
Risk Factors

1. Financial Market Risks p. 12
2. Business-Related Risks p. 14
3. Legal Risks p. 17
4. Industrial and Environmental Risks p. 18

Risk Factors

1. Financial Market Risks

EADS and its subsidiaries (the “**Group**”) are subject to many risks and uncertainties that may affect its financial performance. The business, financial condition or results of operations of EADS could be materially adversely affected by the risks described below. These risks are not the only ones facing EADS. Additional risks not presently known to EADS or that it currently deems immaterial may also impair its business operations.

1. Financial Market Risks

Exposure to Foreign Currencies

EADS’ revenues are mainly denominated in U.S. Dollars, while a substantial portion of its costs is incurred in Euro and Pounds Sterling. Consequently, to the extent EADS were not to use financial instruments to cover its exposure resulting from this foreign currency mismatch, its profits would be affected by changes in the Euro-U.S. Dollar and Pound Sterling- U.S. Dollar exchange rates. EADS has, therefore, implemented an exchange rate strategy in order to manage and minimize such exposure. In order to secure the rates at which U.S. Dollar revenues (arising primarily at Airbus and in the commercial satellite business) are converted into Euro or Pounds Sterling, EADS manages a long-term hedging portfolio. There are complexities inherent in determining whether and when foreign exchange rate exposure of EADS will materialize, in particular given the possibility of unpredictable revenue variations arising from order cancellations and postponements. Furthermore, as a significant portion of EADS’ foreign currency exposure is hedged through contractual arrangements with third parties, EADS is exposed to the risk of non-performance by its approximately 40 hedging counterparties. No assurances may be given that EADS’ exchange rate hedging strategy will protect it fully from significant changes in the exchange rate of the U.S. Dollar to the Euro and the Pound Sterling and that such changes will not affect its results of operation and financial condition.

EADS’ consolidated revenues, costs, assets and liabilities denominated in currencies other than the Euro are translated into the Euro for the purposes of compiling its financial statements. As EADS’ exchange rate hedging strategy aims to cover its cash flows, and, to a large extent, EBIT*, changes in the value of these currencies relative to the Euro will have

an effect on the Euro value of EADS’ reported revenues, costs, assets and liabilities and, to a lesser extent, EBIT*.

Currency exchange rate fluctuations in those currencies other than the U.S. Dollar in which EADS incurs its principal manufacturing expenses (mainly the Euro) may have the effect of distorting competition between EADS and competitors whose costs are incurred in other currencies. This is particularly true with respect to fluctuations relative to the U.S. Dollar, as many of EADS’ products and those of its competitors (e.g., in the defence export market) are priced in U.S. Dollars. EADS’ ability to compete with competitors may be eroded to the extent that any of EADS’ principal currencies appreciates in value against the principal currencies of such competitors.

See “1.1.4.3 EBIT* Performance by Division — Hedging Impact on EBIT*” for a discussion of EADS’ foreign currency hedging policy. See “1.1.3.5 Accounting for Hedged Foreign Exchange Transactions in the Financial Statements” for a summary of EADS’ accounting treatment of foreign currency hedging transactions.

Exposure to Sales Financing Risk

In support of sales, EADS (primarily through Airbus and ATR with respect to commercial aircraft) may agree to participate in the financing of customers. As a result, EADS has a significant portfolio of leases and other financing arrangements with airlines. The risks arising from EADS’ sales financing activities may be classified into two categories: (i) credit risk, which concerns the customer’s ability to perform its obligations under a financing arrangement and (ii) aircraft value risk, which primarily relates to unexpected decreases in the future value of aircraft. Measures taken by EADS to mitigate these risks include

optimised financing and legal structures, diversification over a number of aircraft and customers, credit analysis of financing counterparties, provisioning for the credit and asset value exposure, and transfers of exposure to third parties. No assurances may be given that these measures will protect EADS fully from defaults by its customers or significant decreases in the value of the financed aircraft in the resale market.

EADS' sales financing arrangements expose it to aircraft value risk, because it retains collateral interests in aircraft for the purpose of securing customers' performance of their financial obligations to EADS, and because it guarantees part of the market value of certain aircraft during limited periods after their delivery to customers. Under adverse market conditions, the market for used aircraft could become illiquid and the market value of used aircraft could significantly decrease below projected amounts. In the event of a financing customer default at a time when the market value for a used aircraft has unexpectedly decreased, EADS would be exposed to the difference between the outstanding loan amount and the market value of the aircraft. Similarly, if an unexpected decrease in the market value of a given aircraft coincided with the exercise window of an asset value guarantee ("AVG") with respect to that aircraft, EADS would be exposed to losing as much as the difference between the market value of such aircraft and the AVG amount. No assurances may be given that the provisions taken by EADS will be sufficient to cover these potential shortfalls.

Through the Airbus Asset Management Division or as a result of past financing transactions, EADS is the owner of used aircraft, exposing it directly to fluctuations in the market value of these used aircraft.

Counterparty Credit Risk

EADS is exposed to credit risk to the extent of non-performance by its financial instrument counterparties. However, the Group has policies in place to avoid concentrations of credit risk and to ensure that credit risk is limited.

Cash transactions and derivative counterparties are limited to high credit quality financial institutions. EADS has set up a credit limit system to actively manage and limit its credit risk

exposure. This limit system assigns maximum exposure lines to counterparties of financial transactions, based at a minimum on their credit ratings as published by Standard & Poor's, Moody's and Fitch IBCA. The respective limits are regularly monitored and updated.

As counterparty credit risk also arises in the context of sales financing transactions, EADS' general policy is to provide financing to customers and through structures with an appropriate credit standing. See "1.1.7.4 Sales Financing".

Exposure on Equity Investment Portfolio

EADS holds several equity investments for industrial reasons. None of the equity investments are held for speculative or trading purposes. Equity investments are either accounted for using the equity method (associated companies), if EADS has the ability to exercise significant influence, or at fair value. If fair value is not readily determinable, the investment is measured at cost.

Changes in the value of equity investments mainly depend on their performance. EADS' principal investment in associates is Dassault Aviation. The net asset value of this investment was €1.9 billion at 31st December 2005. EADS considers its risk to unexpected changes in the value of Dassault Aviation as well as to all other associated companies as remote.

For equity investments other than associates, which make up only a fraction of EADS' total assets, EADS regards the risk of negative changes in fair value or impairments on these investments as non-significant.

Treasury shares held by EADS are not considered to be equity investments. Additionally, treasury shares are not regarded as being exposed to risk, as any change in value of treasury shares is recognised directly in equity only when sold to the market and never affects net income. Treasury shares are held to hedge the dilution risk arising from employee stock ownership plans and the exercise by employees of stock options.

2. Business-Related Risks

Aircraft Market Cyclicity

In 2005, the combined revenues generated from Airbus and ATR represented approximately two thirds of EADS' consolidated revenues. Historically, the commercial passenger aircraft market has shown cyclical trends due in part to the sensitivity of passenger demand in the air travel market to growth in gross domestic product ("GDP"). The growth in EADS' commercial aircraft activities has consequently been correlated to growth in GDP. Other factors, however, play an important role, such as (i) the average age and technical obsolescence of the fleet relative to new aircraft, (ii) the number and characteristics of aircraft taken out of service and parked pending potential return into service, (iii) passenger load factors, (iv) airline pricing policies, (v) airline financial health and (vi) deregulation.

EADS and the Airbus Division have implemented a flexible manufacturing organisation that is intended to help them adapt to cyclical market changes in demand. See "Part 2 / 1.1.2 Airbus — Market". Nevertheless, EADS expects that the market for passenger aircraft will continue to be cyclical and downturns in broad economic trends, such as those currently being experienced, may have a negative effect on its future results of operation and financial condition.

Impact of Terrorism, Epidemics and Catastrophic Events On Aircraft Market

As the terrorist attacks in New York and Madrid, and the spread of the Severe Acute Respiratory Syndrome ("SARS") virus have demonstrated, terrorism and epidemics may negatively affect public perception of air travel safety and comfort and the demand for air travel and commercial aircraft. Furthermore, major airplane crashes may have a negative effect on the public's or regulators' perceptions of the safety of a given class of aircraft, form of design, or airline. As a consequence of terrorism, epidemics and other catastrophic events, an airline may be confronted with sudden reduced demand for air travel and be compelled to take costly security and safety measures. In response to such events, and the resulting negative impact on the airline

industry or particular airlines, EADS may suffer from a decline in demand for all or certain types of its aircraft and EADS' customers may postpone delivery of new aircraft or cancel orders.

Dependence on Defence Spending

In 2005, approximately 23% of EADS' consolidated revenues was derived from defence spending. In any single market, defence spending depends on a complex mix of geopolitical considerations, budgetary constraints and the ability of the armed forces to meet specific threats and perform certain missions. Defence spending may be subject to significant fluctuations from year to year and country to country. Adverse economic and political conditions, as well as downturns in broad economic trends in EADS' defence markets, may have a negative effect on EADS' future results of operations and financial condition.

In the case where several countries undertake to enter together into defence procurement contracts, economic, political and / or budgetary constraints in any one of these countries may have a negative effect on the ability of EADS to enter into or perform such contracts.

Emergence of Public-Private Partnerships and Private Finance Initiatives

Defence customers, particularly in the U.K., increasingly request proposals and grant contracts under schemes known as public-private partnerships ("PPPs") or private finance initiatives ("PFIs"). PPPs and PFIs differ substantially from traditional defence equipment sales, as they often incorporate elements such as:

- the provision of extensive operational services over the life of the equipment;
- continued ownership and financing of the equipment by a party other than the customer, such as the equipment provider;

- mandatory compliance with specific customer requirements pertaining to public accounting or government procurement regulations; and
- provisions allowing for the service provider to seek out additional customers for unused capacity.

EADS is party to PPP and PFI contracts, for example through Paradigm with Skynet 5 and related telecommunications services, and involved in additional PFI proposals, such as the Airtanker (FSTA) project. One of the complexities presented by PFIs lies in the allocation of risks and the timing thereof among different parties over the lifetime of the project.

There can be no assurances of the extent to which EADS will efficiently and effectively (i) compete for future PFI or PPP programmes, (ii) administer the services contemplated under the contracts, (iii) finance the acquisition of the equipment and the ongoing provision of services related thereto, or (iv) access the markets for the commercialisation of excess capacity. Nor can EADS be certain that it will not encounter unexpected political, budgetary, regulatory or competitive risks over the long duration of PPP and PFI programmes.

Competition and Market Access

Most of EADS' businesses are subject to significant competition, in particular in the commercial aircraft market, where Airbus has been affected by downward price pressure resulting from such competition. EADS believes that some of the underlying causes of such price competition have been mitigated by restructuring in the aerospace and defence industry. However, the recent weakening of demand has led to greater leverage for certain customers to encourage competition in respect of a variety of issues, including price and payment terms. No assurance can be given that competition may not intensify, particularly in the context of a prolonged downturn.

In addition, the contracts for many aerospace and defence products are awarded, implicitly or explicitly, on the basis of home country preference. Although EADS constitutes a multinational combination broadening a domestic market constituency, it may remain at a competitive disadvantage in certain countries, especially outside of Europe, relative to local contractors for certain products. The strategic

importance and political sensitivity attached to the aerospace and defence industries means that political considerations will persist for many products for the foreseeable future.

Availability of Government Financing

In prior years, EADS and its principal competitors have benefited from government financing of product research and development. EADS has recently received financing from certain governments in relation to the A380 commercial aircraft program, and certain E.U. countries have already committed to fund the development of the A350 commercial aircraft program. No assurances can be given that financing will continue to be made available for future projects. Since 1992, the E.U. and the U.S. have operated under an agreement that sets the terms and conditions of financial support that governments may provide to civil aircraft manufacturers. The unilateral withdrawal from the 1992 agreement by the U.S. government in late 2004 eventually led to formal claims and counterclaims being made by the U.S. and the E.U. respectively with the World Trade Organisation ("WTO"). The E.U. and the U.S. have also entered into negotiations to seek a resolution to the issues being disputed in the formal WTO process, with the goal of agreeing a new system that provides for a level playing field when funding future aircraft developments. The terms and conditions of any new agreement, or the outcome of the formal WTO proceedings, may limit access by Airbus to risk-sharing-funds for large projects or establish an unfavourable balance of access to government funds by EADS as compared to its U.S. competitors.

Technologically Advanced Products and Services

EADS develops and manufactures products and programs that are, for the most part, technologically advanced and, sometimes, novel. Most of EADS' products must function under demanding operating conditions. Even though EADS believes it employs sophisticated design, manufacturing and testing practices, there can be no assurance that EADS' products or programs will be successfully developed or operated or that they will be developed or will perform as intended.

Risk Factors

2. Business-Related Risks

Certain of EADS' contracts require it to forfeit part of its expected profit, to receive reduced payments, to provide a replacement launch or other product or service, or to reduce the price of subsequent sales to the same customer if its products fail to be delivered on time or to perform adequately. For example, EADS has commitments under telecommunication satellite manufacturing contracts that were signed during a period when tight delivery schedules were provided in these contracts, but market practice allowed extension of schedules to meet ever more complex technological requirements. No assurances can be given that performance penalties or contract cancellations will not be imposed should EADS fail to meet delivery schedules or other measures of contract performance.

EADS, like other organisations, has experienced occasional product failures and other problems. There can be no assurances that such problems will not occur in the future. In addition to any costs resulting from product warranties, contract performance or required remedial action, such failures may result in increased costs or loss of revenues and may also have a significant adverse effect on the competitive reputation of EADS' products. See "3. Legal Risks — Product Liability and Warranty Claims".

Major Research and Development Programmes

The business environment in many of EADS' principal operating business segments is characterised by extensive research and development costs requiring significant up-front investment. Business plans underlying such investment contemplate a long payback period before this investment is recouped. There can be no assurances that the commercial, technical and market assumptions underlying such business plans will be met, and consequently, the payback period or returns contemplated therein achieved.

U.K. Pension Commitments

EADS has several common investments with BAE Systems, of which the most significant in terms of employees are Airbus and MBDA. In respect of each investment, for so long as BAE Systems remains a shareholder, U.K. employees may stay in the BAE Systems pensions schemes, which currently qualify as multi-employer defined benefit plans.

BAE Systems defined benefit obligations have to be funded with post retirement pension assets. As of 1st January 2005, BAE Systems is applying International Financial Reporting Standards ("IFRS"). International Accounting Standard ("IAS") 19 "Employee Benefits" requires an entity to recognise a pension provision whenever its defined benefits plans are not sufficiently covered by corresponding asset and consequently underfunded. Applying IAS 19, BAE Systems calculated for its U.K. and U.S. pensions schemes a total underfunding amounting to £3,870 million for year end 2004. Through its investments Airbus and MBDA, EADS is potentially affected by the shortfall in BAE Systems pension schemes. However, the agreements between EADS and BAE Systems have the effect of capping the contributions that the investment has to make to the pension scheme for a certain period of time (e.g., until July 2011 for Airbus and until December 2007 for MBDA). Any additional contribution would be paid by BAE Systems. EADS is therefore not exposed to increased contribution payments resulting from the pension underfunding during the period of the contribution caps. Based on information currently available, EADS judges this information not to be sufficient to determine a reliable basis to calculate its share in the pension deficit. Consequently, EADS expenses the contributions made to the pension scheme as if the plans were defined contribution plans.

On 1st November 2003, EADS established a new pension scheme for Astrium U.K. The defined benefit obligation of the new plan, calculated as of 31st December 2005, amounts to £168 million. Plan assets are recorded at £114 million, resulting in a net liability of £54 million, which covers the maximum risk associated with the creation of the new plan. See "Notes to the Consolidated Financial Statements (IFRS) - Note 21(b): Provisions for Retirement Plans".

3. Legal Risks

Dependence On Joint Ventures and Minority Holdings

EADS generates a substantial proportion of its revenues through various consortia, joint ventures and equity holdings and believes that its alliances and partnerships are a source of competitive advantage. These arrangements include primarily:

- the Eurofighter consortium;
- two principal joint ventures: MBDA and ATR;
- majority interests: (a) Airbus, and (b) Dornier GmbH; and
- investment in associates: Dassault Aviation.

The formation of partnerships and alliances with other market players is an integral strategy of EADS and the proportion of sales generated from consortia, joint ventures and equity holdings may rise in future years. This strategy may from time to time lead to changes in the organisational structure, or realignment in the control, of EADS' existing joint ventures.

EADS exercises varying and evolving degrees of control in the consortia, joint ventures and equity holdings in which it participates. While EADS seeks to participate only in ventures in which its interests are aligned with those of its partners, the risk of disagreement or deadlock is inherent in a jointly controlled entity, particularly in those entities that require the unanimous consent of all members with regard to major decisions and specify limited exit rights. The other parties in these entities may also be competitors of EADS, and thus may have interests which differ from those of EADS.

In addition, in those holdings in which EADS is a minority partner or shareholder, EADS' access to the entity's books and records, and as a consequence, EADS' knowledge of the entity's operations and results, is generally limited as compared to entities in which EADS is a majority holder or is involved in the day-to-day management.

Product Liability and Warranty Claims

EADS designs, develops and produces a number of high profile products of large individual value, particularly civil and military aircraft and space equipment. EADS is subject to the risk of product liability and warranty claims in the event that any of its products fail to perform as designed. While EADS believes that its insurance programs are adequate to protect it from such liabilities and that no material claims have been made against it, no assurances can be given that claims will not arise in the future or that such insurance cover will be adequate.

Export Controls and Other Regulations

The export market is a significant market for EADS. In addition, many of the products EADS designs and manufactures for military use are considered to be of national strategic interest. Consequently, the export of such products outside of EADS' domestic markets may be restricted or subject to licensing and export controls, notably by the U.K., France, Germany and Spain, where EADS carries out its principal military activities as well as by other countries where suppliers come from, notably, the U.S. There can be no assurance (i) that the export controls to which EADS is subject will not become more restrictive, (ii) that new generations of EADS products will not also be subject to similar or more stringent controls or (iii) that geopolitical factors will not make it impossible to obtain export licenses for one or more clients or constrain EADS' ability to perform under previously signed contracts. Reduced access to military export markets may have a material adverse effect on EADS' business, financial condition and results of operations.

EADS is also subject to a variety of other governmental regulations that may adversely affect its business and financial condition, including among others, regulations relating to the protection of the environment, the use of its products, labour practices and dealings with foreign officials. In addition, EADS' ability to market new products and enter new markets may be dependent on obtaining government certifications and approvals in a timely manner.

4. Industrial and Environmental Risks

Together with other companies in the principal industries in which it operates, EADS is subject to numerous E.U., national, regional and local environmental laws and regulations concerning emissions into the environment, discharges to surface and subsurface water and the disposal and treatment of waste materials. EADS believes that its current operations are in substantial compliance with all applicable environmental regulations. EADS believes that it is currently capable of satisfying the stricter environmental standards for the future contemplated by current laws or

regulations, including increasingly stringent environmental product quality standards that will be implemented over the next few years, without incurring significant capital expenditure. However, there can be no assurance that increased capital expenditure and operating costs resulting from future environmental regulations will not adversely affect the results of EADS' operations and its financial condition.

For more information, please see "Part 2 / 2.3 Environmental Care".