | 0 | 1 | 10 | 1 | 9 |
| Other | 13 | 11 | 2 | 22 | 18 | 4 |
| | **705** | **34** | **671** | **665** | **45** | **620** |

Amounts to banks of €21 million (previous year: €18 million) are secured by land charges and similar rights. In addition, €9 million of the financing for the property owned by the consolidated special purpose entity is secured by land charges as in the previous year.

The analyses below reflect the terms, and book and fair values, of financial debts, the fair values being determined on the basis of interest rates current at the balance sheet date for corresponding maturities/redemption patterns:

*€ million*

| | | | | Dec. 31, 2010 | | Dec. 31, 2011 | |
|---|---|---|---|---|---|---|---|
| Interest terms | Weighted interest rate (in %) | Currency (ISO code) | Maturing in | Book value | Fair value | Book value | Fair value |
| **Bond** | | | | | | | |
| Fixed | 4.0 | EUR | 2017 | 493 | 499 | 494 | 508 |
| | | | | **493** | **499** | **494** | **508** |
| **Promissory notes** | | | | | | | |
| Fixed | 6.8 | EUR | 2014 | 38 | 45 | 35 | 40 |
| Variable | | EUR | 2013 | 49 | 49 | 50 | 50 |
| Variable | | EUR | 2014 | 62 | 62 | - | - |
| | | | | **149** | **156** | **85** | **90** |
| **Bank liabilities** | | | | | | | |
| Fixed | 8.0 | ZAR | 2012 | - | - | 8 | 8 |
| Fixed | 4.9 | EUR | 2013 | 1 | 1 | 0 | 0 |
| Fixed | 3.7 | EUR | 2016 | 3 | 3 | 3 | 3 |
| Fixed | 4.4 | EUR | 2020 | 10 | 10 | 9 | 8 |
| Fixed | 3.8 | EUR | 2021 | - | - | 3 | 2 |
| Fixed | 3.7 | EUR | 2025 | 5 | 5 | 4 | 3 |
| Variable | | INR | 2011/2012 | 4 | 4 | 6 | 6 |
| Variable | | CNY | 2011/2012 | 1 | 1 | 2 | 2 |
| Variable | | EUR | 2011/2012 | 16 | 16 | 10 | 10 |
| Variable | | EUR | 2023 | 9 | 9 | 9 | 9 |
| | | | | **49** | **49** | **54** | **51** |
| **Leases** | | | | | | | |
| Fixed | 4.7 - 6.5 | EUR | 2012 | 1 | 1 | 0 | 0 |
| Fixed | 2.4 | EUR | 2026 | - | - | 10 | 7 |
| | | | | **1** | **1** | **10** | **7** |
| **Other financial debts** | | | | | | | |
| Fixed | 7.2 | ZAR | 2012 | - | - | 8 | 8 |
| Fixed | 1.1 | EUR | 2012 | - | - | 9 | 9 |
| Fixed | 7.0 | ZAR | 2013 | - | - | 2 | 2 |
| Variable | | ZAR | 2011 | 9 | 9 | - | - |
| Variable | | EUR | sundry until 2026 | 4 | 4 | 3 | 3 |
| | | | | **13** | **13** | **22** | **22** |
| | | | | | | | |
| **Total** | | | | **705** | **718** | **665** | **678** |

# Notes to the consolidated financial statements
# Notes on the balance sheet

## (20) »Trade payables«

*€ million*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Trade liabilities | 593 | 667 |
| *Of which from joint ventures and associated companies* | *14* | *10* |

€1 million of trade payables have a remaining term of more than one year (previous year: €5 million). The carrying amount of trade payables roughly equals their fair value.

## (21) »Other liabilities«

The other liabilities break down as follows:

*€ million*

| | Dec. 31, 2010 | Of which current | Of which noncurrent | Dec. 31, 2011 | Of which current | Of which noncurrent |
|---|---|---|---|---|---|---|
| Advance payments received | 256 | 256 | - | 325 | 325 | - |
| Monies in transit from debt collection | 87 | 87 | - | 82 | 82 | - |
| Liabilities from other taxes | 37 | 29 | 8 | 54 | 44 | 10 |
| Purchase price liability | - | - | - | 37 | 37 | - |
| Derivatives in cash flow hedge | 19 | 9 | 10 | 24 | 15 | 9 |
| Derivatives without hedge accounting | 19 | 11 | 8 | 22 | 12 | 10 |
| Liabilities from social security | 17 | 15 | 2 | 16 | 15 | 1 |
| Deferred income | 18 | 10 | 8 | 12 | 10 | 2 |
| Liabilities due to employees | 16 | 16 | - | 11 | 11 | - |
| Other | 40 | 39 | 1 | 29 | 27 | 2 |
| | **509** | **472** | **37** | **612** | **578** | **34** |
| *of which financial liabilities as defined by IFRS 7* | 204 | 176 | 28 | 183 | 164 | 19 |

As in the previous year, all of the advance payments received on orders have a remaining term of up to one year. The payables for derivatives have been marked to market, the carrying amount of the remaining liabilities approximating their fair value.

The purchase price liability of €37 million is the result of the acquisition of the wheeled military vehicles division.

Liabilities resulting from derivative financial instruments largely relate to market value of currency and interest rate hedging transactions as in the previous year. These fair values would only be realized if the derivatives were terminated early, which is unlikely at present. See Note “Additional information on financial instruments” for details of the Rheinmetall Group’s hedging strategies.

# Notes to the consolidated financial statements
# Notes on the income statement

## (22) »Total operating performance«

*€ million*

| | 2010 | 2011 |
|---|---|---|
| Sales | | |
| from sale of products | 3,523 | 4,005 |
| from services | 278 | 261 |
| from development contracts | 188 | 188 |
| **Total sales** | **3,989** | **4,454** |
| | | |
| Increase/decrease in inventory of finished products and services and WIP | 20 | 0 |
| Other work performed by the enterprise and capitalized | 49 | 51 |
| | **4,058** | **4,505** |

## (23) »Other operating income«

*€ million*

| | 2010 | 2011 |
|---|---|---|
| Reversal of provisions | 43 | 55 |
| Income from the transition from the equity approach to full consolidation | - | 11 |
| Credit notes for previous years | 15 | 9 |
| Disposal of assets/divestments | 4 | 8 |
| Refunds | 12 | 8 |
| Sundry rental agreements and leases | 7 | 7 |
| Grants and subsidies | 5 | 6 |
| Income from reversal of value adjustments | 1 | 5 |
| Income from canteens and ancillary operations | 4 | 4 |
| Income from residue utilization | 5 | 3 |
| Badwill | 8 | 1 |
| Other secondary income | 32 | 34 |
| | **136** | **151** |

## (24) »Cost of materials«

*€ million*

| | 2010 | 2011 |
|---|---|---|
| Cost of raw materials, supplies, and merchandise purchased | 1,731 | 2,012 |
| Cost of services purchased | 258 | 279 |
| | **1,989** | **2,291** |

# Notes to the consolidated financial statements
# Notes on the income statement

### (25) »Personnel expenses«

*€ million*

| | 2010 | 2011 |
|---|---|---|
| Wages and salaries | 975 | 1,037 |
| Social security and related employee benefits | 121 | 135 |
| Pension expenses | 85 | 88 |
| | **1,181** | **1,260** |

Annual average head count (FTE)

| | 2010 | 2011 |
|---|---|---|
| Automotive sector | 10,600 | 11,079 |
| Defence sector | 9,354 | 9,204 |
| Rheinmetall AG / Other | 125 | 130 |
| | **20,079** | **20,413** |

### (26) »Amortization/depreciation«

For the allocation of these charges to intangible assets, property, plant and equipment and investment property, see the statement of changes in assets.

Impairments break down as follows:

*€ million*

| | 2010 | 2011 |
|---|---|---|
| Intangible assets | 0 | 4 |
| Property, plant and equipment | 6 | 4 |
| Investment property | 2 | 0 |
| | **8** | **8** |

Of impairments, €5 million (previous year: €6 million) relate to the Automotive sector and €3 million to the Defence sector. In the previous year, impairment of €2 million was carried out for a service company.

## (27) »Other operating income«

*€ million*

| | 2010 | 2011 |
|---|---|---|
| Administrative costs | 152 | 165 |
| Repairs and maintenance | 75 | 81 |
| Distribution costs | 62 | 69 |
| Rents, leases | 44 | 47 |
| Audit, legal and consultancy fees | 40 | 47 |
| Additions to provisions | 59 | 37 |
| Incidental staff costs | 39 | 33 |
| Promotion and advertising expenses | 17 | 22 |
| Services purchased | 12 | 14 |
| Facility cleaning and security/surveillance | 12 | 12 |
| Expenses for redundancy plans, termination indemnities, partial retirement | 17 | 8 |
| Other taxes | 7 | 7 |
| Write-down of receivables | 3 | 3 |
| Losses on disposal of fixed assets/divestments | 4 | 1 |
| Other | 36 | 39 |
| | **579** | **585** |

General administrative costs primarily comprise IT costs, travel costs and insurance fees.

## (28) »Net interest«

*€ million*

| | 2010 | 2011 |
|---|---|---|
| | | |
| Other interest and similar income | 4 | 6 |
| **Interest income** | **4** | **6** |
| | | |
| Interest expense for pension obligations | 24 | 15 |
| Accrual of other non-current provisions | 3 | 4 |
| Other interest and similar expenses | 45 | 46 |
| **Interest expenses** | **72** | **65** |
| **Net interest** | **(68)** | **(59)** |

# Notes to the consolidated financial statements
# Notes on the income statement

## (29) »Net investment income and other net financial income«

*€ million*

| | 2010 | 2011 |
|---|---|---|
| **Investment income** | | |
| Defence Sector | 12 | 7 |
| Automotive Sector | 9 | 11 |
| Other | 1 | 0 |
| | **22** | **18** |
| **Other financial results** | | |
| Currency result | (4) | 11 |
| Profit from derivative financial instruments | 4 | (9) |
| Guarantee commissions | (2) | (1) |
| Other | (1) | (1) |
| | **(3)** | **0** |
| **Investment profit and other financial results** | **19** | **18** |

The result from derivatives of €-9 million (previous year: €4 million) primarily includes the net hedging result, against which the provisions on hedge accounting in accordance with IAS 39 are not applied, and mainly relates to currency and interest rate hedges.

## (30) »Income taxes«

*€ million*

| | 2010 | 2011 |
|---|---|---|
| Current income tax expense | 34 | 59 |
| Earlier-period income taxes | 12 | (3) |
| Deferred taxes | 9 | 14 |
| | **55** | **70** |

The tax effect on income and expenses recognized directly in equity is presented in the following overview:

*€ million*

| | 2010 | | | 2011 | | |
|---|---|---|---|---|---|---|
| | Gross amount | Tax effect | Net amount | Gross amount | Tax effect | Net amount |
| Actuarial gains and losses from pensions | (69) | (15) | (54) | (55) | (10) | (45) |
| Currency conversion | 89 | - | 89 | (10) | - | (10) |
| Cash flow hedges | 18 | 5 | 13 | (39) | (11) | (28) |
| Revaluation of properties required for business purposes | 0 | 0 | 0 | 0 | 0 | 0 |
| Income/expenses from investments accounted for using the equity method | (7) | - | (7) | (1) | - | (1) |
| | **31** | **(10)** | **41** | **(105)** | **(21)** | **(84)** |

The table below presents a reconciliation of expected tax expense to recognized actual tax expense. A tax rate of 30% is applied to earnings before taxes in order to calculate the expected tax expense. This rate covers German corporate income tax, the solidarity surtax thereon and municipal trade tax.

*€ million*

| | 2010 | 2011 |
|---|---|---|
| EBT | 229 | 295 |
| **Expected income tax expense (tax rate of 30%; previous year: 30%)** | **69** | **89** |
| Foreign tax rate differentials | (4) | (6) |
| Effects of loss carryforwards and change in value adjustment | (9) | 6 |
| Reduction of tax expense due to previously unrecognized loss carryovers and temporary differences | (10) | (11) |
| Tax-exempt income | (7) | (6) |
| Non-deductible expenses | 7 | 7 |
| Earlier-period income taxes | 12 | (3) |
| Other | (3) | (6) |
| **Actual income tax expense** | **55** | **70** |

Of other effects, €1 million (previous year: €1 million) relates to changes in tax rates for foreign companies.

Deferred taxes can be allocated to the following balance sheet items:

*€ million*

| | Dec. 31, 2010 | | Dec. 31, 2011 | |
|---|---|---|---|---|
| | Deferred tax assets | Deferred tax liabilities | Deferred tax assets | Deferred tax liabilities |
| Loss carryforwards and tax credits | 65 | 0 | 63 | 0 |
| Fixed assets | 19 | 140 | 21 | 173 |
| Inventories and receivables | 37 | 59 | 48 | 63 |
| Pension provisions | 65 | 4 | 72 | 1 |
| Other provisions | 35 | 1 | 33 | 3 |
| Liabilities | 23 | 16 | 29 | 23 |
| Other | 3 | 6 | 8 | 7 |
| | **247** | **226** | **274** | **270** |
| Set off | (176) | (176) | (189) | (189) |
| | **71** | **50** | **85** | **81** |
| *Of which noncurrent* | *55* | *14* | *68* | *49* |
| *Of which not affecting income* | *47* | *50* | *60* | *39* |

# Notes to the consolidated financial statements
# Notes on the income statement

In addition to capitalized deferred tax assets from loss carryovers and tax credits, further tax loss carryovers and tax credits exist in Germany and abroad totaling €453 million (previous year: €468 million) which cannot be utilized or whose deferred tax assets were adjusted by value adjustments. Of this, €280 million (previous year: €286 million) is allocable to German loss carryovers, €170 million (previous year: €172 million) to foreign loss carryovers and another €3 million to tax credits (previous year: €10 million). The German loss carryovers, and €0 million of the foreign loss carryforwards (previous year: €10 million), are not subject to expiration. Most of the foreign loss carryovers subject to expiration can still be utilized for more than 9 years as in the previous year. Write-downs of deferred tax assets changed by €1 million in 2011 (previous year: €3 million). Outside Germany, companies have capitalized deferred tax assets of €2 million (previous year: €3 million) which have posted ongoing losses due to realigned business operations.

€-33 million of deferred taxes recognized directly in equity (previous year: €–33 million) relate to land revaluation, €55 million to pensions (previous year: €41 million) and €0 million to hedges (previous year: €-10 million).

€1 million in non-current taxes (previous year: €1 million) in line with Section 37 (4) of the German Corporation Income Tax Act (KStG) are reported under income tax receivables.

### (31) »Minority interests«
Minority interests in profit came to €13 million (previous year: €12 million) and minority interests reporting a loss to €1 million (previous year: €0 million).

### (32) »Earnings per share«
Earnings per share are calculated as a ratio of the consolidated result of the shareholders of Rheinmetall AG and the weighted average number of shares in circulation during the fiscal year. Since there were no shares, options or similar instruments outstanding as of December 31, 2011 or December 31, 2010 that could dilute earnings per share, basic and diluted earnings per share are identical. The repurchase of treasury shares is included in the weighted number of shares.

*€ million*

| | 2010 | 2011 |
|---|---|---|
| Consolidated net profit/loss for the year for shareholders of Rheinmetall AG | 162 | 213 |
| Weighted number of shares *million* | 38.23 | 38.33 |
| **Earnings per share** | **€4.23** | **€5.55** |

### (33) »Adjusted EBIT«

| | 2010 | 2011 |
|---|---|---|
| **EBIT** | **297** | **354** |
| One-off expenses and income in connection with: | | |
| Investments | 2 | 1 |
| Properties | 2 | (6) |
| Restructuring | 19 | (3) |
| **EBIT (adjusted)** | **320** | **346** |

# Notes to the consolidated financial statements
# Notes on the cash flow statement

**(34) »Cash flow statement«**
Of the net interest included in the cash flow from operating activities, €8 million (previous year: €4 million) related to interest payments received and €23 million (previous year: €46 million) to interest payments made.

The cash outflow of €74 million (previous year: €109 million) for the acquisition of consolidated companies related to the acquisitions described under Note (2) and includes the purchase price paid less the addition of cash and cash equivalents. Of the purchase prices agreed, an amount of €37 million (previous year: €6 million) had not yet been paid by the end of the fiscal year in question.

Cash and cash equivalents of €5 million (previous year: €4 million) were assumed as part of company acquisitions.

The dividends received from joint ventures and associated companies are included in cash receipts from financial assets and are listed under Note (10).

# Notes on segment reporting

**(35) »Segment reporting«**
The Group bundles its activities in two sectors, Defence and Automotive, which are organized and run as independent segments where the respective products, services and customer profiles are grouped accordingly. Reporting on these reportable segments is in accordance with the Rheinmetall Group's internal organizational and reporting structures.

The Defence segment brings together all activities in the area of armed forces technology. Rheinmetall Defence supplies a broad portfolio of platforms and components available to the armed forces as individual solutions or as networked systems. The core capabilities cover the Weapon and Munitions, Propellants, Tracked Vehicles, Wheeled Vehicles, Air Defence, C4ISTAR and Simulation & Training divisions.

The activities of the Rheinmetall Group within the context of automotive supplies are pooled in the Automotive sector. The automotive industry is supplied with engine modules and components, such as pistons, pumps, plain bearings, engine blocks and emissions reduction and air management systems. As well as supplying automotive manufacturers, the Automotive sector also operates in the aftermarket business, supplying wholesalers, engine repair shops and independent garages with replacement parts through a global distribution network.

As well as the Group holding company (Rheinmetall AG), "Other/Consolidation" includes Group service companies and other non-operating companies, plus consolidation transactions.

# Notes to the consolidated financial statements
# Notes on segment reporting

The sectors of the Rheinmetall Group are controlled by means of EBIT and EBT performance indicators and sales. Furthermore, the management also uses key figures for order intake, order backlog and net financial liabilities to monitor and control the sectors. Profitability is assessed by the management on the basis of ROCE calculated on an annual basis, which represents the ratio of EBIT to average capital employed (average of values as at the December 31 balance sheet date of the previous year and the year under review).

Net financial debts reflect financial debts less cash and cash equivalents. Inter-segment loans within the Group are assigned to cash and cash equivalents. Capital employed is calculated as the sum of equity, pension provisions and net financial debts. Additions to capital employed include amortization of goodwill accumulated in the past.

Capital expenditure relates to the intangible assets, property, plant and equipment and investment properties. Goodwill or assets resulting from acquisition price allocation are not counted towards capex.

The indicators for internal controlling and reporting purposes are based on the accounting principles described in Note (6) to the IFRS consolidated financial statements.

The following reconciles the net financial debts of the sectors to those of the Group and the operating result of the sectors to consolidated EBT:

*€ million*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| **Net financial debts** | | |
| Net financial debts of sectors | (387) | (281) |
| Others | 543 | 453 |
| Consolidation | (80) | (42) |
| **Net financial debts of Group** | **76** | **130** |
| | | |
| **EBIT** | | |
| EBIT of sectors | 315 | 374 |
| Others | 64 | 209 |
| Consolidation | (82) | (229) |
| **Group EBIT** | **297** | **354** |
| Group net interest | (68) | (59) |
| **Group EBT** | **229** | **295** |

When presenting segment information by geographical region, foreign sales in the Defence sector are reported based on the country of destination, while those of the Automotive sector are reported according to where the customer is based. Segment assets include intangible assets, property, plant and equipment and investment properties according to the respective location of the company.

# Notes to the consolidated financial statements
# Other notes

### (36) »Contingent liabilities«

Surety bonds and guarantees exist in connection with the divestment of former business activities. This primarily relates to rental loss sureties and performance bonds for sold companies. These companies regularly and duly perform their obligations and there are no signs of any future enforcement of such guarantees or bonds.

Furthermore, several guarantees have been issued in favor of non-consolidated interests as part of joint projects, which are primarily carried out in the form of joint ventures. Performance bonds exist whereby Rheinmetall may also be held liable for the performance of the other joint venture partners in its relations with third parties. However, in internal relations, it is only liable for its own share of products and services by virtue of corresponding rights of recourse. Moreover, a letter of comfort involving a joint and several liability has been issued to secure the financing of the capex costs for a joint venture. No cash outflows are expected.

In addition, guarantees exist in favor of joint ventures and associated affiliates for credit facilities granted to the affiliated companies. Rheinmetall's liability is equal to the equity interest held. No cash outflows are expected here.

As part of restructuring measures under company law, three legal proceedings have been initiated by external shareholders with a view to reviewing the suitability of the share exchange ratio and the amount of cash compensation offered.

In the wake of the merger of Kolbenschmidt AG with Rheinmetall Beteiligungen AG (now KSPG AG) in 1998, judicial review proceedings were initiated in order to examine the suitability of the share exchange ratio. Appeals were lodged with the Stuttgart Higher Regional Court against the decision of the Heilbronn Regional Court to dismiss the applications in 2007. At the hearing before the senate of the Stuttgart Higher Regional Court on January 19, 2011, the proposal for the amicable termination of proceedings was accepted by the parties and the appeals lodged by the applicants were then withdrawn. With the resolution of February 1, 2011 of the 20th civil senate of Stuttgart Higher Regional Court, the proceedings were thus terminated and the verdict issued by Heilbronn Regional Court became legally binding.

In the proceedings instituted regarding the squeeze-out of KSPG AG in 2007, the applications of 108 persons involved in the proceedings were dismissed by the Stuttgart District Court on September 1, 2008. 55 applicants immediately lodged appeals with the Stuttgart Higher Regional Court. The appeal was dismissed by the Stuttgart Higher Regional Court on July 5, 2011, meaning that the legal proceedings have thus come to an end.

With regard to the squeeze-out initiated in 2003 of Aditron AG, which was merged with Rheinmetall AG in the same reporting year, the legal proceedings initiated are still pending.

# Notes to the consolidated financial statements
# Other notes

### (37) »Other financial obligations«

Various financial commitments in line with customary business standards exist under master agreements with suppliers, as well as under contracts for services. For the purchasing obligations for capital expenditure projects, refer to the comments in the Note "Property, plant and equipment".

In the reporting year, €47 million was posted as expenses for operating leasing (up from €44 million). Apart from business property leases, the other standard contracts cover the rental of vehicles and business, factory and office equipment, which includes hardware and software.

The following discounted cash outflows under leases are expected in future periods:

*€ million*

| | 2010 | | | | 2011 | | | |
|---|---|---|---|---|---|---|---|---|
| | 2011 | 2012-2015 | from 2016 | **Total** | 2012 | 2013-2016 | from 2017 | **Total** |
| Buildings | 24 | 64 | 41 | **129** | 23 | 66 | 45 | **134** |
| Other leases | 13 | 20 | 0 | **33** | 13 | 23 | 1 | **37** |
| | **37** | **84** | **41** | **162** | **36** | **89** | **46** | **171** |

In addition, under an agreement on the divestment of a business segment in earlier years, Rheinmetall committed itself to assume the lease for a partially let property with a term to the end of 2014. The future (unrecognized) accumulated obligations under this assumed lease totaled €0 million (previous year: €2 million). Provisions of €8 million were established for subleasing risks (previous year: €11 million).

€0 million was generated in the period from subleasing further properties leased by Rheinmetall (down from €2 million). The future income expected during the non-cancelable lease term totals €1 million (down from €4 million).

(38) »Additional information on financial instruments«

This note provides a comprehensive summary of the significance of financial instruments to the Rheinmetall Group. Additional disclosures relevant to financial instruments are also made.

The table below breaks down recognized financial assets and liabilities by valuation category and class, additionally stating their current fair values.

Financial instruments *€ million*

| 2010 | Note | Balance sheet value | Loans and receivables/ liabilities | Available for sale | Held for trading purposes | Outside valuation categories of IAS 39 | Fair value |
|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | |
| Trade receivables | (12) | 909 | 909 | - | - | - | 909 |
| Other financial assets | (13) | 91 | | | | | |
| Securities | | | - | 3 | - | - | 3 |
| Derivatives without hedge accounting | | | - | - | 19 | - | 19 |
| Derivatives with cash flow hedge | | | - | - | - | 56 | 56 |
| Other financial assets | | | 13 | - | - | - | 13 |
| Cash and cash equivalents | (15) | 629 | 629 | - | - | - | 629 |
| | | **1,629** | **1,551** | **3** | **19** | **56** | **1,629** |
| *Of which valuation* | | | | | | | |
| *at amortized cost* | | | *1,551* | *3* | - | - | |
| *at fair value* | | | - | - | *19* | *56* | |
| | | | | | | | |
| **Financial liabilities** | | | | | | | |
| Financial debts | (19) | 705 | | | | | |
| Financial debts excl. leases | | | 704 | - | - | - | 717 |
| Lease liabilities | | | - | - | - | 1 | 1 |
| Trade liabilities | (20) | 593 | 593 | - | - | - | 593 |
| Other liabilities | (21) | 509 | | | | | |
| Non-financial liabilities | | (305) | | | | | |
| Financial liabilities | | 204 | | | | | |
| Derivatives without hedge accounting | | | - | - | 19 | - | 19 |
| Derivatives with cash flow hedge | | | - | - | - | 19 | 19 |
| Other financial liabilities | | | 166 | - | - | - | 166 |
| | | **1,502** | **1,463** | **-** | **19** | **20** | **1,515** |
| *Of which valuation* | | | | | | | |
| *at amortized cost* | | | *1,463* | - | - | *1* | |
| *at fair value* | | | - | - | *19* | *19* | |

# Notes to the consolidated financial statements
# Other notes

Financial instruments *€ million*

| 2011 | Note | Balance sheet value | Loans and receivables/ liabilities | Available for sale | Held for trading purposes | Outside valuation categories of IAS 39 | Fair value |
|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | |
| Trade receivables | (12) | 1,027 | 1,027 | - | - | - | 1,027 |
| Other financial assets | (13) | 49 | | | | | |
| Securities | | | - | 3 | - | - | 3 |
| Derivatives without hedge accounting | | | - | - | 9 | - | 9 |
| Derivatives with cash flow hedge | | | - | - | - | 21 | 21 |
| Other financial assets | | | 16 | - | - | - | 16 |
| Cash and cash equivalents | (15) | 535 | 535 | - | - | - | 535 |
| | | **1,611** | **1,578** | **3** | **9** | **21** | **1,611** |
| *Of which valuation* | | | | | | | |
| *at amortized cost* | | | *1,578* | *3* | - | - | |
| *at fair value* | | | - | - | *9* | *21* | |
| | | | | | | | |
| **Financial liabilities** | | | | | | | |
| Financial debts | (19) | 665 | | | | | |
| Financial debts excl. leases | | | 655 | - | - | - | 671 |
| Lease liabilities | | | - | - | - | 10 | 7 |
| Trade liabilities | (20) | 667 | 667 | - | - | - | 667 |
| Other liabilities | (21) | 612 | | | | | |
| Non-financial liabilities | | (429) | | | | | |
| Financial liabilities | | 183 | | | | | |
| Derivatives without hedge accounting | | | - | - | 22 | - | 22 |
| Derivatives with cash flow hedge | | | - | - | - | 24 | 24 |
| Other financial liabilities | | | 137 | - | - | - | 137 |
| | | **1,515** | **1,459** | **-** | **22** | **34** | **1,528** |
| *Of which valuation* | | | | | | | |
| *at amortized cost* | | | *1,459* | - | - | *10* | |
| *at fair value* | | | - | - | *22* | *24* | |

Given mainly the short-term to maturity of such instruments, the fair value of cash, cash equivalents, current receivables, trade payables and other financial liabilities substantially equals book value.

Rheinmetall measures noncurrent fixed and floating-rate receivables taking into account customer credit standing, specific country risks, and the structure of the financing transaction. Taking this approach, expected collection or default risks are duly allowed for. Non-interest receivables are discounted by applying rates that match their maturity. The current book values of such receivables (less any allowances) will then substantially correspond to their fair values.

The exchange-listed bond issue is marked to market as of the balance sheet date. The fair value of liabilities to banks and other financial debts, payables under capital leases, as well as of other noncurrent financial payables was determined by discounting the associated future cash flows at rates that match the time to maturity of similar debts.

### Further balance sheet disclosures

#### »Derecognition«

Under an asset backed securities program, the Rheinmetall Group sells customer receivables each month on a revolving basis. The maximum volume in 2011 was €170 million (previous year: €170 million). As of December 31, 2011, the nominal value of receivables sold came to €170 million (previous year: €158 million).

In line with IAS 39, sales of receivables apply as disposal. The remaining risks are insignificant for the Group. An asset item of €3 million is established for the maximum continuing involvement (previous year: €3 million), along with a corresponding liability item for the associated liabilities.

#### »Collateral provided«

Liens of €2 million (previous year: €3 million) rest on financial assets to protect employees from insolvency risks in connection with pension systems.

#### »Other disclosures on the income statement«

The other interest income of €6 million (previous year: €5 million) and other interest expense of €45 million (previous year: €32 million) result primarily from loans and receivables as well as financial liabilities carried at amortized cost.

The net currency/foreign exchange result (which is included in the other financial result) which constitutes a net profit of €11 million (previous year: net expense of €4 million) relates to loans and receivables as well as liabilities carried at amortized cost.

The remaining other financial result is broken down into the valuation categories of IFRS 7 as follows:

€0 million (previous year: €-4 million) relate to loans and receivables, which are composed of the following:

*€ million*

| | 2010 | 2011 |
|---|---:|---:|
| Other financial income and expenses | (2) | (2) |
| Write-ups | 1 | 5 |
| Write-downs and additional allowances | (3) | (3) |
| | **(4)** | **0** |

Expenses of €2 million (previous year: €2 million) are allocable to financial liabilities stated at amortized cost and mainly relate to guaranty commissions.

The category financial assets available for sale produced a net profit of €1 million in the year under review (previous year: net profit of €1 million), mainly from the sale of securities.

The loss resulting from derivatives was €-9 million (previous year: €4 million).

# Notes to the consolidated financial statements
# Other notes

### »Finance market risks«

The operations and financing transactions of the Rheinmetall Group as an international group are exposed to financial risks, mainly from liquidity, counterparty default, electricity and commodity prices, exchange rate volatility and interest rate changes. In accordance with the Group-wide implemented risk management system of Rheinmetall AG, such risks are not only identified, analyzed and measured, but also managed by taking actions to avoid, contain or limit such risks, including contracting derivative financial instruments. No such derivatives may be acquired for speculation. All transactions involving derivatives are subject to stringent monitoring, which is particularly ensured through the strict separation of the contracting, settlement and control functions. The effectiveness is subject to ongoing monitoring, using the critical terms match method prospectively and the dollar offset testing method retrospectively. Inherent financial risks are proactively managed to ensure that at the balance sheet date, no significant risks emanate from financial instruments.

### »Foreign currency risk«

Due to the international nature of the Rheinmetall Group's business, certain operational currency risks arise from the fluctuating exchange rates between the functional currencies of Group companies and other currencies. Open positions exposed to a currency risk are hedged through derivatives, generally currency forwards, as well as currency swaps. In the Defence sector, in the context of central financing, Rheinmetall AG has begun assuming the foreign exchange management for subsidiaries. Here, currency hedge transactions are concluded with subsidiaries and the relevant counter-transactions with banks. In the Automotive sector, these transactions are concluded on a central basis via KSPG AG. The transactions are only concluded with banks which have ratings ensuring that they can fulfill the obligations from these contracts. The most important currency hedges contracted by German companies refer to US dollar, Swiss franc, Canadian dollar and South African rand sales transactions, while the foreign companies mostly hedge euro-based purchasing and sales transactions. These hedges are measured as of the balance sheet date and recognized at a fair value which is determined according to the DCF method. Provided that the necessary criteria are met, the changes in the fair value of hedging transactions are recognized in the hedge reserve in the context of cash flow hedge accounting.

As at the reporting date, the nominal volume of cash flow hedge accounting totaled €612 million (previous year: €540 million). In the year under review, fair value changes of €14 million before deduction of deferred taxes (previous year: €30 million) were recognized in OCI only, while €5 million (previous year: €13 million) was reclassified from OCI to the income statement (mainly net sales). There were only immaterial ineffective portions of currency hedges. Hedges covering a nominal volume of €633 million (previous year: €637 million) were not recognized in hedge accounting as defined by IAS 39 since either automatic offsetting mechanisms existed or the documentation requirements were not satisfied.

The table below shows the nominal volume, time to maturity and fair value of all currency hedges at December 31. The fair values at the balance sheet date correspond to prices for financial instruments in arm's length transactions.

Currency hedges *€ million*

| | Nominal volume | | Remaining term > 1 year | | Fair value | |
|---|---|---|---|---|---|---|
| | Dec. 31, 2010 | Dec. 31, 2011 | Dec. 31, 2010 | Dec. 31, 2011 | Dec. 31, 2010 | Dec. 31, 2011 |
| **Without hedge accounting** | | | | | | |
| Foreign exchange contract | 567 | 574 | 63 | 19 | 7 | (3) |
| Other | 70 | 59 | 32 | 4 | (1) | 0 |
| | **637** | **633** | **95** | **23** | **6** | **-3** |
| | | | | | | |
| **With hedge accounting** | | | | | | |
| Foreign exchange contract | 540 | 612 | 206 | 248 | 25 | (3) |

**»Sensitivity analysis«**

If all exchange rates between the local currency used by the Company and the hedged currency had been altered by +/–10% as at the balance sheet date, the following changes would have resulted with regard to currency hedge derivatives on the other net financial income and the hedge reserve before taking into account deferred taxes.

Sensitivity analysis currency hedge *€ million*

| | - 10 percent | | + 10 percent | |
|---|---|---|---|---|
| | Dec. 31, 2010 | Dec. 31, 2011 | Dec. 31, 2010 | Dec. 31, 2011 |
| **Currency hedges** | | | | |
| Net financial result | (2) | 8 | 2 | (8) |
| Hedging reserve | 2 | (3) | (2) | 3 |

**»Interest rate risk«**

As part of the Group-wide management of interest rate risks, Rheinmetall AG uses interest rate hedging instruments (interest rate swaps and interest rate caps). The interest rate swaps essentially serve to hedge variable interest on promissory note loans and future variable interest payments. The interest rate caps were concluded to hedge future interest payments from floating-rate loans.

# Notes to the consolidated financial statements
# Other notes

The table below shows the nominal volume, time to maturity and fair value of all hedges to limit interest rate risks at December 31. The fair values at the balance sheet date correspond to prices for financial instruments in arm's length transactions.

Interest rate hedges *€ million*

| | Nominal volume | | Remaining term > 1 year | | Fair value | |
|---|---|---|---|---|---|---|
| | Dec. 31, 2010 | Dec. 31, 2011 | Dec. 31, 2010 | Dec. 31, 2011 | Dec. 31, 2010 | Dec. 31, 2011 |
| **Without hedge accounting** | | | | | | |
| Interest rate options | 200 | 200 | 200 | 200 | 1 | 0 |
| Interest rate swaps | 126 | 185 | 125 | 183 | (7) | (11) |
| | **326** | **385** | **325** | **383** | **(6)** | **(11)** |
| | | | | | | |
| **With hedge accounting** | | | | | | |
| Interest rate swaps | 112 | 50 | 112 | 50 | (3) | (1) |

As at the reporting date, the nominal volume of cash flow hedge accounting totaled €50 million (previous year: €112 million). These relate to interest swaps bought to hedge the variable interest of promissory notes. The hedging relationship between the floating-rate promissory note loans repaid earlier than scheduled in 2011 (with nominal values totaling €65 million) and the corresponding interest rate swaps came to an end. The interest rate swaps in question, which still have a duration up to 2014, are included in the Derivatives without hedge accounting item.

In the year under review, changes in market value totaling €-1 million before deduction of deferred taxes (previous year: €2 million) were taken into equity in the hedging reserve.

### »Sensitivity analysis«

If the yield curve had been 100 basis points (bp) higher or lower as at the balance sheet date, the following changes would have resulted with regard to the interest rate derivatives on the other net financial income and the hedge reserve, before taking into account deferred taxes.

Sensitivity analysis interest rate hedges *€ million*

| | - 100 Bp | | + 100 Bp | |
|---|---|---|---|---|
| | Dec. 31, 2010 | Dec. 31, 2011 | Dec. 31, 2010 | Dec. 31, 2011 |
| **Interest rate hedges** | | | | |
| Net financial result | (11) | (6) | 15 | 6 |
| Hedging reserve | (5) | (1) | 5 | 1 |

### »Commodity price risk«

The Rheinmetall Group is exposed to price volatility risks from commodity buying, such as metals. By means of materials cost escalator agreements with customers, the major part of these risks from volatile metal prices is shifted to customers, albeit with a time lag. Moreover, the Automotive sector (where most of these risks exist) has also used derivative financial instruments for risk management, mainly exchange-traded commodity futures contracted on the basis of a financial settlement.

The hedging strategy provides for these derivatives to be used exclusively to hedge present underlyings or forecast transactions in the scope of the sector's primary operating activities. In the year under review, fair value changes of €7 million before deduction of deferred taxes (previous year: €7 million) were recognized in OCI only, while €5 million (previous year: €4 million) was reclassified from OCI to the cost of materials.

Commodity hedges *€ million*

| | Nominal volume | | Remaining term > 1 year | | Fair value | |
|---|---|---|---|---|---|---|
| | Dec. 31, 2010 | Dec. 31, 2011 | Dec. 31, 2010 | Dec. 31, 2011 | Dec. 31, 2010 | Dec. 31, 2011 |
| **Without hedge accounting** | | | | | | |
| Commodity futures | 2 | 2 | 1 | - | 0 | 0 |
| | | | | | | |
| **With hedge accounting** | | | | | | |
| Commodity futures | 39 | 52 | 16 | 26 | 15 | 2 |

### »Sensitivity analysis«

If the future price curve for commodity prices for the respective hedged metals had been altered by +/– 10%, the following changes would have resulted with regard to commodity futures derivatives on the other net financial income and the hedge reserve before taking into account deferred taxes.

Sensitivity analysis material price hedging *€ million*

| | - 10 percent | | + 10 percent | |
|---|---|---|---|---|
| | Dec. 31, 2010 | Dec. 31, 2011 | Dec. 31, 2010 | Dec. 31, 2011 |
| **Material price hedging** | | | | |
| Net financial result | 0 | 0 | 0 | 0 |
| Hedging reserve | (4) | (3) | 4 | 3 |

### »Electricity price risk«

In addition to previous electricity procurement practices, derivative financial instruments were concluded in 2011 to secure the price of electricity for the consumption volumes planned for 2013 and 2014. Provided that the necessary criteria are met, the changes in the fair value of hedging transactions are recognized in the hedge reserve in the context of cash flow hedge accounting. In the year under review, changes in market value totaling €1 million before deduction of deferred taxes were taken into equity in the hedging reserve.

Electricity price hedges *€ million*

| | Nominal volume | Remaining term > 1 year | Fair value |
|---|---|---|---|
| | Dec. 31, 2011 | Dec. 31, 2011 | Dec. 31, 2011 |
| **Without hedge accounting** | | | |
| Electricity hedging transactions | 0 | 0 | 0 |
| | | | |
| **With hedge accounting** | | | |
| Electricity hedging transactions | 12 | 12 | (1) |

# Notes to the consolidated financial statements
# Other notes

### »Sensitivity analysis«

If the future price curve for electricity prices had been altered by +/–10%, the following changes would have resulted with regard to electricity price derivatives on the other net financial income and the hedge reserve before taking into account deferred taxes.

Sensitivity analysis electricity price hedging *€ million*

| | - 10 percent | + 10 percent |
|---|---|---|
| | Dec. 31, 2011 | Dec. 31, 2011 |
| **Electricity price hedging** | | |
| Net financial result | 0 | 0 |
| Hedging reserve | (1) | 1 |

### »Default risk (credit risk) «

The default risk from financial assets is that the other contractual party does not fulfill his obligations. For loans granted and customer receivables, the maximum risk is at the level of the values carried in the balance sheet. The default risk from derivative finance instruments is limited to the amount of the positive fair value of the derivatives carried on the balance sheet.

In the Rheinmetall Group, the monitoring and the recognition of default risk from customer receivables takes place decentrally in the operating units. However, there are corporate policies for proper debtor management. Individual assessments (where appropriate, based on current trends and qualitative information) may be used in addition to database-supported rating and default data on an external data supplier. Current del credere risks are covered by valuation allowances.

The past due analysis for customer receivables received within trade receivables below clearly shows that receivables for which value allowances are made are insignificant. Due to the type of transaction and the customer structure, non-payment rarely occurs and there is only the need to post defaults. As of the balance sheet date, there were no indications that any unimpaired and overdue receivables of the A/R portfolio would remain unpaid.

Aged analysis of customer receivables past due *€ million*

| | **Dec. 31, 2010** | **Dec. 31, 2011** |
|---|---|---|
| Trade receivables unimpaired but past due | | |
| for up to 30 days | 48 | 67 |
| for up to 180 days | 34 | 30 |
| for more than 180 days | 40 | 39 |
| | 122 | 136 |
| | | |
| Impaired | 28 | 13 |
| Neither impaired nor past due | 365 | 451 |
| | **515** | **600** |
| Individual value adjustments | (8) | (12) |
| | **507** | **588** |

In order to minimize the default risk with derivative financial instrument contracts, the Rheinmetall Group sets high requirements in respect of its counterparties, restricting itself exclusively to German and foreign banks with impeccable ratings.

To a small extent, companies in the Rheinmetall Group have made financial commitments by granting loans to associates. Over and above this scope, the Rheinmetall Group has no important credit concentrations.

**»Liquidity risk«**

Sufficient liquidity at all times is ensured by the Rheinmetall Group especially by a cash budget and forecast over a specified time horizon, as well as through existing, partly unutilized finance facilities, including credit lines granted by banks on a syndicated basis, a commercial paper (CP) program, an asset backed securities program, promissory notes, and the bond issued in 2010. For further details of such credit facilities, see the management report.

The table below shows as of December 31 all undiscounted contractually agreed payments for recognized financial debts, as well as the derivative financial instruments and their fair value.

Cash outflows *€ million*

| | **Dec. 31, 2010** | | | **Dec. 31, 2011** | | |
|---|---|---|---|---|---|---|
| | 2011 | 2012-2015 | from 2016 | 2012 | 2013-2016 | from 2017 |
| Bond | 20 | 80 | 533 | 20 | 80 | 514 |
| Promissory notes | 8 | 171 | - | 4 | 90 | - |
| Other bank liabilities | 18 | 11 | 21 | 28 | 13 | 23 |
| Capital lease liabilities | 0 | 1 | - | 1 | 4 | 6 |
| Other financial debts | 1 | 2 | 1 | 18 | 3 | 1 |
| | **47** | **265** | **555** | **71** | **190** | **544** |
| | | | | | | |
| Financial derivatives with | | | | | | |
| negative fair value | 20 | 18 | - | 27 | 19 | - |
| positive fair value | 51 | 24 | - | 26 | 4 | - |

The associated cash flow risk from the financial debts is confined to cash outflows.

The fair values of derivatives on the reporting date should be seen in the context of the associated underlyings, whose values generally show an opposite trend, irrespective of whether these have already been accounted for or are pending. The derivatives would only produce a cash outflow at the amount shown above if they were terminated early.

The Rheinmetall Group's financial resources comprise cash and cash equivalents, financial current assets available for sale, and the cash provided by operating activities. In contrast, the capital requirements cover the redemption of financial debts (principal and interest), capital expenditure, and the funds needed for operating activities.

# Notes to the consolidated financial statements
# Other notes

### (39) »Share-based remuneration«

A long-term incentive program exists within the Rheinmetall Group, under which beneficiaries receive Rheinmetall shares with a four-year lock-up period in addition to a cash payment. The number of shares granted is based on the average price on the last five trading days in February of the subsequent fiscal year. The expense recognized in 2011 for share-based remuneration totaled €7 million (previous year: €6 million). A provision was recognized in the corresponding amount.

As part of the Rheinmetall Group's share purchase program, eligible staff of the Rheinmetall Group in Germany and other European countries may purchase Rheinmetall AG shares on preferential conditions. Such shares are subject to a lockup period of 2 years. Within specified subscription periods, the employees are given the opportunity to acquire a limited number of shares at a discount of 30% on the applicable share price. In fiscal 2011, Rheinmetall Group employees purchased 169,743 shares altogether (previous year: 100,338) for €6 million (previous year: €3 million). Expenses of €2 million (previous year: €2 million) were incurred for this program, recognized as personnel expenses.

| **Subscription window** | Share price in € | Discount per share in € | No. of shares purchased by staff | Sales proceeds from shares purchased by employees in € million |
|---|---|---|---|---|
| April 27 - May 10, 2011 | 58.34 | 17.50 | 76,335 | 3 |
| Oct. 26 - Nov 8, 2011 | 37.53 | 11.26 | 93,408 | 3 |

### (40) »Other information on related parties«

For the Rheinmetall Group, corporate related parties are the joint ventures and associated companies carried at equity. The joint ventures, in particular, contribute to the expansion of operations in the Defence and Automotive sectors. The volume of products/services provided to corporate related parties primarily relates – as in the previous year – to sales proceeds from the sale of finished and unfinished goods to project companies, services performed as part of construction contracts with project companies of the Defence sector and sales proceeds from army maintenance services under a public-private partnership model in the Defence sector. As well as customer receivables and trade payables, the volume of unpaid items also includes prepayments received and made and loans to joint ventures and associated companies of €6 million (previous year: €3 million). The interest income from such loans amounts to an unchanged €0 million. The scope of related-party transactions is shown in the table below.

*€ million*

| | Volume of products/ services provided | | Volume of products/ services received | | Volume of open items | |
|---|---|---|---|---|---|---|
| | **2010** | **2011** | **2010** | **2011** | **2010** | **2011** |
| Joint ventures | 100 | 191 | 11 | 21 | (1) | (16) |
| Associated companies | 31 | 18 | 10 | 10 | 22 | 32 |
| | **131** | **209** | **21** | **31** | **21** | **16** |

As previously, no transactions were made with individuals who constitute related parties of the Rheinmetall Group in the year under review.

**»Remuneration of the Executive Board and the Supervisory Board«**

The reportable compensation of senior management within the Group comprises that paid to active Executive Board and Supervisory Board members.

The expenses for compensation paid or payable to active members of the Executive Board break down as follows:

*€ million*

| | 2010 | 2011 |
|---|---|---|
| Short-term payments due | 5,982 | 6,272 *) |
| Deferred compensation | 76 | 76 |
| | **6,058** | **6,348** |
| Additional post-retirement benefits | 760 | 519 |

*) of which €56,000 for fiscal 2010

The post-retirement benefit amounts reflect the current service cost for pension entitlements.

Supervisory Board fees amounted to €1,236K in the year under review (previous year: €1,081K) and are all due in the short term. Costs in the amount of €46K (previous year: €34K) were also refunded. In addition to Supervisory Board remuneration, those employee representatives who are employees of the Rheinmetall Group also receive compensation unrelated to their service on the Supervisory Board. The employee representatives received a total of €365K (previous year: €361K) from these services.

For further details and itemization of each member's remuneration, see the Board remuneration report within the Group management report.

€1,532K (previous year: €1,517K) was paid to former members of the Executive Board or their surviving dependents. Pension provisions for these persons total €14,573K (previous year: €15,141K). €484K (previous year: €481K) was paid to former Executive Board members or their surviving dependents of Rheinmetall DeTec AG (merged with Rheinmetall AG in 2005). Pension provisions for these persons total €5,506K (previous year: €5,509K).

# Notes to the consolidated financial statements
# Other notes

### (41) »Auditor's fees«

In fiscal 2011 and 2010, the following fees of the statutory auditor PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft (PwC) were expensed in Germany:

*€ million*

| | 2010 | 2011 |
|---|---|---|
| End-of-year auditing services | 2,077 | 2,248 |
| Other verification services | 295 | 1,152 |
| Tax consultancy services | 27 | 11 |
| Other services | 257 | 226 |
| | **2,656** | **3,637** |

The auditing fees cover Rheinmetall AG's single-entity and consolidated financial statements and the accounts of all subsidiaries audited by PwC in Germany. Tax consultancy fees primarily comprised fees for project-related consultancy services. Fees for other services mainly relate to activities in the context of audits accompanying projects. All services not related to the audit of the financial statements were approved by the Audit Committee.

### (42) »Corporate governance«

In December 2011, Rheinmetall AG published its declaration of conformity according to the German Corporate Governance Code pursuant to Section 161 AktG on the internet at www.rheinmetall.com in the section "Group – Corporate Governance", thus making it available to shareholders.

Düsseldorf, March 15, 2012

Rheinmetall Aktiengesellschaft
The Executive Board

Klaus Eberhardt Dr. Gerd Kleinert Dr. Herbert Müller Armin Papperger

# Notes to the consolidated financial statements
## Shareholdings

| Company | | | Direct share of capital in % | Indirect share of capital in % |
|---|---|---|---|---|
| **Fully consolidated subsidiaries** | | | | |
| **Holding companies / service companies/ other** | | | | |
| EMG EuroMarine Electronics GmbH, Neckarsulm / Germany | | | | 100 |
| MEG Marine Electronics Holding GmbH, Bremen / Germany | | | | 100 |
| Rheinmetall Berlin Verwaltungsgesellschaft mbH, Berlin / Germany | | | 100 | |
| Rheinmetall Bürosysteme GmbH, Düsseldorf / Germany | | | 100 | |
| Rheinmetall Immobilien GmbH, Düsseldorf / Germany | | | 100 | |
| Rheinmetall Industrietechnik GmbH, Düsseldorf / Germany | | | 100 | |
| Rheinmetall Maschinenbau GmbH, Düsseldorf / Germany | | | 100 | |
| Rheinmetall Insurance Services GmbH, Düsseldorf / Germany | | | 100 | |
| Rheinmetall Verwaltungsgesellschaft mbH, Düsseldorf / Germany | | | | 100 |
| SUPRENUM Gesellschaft für numerische Superrechner mbH, Bremen / Germany | | | | 100 |
| **Defence sector** | | | | |
| ADS Gesellschaft für aktive Schutzsysteme mbH, Lohmar / Germany | | | | 74 |
| American Rheinmetall Munition Inc., Stafford, Virginia / USA | USD | | | 100 |
| Benntec Systemtechnik GmbH, Bremen / Germany | | (1) | | 49 |
| BIL Industriemetalle GmbH & Co. 886 KG, Grünwald / Germany | | | 94 | |
| Eurometaal Holding N.V., Hengelo / Netherlands | | | | 100 |
| Eurometaal N.V., Hengelo / Netherlands | | | | 100 |
| I.L.E.E. AG, Urdorf / Switzerland | CHF | | | 100 |
| Laser 2000 (Schweiz) AG, Urdorf / Switzerland | CHF | | | 80 |
| LDT Laser Display Technology GmbH, Jena / Germany | | | | 100 |
| MarineSoft Entwicklungs- und Logistikgesellschaft mbH, Rostock / Germany | | (1) | | 49 |
| Nitrochemie AG, Wimmis / Switzerland | CHF | | | 51 |
| Nitrochemie Aschau GmbH, Aschau / Germany | | | | 55 |
| Nitrochemie Wimmis AG, Wimmis / Switzerland | CHF | | | 55 |
| Oerlikon Contraves GmbH, Zurich / Switzerland | CHF | | 100 | |
| Oerlikon Contraves Pte Ltd., Singapore / Singapore | SGD | | | 100 |
| Rheinmetall Air Defence AG, Zurich / Switzerland | CHF | | 100 | |
| Rheinmetall Airborne Systems GmbH, Bremen / Germany | | | 100 | |
| Rheinmetall Australia Pty Ltd., Canberra / Australia | AUD | | 100 | |
| Rheinmetall Canada Inc., St.-Jean-sur-Richelieu / Canada | CAD | | 100 | |
| Rheinmetall Chempro GmbH, Bonn / Germany | | | | 51 |
| Rheinmetall Defence Electronics GmbH, Bremen / Germany | | | 100 | |
| Rheinmetall Defence UK Limited, London / Great Britain | GBP | | 100 | |
| Rheinmetall Denel Munition Pty. Ltd., Somerset West / South Africa | ZAR | | | 51 |
| Rheinmetall Dienstleistungszentrum Altmark GmbH, Letzlingen / Germany | | | 100 | |
| Rheinmetall Hellas S.A., Athen / Greece | | | 100 | |
| Rheinmetall Italia S.p.A., Rom / Italy | | | | 100 |

# Notes to the consolidated financial statements
## Shareholdings

| Company | | | Direct share of capital in % | Indirect share of capital in % |
|---|---|---|---|---|
| Rheinmetall Laingsdale (Pty) Ltd.,Cape Town / South Africa | ZAR | | | 76 |
| Rheinmetall Landsysteme GmbH, Kiel / Germany | | | 100 | |
| Rheinmetall MAN Military Vehicle Systems RSA (Pty) Ltd., Pretoria / South Africa | ZAR | (1) | | 36 |
| Rheinmetall MAN Military Vehicles Australia Pty Ltd., Canberra / Australien | AUD | | | 51 |
| Rheinmetall MAN Military Vehicles Canada Ltd., Ottawa / Canada | CAD | | | 51 |
| Rheinmetall MAN Military Vehicles GmbH, Munich/ Germany | | | 51 | |
| Rheinmetall MAN Military Vehicles Österreich GesmbH, Vienna / Austria | | | | 51 |
| Rheinmetall MAN Military Vehicles Österreich Holding GesmbH, Vienna / Austria | | | | 51 |
| Rheinmetall Nederland B.V., Amsterdam / Netherlands | | | | 51 |
| Rheinmetall Nordic AS, Nøtterøy / Norway | NOK | | 100 | |
| Rheinmetall North America Inc., Southfield / USA | USD | | 95 | 5 |
| Rheinmetall Schweiz AG, Zurich / Switzerland | CHF | | | 100 |
| Rheinmetall Simulation Australia Pty. Ltd., Deakin West / Australia | AUD | | | 100 |
| Rheinmetall Soldier Electronics GmbH, Stockach / Germany | | | 100 | |
| Rheinmetall Technical Publications GmbH, Bremen / Germany | | | 100 | |
| Rheinmetall Verseidag Ballistic Protection GmbH, Krefeld / Germany | | | | 100 |
| Rheinmetall Waffe Munition ARGES GmbH, Schwanenstadt / Austria | | | | 100 |
| Rheinmetall Waffe Munition GmbH, Unterlüß / Germany | | | 100 | |
| Rheinmetall Waffe Munition South Africa (Pty) Ltd., Somerset West / South Africa | ZAR | | | 100 |
| RF Engines Limited, Newport, Isle of Wight / Great Britain | GBP | | | 100 |
| RM Euro B.V., Hengelo / Netherlands | | | 100 | |
| RTP-UK Ltd., Bristol / Great Britain | GBP | | | 100 |
| RWM Beteiligungsverwaltung Austria GmbH, Schwanenstadt / Austria | | | | 100 |
| RWM Italia S.p.A., Ghedi / Italy | | | | 100 |
| RWM Schweiz AG, Zurich / Switzerland | CHF | | | 100 |
| RWM Zaugg AG, Lohn-Ammannsegg / Switzerland | CHF | | | 100 |
| Swiss SIMTEC AG, Thun / Switzerland | CHF | | | 100 |
| Vinghøg AS, Nøtterøy / Norway | NOK | | | 100 |
| Vingtech Australia Pty. Ltd., Alphington, Victoria / Australia | AUD | | | 55 |
| Vingtech Corp., Biddeford, Maine / USA | USD | | | 100 |
| VingTech Holding Inc., Fountain Inn / USA | USD | | | 100 |
| Servo Kontroll AS, Oslo / Norway | NOK | | | 100 |

| Company | | Direct share of capital in % | Indirect share of capital in % |
|---|---|---|---|
| **Automotive sector** | | | |
| BF Germany GmbH, Neuenstadt / Germany | | | 100 |
| GVG Grundstücksverwaltung Gleitlager GmbH & Co. KG, Neckarsulm / Germany | | | 100 |
| GVH Grundstücksverwaltung Hamburg GmbH & Co. KG, Neckarsulm / Germany | | | 100 |
| GVMS Grundstücksverwaltung Service GmbH & Co. KG, Neckarsulm / Germany | | | 100 |
| GVN Grundstücksverwaltung Neckarsulm GmbH & Co. KG, Neckarsulm / Germany | | | 100 |
| Intec France S.A.S., Meyzieu / France | | | 100 |
| Karl Schmidt Trading Company S. de R.L. de C.V., Celaya / Mexico | MXN | | 100 |
| Karl Schmidt Unisia Inc., Marinette / USA | USD | | 92 |
| Kolbenschmidt de México S. de R.L. de C.V., Celaya / Mexico | MXN | | 100 |
| Kolbenschmidt K.K., Yokohama / Japan | JPY | | 100 |
| Kolbenschmidt Liegenschaftsverwaltung GmbH Berlin, Berlin / Germany | | | 100 |
| Kolbenschmidt Pierburg Innovations GmbH, Neckarsulm / Germany | | | 100 |
| Kolbenschmidt USA Inc., Marinette / USA | USD | | 100 |
| KS Aluminium-Technologie GmbH, Neckarsulm / Germany | | | 100 |
| KS ATAG Beteiligungsgesellschaft m.b.H., Neckarsulm / Germany | | | 100 |
| KS ATAG GmbH, Neckarsulm / Germany | | | 100 |
| KS ATAG Romania S.R.L. , Bukarest / Romania | RON | | 100 |
| KS France S.A.S., Basse-Ham (Thionville) / France | | | 100 |
| KS Gleitlager de México S. de R.L. de C.V., Celaya / Mexico | MXN | | 100 |
| KS Gleitlager GmbH, St. Leon-Rot / Germany | | | 100 |
| KS Gleitlager North America LLC, Marinette / USA | USD | | 100 |
| KS Grundstücksverwaltung Beteiligungs GmbH, Neckarsulm / Germany | | | 100 |
| KS Grundstücksverwaltung GmbH & Co. KG, Neckarsulm / Germany | | | 100 |
| KS Kolbenschmidt Czech Rebublic a.s., Usti / Czech Republic | CZK | | 100 |
| KS Kolbenschmidt France S.A.S., Basse-Ham (Thionville) / France | | | 100 |
| KS Kolbenschmidt GmbH, Neckarsulm / Germany | | | 100 |
| KS Large Bore Pistons Inc., Marinette / USA | USD | | 100 |
| KS Personaldienstleistungsgesellschaft mbH i.L., Neckarsulm / Germany | | | 100 |
| KS Produtos Automotivos Ltda., Nova Odessa / Brazil | BRL | | 100 |
| KSPG AG, Neckarsulm / Germany | | | 100 |
| KSPG Automotive Brazil Ltda., Nova Odessa / Brazil | BRL | | 100 |
| KSPG Automotive India Private Ltd., Mumbai Maharashtra/India | INR | | 100 |
| KSPG Finance & Service Ltd., St. Julians / Malta | | | 100 |
| KSPG Malta Holding Ltd., St. Julians / Malta | | 21 | 79 |
| KSPG Netherlands Holding B.V., Amsterdam / Netherlands | | | 100 |
| KSPG North America Inc., Marinette / USA | USD | | 100 |
| KSUS International LLC., Marinette / USA | USD | | 100 |
| KUS Canada Inc., Leamington / Canada | USD | | 92 |
| MS Motor Service Aftermarket Iberica S.L., Abadiano / Spain | | | 100 |
| MS Motor Service Asia Pacific Co., Ltd., Shanghai / China | CNY | | 100 |
| MS Motor Service Deutschland GmbH, Weinstadt / Germany | | | 100 |

# Notes to the consolidated financial statements
## Shareholdings

| Company | | Direct share of capital in % | Indirect share of capital in % |
|---|---|---|---|
| MS Motor Service France S.A.S., Villepinte/ France | | | 100 |
| MS Motor Service International GmbH, Neuenstadt / Germany | | | 100 |
| MS Motor Service Istanbul Dis Ticaret ve Pazarlama A.S., Istanbul / Turkey | TRL | | 51 |
| Pierburg China Ltd., Kunshan City / China | CNY | | 100 |
| Pierburg Gestion S.L., Abadiano / Spain | | | 100 |
| Pierburg GmbH, Neuss / Germany | | | 100 |
| Pierburg Inc., Fountain Inn (Greenville) / USA | USD | | 100 |
| Pierburg Mexico S.A. de C.V., Chihuahua / Mexico | MXN | | 100 |
| Pierburg Mikuni Pump Technology Corporation, Odawara / Japan | JPY | | 51 |
| Pierburg Pump Technology GmbH, Neuss / Germany | | | 100 |
| Pierburg Pump Technology India Private Limited, Mumbai Maharashtra / India | INR | | 100 |
| Pierburg Pump Technology Italy S.p.A., Lanciano / Italy | | | 100 |
| Pierburg Pump Technology France S.à r.l., Basse-Ham (Thionville) / France | | | 100 |
| Pierburg Pump Technology Mexico S.A. de C.V., Mexico City / Mexiko | MXN | | 100 |
| Pierburg Pump Technology UK Ltd., London/Great Britain | GBP | | 100 |
| Pierburg Pump Technology US LLC., Marinette / USA | USD | | 100 |
| Pierburg S.A., Abadiano / Spain | | | 100 |
| Pierburg s.r.o., Usti / Czech Republic | CZK | | 100 |
| Pierburg Systems S.L., Abadiano / Spain | | | 100 |
| Société Mosellane de Services S.C.I., Basse-Ham (Thionville) / France | | | 100 |
| Werkzeugbau Walldürn GmbH, Walldürn / Germany | | | 100 |

| Company | | | Direct share of capital in % | Indirect share of capital in % |
|---|---|---|---|---|
| **Investments carried at equity** | | | | |
| **Holding companies / service companies/ other** | | | | |
| casa altra development GmbH, Düsseldorf / Germany | | | | 35 |
| doubleU development GmbH, Düsseldorf / Germany | | (2) | | 10 |
| LIGHTHOUSE Development GmbH, Düsseldorf / Germany | | (2) | | 10 |
| Unternehmerstadt GmbH, Düsseldorf / Germany | | (3) | | 50 |
| **Defence sector** | | | | |
| Advanced Pyrotechnic Materials Pte Ltd, Singapore / Singapore | SGD | (3) | | 49 |
| AIM Infrarot-Module GmbH, Heilbronn / Germany | | | | 50 |
| ARGE RDE/CAE (GbR), Bremen / Germany | | (3) | | 50 |
| ARTEC GmbH, Munich / Germany | | (2) (3) | | 64 |
| Burkan Munitions Systems L.L.C., Abu Dhabi / UAE | AED | | | 40 |
| Contraves Advanced Devices Sdn Bhd, Malaka / Malaysia | MYR | (3) | | 49 |
| DynITEC GmbH, Troisdorf / Germany | | | | 45 |
| EuroSpike GmbH, Röthenbach/Peg / Germany | | (3) | | 40 |
| GIWS Gesellschaft für Intelligente Wirksysteme mbH, Nürnberg / Germany | | (3) | | 50 |
| Hartchrom Defense Technology AG, Steinach / Switzerland | CHF | | | 38 |
| HFTS Helicopter Flight Training Services GmbH, Hallbergmoos / Germany | | (3) | | 25 |
| HIL Industrie-Holding GmbH, Bonn / Germany | | (3) | | 33 |
| LOG Logistik-Systembetreuungs-Gesellschaft mbH, Bonn / Germany | | | | 25 |
| N2 Defense LLC, Arlington, Virginia / USA | USD | (3) | | 50 |
| Oy Finnish Defence Powersystems Ab, Helsinki / Finland | | | | 30 |
| PSM Projekt System & Managment GmbH, Kassel / Germany | | (3) | | 50 |
| SysFla GmbH, Unterschleißheim / Germany | | (3) | | 50 |
| Werk Aschau Lagerverwaltungsgesellschaft mbH, Aschau / Germany | | (3) | | 28 |
| **Automotive sector** | | | | |
| Advanced Bearing Materials LLC., Greensburg / USA | USD | (3) | | 50 |
| Kolbenschmidt Pierburg Shanghai Nonferrous Components Co. Ltd., Shanghai / China | CNY | (3) | | 50 |
| Kolbenschmidt Shanghai Piston Co. Ltd., Shanghai / China | CNY | (3) | | 50 |
| KS ATAG TRIMET Guss GmbH, Harzgerode / Germany | | (3) | | 50 |
| Shriram Pistons & Rings Ltd., New Delhi / India | INR | | | 20 |

(1) Full consolidation due to majority of voting rights
(2) Controlling influence owing to distribution of voting rights
(3) Joint Venture

# Responsibility statement

We represent that, to the best of our knowledge and in accordance with applicable accounting principles, the consolidated financial statements of Rheinmetall AG present a true and fair view of the Rheinmetall Group's assets, financial situation and earnings, and that the Group management report, which is consolidated with the management report of Rheinmetall AG, describes fairly, in all material respects, the Group's business trend and performance, the Group's position and the significant risks and opportunities of the Group's expected future development.

Düsseldorf, March 15, 2012

Rheinmetall Aktiengesellschaft
The Executive Board

Klaus Eberhardt Dr. Gerd Kleinert Dr. Herbert Müller Armin Papperger

# Auditor’s report and opinion

**»Rheinmetall AG, Düsseldorf, Independent Auditor’s Report and Opinion«**
We have audited the consolidated financial statements prepared by the Rheinmetall AG, Düsseldorf, comprising the statement of financial position, the statement of comprehensive income, statement of changes in equity, cash flow statement and the notes to the consolidated financial statements, together with the group management report, which is combined with the management report of the Rheinmetall AG, Düsseldorf, for the business year from January 1 to December 31, 2011. The preparation of the consolidated financial statements and the combined management report in accordance with the IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § (Article) 315a Abs. (paragraph) 1 HGB (“Handelsgesetzbuch”: German Commercial Code) are the responsibility of the parent Company's Board of Managing Directors. Our responsibility is to express an opinion on the consolidated financial statements and the combined management report based on our audit. In addition we have been instructed to express an opinion as to whether the consolidated financial statements comply with full IFRS.
We conducted our audit of the consolidated financial statements in accordance with § 317 HGB and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the combined management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and in the combined management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of the companies included in consolidation, the determination of the companies to be included in consolidation, the accounting and consolidation principles used and significant estimates made by the Company's Board of Managing Directors, as well as evaluating the overall presentation of the consolidated financial statements and the combined management report. We believe that our audit provides a reasonable basis for our opinion.
Our audit has not led to any reservations.
In our opinion based on the findings of our audit the consolidated financial statements comply with the IFRSs as adopted by the EU, and the additional requirements of German commercial law pursuant to § 315a Abs. 1 HGB and full IFRS and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these provisions. The combined management report is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group’s position and suitably presents the opportunities and risks of future development.".

Düsseldorf, March 5, 2012/March 15, 2012

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

| | |
|---|---|
| Gerd Bovensiepen | Uwe Schwalm |
| (German Public Auditor) | (German Public Auditor) |

# Balance sheet of Rheinmetall Aktiengesellschaft as of December 31, 2011

Assets *€ '000*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| **Fixed assets** | | |
| Intangible assets | 303 | 429 |
| Property, plant and equipment | 22,880 | 21,744 |
| Finacial assets | 1,120,263 | 1,170,053 |
| | **1,143,446** | **1,192,226** |
| | | |
| **Current assets** | | |
| Receivables and other assets | 418,665 | 432,157 |
| Cash in hand | 524,563 | 407,444 |
| | **943,228** | **839,601** |
| | | |
| **Deferred income** | **4,939** | **4,184** |
| | | |
| **Total assets** | **2,091,613** | **2,036,011** |

Equity and Liabilities *€ '000*

| | Dec. 31, 2010 | Dec. 31, 2011 |
|---|---|---|
| Share capital | 101,373 | 101,373 |
| Treasury stock (notional value relating to the share capital) | (3,310) | (3,458) |
| | 98,063 | 97,915 |
| Capital reserves | 304,098 | 306,699 |
| Retained earnings | 50,451 | 107,596 |
| Net earnings | 57,800 | 69,000 |
| **Equity** | **510,412** | **581,210** |
| | | |
| **Provisions** | **122,312** | **131,507** |
| | | |
| **Liabilities** | | |
| Bond | 500,000 | 500,000 |
| Liabilities due to banks | 150,167 | 85,500 |
| Other liabilities | 808,722 | 737,794 |
| | **1,458,889** | **1,323,294** |
| | | |
| **Total liabilities** | **2,091,613** | **2,036,011** |

# Income Statement of Rheinmetall Aktiengesellschaft for fiscal 2011

*€ '000*

| | 2010 | 2011 |
|---|---|---|
| Investment income | 67,576 | 178,707 |
| Net interest | (31,017) | (31,879) |
| **Net financial income** | **36,559** | **146,828** |
| | | |
| Other operational income | 62,537 | 126,471 |
| Staff costs | 28,198 | 26,548 |
| Amortization of intangible and depreciation of tangible assets (incl. write-down) | 1,595 | 1,584 |
| Other operating expenses | 50,469 | 106,040 |
| Extraordinary expenses | 956 | 922 |
| **Earnings before taxes (EBT)** | **17,878** | **138,205** |
| Taxes on income and revenue | (2,337) | (9,508) |
| **Net profit for the year** | **15,541** | **128,697** |
| | | |
| Appropriations of retained earnings | 98,916 | - |
| Appropriation to retained earnings | 56,657 | 59,697 |
| | | |
| **Net earnings** | **57,800** | **69,000** |

# Supervisory Board

**Klaus Greinert**
Mannheim
Businessman
Chairman

*Membership in Supervisory Boards*

DURAVIT AG
(Vice Chairman)
DURAVIT S.A.

**Joachim Stöber** *)
Biebergemünd
Member of the German Metalworkers' Union
General Secretariat
Vice Chairman

*Membership in Supervisory Boards*

GEA Group AG
(up to April 30, 2011)

**Professor Dr. Andreas Georgi**
Starnberg
Professor of Leadership and Control Problems
in Enterprise
Ludwig-Maximilians-Universität Munich
Consultant

*Membership in Supervisory Boards*

Asea Brown Boveri Aktiengesellschaft
Felix Schoeller Holding GmbH & Co. KG
Oldenburgische Landesbank AG
RWE Dea AG

**Dr. Siegfried Goll**
Markdorf
Consulting Engineer
Former CEO of ZF Friedrichshafen AG

*Membership in Supervisory Boards*

Leuze Geschäftsführungs-GmbH
Voss Holding GmbH & Co. KG
Witzenmann GmbH

**Heinrich Kmett** *)
Fahrenbach/Robern
Chairman of Location Works Council of
KSPG AG
KS Kolbenschmidt GmbH
KS ATAG GmbH
KS Aluminium-Technologie GmbH
MS Motor Service International GmbH

*Membership in Supervisory Boards*

KSPG AG

**Dr. Rudolf Luz** *)
Weinsberg
1st delegate of the German Metalworkers' Union
Heilbronn-Neckarsulm

*Membership in Supervisory Boards*

KSPG AG (Stellvertretender Vorsitzender)

**Dr. Michael Mielke** *)
Berlin
Head of Product Division Actuators
Pierburg GmbH,
Werk Berlin

**Dr. Peter Mihatsch**
Sindelfingen
Consulting engineer

*Membership in Supervisory Boards*

Vodafone D2 GmbH

**DDr. Peter Mitterbauer**
Gmunden, Austria
CEO of Miba AG

*Membership in Supervisory Boards*

Andritz AG
Erste Österreichische Spar-Casse Privatstiftung
FFG Österreichische Forschungsförderungsgesellschaft mbH
(Chairman)
Oberbank AG
ÖIAG Österreichische Industrieholding AG
(Chairman)

*) *Selected by employees*

**Detlef Moog**
Mülheim an der Ruhr
Consulting engineer

*Membership in Supervisory Boards*

Rheinmetall Waffe Munition GmbH
(Chairman)
(up to December 31, 2011)
Rheinmetall Landsysteme GmbH
(Chairman)
(up to March 31, 2011)

**Wolfgang Müller** *)
Bad Rappenau
Chairman of Works Council of
KS Aluminium-Technologie GmbH and
Werkzeugbau Walldürn GmbH

Vice Chairman of Location Works Council of
KSPG AG
KS Kolbenschmidt GmbH
KS ATAG GmbH
KS Aluminium-Technologie GmbH
MS Motor Service International GmbH

*Membership in Supervisory Boards*

KS Aluminium-Technologie GmbH
KS ATAG GmbH

**Professor Dr. Frank Richter**
Ulm
CEO of DURAVIT AG

*Membership in Supervisory Boards*

Advisory Board Gebr. Röchling KG

**Harald Töpfer** *)
Kassel
Chairman of Works Council of
Rheinmetall Radfahrzeuge GmbH and
Rheinmetall MAN Military Vehicles GmbH,
Kassel operation

*Membership in Supervisory Boards*

Rheinmetall MAN Military Vehicles GmbH
(Vice Chairman)

**Wolfgang Tretbar** *)
Nettetal
Chairman of Works Council of
Pierburg GmbH, Nettetal plant

**Toni Wicki**
Oberrohrdorf, Schweiz
Consulting engineer

*Membership in Supervisory Boards*

Implenia AG

**Peter Winter** *)
Achim
Member of Works Council of
Rheinmetall Defence Electronics GmbH

*Membership in Supervisory Boards*

Rheinmetall Defence Electronics GmbH

*) *Selected by employees*

# Executive Board Rheinmetall AG

### Klaus Eberhardt

Düsseldorf

Chairman (CEO)

Director of Industrial Relations

Chairman of Defence Sector
(up to December 31, 2011)

*Membership in Supervisory Boards*

KSPG AG
(Chairman)

Rheinmetall MAN Military Vehicles GmbH
(Chairman)

Hirschmann Automotive GmbH

MTU Aero Engines Holding AG
(Chairman)

MTU Aero Engines GmbH
(Chairman)

Familienstiftungen Dietrich und Eckart Wälzholz

### Armin Papperger

Düsseldorf

Chairman of Defence Sector
(from January 1, 2012)

*Membership in Supervisory Boards*

Rheinmetall Landsysteme GmbH
(Chairman)

Rheinmetall MAN Military Vehicles GmbH

Rheinmetall Waffe Munition GmbH
(from January 1, 2012)

Rheinmetall Defence Electronics GmbH

Rheinmetall Defence UK Ltd.
(Chairman)

Rheinmetall Waffe Munition ARGES GmbH
(Chairman)

RWM Zaugg AG
(Chairman)

Nitrochemie Aschau GmbH
(Chairman)

Nitrochemie AG
(President)

Nitrochemie Wimmis AG
(President)

Rheinmetall Canada Inc.
(Chairman)

American Rheinmetall Munition Inc.
(Chairman)

Rheinmetall Denel Munition (Pty) Ltd
(Chairman)

Rheinmetall Waffe Munition South Africa (Pty) Ltd
(Chairman)

Rheinmetall Laingsdale (Pty) Ltd
(Chairman)

PSM Projekt System & Management GmbH

### Dr. Gerd Kleinert

Gottmadingen

CEO of KSPG AG

*Membership in Supervisory Boards*

Kolbenschmidt Pierburg Shanghai
Nonferrous Components Co. Ltd.
(Vice Chairman)

KS Shanghai Piston Co. Ltd.
(Chairman)

Rheinmetall North America Inc.
(Director)

KS Aluminium-Technologie GmbH
(Chairman)

KS ATAG GmbH
(Chairman)

KS Gleitlager GmbH
(Chairman)

KS Kolbenschmidt GmbH
(Chairman)

Läpple AG
(Chairman)

Pierburg GmbH
(Chairman)

Advisory Board Gebr. Röchling KG

Shareholders' Committee Hella KGaA Hueck & Co

### Dr. Herbert Müller

Bonn

Finance and Controlling

*Membership in Supervisory Boards*

KSPG AG

## Senior Executive officers

**Dr. Andreas Beyer, LL.M.**
Sindelfingen
Law, Internal Auditing, Merger & Acquisitions,
Chief Compliance Officer

**Ingo Hecke**
Meerbusch
Human Resources and Senior Management

## Executive Board Automotive

**Dr. Gerd Kleinert**
Gottmadingen
Chairman
Strategy, Marketing, Operations

**Horst Binnig**
Bad Friedrichshall
(from January 1, 2012)
Operations

**Peter-Sebastian Krause**
Erkrath
Human Resources, Law

**Dr. Peter P. Merten**
Herrsching
Finance and Controlling, IT

## Management Board Defence

**Klaus Eberhardt**
Düsseldorf
Chairman
(up to December 31, 2011)

**Armin Papperger**
Düsseldorf
Chairman
(from January 1, 2012)
Tracked vehicles, Weapon and Munitions, Propellants

**Helmut P. Merch**
Erkrath
Finance and Controlling, IT

**Bodo Garbe**
Zürich
(from July 1, 2011)
Air Defence, C4ISTAR, Simulation and Training

**Heinz Dresia**
Krefeld
Management Board Projects

**Ingo Hecke**
Meerbusch
Human Resources

**Pietro Borgo**
Munich
(from February 1, 2012)
Wheeled Vehicles

# Legal Information

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This report contains statements and forecasts referring to the future development of the Rheinmetall Group which are based on assumptions and estimates made by the management. A number of factors, many of which are beyond Rheinmetall's control, influence the business activities, success, business strategy and results of the Company. Statements regarding the future are based on current plans, targets, estimates and forecasts and only take into account findings made up to and including the date this report was produced. If the underlying assumptions do not materialize, the actual figures may differ from such estimates. Uncertain factors include changes in the political and economic environment, changes to national and international laws and regulations, market fluctuations, the development of global market prices for commodities, exchange rate and interest rate fluctuations, the impact of rival products and competitive prices, the acceptance of and demand for new products, the effect of changes to customer structures and changes to the business strategy. Rheinmetall does not intend, nor does it undertake a particular commitment, to update statements referring to the future or to adjust these to events or developments following the publication of this annual report.

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