

President and CEO of Atlas Copco Gunnar Brock's address to the shareholders on April 27, 2006

Translated from his speech.

Dear shareholders, ladies and gentlemen! One year has passed since many of us last met here in Aula Magna.

I would like to describe events of the past year and then devote some time to explaining how we will fulfill and achieve our goals – an aspect that is most emphatically progressive and looks to the future.

Let's first study some of the things that have happened. The group is currently undergoing a transformation of sorts. If we look at what we today offer our customers, naturally we find the same core competence that we have had for many years. That is why I am showing the somewhat dated picture we see here – to demonstrate that Atlas Copco does possess a strong past and it is upon this foundation we continue to build.

Nowadays we talk about the mining and construction industry. This is a customer group that we have served for many years. We talk about compressor business, compressors and air treatment systems. We have Industrial Technique, which today is considerably smaller after our divestment of electrical tools. Once we have sold the rental business we call *Rental Service* or equipment rental to the construction industries, we will still have some operations within both CMT - *Construction and Mining Technique* - and *Compressor Technique* in respect to renting our own designed and manufactured special products.

More and more we provide our customers with services. More and more emphasis is on expertise. We try to erect walls around our customers to defend ourselves against the competition. These walls are created not only in Sweden, but around the world through a rather ingenious global network where we have production in many countries. We have both R&D activities and application expertise in many countries. All of which we are tying together. Today, we provide our customers with both products and, to a greater extent, services and expertise.

Let us summarize the year 2005. I think we can say we successfully exploited our strong market position and we will continue to build on our position. This resulted in excellent sales and profit figures.

Let us study our target fulfillment rate. We see that we exceeded our goals in 2005. Our growth rate is at 8% and we need to remember that the underlying demand in the industries where we are active is about 2-4% with GNP. In other words this means that our growth is more than double. 8% may appear modest, but this figure must be viewed in relation to the economy in which we do business.

We talk about reaching a 15% operating margin and here too we have succeeded. As we can see, we accelerated toward the close of the period. Return on capital should exceed capital cost and is currently at about 11-11.5% for the Group.

Even more interesting perhaps are the components that together produce these results. We see here that Compressor Technique had an operating margin of almost 20% in 2005 and about a 70% return on capital. Construction and Mining Technique has gradually confirmed its position as leading provider the last four-five years and achieved excellent results both in terms of growth and operating profit.

Industrial Technique, the smallest of the three industrial business areas, reports very good profitability and growth. Rental Service continues to do well.

What does all this mean for our preferred target group – all of you here? We have been grateful for the past three years of growth and in particular the growth seen as we reached the close of the period. If we look at what we call total yield – which is a function of both share prices and dividends – we see that this has also been good during the period.

We announced on February 2 that we were going to sell and divest our business area, Rental Service, for reasons that we described in detail at the time. It is a very different type of business in relation to the other segments of Atlas Copco, our traditional industrial businesses. It is capital intense with severe seasonal fluctuation. It is also actually only related to North America and it would require enormous capital investments were we to globally expand. We would also face competition with many of our largest customers since we have quite a few product categories that we sell to rental companies.

So much for background. It is gratifying that the business is doing well when we are in the midst of this type of sales process. We have reached a situation where we have a well-functioning business to sell. The time schedule mentioned in February, namely that we expect to have closed a deal by mid year, still applies.

Our target of 8% growth and a 15% operating margin and thereby also a return on capital that exceeds costs, stands firm. We will generate a great deal of value if we are successful.

How then are we to manage to grow by 8% per year when the underlying market growth only motivates 2-4% if we retain our market share? Foremost of course is a strong portfolio of products and services and market leading positions. Our size needs to be considerably larger in relation to number two on the market.

Product development

But in the long run, only one factor generates long-term sustainability and good margins. Naturally, this is a product development that continuously generates new products. We can measure this in many ways. We can measure engineers, money, patents, and drawings. But in the end, there is only one sane way to look at it and that is to see how much of our sales comes from new products. If the age profile is too unfavorable, then we have an unfortunate exposure. We try to run all business areas so that about half of our sales stem from products that are a maximum three years old. It is crucial that we remain aware, focused and study the trends. It might be a bit more and it might be a bit less now and again, but we must also be on our guard for regeneration.

I am going to show a few examples of what has happened the past year with regard to product development. This issue has another aspect - namely that every time you have a new product you have the opportunity to talk price, raise the price and improve the margins – a higher price and a lower cost for the product.

What I am showing here is a portable compressor I think we all recognize. This was Atlas Copco to me long before I joined Atlas Copco. It shows that this is not a dead product although it has been around for decades. We launched a very successful new model of a portable compressor last year called the Hard Hat.

It is not only rugged, it also makes less noise. It requires less power and has lower maintenance costs. In other words, quite a few features that makes this an incredible hit for the business. It doesn't make much noise, I said. CMT has also joined in the battle against noise and produced an interesting drilling rig.

You might wonder if this is something worth bragging about. It may not make much difference if you are standing in northernmost Sweden or Alaska. But increasingly more of these types of rigs are working in cities or metropolitan areas, meaning you cannot work if you have a noise level like its previous generations. This is actually a very practical useable development concept that has caught on quickly.

The third business area, Industrial Technique, also reports an incredible innovation rate. I should perhaps mention that this is the business area in which we presently invest most, relatively speaking. We invest about 5% of our sales in product R&D. That is a lot. See it as a minor insurance to cover the incredibly strong market position that this product area holds.

Today, I am particularly pleased to show one special product development, since the person that has improved and developed our famous tightening tool Tensor will be awarded the John Munk award later today. The award goes to Karl Brodin, who has done a fabulous job in developing a tightening instrument that is already far superior to anything our competitors have. This tool is much faster than earlier generations. Can such a minor difference really be important? Yes. Over an extended period it makes an incredible difference in a car factory assembly line. This is not only a mechanical product - a huge amount of software was also used to make this tightening tool. The combination of traceability after tightening and an ergonomically designed product is an enormous contribution.

Market presence

We talked about strategic initiatives. The past three years, the Group has been focused on four markets - India, China, Russia and the United States. Our interest in India, China and Russia is perhaps evident. As for the United States, we decided a few years ago that we were not achieving the success rate we wanted over there. Our relative share in relation to other countries was in fact lower.

We have measured this. Every year for the past three years we have managed to grow by 50% in Russia, 26% in China and 30% in India. Now if we look at the industrial activities in the United States, not including interest, we have grown by 30% per year.

What is important about these initiatives? Anyone can produce. It doesn't take long to learn to produce in China. After 6-12 months, most of our competitors can have production up and running. What takes incredibly longer however is replicating a market presence.

In China we have 102 offices with Chinese colleagues that speak Chinese and know their customers and their local markets. No one else even comes close. This is a mighty weapon against our competitors – much stronger than local production.

We don't have 102 offices in India because India has a completely different industrial structure. We are where we need to be in India.

Let's jump over to Russia. We will soon have 30 offices stretching east to west. None of our competitors have a similar presence. This means we should feasibly be where the business is. In some cases we are the only ones there.

This market development is crucial for us. It is also relatively low risk. We build gradually with several aftermarket engineers and more sales representatives. There are no major initial investment costs. We can stop when we want if we feel the yield on our investment is too low.

Multibrand strategy

The Peter Wallenberg award, will be awarded to two gentlemen, Christian Rougeron and Jean Guerin, who have worked diligently with what we call multi-brand strategy. It is another way to increase our presence, to try and divided the market into segments with common characteristic buying and other customer-related patterns, so as to thereby identify the right price level and right competitive situation.

They have very intelligently managed to market three different compressor brands in France thereby expanding the entire market for Atlas Copco considerably more than would otherwise have been possible. This is very delicate work. Customers are very quick to realize that you have the same product, even if it has a different name, just by going through another channel. This was ingeniously done.

I just want to point out that using several brands is an important step in development, particularly in the compressor segment but also in industrial tools. We can implement this for products with longer lifecycles while managing several brands in other industries may prove more difficult. Product differentiation is important but fully possible for us.

The aftermarket

Another factor that leads me to believe we can sustain our 8% is our substantial investments in the aftermarket. The past three years we have acquired between 20 and

45% more sales reps, aftermarket engineers and service engineers that are in daily contact with our customers.

This market is growing even when the product market is not. This market is less sensitive. And this market is extremely profitable. An aftermarket that works smoothly allows us to build customer loyalty. It is part of our strategic initiatives in which we are involved with both a sales organization and aftermarket on our prominent markets.

Acquisitions

Businesses cannot have only organic growth. We are forced to and want very much to buy associated products and applications. We say that about two-thirds of the 8% will be organic growth. The remaining one-third will be realized through acquisitions. Obviously, these kinds of deals are not standing in line, but occur when there is a willing seller and a price both can agree on. I believe this will prove to be a good solution over time.

We perform continuous strategic reviews of all our 15 divisions in which we study which types of companies, applications and products we want to access. The closer to our core business – for example, we may gain new products for our existing channels or gain new channels where we can introduce our existing products – the stronger and more profitable the outcome.

The further down the value-creating chain we come, the more diffuse and difficult it becomes. We have an excellent example in our acquisition of Ingersoll Rand Drilling Solutions' above-ground drilling rigs two years ago. These were products we did not have at the time and we introduced them in our channels. They in turn had excellent distribution channels in the US where we could introduce our products.

During 2005, we acquired Intermech at New Zealand. This is an interesting application for compressed natural gas for cars. We presently have a superior range of hydraulic, handheld demolition and drilling equipment manufactured by the acquired company Lifton in Bulgaria.

And finally, we made a rather unexpected acquisition. We bought Fuji, an entire Japanese company. Japanese management with 100% Japanese ownership. This acquisition gave us 10% of the Japanese market for industrial tools. This company is included in our regular financial reports as of one month.

Atlas Copco stands strong

When we look at our operating margin, we can say that many of the arguments intended to generate 8% growth will also generate a margin about where we want it. It is vital that we put enough time and effort into becoming proficient at pricing and understanding the mechanisms related to pricing so we do not give away or offer rebates but instead truly use and apply the full potential of our products.

In terms of how we intend to tie everything together I want to say that we adhere to the philosophy that *everything that can be made mobile will be made mobile*. We do not want fixed, large-scale investments. We want flexibility and streamlined flows. We want to

standardize our products. We do not want customized solutions unique for each customer but instead want to standardize our products as much as possible. In this way we will create profitability, efficiency and quality.

We presented our Q1 results a few hours ago. You could say that we are grateful. We have for a rather long time not only maintained a rather high level and rate but now shifted into higher gear. We had an incredible volume increase. Our operating margin climbed as did our earnings per share and return on capital.

The acceleration we see here is interesting. I believe some of this stems from our efforts to get closer to our customers and expand our presence.

On behalf of Atlas Copco I would like to thank you all for your support these past years. I sincerely hope that you find it worthwhile to continue to support us. Thank you all!