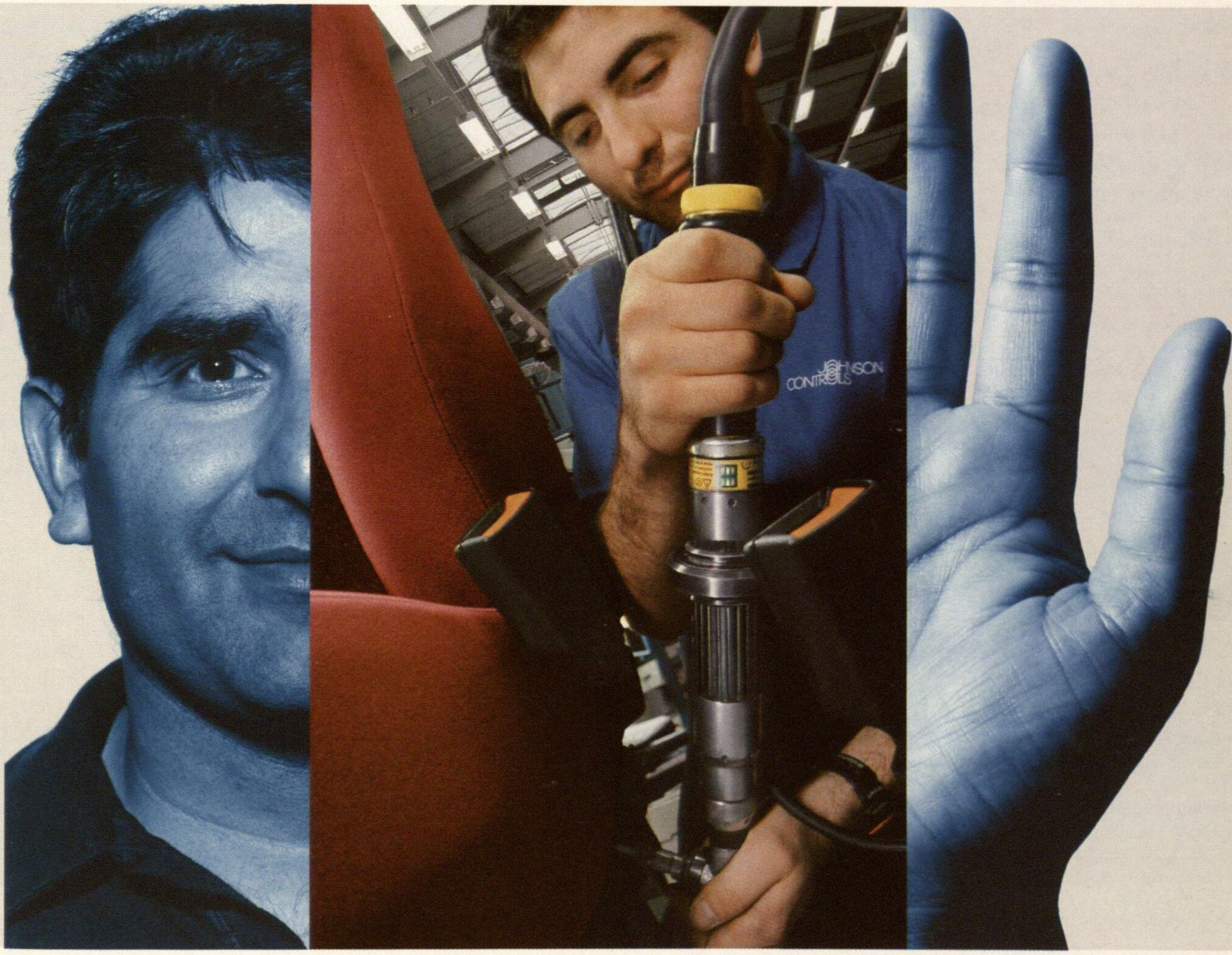
Atlas Copco

97

Annual Report 1997



In 1997, Atlas Copco's operations continued to grow. Revenues increased by 20 percent to SEK 30,032 m. and profit after financial items rose by 15 percent to SEK 3,520 m. Earnings per share amounted to SEK 12.03, compared to 10.56 in the preceding year.

Atlas Copco

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Atlas Copco AB
A Public Company (publ)

Invitation to participate in the Annual General Meeting

Atlas Copco shareholders are hereby notified that the Company's Annual General Meeting will be held on Thursday, April 16, 1998, at 5 p.m. in **Berwaldhallen,** Strandvägen 69, Stockholm.

Financial Information from Atlas Copco

Atlas Copco will publish the following financial reports on 1998 operations:

President's Address to Shareholders at the AGM	April 16, 1998
Interim Report on first three months of operations	April 27, 1998
Interim Report on first six months of operations	August 4, 1998
Interim Report on first nine months of operations	October 22, 1998
1998 Preliminary Year-end Report	February, 1999
1998 Annual Report	March, 1999

Additional copies of Atlas Copco's Annual Report in English can be ordered through Atlas Copco AB, Corporate Communications, SE-105 23 Stockholm, Sweden, Fax: +46-8-643 3718.

Financial Information on Atlas Copco

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Aros Fondkommission, Stockholm	*Per Collén and Mikael Sens*
Banque Paribas, London	*Christian Diebitsch*
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Cover illustration

Johnson Controls is the world's largest independent supplier of automotive seating systems. The company has invested in Atlas Copco's electronically controlled tool Tensor S for tightening of critical joints. The cover photo shows tightening of safety belts at the plant in Schwalbach, Germany.

Atlas Copco 1997

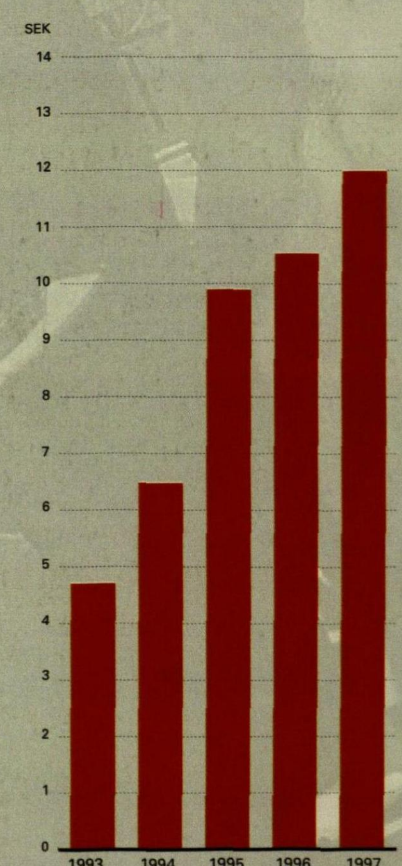
Acquisition Atlas Copco acquired Prime Service, one of the largest equipment rental companies in the USA. This is in line with the strategic direction to increase revenues related to "use of products" such as spare parts, maintenance and accessories as well as equipment rental.

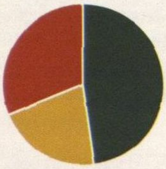
Sales The revenues increased 20 percent to SEK 30,032 m. (25,121).

Earnings The operating profit after financial items rose by 15 percent to SEK 3,520 m. (3,070), corresponding to a profit margin of 11.7 percent. Net profit after tax amounted to SEK 2,208 m. (1,938). Earnings per share rose to SEK 12.03 (10.56).

Dividend The Board of Directors proposes a dividend of SEK 4.25 SEK (3.75) per share.

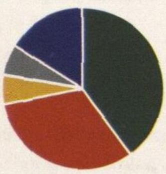
Trend of earnings per share





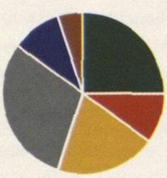
Revenues by business area

- Compressor Technique 48%
- Construction and Mining Technique 21%
- Industrial Technique 31%



Geographic distribution of revenues

- Europe incl CIS 40%
- North America 32%
- South America 6%
- Africa/Middle East 6%
- Asia/Australia 16%



Revenues by customer category

- Engineering Industry 25%
- Automotive Industry 10%
- Process Industry 20%
- Building and Construction Industry 30%
- Mining Industry 10%
- Other 5%

Focus on growth

Growth in order to secure long-term profitability is a top priority for the Atlas Copco Group. The target is an annual sales growth of 8 percent during a business cycle. One strategic direction for growth is services related to "use of products".

Atlas Copco is an international group of industrial companies, with its head office in Stockholm. Of revenues amounting to SEK 30 billion, 97 percent is attributable to countries outside Sweden. The Group has approximately 24,000 employees, of whom 12 percent work in Sweden.

The company, founded in 1873, has been listed on the Stockholm Stock Exchange since 1920 and is also quoted on the London, Frankfurt, Düsseldorf and Hamburg stock exchanges.

Business concept

The Group's business concept is to provide a broad range of products and services which meet the needs of customers in the areas of:

- air and gas compression, as well as air treatment;
- industrial manufacturing and the automotive after-market;
- rock excavation, light construction and demolition;
- installation, equipment rental, repair and service.

Five key strategies

Growth in order to secure long-term profitability is a top priority. This shall be achieved through three main directions. Firstly, organic growth by bringing new products – developed from core technologies – and new applications to new markets. Secondly, strengthening the presence in Asian markets. Finally, increasing revenues related to "use of products", such as maintenance, spare parts and accessories as well as equipment rental.

Most divisions are *product driven* in order to give each product the best chance in the market to satisfy customer needs. Each division is specialized within a specific product area and has total responsibility for product development, manufacturing, and sales and service operations.

This strategy has been complemented by a *customer driven* approach for operations which are specialized in services related to "use of products". This means that the range of products offered can also include products which are not manufactured by Atlas Copco.

Development of the Group is safeguarded by both continuous improvement of existing operations and new development of work processes, products, among other areas.

The *multi-brand* strategy plays a significant role for the Group. Products are differentiated and are marketed via various brands through different distribution channels in order to better satisfy specific customer needs.

Targets for profitable growth

The financial target is to achieve a profit margin after financial items of at least 10 percent during a business cycle. During the last five years the Group's profit margin has averaged 10.6 percent. In 1997 the profit margin amounted to 11.7 percent.

The growth target is an average annual sales growth of 8 percent during a business cycle.

Since 1990, annual growth has averaged approximately 7 percent, mainly due to acquisitions.

Acquisitions 1993–1997

1993: Acquisitions of Robbins, USA (CMT); Kango, UK (IT); and Worthington-Creyssensac's compressor operations in Europe (CT). Creation of joint venture, Nanjing Atlas Copco Construction Machinery, in China (CMT).

1994: Creation of joint venture, Wuxi-Atlas Copco Compressor Company in China (CT). Acquisition of Hamrin Adsorptions & Filterteknik, Sweden (CT).

1995: Creation of joint venture, Atlas Copco Changchun Electric Power Tool, China (IT). Acquisitions of Socapel, Switzerland (IT); Milwaukee Electric Tool Corporation, USA (IT); and ABB's operations within the pressure let-down application area (CT).

1996: Acquisitions of IRMER+ELZE's portable compressor and pneumatic breaker operations, Germany (CT); and Elesta Automation AG, Switzerland (IT).

1997: Creation of joint venture for production of oil-injected screw compressors with Shanghai General Machinery Group in China (CT). Acquisitions of Thomé-Crépelle, France (CT); Prime Service, USA (CT); Hubert Davis, South Africa (CMT); and Ceccato's compressor operations, Italy (CT).

The abbreviations in brackets above correspond to the business areas Compressor Technique (CT), Construction and Mining Technique (CMT) and Industrial Technique (IT).

These businesses which have been acquired the last five years, including joint ventures, accounted for 20 percent of Group sales in 1997.

The Group also has qualitative objectives. Firstly, all products and services should increase customers' productivity. Secondly, divisions shall achieve leadership in the area of environmental protection in order to strengthen the businesses.

Strong market presence

Atlas Copco manufactures products at 58 plants in 14 countries. The major share of manufacturing is conducted within Europe, but an increasing number of plants are also located in the U.S. and in Asia.

Organization

Board of Directors

President and Chief Executive Officer

Executive Group Management and Corporate Functions

Business areas		
Compressor Technique	**Construction and Mining Technique**	**Industrial Technique**
Divisions		
Airtec **Portable Air** **Industrial Air** **Oil-free Air** **Atlas Copco Applied Compressor and Expander Technique** **Prime Service**	**Atlas Copco Rock Drilling Equipment** **Atlas Copco Craelius** **Uniroc** **Atlas Copco Construction Tools** **Atlas Copco Wagner**	**Milwaukee Electric Tool** **Atlas Copco Electric Tools** **Atlas Copco Industrial Tools and Equipment** **Alliance Tools**
Product areas		
Industrial compressors Portable compressors Gas and process compressors Equipment rental	Drilling rigs Rock drilling tools Construction tools Loading equipment	Power tools Assembly systems Motion control products

Operations are conducted through 15 divisions in the business areas Compressor Technique, Construction and Mining Technique and Industrial Technique.

The Atlas Copco Group has a strong market presence and strives to maintain close and long-term relationships with its customers. Products are marketed through the Group's own sales operations in some 70 countries and through distributors in another 80 countries.

Europe has been the dominant Atlas Copco market for many years, accounting for more than 50 percent of revenues. Primarily due to the acquisition of Milwaukee in 1995 and Prime Service in 1997, America's share has increased to nearly 38 percent, while Europe/Africa's share has decreased to 43 percent. Asia/Australia accounts for 19 percent. The long-term prospects for growth in Asian markets have resulted in an increased focus in this region.

Many application areas for compressors

Compressor Technique covers the following product areas: portable compressors, industrial compressors, and gas and process compressors. In addition Prime Service's operations for equipment rental is included in this business area.

Portable air compressors are a reliable power source for machines and tools used mainly within the building and construction sector, but also in other industries.

Originally, industrial air compressors were used as a source of power, but now compressed air is used increasingly as an active part of vari-

Primary factors affecting Atlas Copco Group sales

	Capital Goods 55%	Expendables and services 45%
Industry	Industrial Machine Investments	Industrial Production
Construction	Public Investments	Construction Activity
Mining	Mining Machine Investments	Metal and Ore Production

Revenues from expendables and services have increased mainly due to the acquisitions of Milwaukee Electric Tool and Prime Service.

ous production processes. This application area demands specific air quality. Clean, dry quality air is of crucial importance in i.e. the sensitive electronics industry. Another example is the use of oil-free air during the production of flavor additives for certain food products. To meet the increasing demand for quality air, Atlas Copco offers drying equipment and filters as an integrated part of the compressor package.

Gas and process compressors and expansion turbines are delivered to process industries, such as the chemical, oil and gas industries, as well as to companies specializing in the separation of air and other gases.

Complete supplier of drilling equipment

Construction and Mining Technique offers a wide range of products and services, from pneumatic breakers to packaged solutions for major construction and mining projects.

Drilling rigs are used in tunneling operations, mining and surface drilling operations in construction work and quarrying.

Geotechnical drilling equipment is used mainly in water-well drilling and in construction related drilling such as geotechnical surveys and straight long-hole drilling.

In order to be able to offer a complete range of drilling equipment, Atlas Copco manufactures and markets various rock drilling tools, such as drill steel, drill bits and cutters.

Light rock drills and breakers are used by contractors in the construction sector for demolition. Loading equipment and trucks are used mainly in underground mining operations, as well as in certain construction projects.

From industrial tools to systems

Industrial Technique's product areas consist primarily of power tools, assembly systems and sophisticated motion control products.

Tools powered by compressed air or electricity have many applications within industry, such as drilling, grinding, riveting and tightening of nuts and screws. Electric tools are used extensively within the building sector.

Assembly systems, with computerized control systems, are supplied primarily to the automotive industry and its suppliers. The equipment is used for nut tightening in fixed installations where particularly high precision is required.

Motion control products are used in complex industrial machines and industrial vehicles. The market for such equipment is growing rapidly, due to the increasing need to automate production within industry and the need for better process control.

Main driver is investments in capital goods

The Group is affected by the investments in capital goods made in various areas in the private and public sector, i.e. the manufacturing process or construction of roads.

Sales are mainly influenced by manufacturing industry's machinery and equipment requirements. The largest segment within this sector is the automotive industry, which needs substantial volumes of industrial tools, assembly systems and compressors. Other important segments are the electronics and pharmaceutical industries, which need industrial compressors for their sensitive production processes.

Infrastructure projects are important for Atlas Copco's sales of construction equipment, including drill rigs, breakers, and portable compressors. Infrastructure projects, such as building railways, highways and power plants, are often dependent on political decisions.

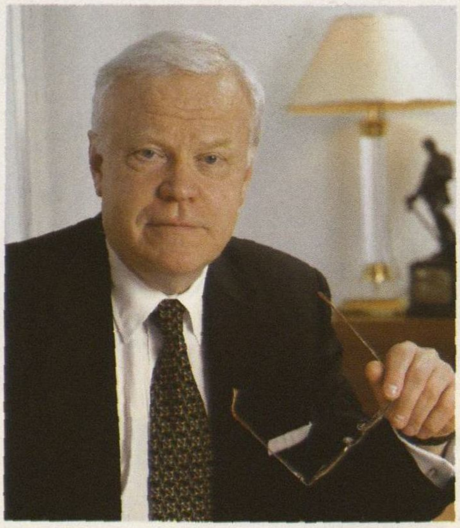
To a large extent, mining-industry demand for drilling equipment and loaders, follows the manufacturing industry's business cycle. Indicators for demand are price and inventory trends for metals.

An increase in the sale of capital goods means in turn that demand for expendables and services also increases. For example, customers will need certain tools, spare parts, drill bits and accessories on a continuous basis. Demand for these products and services is relatively stable compared with capital goods which is more cyclical. These products and services account for approximately 45 percent of Group revenues.

The new generation of surface rigs sets a new standard in ergonomics, offering the operator a completely new working environment.

Dear Shareholders!

In 1997, Atlas Copco strengthened its leading position in the world market. The Group raised its target rate of growth and expanded through extensive marketing initiatives and strategic company acquisitions. At the same time, healthy growth in profitability was sustained.



Europe is still Atlas Copco's domestic market as well as its biggest one. The outstanding sales growth of 1997 originated in the North American market, in great part owing to a major, strategic acquisition. Developments in Europe were influenced by slow growth and the efforts of governments to strengthen their budgets in countries striving to qualify for the European Monetary Union. Such efforts led to low activity in the building and construction business once again this year, while demand in the manufacturing industry was satisfactory.

The economic crisis in Asia has had no noticeable impact on the Group's sales in 1997. However, it is uncertain precisely how the crisis will impact the economies of the OECD countries, which account for the major part of the Group's sales.

As I advised you in last year's annual report, Atlas Copco's sharper focus on growth will be accomplished by expanding market shares in Europe and North America and especially by investing in markets enjoying rapid growth. The biggest potential lies in Asia. Atlas Copco stands firm by its goal to grow in this region, although the Group must take certain measures in the short term to respond to the temporary drop in demand.

A strategic direction for Atlas Copco is to boost revenues from equipment rental and after-sales service. One result of this orientation in 1997 was the strategic acquisition of Prime Service in the U.S., which has transformed Atlas Copco into a major player in the market for equipment rental. This business has generated a higher rate of growth than many other industries, and ongoing growth is expected. By acquiring Prime, Atlas Copco also realized a more even distribution of sales between Europe and the Americas.

The Group's target rate for annual growth has been lifted from 5 percent to 8 percent as a result of its emphasis on growth. Over the business cycle, the Group aims to achieve an average before-tax profit margin of at least 10 percent.

Robust expansion demands steady operating cash flow, which Atlas Copco has also admirably delivered. The additional capital required for the huge Prime acquisition meant that the Group's net indebtedness increased markedly. At the same time, the balance between borrowed capital and shareholders' equity shifted, reducing the Group's average cost of capital.

We shareholders have reason to be pleased with the advance of Atlas Copco's share price and its dividends, which together have generated an average return of 30.8 percent annually during the past five years. Having taken into account the Group's healthy earnings and strong operating cash flow for the year, the Board of Directors proposes the dividend be raised SEK 0.50, to SEK 4.25 per share.

Shareholders can be quite pleased with the Group's performance in 1997, which surpassed the record-breaking year of 1996. Accordingly, I wish to convey the Board's sincere gratitude to the management team and indeed all employees for their efforts during the year. Strong commitment and a comprehensive program for growth have further improved results and fortified the Atlas Copco Group as a whole.

Anders Scharp
Chairman

The Board of Directors' Report on 1997 Operations

SEK m. unless otherwise indicated

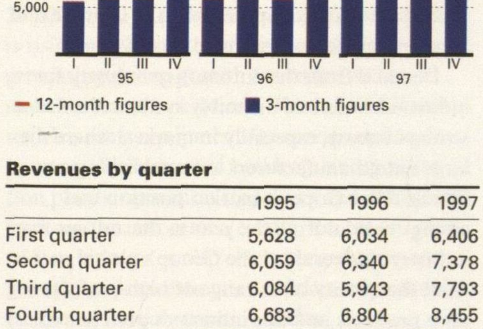
Atlas Copco Group revenues in 1997 increased 20 percent to SEK 30,032 m., compared to SEK 25,121 m. in 1996. Markets outside Sweden accounted for 97 percent of revenues. Orders received amounted to SEK 30,685 m. (25,159). For comparable units, revenues increased 13 percent, and orders received were up 15 percent. The exchange-rate differences, primarily the strengthening of USD, had a positive effect of approximately 7 percent on both revenues and orders received. Atlas Copco Group profit after financial items rose 15 percent, to SEK 3,520 m. (3,070). The profit margin was 11.7 percent (12.2).

	1997	1996
Revenues	30,032	25,121
Change, %	+20	+3
Orders received	30,685	25,159
Change, %	+22	+1
Profit after financial items	3,520	3,070
Change, %	+15	+8
Profit for the year	2,208	1,938
Change, %	+14	+6

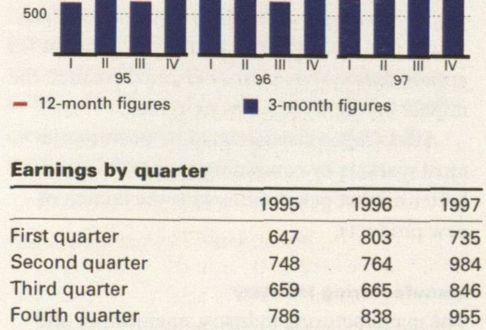
Dividend The Board of Directors proposes a dividend of SEK 4.25 (3.75) per share.

Market outlook for 1998 The recent positive trend in Europe is expected to continue in 1998. Demand in the U.S. is expected to remain on a good level, while a decrease is likely in South America. One concern, however, is the potential impact of economic development in Asia on those markets. Demand in Asia, with the possible exception of China, is in general foreseen to remain low. This will also negatively affect in particular the mining industry worldwide and delay construction projects in the region.

Revenues



Profit after financial income and expense



Revenues by quarter

	1995	1996	1997
First quarter	5,628	6,034	6,406
Second quarter	6,059	6,340	7,378
Third quarter	6,084	5,943	7,793
Fourth quarter	6,683	6,804	8,455
Total	24,454	25,121	30,032

Earnings by quarter

	1995	1996	1997
First quarter	647	803	735
Second quarter	748	764	984
Third quarter	659	665	846
Fourth quarter	786	838	955
Total	2,840	3,070	3,520

Structural changes

Effective July 1, 1997, Atlas Copco acquired Prime Service, Inc., one of the largest equipment rental companies in the United States, for approximately SEK 7,000 m. Atlas Copco also assumed interest-bearing debt of approximately SEK 1,950 m. Prime Service was listed on the New York Stock Exchange. At the acquisition date, Prime Service had 2,200 employees and operated 122 equipment rental locations in 14 states with a base of more than 40,000 customers. Revenues in 1996 were approximately SEK 2,500 m. with operating earnings of SEK 510 m. Since the acquisition, Prime Service has acquired five equipment rental companies in the U.S. with yearly revenues of approximately SEK 560 m. Prime Service constitutes a separate division within the Compressor Technique business area.

Effective January 1998, Atlas Copco acquired the Ceccato industrial compressor business, based in Vicenza in northern Italy. The company, which manufactures and markets small and medium-sized industrial compressors, has annual sales of approximately SEK 200 m. and employs 125 people. Ceccato is part of the Industrial Air division.

During the year, the decision was taken to phase out Atlas Copco's tunnel-boring machine (TBM) operations, which are conducted within the Atlas Copco Robbins division. Raise-boring machines and cutters will be transferred to other divisions within the Construction and Mining Technique business area. Of the division's 115 employees, approximately 80 will be affected by the restructuring. The estimated restructuring cost, SEK 50 m., was charged to 1997 earnings.

Market review

	1997	1996	Change %
Orders received			
Compressor Technique	14,699	11,012	+33
Construction and Mining Technique	6,652	5,867	+13
Industrial Technique	9,334	8,280	+13
Atlas Copco Group	30,685	25,159	+22
Order backlog, Dec 31	4,587	3,728	+23

Demand for Atlas Copco products increased in several markets, particularly in Japan, China, Australia, Latin America, and South Africa. Sales remained high throughout 1997 in southern European markets and increased gradually during the latter part of the year in Europe's main markets, most notably in Germany and France.

The economic and financial unrest in Asia was concentrated in Southeast Asia and South Korea, but since these markets only account for approximately 4 percent of Group revenues, the impact on the Group was marginal.

Atlas Copco strengthened its positions in most markets by combining acquisitions and better market penetration with the launch of new products.

Manufacturing industry
The manufacturing industry, engineering and process companies, accounts for about 55 percent of Atlas Copco Group revenues. The demand from this sector in Europe improved gradually during the year, particularly in such major markets as Germany and France, while some decline was noted in the U.K. Demand in the North American industry remained at a good level.

During the year, an increase in demand was noted for almost all the different types of compressors and air treatment equipment offered by the Group. Manufacturing industries as well as the food, pharmaceutical, air separation and petrochemical industries sustained steady demand. This pattern prevailed in most parts of Europe as well as in North and South America and several Asian markets.

Group sales of industrial power tools to the engineering sector showed a slightly upward trend in Europe and North and South America. Orders received for electric power tools were favorable in the U.S. and Europe except in Germany. The Asian markets, specifically the Chinese and Japanese markets, developed positively.

Demand from the automotive industry for industrial tools and assembly systems showed a strong increase, especially in markets where the large auto manufacturers are establishing new plants. Atlas Copco's market position was strengthened during the year in the automotive industry as a result of the Group's global presence, the quality of its range of high-performance products and this industry's preference to purchase from global suppliers.

Revenues and orders received
SEK m.

Building and construction industry
Activity in the building and construction industry remained weak. A large number of international infrastructure projects have been delayed pending political decisions or financing.

A positive trend in sales of large drilling rigs was noted particularly during the second half of the year in southern Europe and in certain South American and East Asian markets. Despite weak market demand, Atlas Copco was successful in receiving orders for major construction projects, mainly as a result of improved delivery reliability and a high level of service. Orders received for portable compressors within this sector increased in Europe and South America.

The building and construction industry accounts for about 30 percent of Group revenues.

Mining industry
Demand from the mining industry remained favorable as a result of the mining companies' continued need for productivity improvements. Substantial orders for drilling rigs were taken in Latin America, East and Central Europe, and southern Africa. Sales of rock drilling tools and loaders increased, primarily in North and South America and Australia. Investments in equipment to prospect for new ore bodies increased among existing mines.

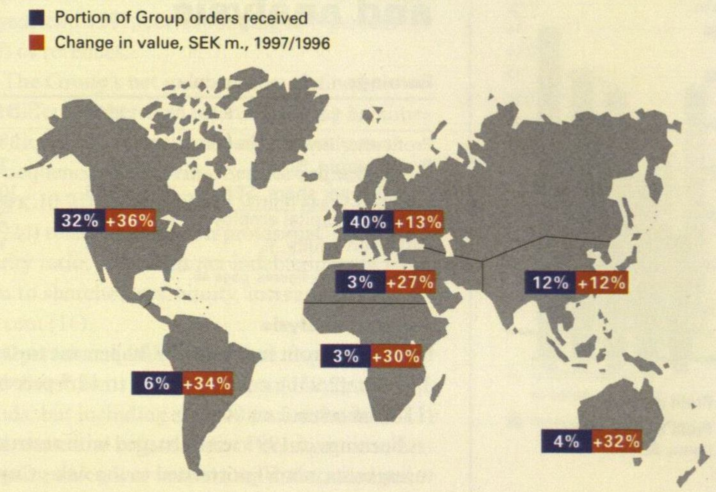
Of total Group revenues, the mining industry accounts for about 10 percent.

Equipment rental
The acquisition of Prime Service provides Atlas Copco with a leading position in the U.S. equipment rental sector, a business that concentrates mainly on contractors and process industries. Thus, the customers can focus on their core operations and gain access to equipment that offers state-of-the-art technologies.

The U.S. equipment rental market is very large. The market is estimated to exceed USD 20,000 m.* The percentage of rented machines is rising in relation to purchased machines, generating strong growth for construction machine rental operations. The industrial sector also rents equipment for service and maintenance of commercial buildings and production plants, operation stoppages and emergency back-up for unforeseen events. Rental of industrial equipment is also characterized by strong growth, with an estimated market value equal to that of the construction sector.

Rental of light construction equipment and machinery to small and medium-sized industrial companies has shown relatively low sensitivity to economic business cycles.

Geographic distribution of orders received

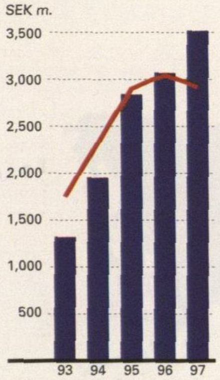


Growth markets
The present financial and economic difficulties in Asia, which particularly affected South Korea and Southeast Asia, have led to lower demand in the region. The present situation has not changed the Group's long-term ambition, to have one third of worldwide turnover in the region, but short-term adjustments are required. During 1997, Atlas Copco's joint ventures have been further developed in Asia, and the ownership structure has been reinforced. Management has been strengthened, and extensive training programs have been conducted.

Eastern European markets continued to show favorable development during 1997. In Russia, where the Group established a new sales company during the year, substantial orders were booked for drilling and loading equipment. Poland accounted for the Group's strongest growth in East Europe last year. A favorable increase was also noted in deliveries to Slovakia, including orders for drilling equipment and accessories, and to Macedonia for mechanization of mines.

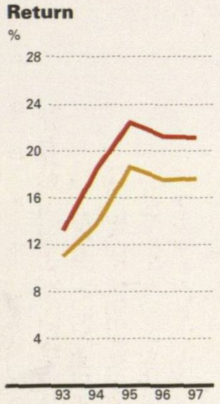
*Source: Bowles Hollowell Conner & Co, 1998

Earnings and profit margin



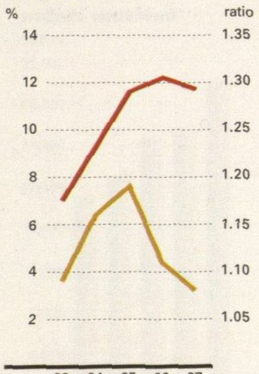
– Profit margin, %
■ Profit after financial items, SEK m.

Return



– Return on capital employed
– Return on equity

Profit margin and capital turnover



– Profit margin, %
– Capital turnover, ratio

Financial summary and analysis

Earnings

	1997	1996
Profit after financial items	3,520	3,070
Profit margin, %	11.7	12.2
Earnings per share, SEK	12.03	10.56
Return on capital employed, %	21.1	21.2
Return on equity, %	17.6	17.5

Definitions of key figures, page 40.

Earnings analysis

Operating profit increased by 30 percent to SEK 3,813 m. (2,931), corresponding to 12.7 percent (11.7) of revenues.

Earnings in 1997 were charged with restructuring costs, SEK 50 m., related to the Atlas Copco Robbins division. Earnings in 1996 included restructuring costs of SEK 225 m. and a capital gain of SEK 342 m. Both these nonrecurring items related to the Industrial Technique business area. Adjusted for nonrecurring items, the operating margin was 12.9 percent (11.2). This improvement was due to volume increases and to favorable exchange rates, which had a positive effect of approximately SEK 450 m.

Depreciation according to plan in 1997 amounted to SEK 1,451 m. (949), of which property and machinery accounted for SEK 775 m. (607), rental equipment for SEK 387 m. (178) and intangible assets amortization for SEK 289 m. (164). The Group applies an amortization period of 40 years for goodwill arising from the acquisitions of the U.S. companies Milwaukee Electric Tool in 1995 and Prime Service in 1997, which provides the most accurate reflection of these strategic acquisitions on Atlas Copco Group earnings and financial position. See also page 33 under Goodwill.

Operating profit for the *Compressor Technique* business area rose 40 percent to SEK 2,537 m. (1,807), corresponding to an operating margin of 17.8 percent (16.3). The improvement was mainly attributable to higher volumes, favorable exchange rates and the Prime Service acquisition.

Operating profit for the *Construction and Mining Technique* business area amounted to SEK 387 m. (396), corresponding to an operating margin of 6.0 percent (6.7). Excluding restructuring costs for the tunnel-boring machine business, the operating margin was 6.8 percent.

Operating profit for the *Industrial Technique* business area rose 13 percent, to SEK 942 m. (836). Excluding nonrecurring items, the profit for 1996 amounted to SEK 719 m. The comparable operating margin was 10.1 percent (8.8). The improvement was mainly due to higher sales volumes.

The Group's net financial items amounted to SEK –293 m. (139), of which net interest items accounted for SEK –306 m. (127) and a capital gain from the sale of shares in SAS Sverige AB for SEK 32 m. Interest expense increased because of higher net borrowing for the Prime Service acquisition. Compared to the previous year, interest income from cash holdings and from currency hedging of foreign net assets had a negative effect of approximately SEK 150 m. due to lower interest rates in Sweden.

Atlas Copco Group profit after financial items rose by 15 percent to SEK 3,520 m. (3,070), corresponding to a profit margin of 11.7 percent (12.2). Adjusted for nonrecurring items in 1996, profit increased 19 percent. Taxes for the year totaled SEK 1,280 m. (1,107).

Profit for the year amounted to SEK 2,208 m. (1,938). Earnings per share amounted to SEK 12.03 (10.56), up 14 percent.

Key figures by business area

	Revenues		Operating profit		Return on capital employed		Investments*	
	1997	1996	1997	1996	1997	1996	1997	1996
Compressor Technique	14,263	11,072	2,537	1,807	28	33	344	285
Construction and Mining Technique	6,453	5,921	387	396	12	14	207	211
Industrial Technique	9,316	8,128	942	836	13	12	279	309
Corporate items			–53	–108			10	17
Total Group	30,032	25,121	3,813	2,931	21	21	840	822

* excluding rental equipment

Balance sheet

	1997	1996
Net indebtedness	10,214	1,899
Debt/equity ratio, %	75	16
Equity/assets ratio, %	39	52

Definitions of key figures, page 40.

Balance sheet analysis

The Group's total assets increased during the year to SEK 34,790 m. (23,175), or by 50 percent, of which acquired companies accounted for 43 percentage points and currency translation for 7 percentage points. The capital turnover ratio was 1.08 (1.11).

Investments

Excluding acquisitions, investments in property and machinery totaled SEK 840 m. (822). The distribution of investments was SEK 204 m. (172) in Sweden and SEK 636 m. (650) outside Sweden.

Major investments related to a new central laboratory for rock drilling equipment in Örebro and to new production equipment in most plants.

Investments in property and machinery during 1997 exceeded depreciation by SEK 65 m. In total, depreciation on these assets during the year amounted to SEK 775 m. (607).

Investments in rental equipment amounted to SEK 920 m. (336). Total depreciations of rental equipment amounted to SEK 387 m. (178).

Geographic distribution of investments in property and machinery

	1997	1996
Europe	519	472
North America	221	237
South America	19	16
North Africa/Middle East	5	6
Southern Africa	13	12
India/East Asia	47	70
Oceania	16	9
Total	840	822

Inventories and accounts receivable

The value of inventories as a proportion of revenues declined to 17.4 percent (17.8). The impact of Prime Service represents half of the improvement, due to the company's low level of inventories in relation to revenues.

Customer receivables in relation to revenues increased during the year to 20.2 percent (19.4). Excluding Prime Service, the ratio was unchanged.

Cash flow and net indebtedness

Liquid assets amounted to SEK 1,613 m. (2,485) at year-end 1997, corresponding to 5 percent (10) of revenues.

The Group's net indebtedness, defined as the difference between interest-bearing liabilities and liquid assets, increased significantly as a consequence of the Prime Service acquisition, to SEK 10,214 m. (1,899), of which SEK 2,016 m. (1,924) related to pension provisions. The debt/equity ratio, defined as net indebtedness in relation to shareholders' equity, increased to 75 percent (16).

Operational cash flow before acquisitions and divestments of businesses and before dividends, but including SEK 800 m. for the sale of real estate and repatriation of equity in associated companies, was very strong and totaled SEK 3,878 m. (1,920). Cash outflow for acquisitions amounted to SEK 10,639 m., and for dividends to SEK 698 m. Consequently, net cash flow during the year was negative and amounted to SEK −7,459 m. (1,322).

Shareholders' equity

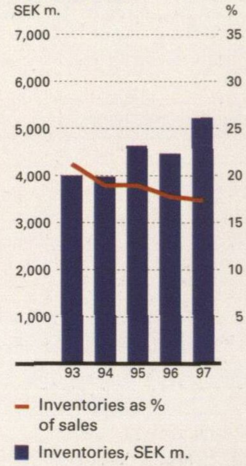
At December 31, 1997, Group shareholders' equity, including minority interests, amounted to SEK 13,635 m. (12,005). Shareholders' equity per share amounted to SEK 74 (65).

The equity portion of total assets was 39 percent (52).

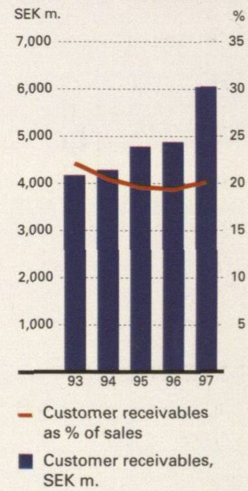
Summary cash-flow analysis

	1997	1996
Surplus liquid funds from operations	5,437	3,546
Change in working capital	267	249
Investment in tangible fixed assets	−1,760	−1,158
Cash flow from operations before financial items	3,944	2,637
Financial items, including tax payments	−66	−717
Cash flow from operations after financial items	3,878	1,920
Company acquisitions/ divestments	−10,639	−39
Dividend to shareholders	−698	−559
Net cash flow	−7,459	1,322

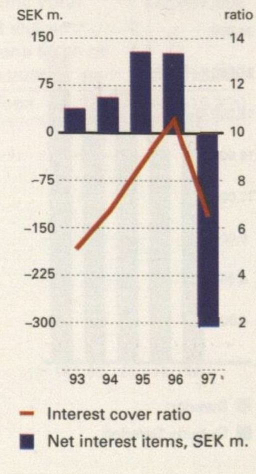
Inventories



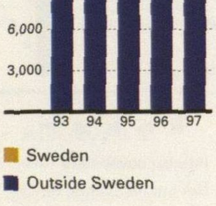
Customer receivables



Net interest items and interest cover ratio



Employees, average



Personnel

	1997	1996
Average number of employees, total	22,296	21,085
Sweden	2,706	2,757
Outside Sweden	19,590	18,328
Business areas		
Compressor Technique	9,235	7,698
Construction and Mining Technique	5,058	5,143
Industrial Technique	7,898	8,119
Other	105	125

The average number of employees within the Atlas Copco Group increased in 1997 by 1,211 to 22,296 (21,085). The proportion of employees in Swedish units was 12 percent (13). See also note 2. At year-end, the Group had a total of 23,923 employees (20,841).

Option plan

A yearly revolving option plan, initially including 25–30 executives within the Group, was introduced in 1997, providing the possibility of annual grants of call options on Atlas Copco shares. The options have a term of five years and give the optionholder the right to purchase existing shares. Accordingly, the exercise of the options will not result in any dilution of the holdings of current shareholders.

The size of the grant is linked to the Group's ability to add value to the Company for its shareholders. The value of options granted depends on the Group's operating cash flow, less Atlas Copco's cost of capital in relation to a predetermined performance target (see note 26).

Based on the Group's performance in 1997, the Board of Directors decided to grant options corresponding to a total amount of SEK 4.4 m., excluding social charges.

The Company's cost is not affected by the development of the stock price, as the option plan is financially hedged.

Product development

	1997	1996
R&D costs	808	770
Total in % of revenues	2.7	3.1

The introduction of new products at increasingly shorter intervals has become a vital element in efforts to strengthen the competitiveness of the Group's divisions. As a result, increased resources were allocated to product development within all business areas during 1997. The lower R&D share is partly due to the Prime Service acquisition.

Within the *Compressor Technique* business area, the Oil-free Air division fully introduced a new generation of large oil-free screw compressors specially aimed at companies that require large quantities of compressed air. The design, which integrates a large number of components and functions, substantially reduces both delivery lead-time and maintenance.

The Industrial Air division developed a series of high-pressure compressors that offer high reliability during continuous operation in a marine environment. A new series of scroll compressors with up to four compressor modules in one unit was also introduced. The new scroll compressors are equipped with electronic control systems that adapt operation to individual customer needs. The division also launched a new separator that uses the latest filter technique to separate oil from water before it is released into waste water systems.

The Portable Air division expanded its product range of large compressors by adding eight new models. The new compressors are equipped with after-cooled, turbo-diesel engines that offer low fuel consumption and meet stringent environmental requirements.

The Atlas Copco Applied Compressor and Expander Technique division concentrated development work in 1997 on higher production capacity and improvements in its range of process compressors and expanders.

Within the *Construction and Mining Technique* business area, construction was completed on a new central laboratory for the development and testing of the Rock Drilling Equipment division's drills in Örebro. The new facility comprises more than 2,000 square meters of laboratory space and will employ 60–70 persons. The new laboratory will offer strongly increased resources for the development of efficient and highly productive drilling rigs for underground and surface applications.

The Uniroc division developed new bench drill bits that increase productivity in quarry operations by as much as 30 percent. A new down-the-hole hammer and refined version of the Coprod system were also launched in the market. The system implies that the rod transfer percussion energy to the rock, without any power loss, to the drilling head. The Craelius division introduced a new range of drill bits and rods for core drilling applications.

The Atlas Copco Wagner division continued its comprehensive program to develop new loaders. In 1997, three new loaders were introduced in the market, characterized by features such as remote control, low operating costs, high productivity, and ergonomic design.

Within the *Industrial Technique* business area, the Milwaukee division continued its comprehensive product development programs, expanding its portfolio of cordless tools with a new series for professional applications. Milwaukee has developed a special microcomputer that extends battery life by controlling the charging mechanism. During the year, Milwaukee and the Atlas Copco Electric Tools division continued cooperating on the development of electric power tools. The latter division launched a new cordless reciprocating saw, ergonomically designed for safe and effective sawing, and a new series of lightweight angle grinders designed for difficult grinding and cutting applications.

The Atlas Copco Industrial Tools and Equipment division supplemented its product range with a new series of nutrunners that broadens the areas of application for customers in the automotive industry and their suppliers, thereby enhancing market potential for this product group. The division also introduced a new series of grinding machines for use in foundries and mechanical engineering companies.

Chicago Pneumatic introduced a series of ergonomically designed grinders. New materials used to manufacture the grinders reduce vibration and noise levels.

Parent company

Earnings from real estate management operations in the Nacka industrial estate are included in the Parent Company through Sickla Industrifastigheter KB, a limited partnership company. Atlas Copco sold the real estate in Nacka in December 1997.

Earnings

Earnings from participations in subsidiaries amounted to SEK 263 m. (526), and from associated companies to SEK 445 m. (–). Profit after financial items totaled SEK 809 m. (692).

The Parent Company reported a net profit after appropriations and taxes of SEK 1,296 m. (1,062). Hence undistributed earnings totaled SEK 3,542 m. (2,934).

Financing

Total assets of the Parent Company increased by SEK 8,482 m. to SEK 18,682 m. At year-end 1997, cash, bank deposits and short-term investments amounted to SEK 107 m. (1,345).

The Parent Company's debt/equity ratio, defined as net indebtedness in relation to shareholders' equity, was 63 percent (16). The increase was primarily due to the financing of the Prime Service acquisition.The equity portion of total assets amounted to 38 percent (62).

Personnel

The average number of employees in the Parent Company was 61 (65).

A specification of the fees and other remuneration made to the Board of Directors, the President and other members of Group management is shown in note 2.

Distribution of shares

Atlas Copco's share capital at year-end 1997 amounted to SEK 918 m.

Each share has a par value of SEK 5. For further information, see page 64.

Outstanding Shares	
A shares (one vote)	122,497,590
B shares (one tenth of a vote)	61,018,330
Total	183,515,920

Dividend

The Atlas Copco Group's unrestricted shareholders' equity amounts to SEK 7,681 m. Of the retained earnings SEK 22 m. will be transferred to restricted reserves.

The Board of Directors and the President propose a dividend of SEK 4.25 (3.75) per share, corresponding to a total of SEK 780 m. (688). See page 42.

Consolidated Income Statement

Amounts in SEK m.		1997	1996
Revenues	Note 1	30,032	25,121
Cost of goods sold		–19,624	–16,684
Gross profit		10,408	8,437
Cost of marketing, administration, research and development	Note 3	–6,510	–5,662
Amortization on goodwill	Note 4	–279	–156
Other income and expenses from operations	Note 5	194	312
Operating profit	Note 2	3,813	2,931
Financial income and expenses	Note 6	–293	139
Profit after financial items		3,520	3,070
Taxes	Note 8	–1,280	–1,107
Minority interest	Note 9	–32	–25
Profit for the year		2,208	1,938
Earnings per share, SEK	*Note* 10	12.03	10.56

Consolidated Balance Sheet

Amounts in SEK m.			Dec. 31, 1997		Dec. 31, 1996	
ASSETS						
Fixed assets	Intangible assets	Note 11	11,051		3,781	
	Tangible assets	Note 12	8,811		5,096	
	Financial assets	Note 13	983	20,845	1,309	10,186
Current assets	Inventories	Note 15	5,231		4,473	
	Current receivables	Note 16	7,101		6,031	
	Investments	Note 17	223		1,097	
	Cash and bank	Note 17	1,390	13,945	1,388	12,989
Total assets				34,790		23,175
SHAREHOLDERS' EQUITY AND LIABILITIES						
Shareholders' equity	**Restricted equity**	Note 18				
	Share capital		918		918	
	Restricted reserves		4,854		4,771	
	Non-restricted equity	Note 18				
	Retained earnings		5,473		4,224	
	Profit for the year		2,208	13,453	1,938	11,851
Minority interest		Note 9		182		154
Provisions	**Interest-bearing provisions**					
	Pensions and similar commitments	Note 20	2,016		1,924	
	Non-interest-bearing provisions					
	Deferred taxes		1,637		1,158	
	Other provision	Note 21	699	4,352	526	3,608
Long-term liabilities	**Interest-bearing liabilities**					
	Liabilities to credit institutions	Note 22	2,201		571	
	Non-interest-bearing liabilities					
	Other liabilities		326	2,527	279	850
Current liabilities	**Interest-bearing liabilities**					
	Liabilities to credit institutions	Note 23	7,610		1,889	
	Non-interest-bearing liabilities					
	Operating liabilities	Note 24	6,666	14,276	4,823	6,712
Total shareholders' equity and liabilities				34,790		23,175
Assets pledged		Note 25		202		165
Contingent liabilities		Note 25		1,374		1,100

Cash Flow Analyses

Amounts in SEK m.	Group 1997	Group 1996	Atlas Copco AB 1997	Atlas Copco AB 1996
Revenues	30,032	25,121		
Operating expense	–26,046	–22,524	–37	–2
Reversal of depreciation	1,451	949	7	7
Operating cash surplus	5,437	3,546	–30	5
Change in				
Inventories	–225	173	–	–
Operating receivables	–531	–136	12	–17
Operating liabilities	1,023	212	625	–164
Change in working capital	267	249	637	–181
Investments in				
Property and machinery	–840	–822	–6	–4
Rental equipment	–920	–336	–	–
Cash flow from operations before financial items	3,944	2,637	601	–180
Net financial income/expense	–318	111	482	693
Dividends from associated companies	510	4	506	–
Sale of property and machinery	600	159	97	0
Group contributions			822	838
Tax payments	–1,041	–985	–162	–220
Other items, net	183	–6	102	–299
Cash flow from operations after financial items	3,878	1,920	2,448	832
Company acquisitions/divestments	–10,639	–39	345	–166
Cash flow before dividend	–6,761	1,881	2,793	666
Dividend to shareholders	–698	–559	–688	–551
Net cash flow	–7,459	1,322	2,105	115

Notes to Atlas Copco Group Cash Flow Analysis

The purpose of the cash flow analysis is to provide a description of a company's capacity to generate cash during a given period. In contrast to the traditional "Statement of changes in financial position", which defines the change in the company's liquid funds, the cash flow analysis describes the change in total net indebtedness, or specifically cash, bank and short-term investments, less interest-bearing liabilities.

The impact on the Group's assets and liabilities of exchange-rate changes, so called translation differences, is not classified as real cash flow and is therefore only reported in the table showing net indebtedness below.

Operating cash surplus

The operating cash surplus, after the reversal of depreciation and capital gains, increased more than 50 percent, to equal 18 percent (14) of Group revenues.

The improvement is primarily due to increased operating profit and to the acquisition of Prime Service with depreciations as a major cost item, which is reversed for cash flow reasons.

Cash flow from operations before financial items

Working capital (operating receivables and inventories less operating liabilities) decreased by 267 (249).

The Prime Service acquisition significantly boosted investment in the rental equipment, from 336 to 920. Investments in property and machinery rose slightly, from 822 to 840.

Despite substantial capital expenditure, cash flow from operations before financial items expanded 50 percent, to 3,944 (2,637).

Cash flow from operations after financial items

Weaker financial net, chiefly a consequence of the Prime Service acquisition, was more than offset by one-time dividend from associated company and by proceeds from the sale of real estate, including properties in Nacka. Cash flow from operations after financial items totaled 3,878 (1,920).

Net cash flow

After acquisitions, primarily related to Prime Service of approximately 9,000, and the dividend to shareholders, net cash flow totaled –7,459 (1,322).

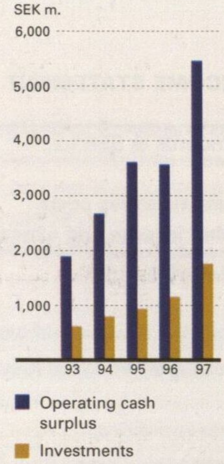
Five-year summary of cash flow analysis 1993–1997

Operating cash surplus	17,096
Change in working capital	444
Investments in tangible fixed assets	–5,281
Cash flow from operations before financial items	12,259
Net financial income/expense	–49
Dividends from associated companies	548
Sale of property and machinery	1,091
Tax payments	–3,946
Other items, net	107
Cash flow from operations after financial items	10,010
Company acquisitions/ divestments	–14,995
Cash flow before dividend	–4,985
Dividend to shareholders	–2,317
Net cash flow	–7,302

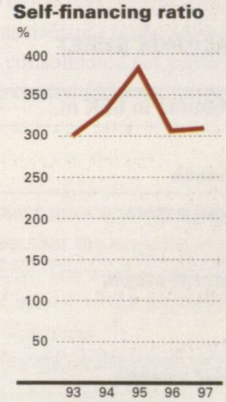
Net indebtedness

	1993	1994	1995	1996	1997
Net indebtedness, January 1	–2,214	–1,779	–351	–3,166	–1,899
Net cash flow	687	1,291	–3,143	1,322	–7,459
Currency exchange-rate effects	–252	137	328	–55	–856
Net from operations	435	1,428	–2,815	1,267	–8,315
Net indebtedness, December 31	–1,779	–351	–3,166	–1,899	–10,214
Provision for pensions	1,905	1,840	1,910	1,924	2,016
Net indebtedness, excluding Provision for pensions, December 31	126	1,489	–1,256	25	–8,198

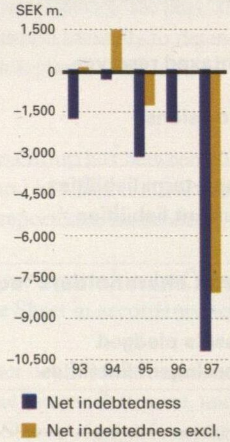
Cash flow and investments



Self-financing ratio



Net indebtedness



Income Statement and Balance Sheet

INCOME STATEMENT

Amounts in SEK m.		1997	1996
Administrative costs		–129	–138
Other income and expenses from operations	Note 5	141	137
Operating profit	Note 2	12	–1
Financial income and expenses	Note 6	797	693
Profit after financial items		809	692
Appropriations	Note 7	649	590
Profit before taxes		1,458	1,282
Taxes	Note 8	–162	–220
Profit for the year		1,296	1,062

BALANCE SHEET

Amounts in SEK m.				Dec. 31, 1997		Dec. 31, 1996
Assets						
Fixed assets	*Tangible assets*	Note 12	17		66	
	Financial assets	Note 13	9,366	9,383	6,628	6,694
Current assets	Current receivables	Note 16	9,192		2,161	
	Investments	Note 17	30		969	
	Cash and bank	Note 17	77	9,299	376	3,506
Total assets				18,682		10,200
Shareholders' equity and liabilities						
Restricted equity	Share capital	Note 18	918		918	
	Restricted reserves		1,737		1,737	
Non-restricted equity	Retained earnings	Note 18	2,246		1,872	
	Profit for the year		1,296	6,197	1,062	5,589
Untaxed reserves		Note 19		1,214		1,042
Provisions	Pensions and similar commitments	Note 20	423		428	
	Other provisions	Note 21	8	431	–	428
Long-term liabilities	Interest-bearing liabilities	Note 22		2,272		658
Current liabilities	Interest-bearing liabilities	Note 23	7,838		2,371	
	Operating liabilities	Note 24	730	8,568	112	2,483
Total shareholders' equity and liabilities				18,682		10,200
Assets pledged				–		–
Contingent liabilities		Note 25		529		512

Notes to financial statements

SEK m. unless otherwise noted

Accounting principles

Changes in accounting principles

Effective from 1997, Atlas Copco has followed the new Swedish Annual Accounts Act, which conforms to EU requirements. The main effect of this change is a reordering of items in the income statement and balance sheet. The new Act has but a marginal effect on valuation principles previously applied. Income statements and balance sheets for previous years, provided for comparison, have been adjusted to comply with the new regulations.

Prior to the acquisition of Prime Service, the rental equipment was reported as inventory. The rental equipment has been reclassified and is now included in fixed assets. Previous years' figures have been restated accordingly.

The Company follows the recommendations of the Financial Accounting Standards Council with the exception of its principles for treatment of goodwill, as described below.

International guidelines

In all essential respects, Atlas Copco follows the guidelines prepared by the OECD for companies with international operations.

These guidelines have been observed in the preparation of this Annual Report, with the exception of certain information which, for competitive reasons, cannot be disclosed.

The Company also views positively the guidelines with respect to multinational companies and the labor market, which have been prepared by the United Nations Organization for labor matters (ILO). In conformity with international standards, the following designations have been used in this Annual Report: Currency: SEK = Swedish kronor. Other currencies: See page 37. Suffix m. = millions.

Consolidation

The Consolidated Income Statement and Balance Sheet of the Atlas Copco Group cover all companies in which the Parent Company, directly or indirectly, holds more than 50 percent of the voting rights, as well as those companies in which the Group in some other manner has a decisive influence and a substantial participation in the income from their operations. The consolidated accounts have been prepared in accordance with the purchase method, which means that assets and liabilities are reported at market value including deferred taxes according to the acquisition plan. If the acquisition cost exceeds the market value of the company's net assets, calculated as above, the difference is reported as goodwill, see below.

Companies acquired during the year have been reported in the Consolidated Income Statement, with the amounts relating to the period following the date of acquisition. Earnings of companies divested during the year have been deducted from consolidated earnings on the basis of the Group's reported net assets in these companies at the time of the divestment.

The Consolidated Income Statement and Balance Sheet are shown without untaxed reserves and appropriations. Under Swedish law, this may only be done in consolidated statements. Untaxed reserves reported in individual Group companies have been apportioned in such a manner that deferred taxes are reported as a long-term liability, while the remaining amount is included in restricted reserves in the Consolidated Balance Sheet.

Deferred taxes are thus calculated individually for each company on the basis of current local income tax rates at the estimated date of the reversal for taxation, i.e. generally the next accounting year. The tax calculated in this manner, relating to the appropriations for the year in the individual companies, is included in the Group's tax expense as deferred taxes, while the remaining amount is included in the consolidated net profit. If the tax rate is changed, the change in tax liabilities is reported as tax expenses for the year.

Goodwill

The acquisition of well-established companies active in an international environment, normally means that the acquisition price substantially exceeds tangible net worth. The market price is determined primarily by future expectations, which are based on the company's market position and know-how.

A company acquisition, in which the acquisition price exceeds the company's net assets, valued at market prices, results in intangible assets which are capitalized and amortized over a certain period. Goodwill is normally amortized over ten years, while goodwill arising from strategic acquisition is amortized over a period of 20–40 years. For reporting of goodwill regarding the acquisitions of Milwaukee and Prime Service, see page 33.

The economic life of assets is appraised annually to determine whether the selected amortization plan is sufficient.

Associated companies

Companies in which the Atlas Copco Group has between 20 and 50 percent of the voting rights, and in which it has a substantial ownership involvement, are reported as associated companies.

Holdings in associated companies are reported in the Consolidated Income Statement and Balance Sheet in accordance with the equity method.

Atlas Copco's share of income after net financial items in associated companies is reported in the Income Statement, under the heading Other operating income. Shares of taxes in associated companies are reported in consolidated tax expense.

The related acquisition costs are reported under Financial assets in the Balance Sheet, increased or reduced by shares of income and less dividend received. Undistributed income in these companies is reported among restricted reserves in consolidated shareholders' equity.

Internal profits have been eliminated in appropriate cases.

Translation of accounts of foreign subsidiaries

Atlas Copco applies the current-rate method in translating the accounts of foreign subsidiaries, in accordance with the suggested recommendations of the Swedish Institute of Authorized Public Accountants FAR. In applying this method, the subsidiaries are primarily reported as independent units with operations conducted in foreign currencies and in which the Parent Company has a net investment. The exceptions to this approach are those subsidiaries which are located in high-inflationary countries and so called integrated companies. The accounts of such subsidiaries are translated according to the monetary/non-monetary method.

In accordance with this suggested recommendation, such a procedure is regarded as providing a more accurate picture of the earnings and financial positions of these companies. In accordance with the current-rate method, all assets and liabilities in the balance sheets of subsidiaries are translated at year-end rates, and all items in the income statements at the average exchange rate for the year. Translation differences that arise are a result of the fact that net investments are translated at year-end at a rate different from that used at the beginning of the year. This does not affect earnings, but is instead transferred directly to shareholders' equity.

For those subsidiaries treated according to the monetary/non-monetary method, all non-monetary items, real estate (land and buildings), machinery and equipment, inventories, shareholders' equity, and deferred tax, are translated at the acquisition date rates. Other items, monetary items, are translated at year-end rates. The income statement items have been translated at the average rate for the year, except for the cost of goods sold, depreciation and deferred taxes, which have been translated at the investment rate. Exchange differences arising in connection with the translation of the accounts, and which accordingly relate to companies in countries with high inflation, have been included in the Income Statement.

Classification of foreign subsidiaries

In a particular respect, FAR's suggested recommendations require that the user chooses translation procedures according to the specific situation. This applies to the classification of the foreign subsidiaries as either independent or integrated companies. How the company is defined leads directly to the choice of translation method. The accounts of independent companies are translated according to the current-rate method, and integrated companies according to the monetary/non-monetary method.

Based on the criteria defined for classification of companies, the great majority of Atlas Copco's subsidiaries should be regarded as independent companies. As a consequence, the accounts of all subsidiaries of the Atlas Copco Group are translated according to the current-rate method, except for the companies in high-inflationary countries, primarily Latin America. The operational currency of these companies is regarded as being the USD, and is therefore translated in two stages. In the first stage, translation is made to USD in accordance with the monetary/non-monetary method, whereby translation differences arising are charged to consolidated income. In the second stage, the company's balance sheet items are translated to SEK according to the year-end rate and the income statement items according to the average rate for the year. The resulting translation differences are transferred directly to shareholders' equity.

Inventories

Inventories are valued at the lower of cost or market, in accordance with the first in/first out principle and the net sales value. Group inventories are shown after deductions for obsolescence and for internal profits arising in connection with deliveries from the product companies to the sales companies. Deferred tax has been taken into account in connection with these latter transactions. Transfer pricing between the companies is based on market price setting.

Receivables and liabilities in foreign currencies

Receivables and liabilities in foreign currencies are translated at the year-end rate.

For individual Swedish companies, these receivables and liabilities are reported in accordance with Directive R7 of the Swedish Accounting Standards Board. Unrealized exchange-rate gains on long-term receivables and liabilities are allocated to a currency exchange reserve and are reported as appropriations.

In case of currency exchange through a swap agreement, the loan is valued at the year-end rate for the swapped currency. In cases where the swapped loan, translated at the year-end rate for the original currency, exceeds the booked liability, the difference is included under contingent liabilities.

Exchange rates for major currencies used in the year-end accounts are shown on page 37.

Financial investments

Financial and other investments, that are to be held to maturity, are valued at acquisition cost.

Investments intended for trading are valued at the lower of cost or market.

Hedging of net investments

Forward contracts, currency swaps, and loans in foreign currencies have been arranged in order to hedge the Group's net assets in foreign subsidiaries. Foreign exchange gains and losses on such contracts, less current and deferred tax, are not included in income for the year, but are offset against translation differences arising in connection with the translation of the foreign subsidiaries' net assets. In the individual subsidiaries, such contracts are valued in accordance with the lowest-value principle for receivables and with the highest-value principle for liabilities. The interest-rate differences between currencies are included in the net interest items and are distributed evenly over the term of each contract.

Hedging of commercial flows

When calculating the value of the forward contracts outstanding, provision is made for unrealized losses to the extent these exceed unrealized gains. Unrealized gains which exceed unrealized losses are not recognized as revenue. When calculating unrealized exchange-rate differences, that portion of the hedged amounts is excluded for which currency flows, through currency transactions, are most likely to cover the forward contracts.

Research and development costs

Atlas Copco's own research and development costs are expensed as incurred.

Product development costs and warranty costs

Product development costs are charged against operations when they are incurred.

Estimated costs of product warranties are charged against cost of sales at the time the products are sold.

Depreciation

The Atlas Copco Group uses three depreciation concepts; cost depreciation, book depreciation, and current cost depreciation.

Cost depreciation is based on original cost and is applied according to the straight-line method over the economic life of the asset.

Book depreciation is used in each individual company in accordance with the maximum amount permitted by tax legislation in each country. The difference between book depreciation and cost depreciation is reported under Appropriations in the Income Statement. The total value is reported in the Balance Sheet among untaxed reserves under the heading Accumulated additional depreciation. In the case of the Group, untaxed reserves and appropriations are eliminated.

Current cost depreciation is used as the basis for price and profitability calculations and is based on the replacement value of the asset. Depreciation is applied on a straight-line basis over the economic life of the asset.

The following economic lives are used for cost depreciation and current cost depreciation:

Goodwill and other intangible assets	5–40 years
Buildings	25–50 years
Machinery and equipment	3–10 years
Vehicles	4–5 years
Computer equipment	3–4 years
Rental equipment	3–10 years

Leasing

Leases are classified in the consolidated financial statement as either financial leases or operating leases. A financial lease entails the transfer to the lessee, to a material extent, of the economic risks and benefits connected to ownership. If this is not the case, the lease is an operating lease. Financial leasing implies that the fixed asset in question is reported as an asset in the balance sheet and that a corresponding liability is entered on the liabilities side. In the income statement, the costs of financial leases are divided into depreciation and interest expense. An operating lease implies that there are no asset or liability entries to report in the balance sheet. In the income statement, the costs of operating leases are distributed over a number of years based on use, which can differ from the actual amount of leasing fees paid in any particular year.

The Parent Company reports all leases based on the principles for operating leases.

Taxes

The Company calculates deferred tax based on the differences between reported values in the balance sheet and residual value available for tax purposes. Those tax-loss carryforwards arising are anticipated in instances where it is more likely than not that they will result in lower tax payments in the future. When calculating deferred tax, the nominal tax rates prevailing in each country have been used individually for each company. Deferred tax relating to 1997 operations is shown under the entry Taxes in the Income Statement and is specified in note 8 and under Financial assets, note 13, and Non-interest-bearing provisions in the Balance Sheet.

Notes

1 Revenues by business area and market

Revenues by business area

	Group 1997	Group 1996
Compressor Technique	14,263	11,072
Construction and Mining Technique	6,453	5,921
Industrial Technique	9,316	8,128
	30,032	25,121

Revenues by market

	Group 1997	Group 1996
Europe incl CIS	11,799	10,841
of which Sweden	*1,015*	*1,049*
of which EU	*10,084*	*9,364*
North America	9,787	7,117
South America	1,964	1,415
North Africa/Middle East	900	700
Southern Africa	933	755
India/East Asia	3,410	3,250
Oceania	1,239	1,043
	30,032	25,121

Group operating profit by business area is reported in the Board of Directors' Report and in the sections for each business area. Revenues and operating profit per quarter are shown on page 40.

2 Employees and personnel expenses

Average number of employees

	Women	Men	1997 Total	1996 Total
Parent Company				
Sweden	31	30	61	65
Subsidiaries				
Europe incl CIS	1,750	8,746	10,496	10,495
of which Sweden	*383*	*2,262*	*2,645*	*2,692*
of which EU	*1,652*	*8,304*	*9,956*	*9,990*
North America	1,378	4,433	5,811	4,772
South America	135	809	944	964
North Africa/Middle East	56	149	205	193
Southern Africa	130	645	775	692
India/East Asia	384	3,039	3,423	3,316
Oceania	108	473	581	588
Total in subsidiaries	3,941	18,294	22,235	21,020
Grand total	3,972	18,324	22,296	21,085

Salaries and other remuneration

	1997 Board and Presidents	1997 Other Employees	1996 Board and Presidents	1996 Other Employees
Parent Company				
Sweden	17	25	15	24
(of which bonuses)	(4)		(3)	
Subsidiaries				
Europe incl CIS	87	3,072	92	2,914
of which Sweden	*9*	*692*	*9*	*681*
of which EU	*72*	*2,919*	*79*	*2,813*
North America	32	1,808	26	1,277
South America	13	187	11	135
North Africa/Middle East	3	29	2	23
Southern Africa	4	81	3	63
India/East Asia	9	497	12	204
Oceania	3	164	2	144
Total in subsidiaries	151	5,838	148	4,760
(of which bonuses)	(17)		(17)	
Grand total	168	5,863	163	4,784

	Group 1997	Group 1996	Parent Company 1997	Parent Company 1996
Salaries and other remuneration	6,031	4,947	42	39
Contractual pension benefits for Board members and Presidents	16	11	1	3
Contractual pension benefits for other employees	365	314	12	27
Other social costs	1,391	1,313	15	15
Total	7,803	6,585	70	84
Capitalized pension obligations to Board members, and Presidents	60	55	29	30

Other information regarding personnel

Certain members of the Board, the President and CEO, and other members of Group management received remuneration and other fees for the year.

In 1997, the Chairman of the Board received SEK 1,000,000 in fees. Other Board members not employed by the Company each received SEK 200,000 in fees.

In addition, the Vice Chairman received a special remuneration of SEK 44,290; FRF 50,000 and USD 12,500 in fees from Group companies; and a 10-year pension effective from the age of 65. Board member Paul-Emmanuel Janssen received fees from Group companies in the amount of BEF 930,000. Board member Hari Shankar Singhania received fees from Group companies in the amount of INR 6,000.

The President and Chief Executive Officer, Giulio Mazzalupi, received a salary of SEK 2,708,480, corresponding to an annual salary of SEK 4,500,000. The former President and Chief Executive Officer, Michael Treschow, received a salary of SEK 2,328,358 for the period he was President, a bonus of SEK 4,135,000 and a fee of SEK 150,000. In addition, he received fees of USD 16,500 and FRF 50,000 from Group companies.

The present CEO has a pension commitment from the Company equal to the difference between the substantial pension rights he has earned during his long-term service abroad and 47 percent of his base salary, if he continues in his present position until the age of 65.

For the business area executives, there are defined pension plans based on company contributions with a maximum of 43 percent of home base salary.

If the Company terminates their employment prior to retirement, they will receive a compensation of maximum two years corresponding to final base salary. If they receive income from other employment during this period, Atlas Copco is entitled to deduct an amount corresponding to the additional income from the compensation it pays.

Value added and stakeholders

Value added corresponds to the Group's total revenues, 30,032 less costs for the purchase of raw materials, wholly and semi-finished goods and services, 16,965. The resulting figure is a measure of the company's productive contribution, that is, the value added through processing, management, and other activities.

In 1997, the value added amounted to 13,067 (10,465), an increase of approximately 25 percent, while value added per employee increased approximately 18 percent.

Distribution of value added:

	1997		1996	
	SEK m.	%	SEK m.	%
Wages and salaries	6,031	46	4,947	47
Social costs	1,772	14	1,638	16
Depreciation and amortization	1,451	11	949	9
Capital costs	293	2	–139	–1
Corporate and municipal taxes	1,280	10	1,107	11
Dividends paid	698	5	559	5
Retained in business	1,542	12	1,404	13
Value added	13,067	100	10,465	100
Value added per employee, SEK thousands	586		496	

The value added is distributed among stakeholders, that is, employees, creditors, the government, municipalities, and shareholders. Remaining funds are retained in the Company to cover the cost of wear on plant and equipment (depreciation) and to provide for continued expansion of operations (retained in the business).

3 Cost of marketing, administration, research and development

	Group	
	1997	1996
Marketing costs	3,563	3,010
Administrative costs	2,139	1,882
Research and development expenditure	808	770
	6,510	5,662

The above costs include taxes in Sweden amounting to 20 (16), based on pension liabilities and pension payments in the form of taxes on pension savings and payroll tax, respectively.

4 Depreciation according to plan

	Group		Parent Company	
	1997	1996	1997	1996
Goodwill	279	156	–	–
Patents etc.	10	8	–	–
Buildings and land	179	92	2	2
Machinery and other technical plant	418	361		
Equipment etc.	178	154	5	5
Rental equipment	387	178	–	–
	1,451	949	7	7

5 Other income and expenses from operations

	Group		Parent Company	
	1997	1996	1997	1996
Nonrecurring items	–50	117	–	–
Other operating income	272	216	142	144
Other operating expenses	–28	–21	–1	–7
	194	312	141	137

Nonrecurring items refer to the costs of winding down Atlas Copco's tunnel-boring machine (TBM) business, conducted in the Atlas Copco Robbins division, which resulted in a charge of 50 to 1997 operating profit. The preceding year's operating profit included a gain of 342 on the sale of VOAC Hydraulics and restructuring charges of 225, both in the Industrial Technique business area.

Other operating income includes commissions received of 55 (57), capital gains of 28 (16) on the sale of fixed assets, rental income of 41 (38), and profits from insurance activities and exchange rate gains attributable to operations. Other operating income for the Parent Company includes commissions received totaling 90 (140) and capital gains of 49 (–) on the divestment of real estate.

Other operating expenses refer to costs such as those attributable to the rental of real estate.

6 Financial income and expense

	Group		Parent Company	
	1997	1996	1997	1996
Profit from shares in Group companies				
Dividends received			425	526
Capital gain/loss on divestment of shares			–162	–
			263	526
Profit from shares and participations in associated companies				
Dividends			506	–
Write-downs			–61	–
			445	–
Profit from financial fixed assets				
Dividends received	2	14	1	14
Interest income				
Group companies			226	158
Others	7	6	1	1
Capital gains	32	–	32	–
	41	20	260	173
Other interest income				
Interest income				
Group companies			300	86
Others	310	440	169	337
	310	440	469	423
Interest expenses and similar expenses				
Interest expense				
Group companies			–193	–290
Others	–623	–319	–431	–157
Foreign exchange differences	–21	–2	–16	18
	–644	–321	–640	–429
Financial income and expenses	–293	139	797	693

The interest portion of this year's provision for pensions is not charged against operating income but is shown as interest expense for both Swedish and foreign companies. The amount is based on the average of the opening and closing pension provisions. For Swedish companies, interest has been calculated at 3.7 percent (6.0). The interest portion for 1997 amounted to 92 (97), of which Swedish companies accounted for 31 (47). In the Parent Company, the corresponding amount was 16 (25).

The interest differential between international and Swedish interest rates on forward contracts and swap agreements used to hedge shareholders' equity in non-Swedish companies in the Group amounted to 140 (231) and is included in the item Interest income, others.

7 Appropriations

Tax legislation in Sweden and in certain other countries allows companies to retain untaxed earnings through tax-deductible allocations to untaxed reserves. By utilizing these regulations, companies can appropriate and retain earnings within the business without being taxed. The untaxed reserves created in this manner cannot be distributed as dividends.

The untaxed reserves are subject to tax only when they are utilized. If the company reports a loss, certain untaxed reserves can be utilized to cover the loss without being taxed.

	Parent Company	
	1997	1996
Difference between book depreciation and depreciation according to plan		
Buildings and land	7	–
Equipment etc.	3	3
Appropriation to tax allocation reserve	–144	–260
Appropriation to foreign exchange reserve	–95	–48
Dissolution of tax equalization reserve	57	57
Group contributions, net	821	838
	649	590

Under certain circumstances, the transfer of earnings in the form of group contributions can be made between Swedish companies within the same group. The contribution is a tax-deductible expense for the donor and taxable income for the recipient.

The Parent Company received group contributions from Atlas Copco Tools AB, Atlas Copco Construction and Mining Technique AB, Atlas Copco Rock Drills AB, Atlas Copco Compressor AB, and others.

8 Taxes

	Group 1997	Group 1996	Parent Company 1997	Parent Company 1996
Taxes paid				
Swedish taxes	167	227	161	220
Foreign taxes	874	758	1	
Deferred taxes	235	115		
Taxes in associated companies	4	7		
	1,280	1,107	162	220

The tax expense for the year totaled 1,280 (1,107), equal to 36.4 percent (36.1) of profit after financial items. Changes in tax rates used to calculate deferred tax had a positive impact of 5 (2) on tax expense for the year.

The Group's total tax expense is adversely affected compared to Swedish corporate tax rate by its strong position in countries with higher tax rates, including Belgium, France, and the U.S.

Non-deductible goodwill also has an adverse effect on the tax burden. Adjusted for such goodwill, the Group's tax rate was 33.7 percent (34.7).

The Swedish corporate tax rate is 28 percent. The tax is estimated on the basis of the nominal net profit reported, plus non-deductible expenses and less tax-free income and other deductions. For the Parent Company, this primarily involves tax-free dividends from shareholdings in subsidiaries and associated companies.

In Sweden, companies can make provisions to a tax allocation reserve. Appropriations to such reserves were 149 (271), of which the Parent Company was 144 (260). If the Parent Company reported deferred tax on untaxed reserves and other appropriations, as the Group does, deferred tax would have equaled 48 for the year.

Capital-based tax equalization reserves (K-Surv) in the Group's Swedish companies amounted to 181 (241). Existing reserves must be reversed by the end of the year 2000.

9 Minority interest in subsidiaries' equity and earnings

Minority interest in profit after financial items amounted to 47 (44).

The income statement reports minority shares in the Group's profit after tax of 32 (25). These minority interests relate primarily to Atlas Copco India, Atlas Copco Malaysia, subsidiaries in China, and subsidiaries of Chicago Pneumatic India.

	Group
Minority interest, Jan. 1	154
Minority acquired	0
Dividends	–10
Translation differences	6
Profit for the year	32
Minority interest, Dec. 31	182

10 Earnings per share

	1997	1996
Profit for the year	2,208	1,938
Average number of shares	183,515,920	183,515,920
Earnings per share, SEK	12.03	10.56

11 Intangible assets

	Goodwill	Patents etc.	Total
Accumulated cost			
Opening balance, Jan. 1	4,682	78	4,760
Investments	6,892	13	6,905
Acquisition of subsidiaries		8	8
Divestment and retirement	–193	–6	–199
Translation differences for the year	724	3	727
Closing balance, Dec. 31	12,105	96	12,201
Accumulated amortization			
Opening balance, Jan. 1	924	55	979
Amortization for the year	279	10	289
Acquisition of subsidiaries		3	3
Divestment and retirement	–193	–6	–199
Translation differences for the year	78	0	78
Closing balance, Dec. 31	1,088	62	1,150
Planned residual value, Dec. 31	11,017	34	11,051
Planned residual value, Jan. 1	3,758	23	3,781

Goodwill is normally amortized over 10 years, while goodwill arising from strategic acquisitions is amortized over 20–40 years. Book values are examined each year to determine whether a write-down exceeding the planned amortization is necessary. The Company has performed such write-downs in several cases.

Amortization in 1997 was distributed as follows:

	1997
Goodwill amortization over 40 years	163
Goodwill amortization over 20 years	58
Goodwill amortization within 10 years	58
	279

Amortization in 1997 and planned residual value by business area:

	Amortization	Planned residual value
Compressor Technique	99	6,990
Construction and Mining Technique	42	210
Industrial Technique	137	3,814
Corporate items	1	3
	279	11,017

Note 11 continued	Original value	Accumulated amortization	Planned residual value	No of years remaining
Goodwill amortized over 40 years:				
Milwaukee Electric Tool Corp.	3,476	210	3,266	38
Prime Service, Inc.	6,834	83	6,751	40
	10,310	293	10,017	
Goodwill amortized over 20 years:				
Desoutter Ltd	709	278	431	13
Atlas Copco Wagner Inc.	357	201	156	12
Chicago Pneumatic Tool Company	192	127	65	10
Atlas Copco Crépelle S.A.	129	4	125	20
	1,387	610	777	
Goodwill amortized within 10 years:				
Atlas Copco Compresseurs Worthington-Creyssensac S.A.	83	35	48	6
Atlas Copco Socapel S.A.	69	19	50	8
Atlas Copco Rotoflow Inc.	72	55	17	3
Others	184	76	108	
	408	185	223	
Total	12,105	1,088	11,017	

12 Tangible assets

Group	Buildings and land	Machinery and equipment	Rental equipment	New construction and advances	Total
Accumulated cost					
Opening balance, Jan. 1	3,262	5,597	1,205	151	10,215
Investments	124	692	920	24	1,760
Acquisition of subsidiaries	181	179	3,289	46	3,695
Divestment and retirement	–798	–399	–418	–2	–1,617
Reclassified items	–2	3	–1		–
Translation differences for the year	99	239	170	12	520
Closing balance, Dec. 31	2,866	6,311	5,165	231	14,573
Accumulated depreciation according to plan					
Opening balance, Jan. 1	998	3,504	617		5,119
Depreciation for the year	179	596	387		1,162
Acquisition of subsidiaries	10	39	0		49
Divestment and retirement	–286	–339	–134		–759
Reclassified items	–1	2	–1		–
Translation differences for the year	22	109	60		191
Closing balance, Dec. 31	922	3,911	929		5,762
Planned residual value, Dec. 31	1,944	2,400	4,236	231	8,811
Planned residual value, Jan. 1	2,264	2,093	588	151	5,096
Plant owned under financial leases					
Purchase cost	4	19	21		44
Accumulated depreciation	1	9	3		13
Planned residual value, Dec. 31	3	10	18		31

	Group 1997	1996	Parent Company 1997	1996
Buildings and land	1,944	2,264	12	59
Machinery and other technical plant	1,857	1,647	–	–
Equipment etc.	543	446	5	7
Rental equipment	4,236	588	–	–
Construction in progress and advances	231	151	–	–
	8,811	5,096	17	66
Tax assessment value, buildings and land	170	447	13	66

The tax assessment values reported for the Group pertain exclusively to buildings and land in Sweden. The book value of these is 153 (699).

Current and long-term liabilities include future payments for financial leases, note 22.

The estimated cost of assets owned through operating leases, such as rented premises, machinery, and major computer and office equipment, is 982 (333) for the Group. The leasing costs for this equipment are reported among operating expenses and amounted to 74 (64). Future costs for non-cancelable leasing contracts amounted to 486 (174). Future costs for non-cancelable leasing contracts come due for payment as follows:

1998	104
1999–2002	273
2003 or later	109
Total	486

Parent Company	Buildings and land	Equipment etc.	Total
Accumulated cost			
Opening balance, Jan. 1	86	74	160
Investments	3	3	6
Divestment and retirement	–74	–57	–131
Closing balance, Dec. 31	15	20	35
Accumulated depreciation according to plan			
Opening balance, Jan. 1	27	67	94
Depreciation for the year	2	5	7
Divestment and retirement	–26	–57	–83
Closing balance, Dec. 31	3	15	18
Planned residual value, Dec. 31	12	5	17
Planned residual value, Jan. 1	59	7	66

13 Financial assets

		Group 1997	1996	Parent Company 1997	1996
Shares in Group companies	Page 34			3,640	4,103
Receivables from Group companies				5,662	2,427
Shares and participations in associated companies	Note 14	177	631	11	72
Other long-term securities		13	23	7	19
Deferred tax receivables		644	563		
Other long-term receivables		149	92	46	7
		983	1,309	9,366	6,628

Shares in Group companies	Parent Company
Accumulated cost	
Opening balance, Jan. 1	3,915
Investments	1
Sales	–464
Closing balance, Dec. 31	3,452
Accumulated write-ups	
Opening and closing balances	764
Accumulated write-downs	
Opening and closing balances	–576
Book value, Dec. 31	3,640

14 Shares and participations in associated companies

	Number of shares	Percentage of capital	Adjusted equity	Book value
Directly owned				
AVC Intressenter AB, 55 65 06-8789, Gothenburg, Sweden	6,750,250	50	104	11
Indirectly owned				
Atlas Copco-CLLS Tools Co Ltd, Hong Kong, China		30	4	
Atlas Copco-Diethelm Ltd, Bangkok, Thailand		49	21	
Dalian Atlas Copco Application Co Ltd, Dalian, China		38	0	
NEAC Compressor Service GmbH & Co KG, Aachen, Germany		50	0	
NEAC Compressor Service Verwaltungs GmbH, Aachen, Germany		50	5	
NEAC Compressor Service USA Inc., Franklin		50	0	
Pneumatic Equipment Corp, Makati City, Philippines		30	0	
Shenzhen Nectar Engineering & Equipment Co Ltd, Shenzhen, China		25	0	
Toku-Hanbai KK, Fukuoka, Japan		50	43	
			177	

	Group	Parent Company
Accumulated capital participations/ purchase cost		
Opening balance, Jan. 1	631	72
Investments	23	
Sales	–9	
Dividends	–510	
Profit for the year	40	
Translation differences for the year	2	
Closing balance, Dec. 31	177	72
Accumulated write-downs		
Opening balance, Jan. 1		–
Write-down for the year		–61
Closing balance, Dec. 31		–61
Book value, Dec. 31	177	11

AVC Intressenter AB, a company in which Atlas Copco AB and Volvo Aero Corporation each holds a 50 percent stake, sold VOAC Hydraulics AB to the U.S. company Parker Hannifin Corporation at the end of February 1996. The gain from the sale was 342. The interest received on the proceeds from the sale is reported under financial items.

Other associated companies are of insufficient size to justify being reported separately. Dividends from associated companies totaled 510 (4). The Group's share in the shareholders' equity and untaxed reserves of associated companies, less deferred tax, equaled 177 (631) at fiscal year-end. The Parent Company's write-down on shares in associated companies refers to AVC Intressenter AB.

15 Inventories

	Group 1997	Group 1996
Raw materials	175	161
Work in progress	956	785
Semi-finished goods	1,356	1,337
Finished goods	2,723	2,177
Advances to suppliers	21	13
	5,231	4,473

16 Current receivables

	Group 1997	Group 1996	Parent Company 1997	Parent Company 1996
Trade receivables	6,053	4,881	1	5
Receivable from Group companies			9,089	2,046
Tax receivables	257	63	51	–
Other receivables	454	464	24	17
Prepaid expenses and accrued income	337	623	27	93
	7,101	6,031	9,192	2,161

Prepaid expenses and accrued income contain the conventional items, such as rent, insurance premiums, commissions, and social costs. The decline from the preceding year resulted from accrued exchange rate differences attributable to hedging the value of equity in foreign subsidiaries.

17 Short-term investments, cash, and bank accounts

	Group		Parent Company	
	1997	1996	1997	1996
Short-term investments				
Treasury bills	27	76	–	–
Government bonds	166	52	–	–
Commercial papers	30	969	30	969
	223	1,097	30	969
Cash and bank accounts	1,390	1,388	77	376
Total	1,613	2,485	107	1,345

The Parent Company's guaranteed, but unutilized, credit lines equaled 11,849. Subsidiaries had been granted but had not utilized overdraft facilities equaling 2,678.

18 Shareholders' equity

Group	Share-capital	Restricted reserves	Retained earnings
Opening balance, Jan. 1	918	4,771	6,162
Dividend to shareholders			–688
Statute-barred dividend			0
Transfers between restricted equity and retained earnings		83	–83
Equity hedging			–283
Translation differences for the year			365
Profit for the year			2,208
Closing balance, Dec. 31	918	4,854	7,681

Parent Company	Share-capital	Legal reserve	Retained earnings
Opening balance, Jan. 1	918	1,737	2,934
Dividend to shareholders			–688
Statute-barred dividend			0
Profit for the year			1 296
Closing balance, Dec. 31	918	1,737	3,542

Group shareholders' equity has been affected by translation differences arising from the application of the current method. By hedging the net assets of subsidiaries, translation differences have been reduced by 283.

The Atlas Copco Group's retained earnings are defined as follows: Parent Company's retained earnings plus the Group's share in each subsidiary's retained earnings, to the extent that they can be distributed without writing down the shares in the subsidiary.

This amount has been reduced by deducting the Group's share in the accumulated losses and other reductions of capital in subsidiaries to the extent that these amounts have not affected share values in the Parent Company's accounts. Internal profit eliminated in the consolidated balance sheet has also been charged against the Group's retained earnings.

Of the Group's retained earnings, 22 will be transferred to restricted reserves based on the proposals of the board of directors in each company.

Any evaluation of the Atlas Copco Group's retained earnings and net profit for the year should take into account that a substantial portion is earned by companies outside Sweden and that in certain cases profits transferred to the Parent Company are subject to taxation or restrictions.

19 Untaxed reserves

Untaxed reserves are reported in the Parent Company balance sheet as a compound item; the breakdown into individual items is shown below. These are totally eliminated in the consolidated accounts, as described in Accounting principles, page 19. Of the Parent Company's total untaxed reserves of 1,214, deferred tax accounts for 340, reported in the consolidated accounts.

	Parent Company	
	1997	1996
Accumulated depreciation in excess of cost depreciation		
Buildings and land	2	9
Equipment etc.	–	3
Tax allocation reserve	898	754
Foreign exchange reserve	143	48
Tax equalization reserve	171	228
	1,214	1,042

Provisions have been made to the tax allocation reserve as shown below:

	1997
1995	240
1996	253
1997	261
1998	144
Total	898

20 Provisions for pensions and similar commitments

	Group 1997	Group 1996	Parent Company 1997	Parent Company 1996
Swedish companies				
FPG/PRI-pensions	741	737	371	376
Other pensions	72	70	52	52
Companies outside Sweden	1,203	1,117		
	2,016	1,924	423	428

Pension liabilities and pension expenses for the year are calculated by Atlas Copco Group companies according to local rules and regulations. To the extent these rules and regulations allow unassailable pension obligations not to be reported as costs as pension rights accrue, adjustments have been made in the consolidated accounts. A certain portion of the pension costs for the year is reported as an interest expense, note 6. Accordingly, the item Provision for pensions is reported among interest-bearing provisions.

The majority of the Group's pension obligations are in Sweden, Germany, the United States, and Belgium. In addition to the statutory pension fees paid to government authorities, there are also costs for supplementary pension benefits based on individual or collective agreements between employer and employee representatives.

In Sweden, salaried employees' pension plans are administrated by the Pensions Registration Institute (FPG/PRI).

The amount for foreign companies includes 251 (232) for health-care benefits. The Atlas Copco Group applies U.S. regulations in accordance with FAS 106 (Employer's accounting for post-retirement benefits other than pensions) for medical care costs and pharmaceuticals for retired employees, which means that the present value of accrued future health care benefits is reported as a provision in the balance sheet.

21 Other provisions

	Group 1997	Group 1996	Parent Company 1997	Parent Company 1996
Provisions for guarantee commitments	247	200		
Other provisions	452	326	8	–
	699	526	8	–

Other provisions include reserves for future restructuring charges. The purchase cost brought forward for companies acquired includes 20 (22) in such restructuring charges.

22 Long-term liabilities to credit institutions

The Parent Company's long-term interest-bearing liabilities are reported in the balance sheet as a compound item; the breakdown into individual items is shown below:

	Parent Company 1997	Parent Company 1996
Liabilities to credit institutions, etc.	2,133	481
Liabilities to Group companies	139	177
Total interest-bearing liabilities	2,272	658

The Group's long-term liabilities to credit institutions and others are as follows.

	1997	1996
Parent Company		
Promissory notes USD 270.0 m.	2,133	481
Subsidiaries		
Financial leasing contracts	22	10
Other long-term loans	57	104
Less: amortization following year	–11	–24
Group loan liabilities	2,201	571

Loan liabilities are amortized as follows, translated at the exchange rates prevailing at December 31, 1997.

	Group	Parent Company
1998	11	–
1999	11	–
2000	404	395
2001	163	158
2002	1,620	1,580
2003 and later	3	–
	2,212	2,133

Group loan liabilities include future leasing costs attributable to financial leasing contracts. Payments due in 1998 are included in amortization following year and in the current loan liability. Future payments will fall due as follows:

Group	
1998	4
1999–2002	11
2003 and later	7
	22

23 Current liabilities to credit institutions

	Group 1997	Group 1996	Parent Company 1997	Parent Company 1996
Liabilities to credit institutions, etc.	7,599	1,865	6,928	985
Amortization following year	11	24	–	–
Liabilities to Group companies			910	1,386
Total interest-bearing liabilities	7,610	1,889	7,838	2,371

Current loan liabilities are reported in the Group's balance sheet as follows:

	1997	1996
Parent Company		
Available under "USD 200 m. Euro Commercial Paper Program"		
Outstanding USD 153.9 m.	1,216	377
DEM –	–	35
Available under "USD 1,200 m. U.S. Commercial Paper Program"		
Outstanding USD 540.5 m.	4,269	364
Available under "BEF 4,000 m. Treasury Note Program"		
Outstanding BEF 3,337.9 m.	714	–
Available under "SEK 400 m. Commercial Paper Program"	296	–
Other short-term loans and promissory notes	433	209
The Parent Company's loan liabilities	6,928	985
Subsidiaries	671	880
Group loan liabilities	7,599	1,865

The Atlas Copco Group's short-term and long-term loans are distributed among the following currencies. The table also reflects the effect of currency swap agreements at year-end.

Currency	Amount m.	SEK m.	1997 %	1996 %
USD	1,161	*9,175*	*93*	*60*
GBP	14	184	2	8
FRF	74	97	1	4
AUD	13	71	1	6
JPY	1,064	65	1	4
ITL	12,164	55	1	7
DEM	6	24	0	1
Others		140	1	10
		9,811	100	100

Atlas Copco AB has commercial paper programs for short-term borrowing in the U.S., Europe and Sweden, with a combined volume of about USD, 1,560 m., corresponding to SEK 12,300 m. These programs have a K1 rating in Sweden and an A1/P2/F1 rating internationally.

24 Operating liabilities

	Group 1997	Group 1996	Parent Company 1997	Parent Company 1996
Advances from customers	541	380	–	–
Accounts payable	1,869	1,543	6	8
Notes payable	128	93	–	–
Income tax liability	256	343	–	22
Other operating liabilities	1,255	933	15	4
Accrued expenses and prepaid income	2,617	1,531	709	78
Total non-interest-bearing liabilities	6,666	4,823	730	112

Accrued expenses and prepaid income for the Group contains the conventional items, such as social costs, deferred vacation pay liability, provisions and accrued interest. Accrued interest increased substantially from the preceding year partly as a result of accrued exchange rate differences attributable to hedging the value of equity in foreign subsidiaries.

25 Assets pledged and contingent liabilities

	Group 1997	Group 1996	Parent Company 1997	Parent Company 1996
Assets pledged for debts to credit institutions				
Real estate mortgages	35	25	–	–
Chattel mortgages	64	48	–	–
Receivables	103	92	–	–
	202	165	–	–
Contingent liabilities				
Notes discounted	62	58	–	–
Sureties and other contingent liabilities	1,312	1,042	529	512
	1,374	1,100	529	512

Of the contingent liabilities reported in the Parent Company, 475 (479) relates to contingent liabilities on behalf of subsidiaries.

26 Atlas Copco's stock option plan

The final outcome of Atlas Copco's yearly revolving stock option plan is linked to the performance of the Atlas Copco class A share. The size of grants will depend on the value added for shareholders in Atlas Copco. Grants will be determined by the fulfillment of a predetermined target for cash-flow performance minus Atlas Copco's cost of capital. This performance benchmark is called cash surplus (CS).

For 1998 grants will be made only if CS is positive and at least 50 percent of the performance target is reached. The maximum grant, approximately SEK 9 m. in all, will be made if CS reaches 120 percent of the target set by the Board.

Definitions

Cash surplus (CS)	Operating cash surplus – (pre-tax WACC x adjusted capital employed)
Operating cash surplus	Net invoiced sales – operating expenses + depreciation and amortization on fixed assets
Pre-tax WACC	WACC/(1–35%), where 35% is the estimated tax rate
Weighted average cost of capital (WACC)	$\dfrac{\text{Interest-bearing liabilities x i + market capitalization x r}}{\text{interest-bearing debt + market capitalization}}$
i:	The Swedish risk-free interest rate (10-year government bonds) plus 0.5 percentage points to compensate for the premium Atlas Copco pays on borrowings compared to that of the Swedish state.
r:	The Swedish risk-free interest rate, plus a risk premium (5.0%) times a risk factor (0.99) which indicates the volatility of Atlas Copco's share price compared to the stock market index.
Adjusted capital employed	Calculated at the beginning of the fiscal year as: Total assets – non-interest-bearing liabilities/provisions – short-term investments, cash, and bank accounts + accumulated depreciation of plant + accumulated amortization of goodwill.

Goodwill

The Group applies an amortization period of 40 years for goodwill arising from the acquisitions of the U.S. companies Milwaukee Electric Tool Corporation in 1995 (SEK 3,100 m.) and Prime Service, Inc. in 1997 (approximately SEK 6,800 m.). This provides the most accurate picture of the strategic acquisitions' impact on the Atlas Copco Group's earnings and financial position.

In taking this position, Atlas Copco deviated from that part of the recommendations of the Swedish Financial Accounting Standards Council, which prescribes amortization of goodwill over a maximum of 20 years. This does, however, not conflict with the legislation now in effect. Neither does this deviation represent a breach of the registration contract with the Stockholm Stock Exchange.

During 1996, the Swedish Financial Accounting Standards Council implemented a general review of its recommendation and published a new version, which became effective on January 1, 1997. However, with regard to the maximum amortization period for goodwill, the Council has elected to delay its recommendation pending the position to be adopted by the International Accounting Standards Committee (IASC). The Committee considers to omit the limitation of the amortization period to 20 years and permit an amortization period corresponding to the economic life, subject to a statement for the underlying assessment of the economic life. Atlas Copco intends to follow the final recommendation of the Council.

There are several strong reasons in these cases for the choice of an amortization period longer than 20 years. One reason being that it provides the most accurate picture of the acquisition. These strategic acquisitions involve two fairly large American groups whose operations and sales are mainly in the United States. The companies generate large cash flows. Another important reason for applying a longer amortization period is attributable to competitive factors. Atlas Copco must be in same position as other parties in calculating the economic consequenses of the purchase price and in the subsequent financial reporting of the acquisition. Currently, profitable companies command a price on the market which to a very large extent exceeds visible shareholders' equity. Consequently, the handling of goodwill becomes significant.

Since Atlas Copco is an international group with 97 percent of its sales outside Sweden – a country where there are no comparable competitors – it is of major importance that the Annual Report is internationally comparable. It is therefore necessary that the Swedish companies can apply rules equivalent to those of foreign competitors. These rules often permit amortization of goodwill over periods of up to 40 years.

For purposes of comparison, the impact on earnings resulting from the application of goodwill amortization over periods of 20 and 40 years is shown below:

Condensed income statement 1997, SEK m.

Amortization period	20 years	40 years
Revenues	30,032	30,032
Operating expense	–26,382	–26,219
Operating profit	3,650	3,813
– as percentage of revenues	12.2	12.7
Profit after financial items	3,357	3,520
– as percentage of revenues	11.2	11.7
Profit for the year	2,045	2,208
Earnings per share, SEK	11.14	12.03

Impact on equity

The equity/assets ratio is 39.2 percent. Based on a 20-year amortization period, the comparable figure is 38.7 percent.

Shares and participations Atlas Copco AB

	Number of shares	Per-cent held[1]	Book value
Direct owned product companies			
Atlas Copco Rock Drills AB, 556077-9018, Örebro	1,000,000	100	200
Atlas Copco Craelius AB, 556041-2149, Märsta	200,000	100	20
Uniroc AB, 556001-9019, Fagersta	2,325,000	100	112
Atlas Copco Berema AB, 556069-7228, Nacka	60,000	100	100
Atlas Copco Tools AB, 556044-9893, Nacka	100,000	100	20
Robbins Europe AB, 556062-0212, Nacka	95,000	100	11
Atlas Copco Controls AB, 556116-6355, Tyresö	35,600	100	30
Direct owned sales companies			
Atlas Copco Construction and Mining Export AB, 556395-7793, Nacka	500	100	7
Atlas Copco MCT Sverige AB, 556100-1453, Nacka	3,000	100	0
Atlas Copco Iran AB, 556155-2760, Nacka	3,500	100	0
Atlas Copco Compressor AB, 556155-2794, Nacka	60,000	100	10
Atlas Copco Ges.m.b.H., Vienna	45,000	100	13
Atlas Copco Brasil Ltda., Barueri	22,909,088	100	65
Atlas Copco Argentina S.A.C.I., Buenos Aires	157	0[2]	0
Atlas Copco Tools spol s. r. o., Praha	500	100	0
Atlas Copco Chilena S.A.C., Santiago de Chile	24,998	100	6
Atlas Copco (Cyprus) Ltd., Nicosia	99,998	100	0
Atlas Copco Kompressorteknik A/S, Glostrup	4,000	100	2
Atlas Copco (India) Ltd., Bombay	2,892,000	40	0
Atlas Copco KK, Tokyo	375,001	100	23
Atlas Copco Kenya Ltd., Nairobi	14,999	100	0
Atlas Copco (Malaysia), Sdn. Bhd., Selangor Darul Ehsan	700,000	70	2
Atlas Copco Maroc SA., Casablanca	3,850	96	1
Atlas Copco (Philippines) Inc., Makati City	121,995	100	3
Soc. Atlas Copco de Portugal Lda., Linda-a Velha	1	100	22
Atlas Copco (South-East Asia) Pte. Ltd., Singapore	2,500,000	100	8
Atlas Copco (Schweiz) AG, Studen/Biel	7,995	100	12
Atlas Copco Venezuela S.A., Caracas	37,920	100	14
Direct owned holding companies and subsidiaries			
Oy Atlas Copco Ab, Masala	150	100	30
Atlas Copco France Holding S.A., Franconville	329,994	100	192
Compresseurs Mauguière S.A., Sermamagny		100	
Atlas Copco Compresseurs S.A., Franconville		100	
Atlas Copco Applications Industrielles S.A., Franconville		100	
Atlas Copco Mines et Travaux Publics S.A., Franconville		100	
S.A. Ets Georges Renault, Nantes		100	
Desoutter S.A., Nanterre		100	
Compresseurs Industriels Holding S.A., Meru		100	
Atlas Copco Crépelle S.A., Lille		100	
Atlas Copco Holding GmbH, Essen	1	99[2]	403
Atlas Copco Energas GmbH, Cologne		100	
Atlas Copco MCT GmbH, Essen		100	
Atlas Copco Tools GmbH, Essen		100	
Atlas Copco Kompressoren GmbH, Essen		100	

	Number of shares	Per-cent held[1]	Book value
Desoutter GmbH, Hochstadt		100	
IRMER+ELZE Kompressoren GmbH, Oyenhausen		100	
Atlas Copco Elektrowerkzeuge GmbH, Essen		100	
Atlas Copco Electric Tools GmbH, Winnenden		100	
Atlas Copco UK Holdings Ltd., Hemel Hempstead	45,423,664	100	504
Atlas Copco Compressors Ltd., Hemel Hempstead		100	
Atlas Copco Construction & Mining Ltd., Hemel Hempstead		100	
Atlas Copco Tools Ltd., Hemel Hempstead		100	
Atlas Copco Kango Ltd, Peterborough		100	
Atlas Copco International Holdings Ltd., Hemel Hempstead		100	
Atlas Copco Namibia (Pty) Ltd., Windhoek		100	
Desoutter Brothers (Holdings) PLC, London		100	
Chicago Pneumatic Tool Co Ltd., Hemel Hempstead		100	
Atlas Copco Beheer b.v., Zwijndrecht	15,712	100	604
Atlas Copco Airpower n.v., Wilrijk		100	
Atlas Copco Coordination Center n.v., Wilrijk	1	0[2]	0
Atlas Copco Compressor International n.v., Wilrijk		100	
Atlas Copco Kompresory s.r.o., Praha		100	
Atlas Copco Kompresor Spolka z.o.o., Warzawa		100	
Atlas Copco Kompresszor Kft., Budapest		100	
Atlas Copco Anest Iwata KK, Fukushima		51	
Atlas Copco Mfg. Korea Co. Ltd, Seoul		100	
Atlas Copco Makinalari Imalat A.S., Istanbul	2,548,020	11[3]	0
Atlas Copco Rental Europe n.v., Wilrijk		100	
Atlas Copco S.A.E., Madrid		100	
Atlas Copco Internationaal b.v., Zwijndrecht		100	
Atlas Copco Australia Pty Ltd., Blacktown		100	
Atlas Copco Belgium n.v., Overijse		100	
Power Tools Distribution n.v., Hoeselt	1	0[2]	0
Atlas Copco Tools Europe n.v., Wilrijk		100	
Power Tools Business Services n.v., Wilrijk		100	
Atlas Copco Colombia Ltda., Bogota		100	
Atlas Copco Hellas AE, Rentis		100	
Atlas Copco (China) Ltd., Kowloon		100	
Nanjing Atlas Copco Construction Machinery Ltd, Nanjing		92	
Wuxi-Atlas Copco Compressor Co Ltd, Wuxi		92	
Shanghai Atlas Copco Machinery Co Ltd, Shanghai		70	
Atlas Copco (HK) Ltd., Kowloon		100	
Atlas Copco Changchun Electric Power Tool Ltd, Changchun		70	
Atlas Copco Italia S.p.A., Milano		100	
Inversora Capricornio S.A. de C.V., Tlalnepantla		100	
Atlas Copco Nederland b.v., Zwijndrecht		100	

	Number of shares	Per-cent held[1]	Book value
Atlas Copco Construction Tools Distribution Center b.v., Zwijndrecht		100	
Atlas Copco Canada Inc., Dorval		100	
Atlas Copco Peruana S.A., Lima		100	
ZAO Atlas Copco, Moscow		100	
Atlas Copco Holdings South Africa (Pty) Ltd., Benoni		100	
Atlas Copco Controls S.A., Penthaz		100	
Atlas Copco Elesta S.A., St.Gallen		100	
Atlas Copco Taiwan Ltd., Taipei		100	
Atlas Copco (Zambia) Ltd, Ndola		100	
Atlas Copco Zimbabwe (Private) Ltd., Harare		100	
Atlas Copco A/S, Langhus	4,498	100	32
Atlas Copco North America Inc., Wayne	35,506	40[2]	796
Atlas Copco Berema Inc., Norwalk		100	
Atlas Copco Comptec Inc., Voorheesville		100	
Atlas Copco Compressors Inc., Holyoke		100	
Atlas Copco Tools Inc., Farmington Hills		100	
Atlas Copco Rental Inc., Fairfield		100	
Atlas Copco Roctec Inc., Denver		100	
Atlas Copco AFS Inc., Detroit		100	
Atlas Copco Rotoflow Inc., Los Angeles		100	
Uniroc, Inc., Commerce City Col.		100	
Atlas Copco Wagner Inc., Portland		100	
Desoutter Inc., Livonia, Michigan		100	
Atlas Copco Controls Inc., Pittsburg		100	
Chicago Pneumatic Tool Company, Rock Hill, SC		100	
Atlas Copco Robbins Inc., Kent, WA		100	
Esstar Inc., New Haven		100	
Milwaukee Electric Tool Corporation, Milwaukee		100	
Prime Service, Inc., Houston		100	
Other direct owned companies			
Atlas Copco Construction & Mining Technique AB, 556277-9537, Nacka	700,500	100	356
Industria Försäkrings AB, 516401-7930, Nacka	50,000	100	5
Atlas Copco Reinsurance S.A., Luxemburg	4,999	100	8
Atlas Copco Fondaktiebolag, 556113-5541, Nacka	2,500	100	0
25 dormant companies			29
TOTAL BOOK VALUE			**3,640**

1) Percentage of number of shares equal to percentage of votes

2) Percent held refers to Atlas Copco AB, remaining holding owned by other Group companies

3) Percent held refers to Atlas Copco AB, 72 percent owned by other companies within the Group

Financial exposure

The objective of Atlas Copco's financial risk policy is to minimize the financial risks to which the Group is exposed. It is designed to create stable conditions for the business operations of the divisions and contribute to a stable growth in shareholders' equity and dividend.

Currency risk

Changes in exchange rates affect Group earnings and equity in various ways:

- Group earnings – when revenues from sales and costs for production are in different currencies (transaction risk).
- Group earnings – when earnings of foreign subsidiaries are translated into Swedish kronor (translation risk).
- Group shareholders' equity – when the net assets of foreign subsidiaries are translated into Swedish kronor (translation risk).

Transaction risk

The Group's net payment flows in foreign currency give rise to transaction risks and corresponded to a value of SEK 7,000 m. in 1997. The largest surplus currencies, meaning those in which revenues exceed costs, and the deficit currencies, are shown in graph 1.

According to the policy such foreign currency flows must be hedged but only for the period it is estimated it takes to adjust prices and/or costs to the new exchange rates. These periods vary among the divisions and amount on average to 3–4 months for the Group.

Consequently, changes in exchange rates have a relatively rapid impact on Group earnings. The hedging of currencies is aimed at securing calculated gross margins, and not maximizing them through speculation.

Translation risk

The risk policy states that the effect of currency changes on the Group's equity, expressed in SEK, shall be reduced by matching the currency of loans with the currency of the net assets, which corresponds to the value of foreign subsidiaries' equity. Derivative contracts like forwards, swaps and options shall not be used for this hedging purpose, as derivative contracts give rise to cashflow risks at roll-over dates.

The percentage of foreign equity that will be effectively hedged against the SEK will vary depending on the borrowing requirements. As per December 31, 1997, approximately 40 percent was hedged.

The described procedure constitutes a change compared to previous years when the policy stated that approximately 80 percent of foreign subsidiaries' equity should be hedged against SEK and that derivative contracts or loans could be used to perform the hedge. Based on the currency and interest-rate situation as per December 31 1997, this change of policy will not have any material impact on Group earnings.

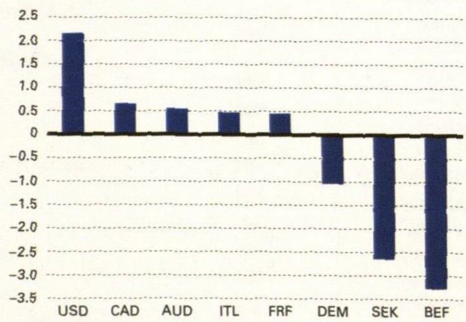
Note 18 in the financial statements shows how shareholders' equity was affected by currency hedging in 1997.

The interest differential between international and Swedish interest rates on forward contracts and swap agreements used in the hedge, prior to the change of policy described above, appears in the Group's interest net and amounted in 1997 to SEK 140 m. (231). The value of the equity of foreign subsidiaries at year-end 1997 corresponded to approximately SEK 9,400 m.

Graph 1

Transaction exposure in the most important currencies

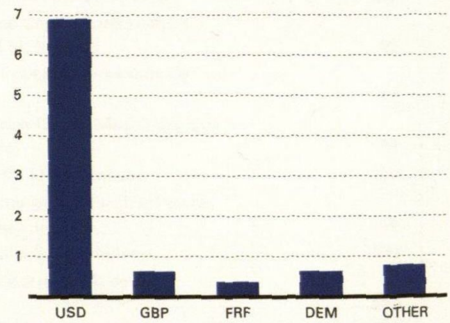
SEK billion



Graph 2

Net assets in foreign currency

SEK billion



and is shown in graph 2, distributed by main currencies.

As a consequence of the Prime Service acquisition in the U.S. the Group increased its net assets in USD with an amount corresponding to more than SEK 4,000 m. In that connection the Group's net assets in BEF decreased with a corresponding amount as the capital injection was submitted from Belgium.

Graph 3 shows the currency translation effects on Group earnings for the year when the earnings of foreign subsidiaries are translated to SEK.

Interest-rate risk

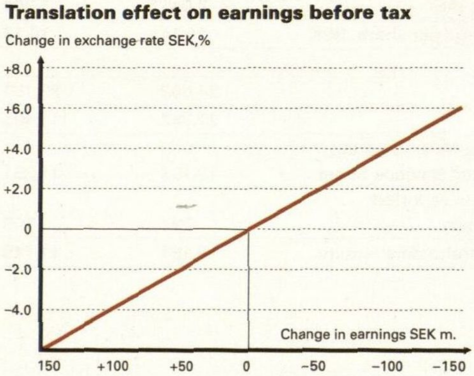
Atlas Copco's net interest items are affected by changes in market interest rates. The speed with which a permanent change in the interest rate can have an impact on net interest income or expense is dependent on the duration of the fixed interest periods on loans and investments. According to the financial risk policy, the average interest-rate period for loans shall not exceed three years and not be less than three months. Deposits with fixed interest shall not exceed 12 months. At year-end 1997, the average period was 20 months for loans and less than one month for investments.

Standardized derivative instruments are used actively to control interest-rate exposure, for example, by extending or reducing the average interest-rate period without replacing the underlying loan or deposit.

Funding risk

Atlas Copco's financial policy states there should always be sufficient funds to cover expected requirements for the next 12 months. Furthermore, a portion of the total debt shall always be long-term. The aim is to have an amount corresponding to all fixed assets covered by equity and interest-bearing debt with longer maturity than five years, including pension debt.

Graph 3
Translation effect on earnings before tax



Exchange rates

Country	Value	Currency code	Year-end rate 1997	Year-end rate 1996	Average rate 1997	Average rate 1996
Australia	1	AUD	5.17	5.48	5.65	5.24
Austria	100	ATS	62.60	62.80	62.80	63.50
Belgium	100	BEF	21.40	21.50	21.40	21.70
Canada	1	CAD	5.49	5.02	5.49	4.92
France	100	FRF	131.70	131.00	131.30	131.50
Germany	100	DEM	440.70	442.10	441.90	446.80
Great Britain	1	GBP	13.14	11.61	12.52	10.52
India	100	INR	20.10	19.10	20.90	19.00
Italy	100	ITL	0.449	0.450	0.449	0.435
Japan	100	JPY	6.09	5.93	6.29	6.18
Luxemburg	100	LUF	21.40	21.50	21.40	21.70
The Netherlands	100	NLG	391.10	393.90	392.60	398.70
Norway	100	NOK	107.30	106.60	108.20	104.10
Singapore	1	SGD	4.71	4.91	5.13	4.76
South Korea	100	KRW	0.483	0.814	0.808	0.834
Spain	100	ESP	5.21	5.25	5.23	5.30
Switzerland	100	CHF	543.20	508.40	527.20	544.10
U.S.	1	USD	7.90	6.87	7.62	6.71
Atlas Copco's currency index for transaction exposure			101.2	96.3	100	94.7

(A higher index indicates a positive effect on Group earnings).

Based on the value of payment flows in various currencies, Atlas Copco applies a weighted currency index, in which the average rate for 1997 is the base period. The index shows how earnings are affected by changes in exchange rates. With the current flows and prevailing exchange rates, each percentage point represents a gross impact – before any hedging or adjustment measures – of SEK 75–80 m. on annual earnings before tax.

Credit risk

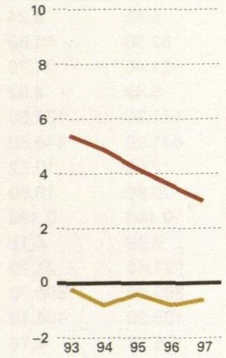
Investments in the money and bond markets are conducted by Group Treasury Center in Sweden. These operations are governed by a restrictive policy with regard to credit risk, with only a very limited group of approved borrowers. No credit losses arose in 1997.

Financial derivative instruments

Atlas Copco uses standardized financial derivatives such as forward transactions, options and swaps, primarily with a view to reducing currency and interest-rate risks.

These financial derivatives are also highly valuable complements to loans and investments in the work to effectively control the Group's cash balance and borrowing. The liquidity of these instruments is also normally higher than in the underlying assets. The difference between market value and book value of all the Group's derivative instruments at year-end 1997 was insignificant.

Difference US GAAP/ Swedish accounting



– Equity
– Earnings per share (the minus sign denotes that the item based on US GAAP is lower)

International accounting principles

The consolidated accounts for the Atlas Copco Group follow Swedish accounting practices. Swedish accounting practices, however, diverge from international practices on certain points. A calculation of the income for the year and financial position, taking into account the major differences between Swedish accounting practice and the U.S. GAAP and IAS standards is provided below.

U.S. accounting principles, U.S. GAAP

Revaluation of assets

Certain properties have been written up to amounts which exceed the acquisition cost. In specific situations, such revaluations are permitted by Swedish accounting practice. According to U.S. GAAP, revaluations of assets are not reported in the Balance Sheet.

Capitalization of interest expenses

In accordance with Swedish accounting practice, the Group has expensed interest payments arising from the external financing of newly constructed fixed assets. According to U.S. GAAP, such interest expenses are capitalized.

Forward contracts

Hedging transactions via forward contracts are reported in the Swedish accounts on the basis of budgeted volume. For a contract to be treated as a hedge in accordance with U.S. GAAP, there must be a firm commitment. The effect of the difference in accounting princples is not substantial and is not included in the accompanying reconciliation.

Pension provisions

In the U.S. other rules govern accounting of pension provisions. In general, these rules are applied by Atlas Copco's U.S. subsidiaries. Compared with Swedish accounting practice for FPG/PRI pension provisions, there are differences, primarily in the selection of the discount rate and in that the calculation of equity value is based on the salary or wage at the date of retirement. Possible differences have not been quantified and are not included in the following U.S. GAAP account presentation.

Application of U.S. GAAP would have the following approximate effect on consolidated net profit for the year and shareholders' equity for the Group:

	1997	1996
Profit for the year as reported in the Consolidated Income Statement	2,208	1,938
Items increasing/decreasing reported net profit:		
Depreciation/sales of revaluations	2	1
Capitalization of interest expenses	−12	−7
Amortization of goodwill	−12	−12
Deferred taxes	8	3
Calculated profit, U.S. GAAP	2,194	1,923
Calculated earnings per share, SEK	11.96	10.48
Total assets	35,242	23,725
Total liabilities	21,383	11,450
Shareholders' equity as reported in the Consolidated Balance Sheet	13,453	11,851
Net adjustments in reported shareholders' equity	406	424
Approximate shareholders' equity	13,859	12,275

Application of IAS would have the following approximate effect on consolidated net profit for the year and shareholders' equity for the Group:

	1997	1996
Profit for the year as reported in the Consolidated Income Statement	2,208	1,938
Items increasing/decreasing reported net profit:		
Amortization of goodwill	−163	−74
Calculated profit, IAS	2,045	1,864
Calculated earnings per share, SEK	11.14	10.16
Total assets	34,503	23,150
Total liabilities	21,342	11,405
Shareholders' equity as reported in the Consolidated Balance Sheet	13,453	11,851
Net adjustments in reported shareholders' equity	−292	−106
Approximate shareholders' equity	13,161	11,745

Company acquisitions

In accordance with Swedish accounting practices, the Secoroc Group has been included in the consolidated accounts for 1988 according to the pooling of interests method. The U.S. GAAP criteria for the application of the pooling of interests method differs in certain respects from the criteria then applicable, according to Swedish practices. One of the criteria in U.S. GAAP is that none of the merging companies may be a subsidiary of another company during the two years preceding the merger. On the date of acquisition, Secoroc was a subsidiary of Kinnevik, as a result of which it is impossible to apply the pooling of interests method according to U.S. GAAP.

Share premium and restructuring reserves

Atlas Copco's accounting principles for allocation of share premiums in company acquisitions and for establishing a reserve for restructuring costs may differ from US GAAP. However, the effect of this difference is not regarded as material.

Deferred taxes

Effective in 1993, Atlas Copco applies FAS 109, which requires that operations in each year be charged with the tax for that year. Consequently, deferred tax is calculated on all the differences between book valuation and valuations for tax purposes (temporary differences).

Tax-loss carryforwards are anticipated in those cases in which it is more likely than not that these will be utilized.

No adjustment has been made for deferred taxes on the translation differences arising from the use of the monetary/non-monetary method, since such differences are regarded as marginal.

Translation differences in shareholders' equity

According to Swedish accounting practice, all account items included in shareholders' equity must be classified in the Balance Sheet as restricted equity (share capital and restricted reserves) or as unrestricted equity. The accumulated exchange differences arising from the translation of the financial statements of foreign companies are distributed among restricted and unrestricted equity in the Consolidated Balance Sheet. According to U.S. GAAP, this currency component is shown as a separate item in the Balance Sheet. In the sale/discontinuation of foreign subsidiaries, the result from the discontinuation shall also include accumulated translation differences.

International Accounting Standards, IAS

With the exception of only a few points, Atlas Copco's accounting principles are in accordance with IAS.

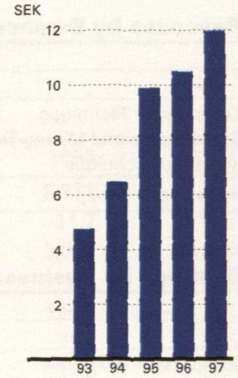
Translation of foreign subsidiaries

In a couple of instances, the monetary/non-monetary method has been applied in the translation of foreign subsidiaries in countries with high inflation. According to the IAS recommendations, such translations are based on the application of an inflation index. In terms of the effect on earnings, the difference is considered marginal.

Amortization of goodwill

The goodwill arising from the acquisition of Milwaukee is being amortized over a period of 40 years. According to IAS, goodwill may be amortized over a period not exceeding 20 years.

Earnings per share according to US GAAP



Sales and earnings by quarter

Revenues by Business Area and Quarter

				1996				1997
	I	II	III	IV	I	II	III	IV
Compressor Technique	2,630	2,792	2,635	3,015	2,809	3,280	3,950	4,224
Construction and Mining Technique	1,448	1,535	1,346	1,592	1,458	1,743	1,557	1,695
Industrial Technique	1,956	2,013	1,962	2,197	2,139	2,355	2,286	2,536
Atlas Copco Group	6,034	6,340	5,943	6,804	6,406	7,378	7,793	8,455

Earnings by Business Area and Quarter

				1996				1997
	I	II	III	IV	I	II	III	IV
Compressor Technique	399	462	445	501	462	581	730	764
Construction and Mining Technique	109	115	60	112	90	126	91	80
Industrial Technique	289	172	153	222	218	258	196	270
Corporate items	–28	–27	–26	–27	–22	–8	–24	1
Operating profit after depreciation	769	722	632	808	748	957	993	1,115
Financial items	34	42	33	30	–13	27	–147	–160
Profit after financial items	803	764	665	838	735	984	846	955

Definitions

Profit margin
Profit after financial items as a percentage of revenues.

Return on capital employed
Profit after financial items plus interest paid and foreign exchange differences as a percentage of average total assets less non-interest-bearing liabilities/provisions.

In calculating capital employed in the business areas, in contrast to the calculation for the Group, deferred tax liabilities are not deducted.

Return on equity
Profit after financial items less full tax and minority interest as a percentage of average shareholders' equity.

Equity/assets ratio
Shareholders' equity and minority interest, as a percentage of total assets.

Self-financing ratio
Surplus liquid funds from operations as a percentage of investments in tangible fixed assets.

Capital turnover ratio
Revenues divided by average total assets.

Net indebtedness
Difference between interest-bearing liabilities/provisions and liquid assets.

Debt/equity ratio
Net indebtedness in relation to shareholders' equity, including minority interest.

Interest coverage ratio
Profit after financial items plus interest paid and foreign exchange differences divided by interest paid and foreign exchange differences.

Earnings per share
Profit after financial items less full tax and minority interest, divided by the average number of shares outstanding.

Five years in summary

Atlas Copco Group

SEK m. unless otherwise noted.*	1993	1994	1995	1996	1997
Operating profit	1,225	1,890	2,665	2,931	3,813
Operating profit margin, %	6.5	9.0	10.9	11.7	12.7
Profit after financial items	1,320	1,955	2,840	3,070	3,520
Profit margin, %	7.0	9.3	11.6	12.2	11.7
Profit for the year	867	1,194	1,823	1,938	2,208
Return on capital employed, %	13.2	18.4	22.4	21.2	21.1
Return on equity, %	11.0	13.7	18.6	17.5	17.6
Equity/assets ratio, %	47.8	51.1	47.8	51.8	39.2
Earnings per share, SEK	4.74	6.51	9.93	10.56	12.03
Dividend per share, SEK	1.80	2.30	3.00	3.75	4.25 **
Orders received	19,194	21,701	24,843	25,159	30,685
Revenues	18,906	20,914	24,454	25,121	30,032
Change, %	+18	+11	+17	+3	+20
Sales outside Sweden, %	95	95	96	96	97
Net interest expense	39	57	129	127	-306
As percent of revenues	0.2	0.3	0.5	0.5	-1.0
Interest coverage ratio	5.1	6.7	8.7	10.6	6.5
Cash flow from operations after financial items	1,306	1,376	1,530	1,920	3,878
Total assets	17,822	18,198	22,106	23,175	34,790
Assets/liabilities ratio	1.9	2.0	1.9	2.1	1.6
Current assets/current liabilities ratio	1.8	2.0	1.7	1.9	1.0
Debt/equity ratio, %	20.9	3.8	29.9	15.8	74.9
Capital turnover ratio	1.09	1.16	1.19	1.11	1.08
Investments in property and machinery	394	632	711	822	840
As percent of revenues	2.1	3.0	2.9	3.3	2.8
Investments in rental equipment	229	169	228	336	920
As percent of revenues	1.2	0.8	0.9	1.3	3.1
Average number of employees	18,247	18,104	19,751	21,085	22,296
Revenues per employee, SEK thousands	1,036	1,155	1,238	1,191	1,347
Value added per employee, SEK thousands	408	480	512	496	586

* For definitions, see page 40.
** According to the Board of Directors' proposal.

Appropriation of profit

Proposed distribution of profit

As shown in the balance sheet of Atlas Copco AB, the following funds are available for appropriation by the Annual General Meeting:

Unappropriated earnings from preceding year	SEK 2,246,622,902
Profit for the year	SEK 1,295,713,155
	SEK 3,542,336,057

The Board of Directors and the President propose that these earnings be appropriated as follow:

To the shareholders, a dividend of SEK 4.25 per share	SEK 779,942,660
To be retained in the business	SEK 2,762,393,397
	SEK 3,542,336,057

Nacka, February 23, 1998

Anders Scharp
Chairman

Tom Wachtmeister, Gösta Bystedt, Michael Treschow

Erik Belfrage, Paul-Emmanuel Janssen, Hari Shankar Singhania

Sune Carlsson, Lennart Jeansson, Giulio Mazzalupi *President*

Tore Hedberg, Lars-Erik Soting, Bengt Lindgren

Auditors' Report

To the General Meeting of the shareholders of Atlas Copco AB, reg. no. 55 60 14-2720.

We have audited the Parent Company and the consolidated financial statements, the accounts and the administration of the Board of Directors and the President of Atlas Copco AB for 1997. These accounts and the administration of the Company are the responsibility of the Board of Directors and the President. Our responsibility is to express an opinion on the financial statements and the administration based on our audit.

We conducted our audit in accordance with Generally Accepted Auditing Standards in Sweden. Those Standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and their application by the Board of Directors and the President, as well as evaluating the overall presentation of information in the financial statements. We examined significant decisions, actions taken and circumstances of the Company in order to be able to determine the possible liability to the Company of any board member or the President or whether they have in some other way acted in contravention of the Companies Act, the Annual Accounts Act or the Articles of Association. We believe that our audit provides a reasonable basis for our opinion set out below.

In our opinion, the Parent Company and the consolidated financial statements have been prepared in accordance with the Annual Accounts Act and, consequently we recommend

that the income statements and the balance sheets of the Parent Company and the Group be adopted, and

that the profit of the Parent Company be dealt with in accordance with the proposal in the Administration Report.

In our opinion, the board members and the President have not committed any act or been guilty of any omission, which could give rise to any liability to the Company. We therefore recommend

that the members of the Board of Directors and the President be discharged from liability for the financial year.

Nacka, March 2, 1998

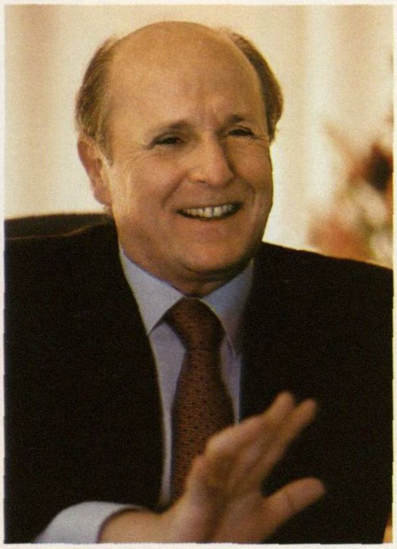
Stefan Holmström
Authorised Public Accountant

Robert Barnden
Authorised Public Accountant

Prime Service rents equipment such as compressors and breakers to mainly contractors and industrial customers.

Increased growth rate

Atlas Copco's operations continued to expand in 1997, and the Group achieved a higher rate of growth than in 1996. Demand in the USA remained on a good level, while Europe began to recover slowly. Although the latter part of the year was characterized by financial uncertainty in Asia, both sales and earnings for the full year improved on those of 1996.



In 1997, we took a number of actions to accelerate the rate of growth. The most significant action was to acquire Prime Service, USA, our biggest acquisition ever. With the Prime acquisition, we have taken a significant step into the equipment rental business in the US. The move reflects our strategic goal to increase revenues related to "use of products," that is service, parts, and accessories as well as equipment rental. The acquisition will generate synergy with other divisions in the Group and has already led to a better balance of sales between Europe and North America.

During the year, North and South America had good demand, although the Brazilian market showed signs of weakening at the end of the year. Europe has been recovering slowly, and the German and French economies performed better in 1997 than in the preceding year. The financial crisis in Asia particularly affected South Korea and Southeast Asia, and we are now seeing signs of its negative impact on Japan and Australia. On the positive side, China continues to perform well.

We improved our profit after financial items, to SEK 3,520 m., corresponding to an increase of 15 percent and a profit margin of 11.7 percent. The Group's objective is to achieve a profit margin of at least 10 percent over a full business cycle. Since 1993 Atlas Copco has recorded an average profit margin of 10.6 percent.

The good results in 1997 were attributable to a higher volume but also to a very favorable currency effect compared to the preceding year, primarily a result of the stronger US dollar. We had a strong operating cash flow, SEK 3,878 m. before dividends and acquisitions, which is necessary if the Group is to keep growing.

Compressor Technique

The Compressor Technique business area generated strong growth in 1997, as all divisions reported increased volume. Business was particularly good in Asia and in eastern and southern Europe. The profit margin improved because of a combination of larger volumes, higher efficiency, and a positive currency effect. The operating margin rose to 17.8 percent.

During the year, Compressor Technique acquired two compressor manufacturers: Thomé-Crépelle, of France, and Ceccato, of Italy.

Construction and Mining Technique

The Construction and Mining Technique business area continued to benefit from higher levels of investment in the mining sector, which led to improved sales of loaders and drilling equipment. The low demand for construction machinery, however, had a dampening effect on sales. The crisis in Asia amplified this situation towards year-end.

Although the business area's divisions attained better stability, further actions are required to enhance efficiency and earnings. The operating margin, which ended at 6.0 percent, has still not reached the expected level.

In 1997, the Group decided to withdraw from the niche market for tunnel-boring machines because of the lack of synergy between that business and other divisions in the business area.

Industrial Technique

The Industrial Technique business area improved revenues for the year, mainly through increased sales of electric power tools and industrial tools. Atlas Copco Industrial Tools and Equipment division continued to perform on a high level. The business area reported an operating margin of 10.1 percent, mainly because of better sales volumes.

Innovative products
In 1997, Compressor Technique fully introduced a new generation of large, oil-free screw compressors aimed at the electronics, pharmaceutical, and automotive industries.

Construction and Mining Technique developed a new range of underground drilling rigs. Another innovation in 1997 was a lightweight, motorized breaker specially designed for construction applications. A range of new bench drill bits, which increase productivity in quarry operations, was also launched. New loaders and truck models were also introduced during the year.

The Industrial Technique area launched a steady stream of new products in 1997. The range of powerful cordless tools was extended by new drills and a new rotary hammer. A new series of nut runners was introduced, as was a range of grinders for foundries and mechanical engineering companies.

Knowledge transfer
Atlas Copco regularly conducts training seminars for managers in the divisions. In 1997, Atlas Copco established a school in China to provide the growing number of employees recruited in the region with professional training and a better understanding of their role in the overall workflow. Also in 1997, the "Atlas Copco Circles" project was completed, which aimed to increase employees' knowledge of the Group and their understanding of Group strategy.

We also consider it important to encourage managers to move between different functions and geographic areas. To support mobility within the Group, an internal project market was introduced where employees can apply for temporary assignments to projects.

Today, senior management is composed of people of many different nationalities and ethnic groups, but we still do not have an adequate balance of female and male managers.

Growth strategies
We reviewed Group strategy in 1997 with further emphasis on growth. One of our strategic directions for growth is to develop new products from our core technologies to serve a wider range of applications on more markets than previously. The other two directions for growth are to increase our revenues in Asia and the revenues related to "use of products". To support organic growth, we will strengthen the Atlas Copco brand.

Our strategic goal for Asia in the long term is to have the region account for one third of the Group's world-wide turnover. We strengthened management in the region during 1997 and we enhanced training programs for employees. We have further developed our joint ventures and reinforced the ownership structure in those companies. The current financial and economic difficulties in Asia have led to certain temporary adjustments in the region, but it has not affected our long-term objectives there.

The driving force behind "use of products" is the fact that rental operations and after-sales service account for an increasing proportion of total sales. Service, parts, accessories, consumables, and equipment rental are fast-growing businesses.

We have increased our target for annual sales growth, from 5 percent to 8 percent, but we still require that our divisions are stable and have achieved reasonable profitability before they focus on growth.

Outlook 1998
We expect demand in the USA to remain on a good level in 1998. The recovery in Europe is expected to continue, while demand in South America is likely to decline. It is difficult to predict the impact of financial instability in Asia on other parts of the world. Construction activity is likely to remain on a low level, and the mining industry is expected to show weaker demand.

What all this means is that we must emphasize flexibility even more and must quickly react to change. We must speed up the launch of new products. At the same time, because our possibilities for increasing prices in the market are limited, we must have better control of costs so we can maintain our competitiveness in the market place.

Our ongoing efforts to improve operations and our ambition to expand will lead to continued favorable growth in 1998.

Giulio Mazzalupi

Increased volumes for all divisions

Stronger demand was evident in 1997 for all types of compressor. Increased volumes and favorable exchange rates helped the business area boost operating profit 40 percent, to SEK 2,537 m. (1,807).

The business area develops Atlas Copco's position as the leader in air compressor business on a worldwide basis. As part of this strategy, the business area markets quality products to industrial customers who demand a high level of operating reliability and productivity in their plants. Each division is responsible for the development, manufacturing and marketing and sales of its own products.

Structural changes

On July 1, 1997, Atlas Copco acquired Prime Service, Inc., one of the biggest equipment rental companies in the United States. At the time of acquisition, Prime Service had 2,200 employees and 122 rental yards in 14 states serving more than 40,000 customers. 1996 revenues totaled roughly SEK 2,500 m. and operating profit SEK 510 m. During the second half of 1997, Prime Service purchased five equipment rental companies in the U.S. with total annual sales of about SEK 560 m. Prime Service is a separate division in the business area.

Atlas Copco acquired the compressor business of Ceccato, in Vicenza, Italy, effected January, 1998. The company manufactures and markets small and medium-sized industrial compressors, has annual revenues of approximately SEK 200 m. and employs 125 people. Ceccato is part of the Industrial Air division.

Effective June 1, 1997, Atlas Copco acquired Thomé-Crépelle, a French manufacturer of large industrial piston compressors. The company has 200 employees and is located in Lille, France. Thomé-Crépelle has annual sales of roughly SEK 250 m. and is now part of the Atlas Copco ACT division.

In March 1997, Worthington Creyssensac, part of the Industrial Air division, signed a joint venture with Shanghai General Machinery Group, China, on the production and sales of oil-injected screw compressors. The joint venture will commence operations during the first half of 1998. Atlas Copco holds a 58-percent of the shares in the company.

Sales

Revenues increased 29 percent, to SEK 14,263 m. (11,072), and orders received were up 33 percent, to SEK 14,699 m. (11,012). For comparable units, invoicing rose 13 percent, and orders received 15 percent. The biggest sales increases were noted in Asia and eastern and southern Europe.

Earnings

Operating profit increased 40 percent, to SEK 2,537 m. (1,807). Earnings corresponded to 17.8 percent (16.3) of revenues. The improvement resulted from higher volumes, better productivity and favorable exchange rates as well as the acquisition of Prime Service. Return on capital employed amounted to 28 percent (33).

Investments

The business area's investments in property and machinery totaled SEK 344 m. (285). The majority of investment was in new production equipment for factories. Investment in rental equipment equaled SEK 666 m.

Business development

During the year, all divisions in the business area noted stronger demand for their products.

Airtec, which makes compressor elements, augmented production capacity in 1997 to meet the higher demand level.

Portable Air boosted sales, primarily of large portable compressors. In the autumn, the division started supplying compressors to Prime Service.

Industrial Air enjoyed favorable growth for all types of screw compressors.

Oil-free Air increased its sales volume on most markets outside western Europe.

The ACT division's deliveries of large customized compressors, had a favorable growth during the year. The demand was on a good level for air separation applications.

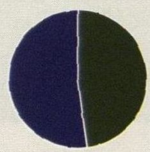
In the autumn, Prime Service acquired five U.S. rental companies, thus improving its market coverage. Since Atlas Copco acquired Prime Service the number of rental yards have increased by 35 percent to 160.

Outlook for 1998

Demand for compressors is expected to grow somewhat in 1998. A negative development is, however, foreseen in Asian markets. Its potential influence on the demand in other markets creates uncertainty regarding the overall development in 1998.

Henri Ysewijn *Hans W Brodbeck* *Johan Molin* *Luc Hendrickx* *James Tapkas* *Thomas E. Bennett*

The Compressor Technique business area develops, manufactures and markets industrial, oil-free and portable air compressors, generators, air dryers, after-coolers, control systems, filters and specially built gas and process compressors, expansion turbines and pumps. The business area is headquartered in Antwerp, Belgium, and has factories in Antwerp as well as Cologne, Germany, Méru, Lille and Belfort, France, Los Angeles and Albany, United States, Wuxi and Shanghai, China and from January 1998 in Vicenza, Italy. Products are also assembled at plants in five other countries. With the acquisition of Prime Service, the business area has entered the business of equipment rental to construction and industrial markets in the U.S.



Compressor Technique

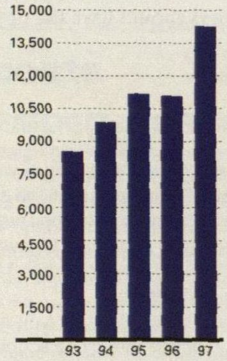
Share of Group revenues 48%

The Compressor Technique business area comprises the following divisions:

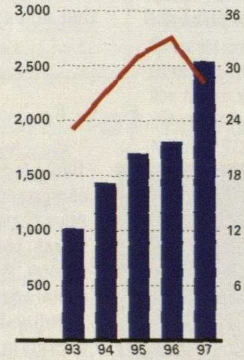
- Airtec, President *Henri Ysewijn*
- Portable Air, President *Hans W Brodbeck*
- Industrial Air, President *Johan Molin* (effective January 15, 1998)
- Oil-free Air, President *Luc Hendrickx*
- Atlas Copco Applied Compressor and Expander Technique (ACT), President *James Tapkas*
- Prime Service, President *Thomas E. Bennett*

	1997	1996
Revenues, SEK m.	14,263	11,072
Operating profit, SEK m.	2,537	1,807
Return on capital employed, %	28	33
Investments, SEK m.	344	285
Number of employees	9,235	7,698

Revenues



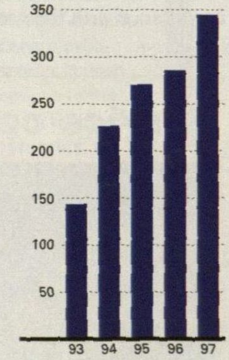
Earnings and return



— Return on capital employed, %

■ Operating profit SEK m.

Investments*



*excluding rental equipment

Service around the clock

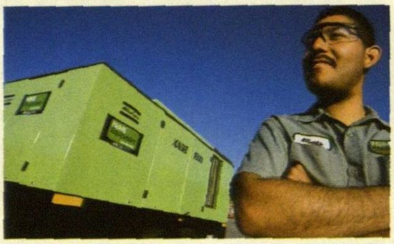
With more than 160 rental yards in 20 U.S. states, Prime Service is oriented toward providing a high level of service. The company maintains an extensive rental fleet to cover changing equipment demands from contractors and industrial customers.

Prime has more than 55,000 customers. The main segment consists of contracting and industrial companies, which account for 50 percent each of total sales.

The company adjusts its product range in accordance with the needs of the local market and strives to cover all possible needs. For example building contractors have a great need of compressors, work platforms and construction equipment. The company's corporate philosophy is that all customers should have the opportunity to rent or purchase all the equipment they require from one rental yard.

For many years, Prime has held a strong position within the petrochemical industry. One of the largest rental yards is close to the harbor in Houston, Texas,

Service concept for increased growth



Through the acquisitions it has made, Prime Service has achieved a leading position in the U.S. equipment rental market. During 1997 alone, the company acquired seven companies, whereof five were acquired after Atlas Copco's acquisition, and opened new stores, resulting in an additional 60 outlets. In total, Prime Service has more than 160 rental yards in the U.S.

Prime Service has established a number of criteria that must be met by an acquisition target. The company must be profitable and offer a product range that is similar to that of Prime Service. Another important factor is that the local market is not dominated by any one industry. Preferably, there should be an equal number of construction and industrial companies in the local market.

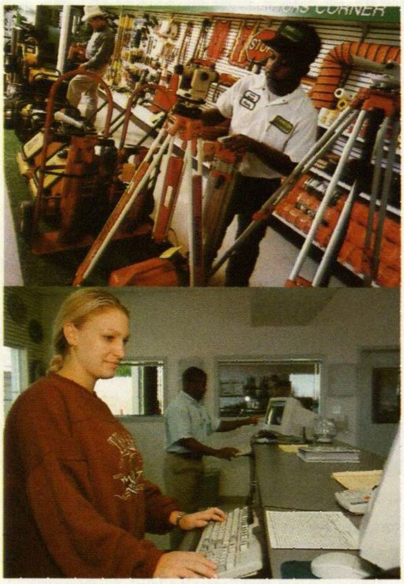
In connection with its acquisitions, Prime Service has set up special project groups to rapidly implement various measures. An important activity in this respect is to expand the customer base by marketing Prime's services via telemarketing channels. The company also installs modern IT systems in the acquired companies in order to provide optimal customer service and effective administration of its operations and routines.

where many refineries and chemicals companies are located. Prime has located its own yard on the customer's premises in certain instances, to provide fast on-site service.

Companies within the process industry periodically need to interrupt their production to carry out maintenance work. Since production stoppages are extremely costly, the need for efficient service is particularly important. Accordingly, Prime has developed a special service concept called the 'Turnaround Central'. Regardless of where in the U.S. the demand for service is needed, a service trailer can quickly be packed with the desired equipment. The concept also features a special computer system with a bar-code function for tracking. Each piece of equipment that is rented is registered against the name of the person who will be using it. This system makes it easier to localize all of the equipment used in connection with maintenance work.

Prime's preventive maintenance is another important service provided during the rental period. More than 500 service technicians conduct regular maintenance on all of the tools and equipment. During extended rental periods, they visit customers and service the equipment on-site. If necessary, replacement equipment is obtained.

In pace with Prime expanding its operations geographically into other areas, the company is also attracting new categories of customer. The film studios in Hollywood require work platforms for recording operations. Another example is found within the automotive sector, where maintenance of production equipment is carried out by service technicians.



Prime's equipment is available at over 160 locations in 20 states. A computerized point of sale system links all rental yards.

New design reduces costs

During 1997, Airtec developed a new series of compressor elements for Atlas Copco's oil-injected compressors. The new series includes both small (4–11 kW) and medium-sized (30–45 kW) screw compressors.

The development of small screw elements was focused on achieving a substantial reduction in costs, without any loss in performance. By integrating various compressor functions, it was possible to reduce the number of components. The same principle to attain a cost-effective design has been applied in the development of medium-sized compressor elements.

The new compressor elements boost better operating performance and lower operating costs due to energy savings. In addition the elements run more silently.

To increase quality and reduce lead times, Airtec has also introduced a fully automatic process for the production of rotors for oil-injected compressor elements.

Strong growth for Atlas Copco's energy-efficient compressors

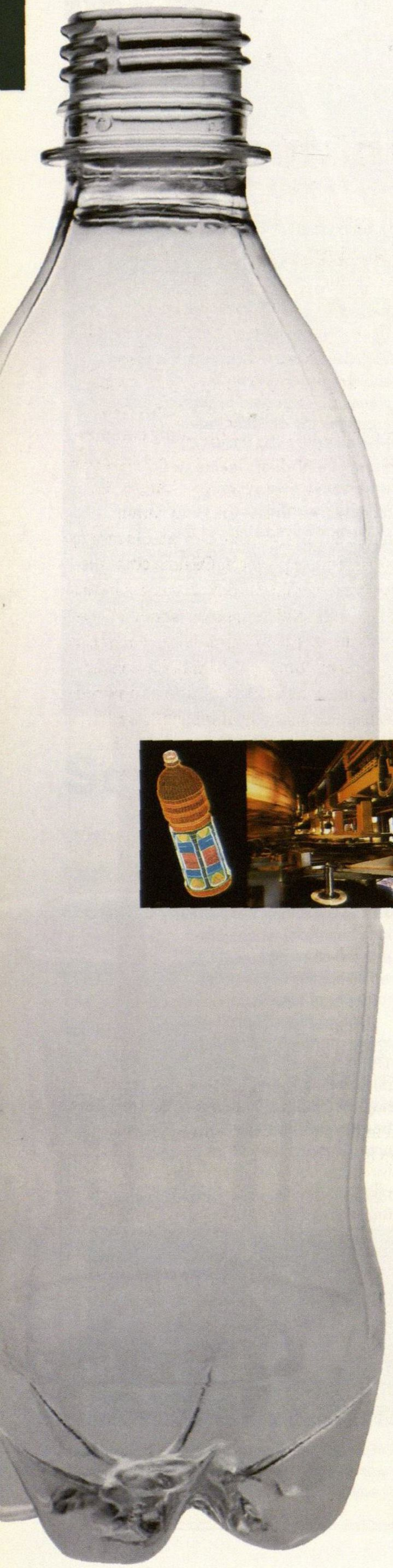
Variable Speed Drive (VSD) compressors are becoming an increasingly important product group for the division Industrial Air. The sales success of these compressors is due to the special drive system, which ensures that the compressor always deliveres the right amount of air, thus reducing energy consumption.

Companies can generate major cost savings by investing in energy-efficient production solutions.

A traditional compressor consumes electricity during the entire period it is in operation, even when it is not delivering compressed air. With a VSD compressor, energy consumption can be significantly reduced by automatically adjusting capacity to actual air requirements. The VSD technique is particularly beneficial when compressed-air requirements vary, which applies in the great majority of installations.

One of Atlas Copco's customers in the Swiss market is TRISA, which is a leading producer of different personal-hygiene products, such as toothbrushes and hair-care products. Compressed air is used for many applications in the production process. By investing in VSD compressors, the company has reduced its energy consumption by about 20 percent.

In Chile, one of the country's largest wineries has invested in VSD compressors, using compressed air to press the juice out of the grapes.



Acquisition in growth segment

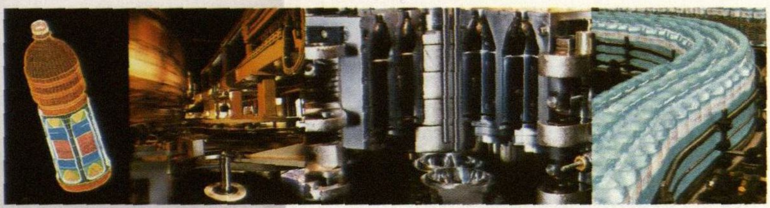
During 1997, Atlas Copco Applied Compressor and Expander Technique acquired the French company, Thomé-Crépelle, which sells primarily high-pressure compressors for the production of plastic (PET) bottles. The company is the second largest supplier in the world within this growing segment.

New environmental regulations are increasing the demand for metal and board packaging to be replaced by biologically degradable plastic packaging.

Atlas Copco Crépelle has developed a complete series of high-pressure compressors and related equipment, specially designed for the production of PET bottles. Compressors for the production of PET bottles constitute a rapidly expanding market, with an annual growth rate of about 10 percent. The plastic is formed into various packagings with the help of the compressed air. Formerly, this packaging technology was used exclusively for carbonated drinks, but today it is also used for some 30 food and other beverage products, such as fruit juices, mineral water and soya.

An increasing number of beverage producers are starting to use PET packaging. Currently, the largest individual market is the United States, where demand for small plastic packagings is expected to increase significantly during the next few years. Asia is another growth market.

To date, Atlas Copco-Crépelle's dominant market for high-pressure compressors has been France. But with access to Atlas Copco's worldwide sales and service network, opportunities in many other markets are explored.



The plastic is formed into various packagings with the help of compressed air.

Major potential for quality air

There was strong demand for oil-free and oil-injected compressors during 1997. Sales of dryers also increased, due to an increase in demand for quality air.

The growth potential for system solutions in the drying equipment area is considerable. Customers need clean, dry air in order to minimize wear and corrosion on their production equipment. Quality air is also needed to maintain a high degree of precision in various instruments and when the compressed air comes into contact with sensitive components or raw materials.

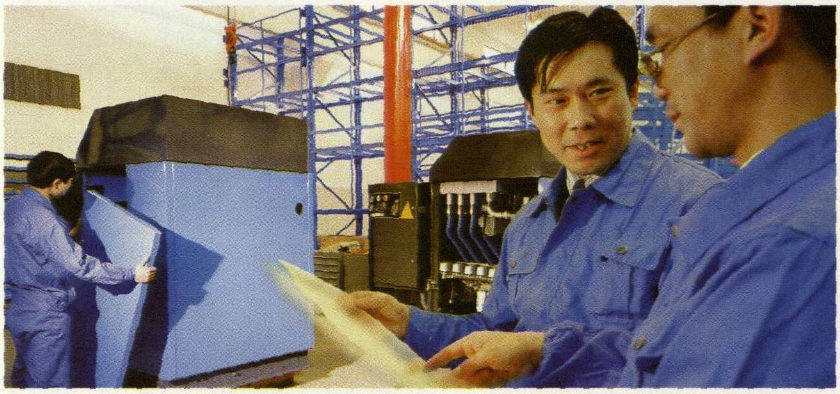
For a number of years, Atlas Copco has also developed and produced dryers and filters. During 1997, Atlas Copco developed a new generation of dryers containing environmentally-friendly coolants that is non-harmful to the ozone layer.

During 1997, Atlas Copco delivered more than 20 oil-injected compressors and refrigerant dryers to the North Carolina plant of the U.S. textile company, Unifi. Compressed air is used to transport the raw material and to manoeuvre certain machines.

Another example is TATA Chemicals in India, which produces fertilizers. The company has installed oil-free compressors together with adsorption dryers.

The relative number of Atlas Copco compressors delivered with integrated dryers is steadily increasing.

Local compressor production in China



Shanghai Worthington Orient Compressor Co. will manufacture oil-injected compressors.

In 1997, the joint venture Shanghai Worthington Orient Compressor Co. was established. This is the second company which has been formed for local production of compressors in China. In 1995, production started at Wuxi Atlas Copco Compressor.

In 1997, Worthington Creyssensac, an Industrial Air division company, and the Shanghai General Machinery Group established Shanghai Worthington Orient Compressor Co. to produce oil-injected compressors in Shanghai, China. The core components are delivered from Europe, while the remainder are purchased from local subsuppliers.

Besides this company, Wuxi Atlas Copco Compressor is manufacturing large oil-injected compressors in China. The company also has an established service organization, with spare parts sales, and its own staff of service technicians.

Wuxi Atlas Copco Compressor also started the introduction of medium sized oil-injected compressors in 1997.

The compressor market in China has enjoyed stable growth in recent years. There are a large number of local producers. The majority of these companies produce traditional reciprocating compressors, but some have started to produce oil-injected screw compressors. Large oil-injected compressors are used within China's engineering industry and for many infrastructure projects. Oil-free compressors are in demand from customers in the textile, automotive, tobacco and food sectors. Yet another factor driving demand is the foreign companies which have established joint ventures in China and which prefer to equip their plants with well-known, high-quality compressors. This has contributed to the growth of Atlas Copco's compressor sales.

Favorable development for portable compressors

Demand for portable compressors and generators has been strong in South American markets. There is an important need to build roads, water distribution systems and pipelines for gas, among other areas. Manufacturing industry is also increasing its capacity.

In most markets, the level of investments in the infrastructure has been extremely low for many years. However, Atlas Copco has maintained a local sales organization throughout this period. The company is well known and its long-term commitment to customers has led to the development of strong customer relations.

Today, many countries need to build and repair their roads, build water-distribution systems and sewage conduits as well as pipelines for gas and distribution networks for electricity. This is the main reason for the increase in new sales of portable compressors and generators.

A number of large infrastructure projects have been started. Notable among these is a 460 km pipeline for natural gas from Argentina to Chile. Portable compressors have been used in the actual construction work, as well as for the testing and cleaning of the pipes. Another example is the 'Valle del Tuy' railway project in Venezuela, which is currently in the process of being built after many years of delay. The project is being conducted by an international joint venture of construction contractors. The railway will connect the capital, Caracas, with the Valle del Tuy area in the southwest.

Steady demand for mining equipment

Sales of rock drilling equipment and loaders to the mining industry continued to grow in most markets. The Group decided to phase out its tunnel-boring machine (TBM) business. The cost of that restructuring measure was charged to earnings for 1997, which amounted to SEK 387 m. (396).

The business area leads its product fields and offers complete programs of products and after-sales services that ensure high productivity for customers. Markets are covered by the business area's own sales organizations and through external distributors. Growth is generated by continuously investing in continued research and development and through working existing and new markets more effectively.

Structural changes

During the year, the decision was made to phase out Atlas Copco's tunnel-boring machine (TBM) business. Raise-boring machines and cutters will be transferred to other divisions in the Construction and Mining Technique business area. Of the division's 115 employees, 80 will be affected by the restructuring, the costs of which were charged to 1997 earnings.

The Wagner division acquired its distributor in South Africa, Hubert Davis Ltd., in June 1997. The company, now integrated into the South African sales company, has 80 employees.

Sales

Revenues rose 9 percent, to SEK 6,453 m. (5,921). Orders received increased 13 percent, to SEK 6,652 m. (5,867). Major orders for drilling and loading equipment came from South America, Australia, Africa and Russia.

Earnings

Operating profit amounted to SEK 387 m. (396). Earnings were charged with nonrecurring costs of SEK 50 m. for restructuring measures in Atlas Copco Robbins. Excluding these restructuring costs, earnings reflected an operating margin of 6.8 percent (6.7).

Return on capital employed was 12 percent (14).

Investments

During the year, the business area invested a total of SEK 207 m. (211) in property and machinery. The majority of investments were attributable to a new central laboratory in Örebro for the Atlas Copco Drilling Equipment division. Investment in rental equipment amounted to SEK 254 m.

Business development

Rock drilling equipment and loaders had continued favorable demand in several markets, while activity in construction and contracting remained weak.

In 1997, Atlas Copco Rock Drilling Equipment received significant orders for drilling equipment from underground mines in Russia, South America and Africa. At year-end 1997, the division formed a separate company to rent drilling equipment in Europe. Despite flat activity in contracting, the division lifted sales of large drilling rigs for construction projects in southern Europe and in certain South American and East Asian markets.

The Craelius division achieved steady growth in North and South America and in Australia during the year. Most deliveries comprised equipment for prospecting for new ore bodies in existing mines.

The Uniroc division conducted an extensive program of investment in its factories with the aim of achieving higher productivity and smoother materials flow. The division's sales of down-the-hole equipment for construction projects increased, chiefly in the U.S. and Japan.

In 1997, Atlas Copco Construction Tools noted much stronger sales of hydraulic demolition equipment in the major European markets. In addition, the division began delivering to Prime Service construction equipment for rental in the U.S. market.

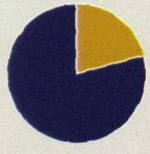
Atlas Copco Wagner's massive efforts to develop a new product program contributed greatly to a hefty lift in sales of loaders and trucks for underground mines. In 1997, production was thoroughly restructured to shorten lead-times, improve materials flow and boost production capacity.

Outlook for 1998

Economic developments in East Asia in 1998 are expected to put a damper on mining industry investment worldwide and delay major infrastructure projects in the region. Activity in the construction and contracting sector will remain weak. The weakening of the metal prices is expected to affect mines to improve productivity, which increases the opportunity for sales of new equipment.

Kjell Carlsson *Freek Nijdam* *Lars Renström* *Claes Ahrengart* *James Henderson*

The Construction and Mining Technique business area develops, manufactures and markets rock drilling tools, tunneling and mining equipment, surface drilling equipment, construction tools, loading equipment and geotechnical drilling equipment. The products are sold to building and construction companies, quarries and mining companies around the world. The business area has manufacturing plants in Sweden, the United States, China and South Africa.



Construction and Mining Technique

Share of Group revenues 21%

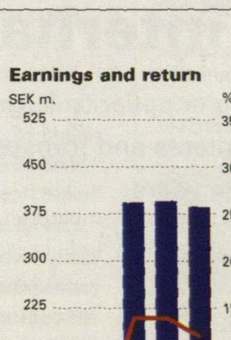
The Construction and Mining Technique business area comprises the following divisions:

- Atlas Copco Rock Drilling Equipment, President *Kjell Carlsson*
- Atlas Copco Craelius, Acting President *Freek Nijdam*, effective from August 1998 *Björn Rosengren*
- Uniroc, President *Lars Renström*
- Atlas Copco Construction Tools, President *Claes Ahrengart*
- Atlas Copco Wagner, President *James Henderson*

	1997	1996
Revenues, SEK m.	6,453	5,921
Operating profit, SEK m.	387	396
Return on capital employed, %	12	14
Investments, SEK m.	207	211
Number of employees	5,058	5,143

Revenues

Earnings and return



Return on capital employed, %

Operating profit, SEK m.

Investments*

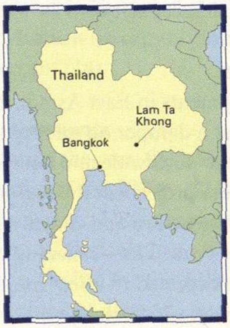
*excluding rental equipment

Focus on international projects

Atlas Copco is a leading supplier to large international infrastructure projects, particularly the construction of power plants and transport links. 300 major rock-drilling projects will be in progress in the next five years.

As a result of Atlas Copco becoming involved in the projects at an early stage, the company is provided with excellent opportunities to use its extensive rock-drilling experience to contribute optimal and profitable solutions for the customers. In many projects, Atlas Copco has appointed its own project managers to function as cooperation partners with the international contractors. As rock-drilling technology becomes increasingly more efficient, project times can often be significantly reduced, benefitting from the Atlas Copco back-up organization. Atlas Copco also offers alternative, commercially favorable solutions which can reduce the risk of a negative cash flow for the contractor, a normal occurance during the initial stages of most large projects. This enables contractors to start new projects earlier. For Atlas Copco, it results in a stronger market position with increased sales of service contracts and spare parts.

One of the international projects currently in progress is the building of the Lam Ta Khong power plant in Thailand, in which an Italian and a Spanish contractor are engaged with a local partner. During the past year, Atlas Copco has



delivered three underground drilling rigs, two surface rigs and two shaft-sinking machines, three loading machines, several portable compressors, and rock-drilling tools and light hand-held construction equipment to this project. In addition, service contracts have been signed for all of the equipment.

European breakthrough for demolition equipment

The crusher crushes the concrete into fine rubble enabling the steel and concrete to be easily separated and recycled.

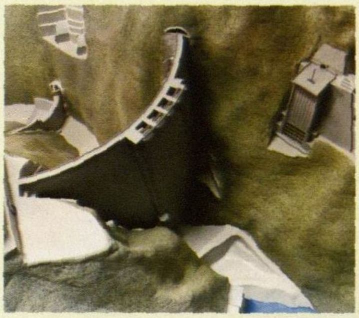
Atlas Copco Construction Tools noted a substantial volume increase in 1997 for its carrier-mounted hydraulic hammers. In the important German market the sales volume increased 50 percent, despite the overall market decline. During the next few years it is estimated that the annual demand for hydraulic hammers in Europe will grow by 10 percent.

During 1997 rental machine companies in Germany, France, Italy and Spain have submitted an increasing number of orders for hydraulic hammers. To date, the division has concentrated its marketing efforts on Europe, which has accounted for 50 percent of the orders received, but only constitutes one third of the global market. There is therefore a substantial potential for achieving increased sales, in North America among other regions. The division has commenced deliveries to the U.S. market through Prime Service to handle equipment rental operations in the American market.

The demolition equipment, which includes breakers as well as concrete crushers and pulverizers mounted on various types of carriers, is used by construction contractors and quarry operators to crush boulders during excavation work, by building contractors for the demolition of buildings, and for the modernization and repair of bridges and roads, and by the mining industry.

For the demolition of reinforced concrete structures, the carriers are to an increasing extent equipped with crushers and pulverizers, which crush the concrete into fine rubble enabling the steel and concrete to be easily separated and recycled. This environmentally friendly method meets the demands for careful demolition work and is expected to be used extensively in Central Europe and crisis-torn countries, where there is a substantial need for clearance and rebuilding.

Reinforcement drilling–a growth area



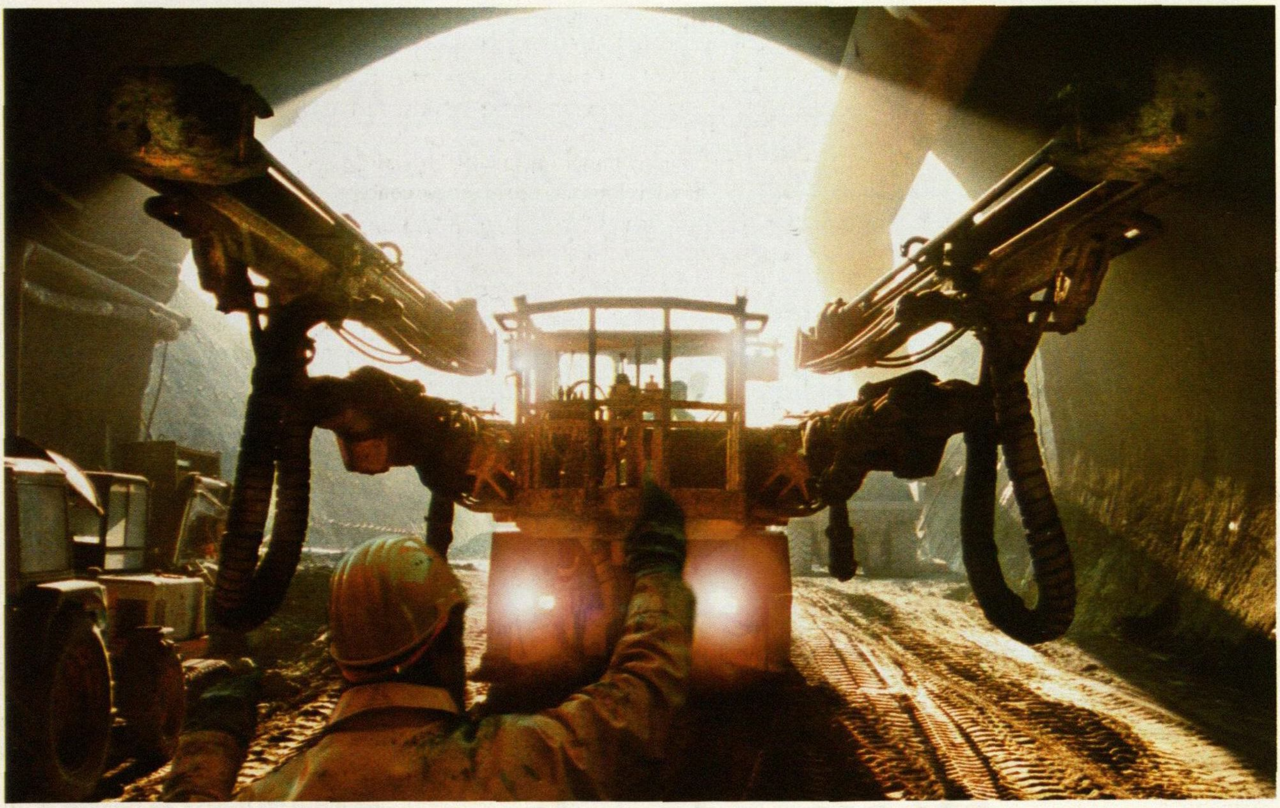
Demand has increased during the past few years for Atlas Copco Craelius rigs for use in grouting operations. The equipment is used for seal and reinforce the bedrock in order to prevent leakage from hydro power plant dams.

During summer 1997, the division delivered nine drilling rigs for rotary drilling to the Berke power plant project in southeastern Turkey, together with ancillary equipment such as drilling rods and drill bits.

The planned project will comprise an underground power plant, with a dam 210 meters high and 270 meters long. In order to ensure the success of the project, extremely precise geological examinations of the bedrock are required, as well as curtain drilling beneath the dam and around its sides to strengthen and seal the bedrock. How closely spaced the grouting holes need to be will be determined based on water-loss measurements taken in the holes. According to estimates, some 3,000–4,000 holes with a depth of 60 meters will need to be drilled, but if the measurements show that water is permeating through the limestone bedrock, the number of holes could need to be doubled.

The Turkish contractor chose Craelius drilling rigs for core drilling because they are compact, facilitating rapid handling of drill steel in the narrow galleries. They also offer high performance and possess highly favorable work-environment characteristics from the operators' standpoint.

European launch of drilling rig rentals



Atlas Copco has rented drilling rigs for construction of a high-speed railway line between Cologne and Frankfurt, Germany.

At year-end 1997, Atlas Copco Rock Drilling Equipment launched a new rental concept in Europe. The rental operations are a supplement to regular sales. Through the rental contracts, customers are guaranteed access to state-of-the-art technology, high capacity utilization and continuous operator training.

The new rental operations create a broader and more profitable total market, as well as more uniform cash flow. Operations are conducted on a pan-European basis in order to attain optimal rental utilization. The sales companies are responsible for securing the rental contracts and for equipment maintenance and operator training. Rock drilling tool sales are also linked to the rental contracts.

Rock drilling tools are linked to the rental contracts.

The increased need for equipment rental derives from the changes which have occured in the market and from the rapid pace of technical development in the drilling rigs area. Construction contractors often require extra capacity during relatively limited periods and mining contractors may also need a special rig for drilling a new mine gallery. Moreover, by renting drilling equipment, smaller contractors can take on projects they would normally find impossible. And if they have a favorable level of work on hand and thus are more profitable, they can purchase the rented equipment after a certain period of time.

The sales companies have conducted small-scale drilling equipment rental operations earlier. In Germany, for example, in connection with the high-speed railway line which is under construction between Cologne and Frankfurt. A number of contractors have rented large drilling rigs for the drilling and blasting of approximately 20 tunnels.

Reduced production costs and increased capacity

An extensive program of production restructuring is in progress at the Atlas Copco Wagner loader and truck plant in Portland, Oregon, in the U.S. This has reduced lead times with 50 percent and results in improved customer service.

A long-term investment in the development of new mine loaders and trucks had led to the design of the various models adapted to increase production and assembly efficiency. The objective is that, within a few years, sales will consist primarily of products that are no more than five years old.

The investment in new, more efficient machine equipment and an improved flow of materials, in combination with the purchase of semi-finished goods, will enable lead times for the production of parts and components to be halved. This in turn means that plant production capacity will increase significantly.

Assembly of the various models is being organized in specialized groups, to which deliveries of parts and components are made on a just-in-time basis. This has enabled the central warehouse to be phased out and has reduced lead times. As a result of these measures, the time needed for the assembly of a loader or truck has been cut from 80 days to 30 days, a factor which naturally strengthens Wagner's position in the market.

Plant rationalization has enabled lead times for production to be halved.

Cooperation agreement with Canadian mine

During the year, Secoroc Canada/Uniroc signed a long-term agreement with one of Canada's largest mines, Brunswick Mining and Smelting Co., which has copper, lead, zinc and silver operations.

The agreement means that Secoroc is now the sole supplier of drill steel for the mine's 16 jumbo rigs and of DTH hammers and drillbits for its 13 down-the-hole rigs.

Earlier, the mine relied on three suppliers of rock-drilling tools. In addition to delivering products, the agreement includes service in the form of drill bit grinding.

The agreement provides both parties with the opportunity to achieve major gains in the form of joint product and applications development, lower costs and optimal logistical solutions.

Favorable demand from the automotive industry

Sales of industrial tools and assembly systems to the automotive industry was favorable in 1997. Chicago Pneumatic and Desoutter formed a new division, Alliance Tools, which offers an improved product range and shorter lead times to the market. Earnings excluding nonrecurring items increased 31 percent, to SEK 942 m. (719).

The business area strives to be a leading supplier of pneumatic and electric power tools and equipment for manufacturing. The products are aimed chiefly at manufacturing and construction industries worldwide.

Operations focus on achieving stable growth and favorable profitability.

Structural changes

Effective January 1, 1998, the new Alliance Tools division was formed by combining the former Chicago Pneumatic, Desoutter and Georges Renault divisions. Alliance Tools will coordinate product development, production, and administration of the three units, while maintaining marketing and sales with separate brands.

Sales

Revenues rose 15 percent, to SEK 9,316 m. (8,128). Orders received were up 13 percent, to SEK 9,334 m. (8,280). Sales of pneumatic tools increased in the European market as well as in the North American, Brazilian and Japanese markets. Electric power tools also enjoyed better sales.

Earnings

Operating profit excluding nonrecurring expenses increased 31 percent, to SEK 942 m. (719), representing an operating margin of 10.1 percent. Nonrecurring items for 1996 totaled SEK 117 m.

Return on capital employed was 13 percent (12).

Investments

The business area's total investments in property and machinery were SEK 279 m. (309). 1997 investments focused mainly on equipment for efficiency gains such as

Milwaukee's investment in a new automated process for manufacturing of saw blades.

Business development

Milwaukee Electric Tool raised the overall level of sales of its electric power tools and accessories in the North American market, although sales growth slowed towards year-end. An increase was also noted in other geographical markets, particularly Latin America and Europe.

During the latter half of 1997, Atlas Copco Electric Tools expanded its market shares in Europe, particularly in its home market of Germany. Sales of electric power tools in the Chinese market increased steadily during the year.

Atlas Copco Industrial Tools and Equipment delivered the biggest sales boost in the business area. The division bolstered its prominent position as supplier of tools and systems to the automotive industry while expanding its market shares in other industries.

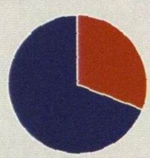
The sales development of the newly formed Alliance Tools division, which consists of Chicago Pneumatic, Desoutter and Georges Renault was favorable for tools to the automotive after-market, while sales of industrial tools showed a slight decline.

Outlook for 1998

Demand for industrial tools and assembly systems is expected to continue on a high level, especially in the automotive industry. Electric power tools should also enjoy stronger demand.

Richard Grove *Paolo Duca* *Peter Möller* *Necip Soyak*

The Industrial Technique business area develops, manufactures and markets pneumatic and electric power tools, assembly systems and sophisticated motion control products. The business area has factories in Sweden, France, Great Britain, Germany, Switzerland, the United States, China and India.



Industrial Technique

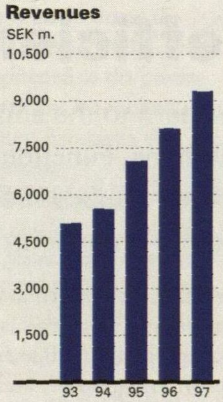
Share of Group revenues 31%

The Industrial Technique business area comprises the following divisions:

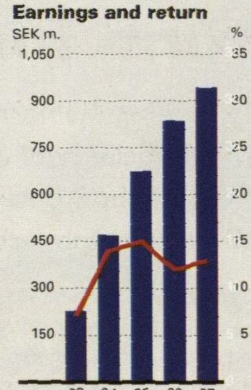
- Milwaukee Electric Tool, President *Richard Grove*
- Atlas Copco Electric Tools, Acting President *Paolo Duca*
- Atlas Copco Industrial Tools and Equipment, President *Peter Möller* (effective February 1, 1998)
- Alliance Tools, President *Necip Soyak*

	1997	1996
Revenues, SEK m.	9,316	8,128
Operating profit, SEK m.	942	836
Return on capital employed, %	13	12
Investments, SEK m.	279	309
Number of employees	7,898	8,119

Revenues



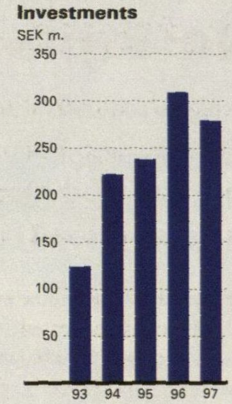
Earnings and return



Return on capital employed, %

Operating profit, SEK m.

Investments

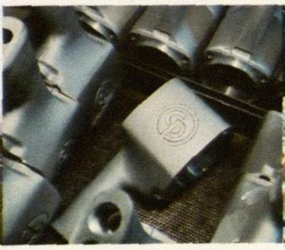


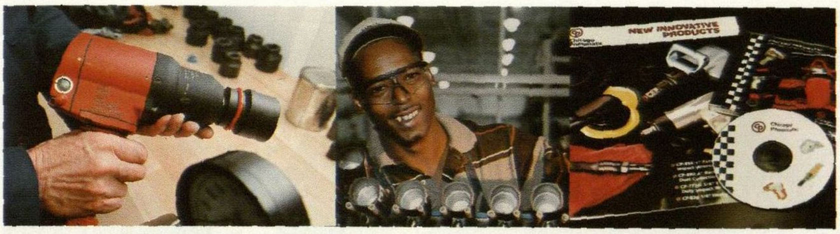
New platform for efficient processes

Chicago Pneumatic's move from the north-eastern to the southern U.S. has created a good platform for enhancing the efficiency of operations. Functions that do not form part of the company's core operations are now outsourced to subcontractors, and projects are under way aimed at making production more customer-order-controlled.

The company's new home in Rock Hill, South Carolina, is located in a region that is experiencing rapid growth and ranks today as one of the foremost business centers in the U.S. Many companies in the automotive, electronics, construction and other sectors have located there. The region has a highly strategic position from a distribution viewpoint, being close both to major interstate highways and to an international airport with frequent flights to Europe. In addition, the local authorities in Rock Hill support business through such measures as free training for fitters and assistance with recruitment.

Planning for Chicago Pneumatic's state-of-the-art facility in Rock Hill, which took only eight months to build, was based on the company's requirement for a flow-oriented and flexible work organization. As a result, the plant functions within a substantially smaller floor area than before. The number of personnel required has also been reduced by





Impact wrenches is one of the products Chicago Pneumatic focus its resources on. During 1997, the company launched products for construction work as well as the automotive aftermarket.

more than 40 percent by organizing operations in a more process-oriented manner.

Other measures which the company is implementing to increase efficiency include outsourcing of various functions which are not part of the core operations, such as casting of components, hardening of tool parts and plant maintenance.

The company has also initiated a number of projects to minimize lead times while further improving product quality and customer service. Production will be entirely customer-order-controlled in order to achieve the most efficient flow possible. Old production equipment will also gradually be replaced with up-to-date machining centers.

Alliance Tools – a new division

During autumn 1997, a decision was made to further streamline operations. Together with Desoutter and Georges Renault, Chicago Pneumatic formed a new division, Alliance Tools. The aim is to promote synergy among the units and better enable sharing of their development and production resources, while marketing and brand positioning are kept separate. As a result, Chicago Pneumatic will now focus its resources on impact wrenches, hammers and compression tools; Georges Renault focus on grinding machines and assembly systems; and Desoutter focus on screwdrivers and drills.

Desoutter strengthens its position in white goods industry

Desoutter has developed a special screwdriver, which is expected to be greeted enthusiastically by the white goods segment. Damage occurring during assembly of household appliances and electronic products is a common problem. Such damage is usually caused when fragile connections are tightened too hard, causing denting or cracks in the appliance.

During the past year, Desoutter has focused on supplying screwdrivers mainly to companies producing household products in the white goods segment and electronic products. The aim is to become the market leader in this segment.

The requirements are very high on Desoutter's new screwdriver. It has a variable tightening strength that is simple to adjust. The screw is initially tightened at full torque, but when it is almost fully tightened, the tool senses the preadjusted setting and reduces the pressure, so that the screw is tightened to the precise degree that is required without damaging the appliance.

This feature is particularly suitable for installing thin sheet metal using self-tapping screws, for example, when attaching a lacquered door component to a refrigerator. If the thin sheet metal is damaged, the entire refrigerator can be ruined. Another example is mounting the plastic cover on a computer. Excessive screwdriver pressure can strip the screw threads or cause the plastic to split.

The introduction of the new screwdriver extends Desoutter's comprehensive series of modular tools, giving increased flexibility to customers and enabling them to rapidly upgrade tools instead of having to purchase new ones. The advantages for Desoutter are the lower storage costs for spare parts and the extensive model range, comprising more than 300 models.

Accessories for continued growth

The power tool accessory market is estimated to be worth over two billion dollars in the U.S. and seven billion dollars worldwide. Milwaukee Electric Tool has realized the importance of accessories, offering one of the broadest accessory lines of any power tool manufacturer. The company's accessory sales growth rate in the U.S. is estimated to be almost twice the industry rate.

By offering a broad range of accessories, Milwaukee has developed close and long-term relationship with its customers. Furthermore the profit margins of most accessories are substantially higher than those achieved for tools. Most of the accessories are consumables and, over the life of a tool, end users can spend several multiples of the initial cost of a power tool on accessories.

Milwaukee endeavors to offer in its product line all of the accessories that can be used with a tool in its varied applications. Its line of over 3,500 accessories ranges from screwdriver bits, saw blades and batteries to diamond core bits.

The company stresses selling the complete product offering to produce a finished job, including tools and accessories. The company also frequently provides incentives to its distributors to purchase and promote both a tool and its related accessories.

Milwaukee will continue to grow the highly profitable accessory business in the U.S. and the rest of the world through aggressive new product development and marketing programs as well as through increased cooperation with other Industrial Technique divisions.

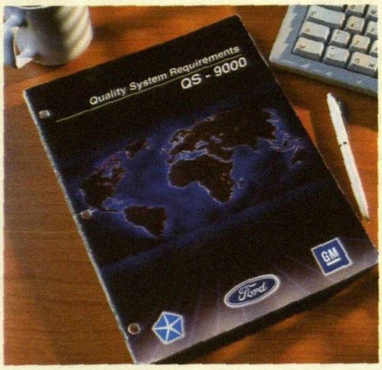
Investments to increase manufacturing capacity and distribution capabilities have been made and additional investments are planned in 1998.

Automotive industry installs own quality system

The major auto producers have developed their own quality system, which places new demands on suppliers. Atlas Copco is the first supplier of tools to meet these demands. It is estimated that the company will qualify for QS-9000 certification during 1998.

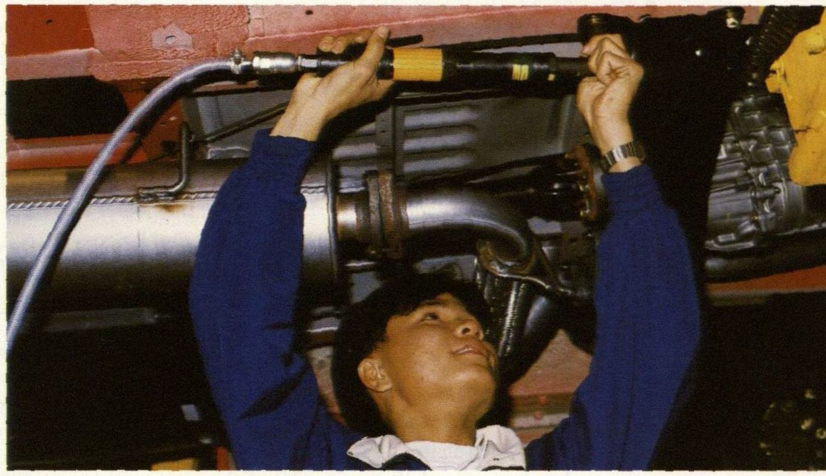
The aim of the quality system is to create a common base for continuous improvements, the prevention of faults and other benefits.

During 1997, Atlas Copco Industrial Tools and Equipment produced the first version of a manual based on the requirements of the new quality system. The work focused on creating comprehensive quality planning within the areas of product development and production. In addition, the division started to measure customer satisfaction in a systematic fashion in Germany, France and the U.S. The introduction of statistical measurement methods provided increased opportunities to achieve a more uniform level of quality in the production process.



Local presence in Vietnam pays off

There was strong demand for power tools and assembly systems from the automotive industry during 1997. Major car manufacturers are now establishing local plants in emerging countries. One example is Ford, which has built an assembly plant in Vietnam, to which Atlas Copco Industrial Tools and Equipment is the exclusive supplier of industrial tools.



Atlas Copco has delivered more than 300 tools to Ford's plant in Vietnam.

The need for suppliers to offer a global service is increasing. With a worldwide sales and service organization, Atlas Copco Industrial Tools and Equipment can provide service to its customers regardless of their location in the world. In Vietnam, the joint venture company, Atlas Copco Diethelm, is the only foreign company to have received permission to provide local service and spare parts operations. A local presence was the decisive factor when Ford Vietnam selected Atlas Copco.

Since the country is still building up its road system, most of the vehicles are commercial, such as buses or trucks. In total, some 25,000 motor vehicles are sold each year in Vietnam. In September 1997, Ford assembled its first vehicle at the Hai Duong plant, near Hanoi. The company will assemble 1,000 minibuses, vans and light trucks during 1998. Production capacity should be up to 7,000 units per year on one shift production by the year 2002.

Atlas Copco has delivered more than 300 tools to the Ford plant, mainly in the form of pneumatic nutrunners and screwdrivers. In addition, oil-free compressors from Atlas Copco are installed in the new Ford plant. The business project is a good example of cross-border cooperation. In London, Ford maintains a special project group with responsibility for the construction of assembly facilities in emerging countries. In cooperation with Atlas Copco's sales company in the U.K., Ford has standardized the routines for the purchasing of tools. Among other developments, a list of tools for different applications, with uniform prices, has been produced. Atlas Copco's local resources in South East Asia are managing the project, and product training is undertaken locally with the assistance of Atlas Copco Diethelm.

Brand positioning contributed to increased sales

Atlas Copco Electric Tools is conducting a strategic marketing program for its two brands. The AEG brand is positioned on independent professional users. The Atlas Copco brand is focused on industrial customers. The program has contributed significantly to increased sales.

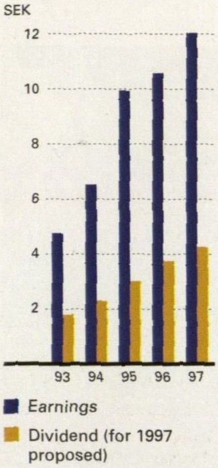
Prize competition in the electric tools market is razor-sharp. A strong contributing factor is the influence of low-price power tools from the Far East, which concentrate on price-sensitive individual consumers. The division has elected not to focus on this particular market segment. Instead, its target group consists of more professional users, which means that the company is developing the best tools for the application rather than focusing on the lowest prize.

AEG is mainly intended to serve the needs of small entrepreneurs, which use such tools during short periods in their operations. Accordingly, the tools themselves must be versatile and suitable for use in a number of different situations.

Atlas Copco offers the highest performance and are usually more specialized. However, common to both types of brands is the so-called "keyless" system, enabling saw blades or grinding wheels, for example, to be rapidly replaced or exchanged. Sales of AEG-branded tools are conducted mainly via large home-centre type of outlets and building-materials suppliers, where exposure of product in the store is extremely important. Atlas Copco-branded tools are distributed mainly through specialist dealers.

The Atlas Copco share

Earnings and dividend per share



Share capital

Atlas Copco's share capital at year-end amounted to SEK 917,579,600 distributed among 183,515,920 shares, each with a par value of SEK 5.

Class A shares entitle the holder to one voting right, and class B shares entitle the holder to one-tenth of a voting right. Each round lot consists of 100 shares. Atlas Copco has 33,831 shareholders. The portion of shares held by institutional investors amounts to 59 percent.

The ten largest shareholders account for 48 percent of the voting rights and 43 percent of the number of shares. The number of foreign-owned shares amounted to 33 percent (37) and represented 30 percent (34) of the voting rights. The proportion of shares in each country is shown in a separate table on this page.

Distribution of shares

Class of share	Shares outstanding	% of votes	% of capital
A shares	122,497,590	95.3	66.8
B shares	61,018,330	4.7	33.2
Total	183,515,920	100.0	100.0

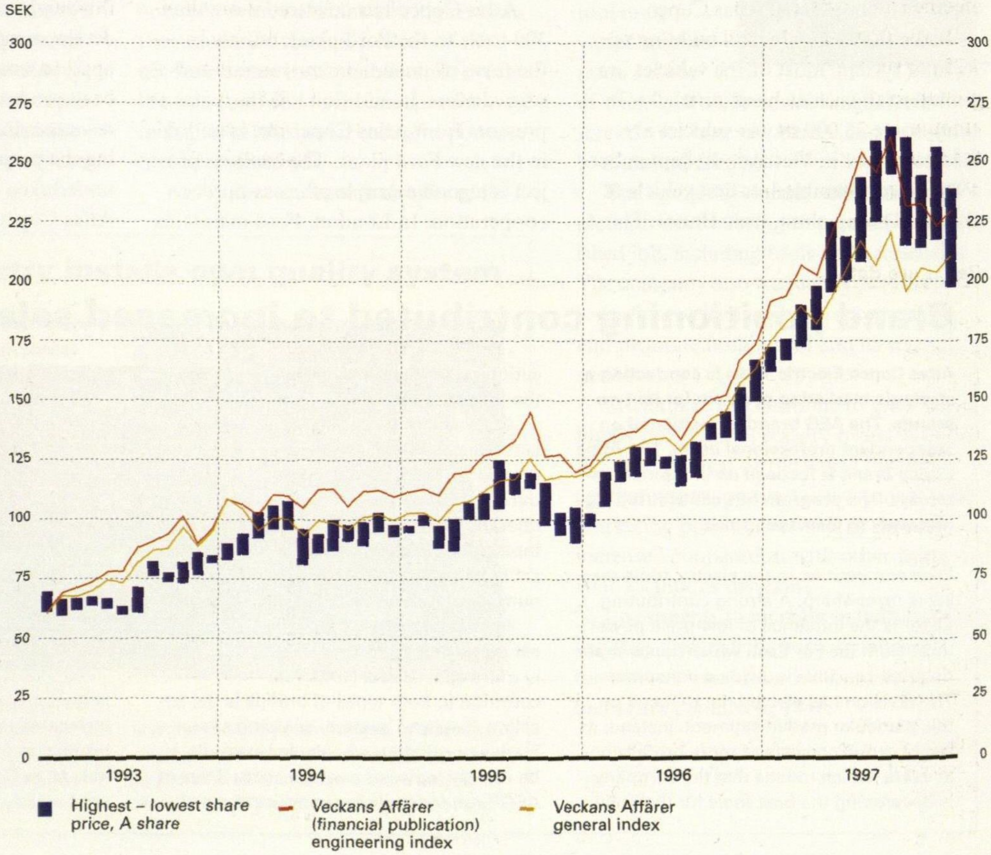
Ownership structure 1997

Number of shares	% of shareholders	% of capital
1 – 500	73.4	2.3
501 – 2,000	20.3	3.7
2,001 – 10,000	4.7	3.5
10,001 – 50,000	0.9	4.0
50,001 – 100,000	0.2	2.9
>100,000	0.5	83.6
Total	100.0	100.0

Foreign owned shares by country

	% of votes	% of capital
Great Britain	13.3	12.1
USA	8.4	11.1
Belgium	2.5	2.3
France	2.1	1.6
Luxemburg	1.0	1.4
Others	3.0	4.0
Total	30.3	32.5

Trends of share prices



Largest shareholders, February 1998

	Number of shares	% of votes	% of capital
Investor Group	25,947,000	20.2	14.1
Sparbankernas Aktie- och Allemansfonder	24,020,500	12.2	13.1
Allm Pensionsfonden, Fjärde Fondstyrelsen	4,368,950	3.4	2.4
SPP Group	6,397,070	3.1	3.5
Föreningsbankens fonder	3,595,800	2.0	2.0
Trygg Hansa Group	3,147,708	1.9	1.7
Skandia Group	2,982,154	1.4	1.6
Svenska Handelsbanken Group	2,815,899	1.4	1.5
Nordbanken fonder	4,133,650	1.2	2.3
Allm Pensionsfonden, Femte Fondstyrelsen	1,575,700	1.2	0.9
	78,984,431	48.0	43.1
Others	104,531,489	52.0	56.9
Total	183,515,920	100.0	100.0

The table above shows the largest shareholders that are directly registered with VPC.

Dividend policy

The Board's objective is that dividends to shareholders should amount to 30 to 40 percent of earnings per share.

Atlas Copco AB's aim is to cover the greater part of the dividend payments with dividend income from foreign subsidiaries.

If the Board of Directors' proposal of SEK 4.25 per share is approved, the average dividend growth for the five-year period 1992 to 1997 will amount to 22 percent. During the same period, the average dividend has been 34.5 percent of earnings per share. Expressed as a percentage of shareholders' equity, the proposed dividend is 5.7 percent (5.8).

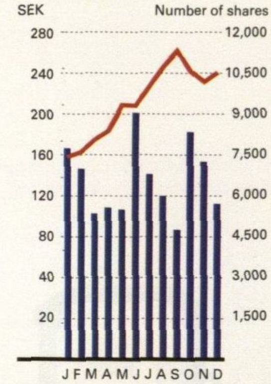
Trading

The Atlas Copco share was the twentieth (eighteenth) most traded share on the Stockholm Stock Exchange during 1997. A total of 79,206,125 shares were traded (of which 49,357,144 class A and 29,848,981 class B), corresponding to a value of SEK 16,840 m. (13,509). An average of 318,097 shares (423,364) were traded per market day. The turnover rate (degree of liquidity) in 1997 was 49 percent (52), compared with the stock market average of 66 percent (65). As per November 1997, foreign trading in the Atlas Copco share showed a net import of SEK 461 m. (1996 total: net export 664).

Share price trend

As of December 31, 1997, the price of the Atlas Copco share was SEK 237. For 1997 as a whole, the price of the A share rose 44 percent. The general index increased 25 percent and the engineering companies' index increased 29 percent. During the past five year-period, the annual average total yield, meaning the sum of the growth in share price and the dividend, was 31 percent. The corresponding return for the Stockholm Stock Exchange as a whole was 29 percent. During the past ten year-period, the annual average total yield was 29 percent for the Atlas Copco share compared to 19 percent for the Stockholm Stock Exchange.

Trends of share prices/ traded shares 1997



— Average share price, A share
■ Traded shares (A+B), thousands, Stockholm Stock Exchange

Per share data

SEK	1992	1993	1994	1995	1996	1997	Av. growth year 92–97,%
Earnings[1]	3.35	4.74	6.51	9.93	10.56	12.03	29
Dividend	1.60	1.80	2.30	3.00	3.75	4.25[2]	22
Dividend as percent of earnings [3]	47.8	38.0	35.4	30.2	35.5	35.3	
Price quotation, Dec. 31, A	67	83	95	102	165	237	29
Price quotation, Dec. 31, B	66	82	95	100	166	237	
Highest price quoted, A	67	86	108	125	167	266	
Lowest price quoted, A	44	60	81	87	97	161	
Average price quoted, A	57	70	94	103	127	214	
Equity [4]	42	46	51	58	65	74	12
Direct yield, percent [5]	2,8	2,6	2,4	2,9	3,0	2,0	
Price/Earnings [6]	16.9	14.9	14.5	10.4	12.0	17.8	
Price/Sales [7]	0.64	0.68	0.83	0.77	0.93	1.31	

1) Profit after financial items, less full tax and minority interests, divided by the average number of shares outstanding.
2) Proposed by the Board of Directors.
3) Dividend as a percentage of earnings per share.
4) Equity and minority interest divided by the number of shares.
5) Dividend as a percentage of the average quoted price during the year.
6) Price/Earnings. The average quoted price during the year in relation to earnings per share as defined in 1).
7) Price/Sales. The average quoted price during the fiscal year in relation to sales per share.

Market value

The market value on December 31 was SEK 43,463 m. (30,341), which corresponds to 2.4 percent (1.9) of the total market value of the Stockholm Stock Exchange.

Foreign Stock Exchanges

The Atlas Copco share has been listed on the London, Frankfurt, Düsseldorf and Hamburg stock exchanges for a number of years.

ADR-program in the U.S.

To increase the availability of the Atlas Copco share for U.S. investors, an ADR (American Depositary Receipt) program has been established in the U.S. since 1990. This means that both A- and B-shares are available as depositary receipts in the U.S. without formal stock exchange registration. An ADR corresponds to a share. The depositary bank is Citibank NA. At year-end 1997, there were 1,049,680 depositary receipts outstanding, of which 653,452 were class A and 396,228 class B.

Share risk

The Atlas Copco share's beta value provides an assessment of its risk. The beta value is a relative measure of the risk attached to the share, measured as its tracking of the stock exchange index during the past 48 months. The beta value of the Atlas Copco A-share was 0.91 (0.88). This means that the share moved 9 percent less than the index. Another statistical measure of risk is the characteristic line, which indicates how large a proportion of the share's percentage return is attributable to the average return on the stock exchange. In the case of Atlas Copco, the characteristic value is 0.38 (0.38), which means that 62 percent (62) of the share's trend is company specific.

Atlas Copco Options

The Atlas Copco options listed on the Stockholm Option Market (OM) consist of call options and put options, each relating to 100 shares. During 1997, approximately 4.6 million shares (4,4) were covered by option contracts, which constitute about 3 percent (2) of the total number of Atlas Copco shares. Each day an average of 18,577 Atlas Copco shares are affected by trading in options. Since the options only provide the holder with the right to buy and sell shares which already exist, the options do not result in any dilution effect.

Share issues 1973–1997

				Increase of share capital SEK m.	Amount paid in SEK m.
1973	Bonus issue	1:2		69.2	
1974	New issue	1:4	SEK 25	51.7	51.7
1976	New issue	1:5	SEK 50	51.7	103.5
1979	Bonus issue	1:6		51.7	
	New issue	1:6	SEK 60	51.7	124.1
1982	Bonus issue	1:4		103.5	
	New issue (non-preferential)	2,765,000 shares at SEK 135		69.1	373.3
1989	Bonus issue	1 B share: 3 A shares		195.5	
1990	New issue (non-preferential)	4,000,000 B shares at SEK 320.13		100.0	1,280.5
	Conversion*	7,930 shares		0.2	1.2
1991	Conversion*	42,281 shares		1.1	6.3
1992	Conversion*	74,311 shares		1.9	11.1
1993	Non-cash issue**	383,500 shares at SEK 317		9.5	121.6
	Conversion*	914,496 shares		22.9	137.2
1994	Split	5:1 par value SEK 5			

* Pertains to 1987/1993 convertible debenture loan.

** Implemented in connection with the acquisition of The Robbins Company.

Formalization of environmental work

A growing number of units have begun formalizing their environmental efforts based on the ISO 14001 framework. Production units that have launched local projects to introduce environmental management systems represent more than 50 percent of production volume.

Atlas Copco's vision is for the Group to be an environmental pacesetter in its businesses. Environmental efforts embrace product development and production as well as distribution and recycling, creating value added for customers. Work in the environmental sphere has gone on for many years and is increasingly becoming part of everyday procedures.

First environmental certificate

Atlas Copco Electric Tools' production plant in Winnenden, Germany, has advanced further than any other unit in implementing environmental management systems. In 1997, the plant conducted a project to create an integrated management system comprising both environmental management and quality management. In early 1998, the unit was formally certified.

Other production plants have also implemented a variety of measures. For example, to avoid using solvent-based paint, Atlas Copco Tools uses powder coating, by which a cadmium-free paint powder is applied to a product in an electrostatic process prior to tempering. Another example is Milwaukee Electric Tools' new equipment for milling gearwheels without using oil-based coolants. In addition to the savings in waste oil, this technology simplifies the recycling of metal shavings.

Atlas Copco Rock Drilling Equipment's new test facility for drilling equipment in Örebro was also designed to comply with environmental standards. The tests performed consume large quantities of water and also generate high levels of noise. Through various measures, though, the facility can reuse almost all process water and the sound level can be kept down.

Atlas Copco is also developing new production methods to reduce the machining of components so that wastage can be minimized. Instead of producing compressor rotors by milling, Airtec is using a bigger proportion of near net shape cast rotors. The rotors need only be ground to their final shape, which creates much less waste, uses much less energy, and has improved productivity.

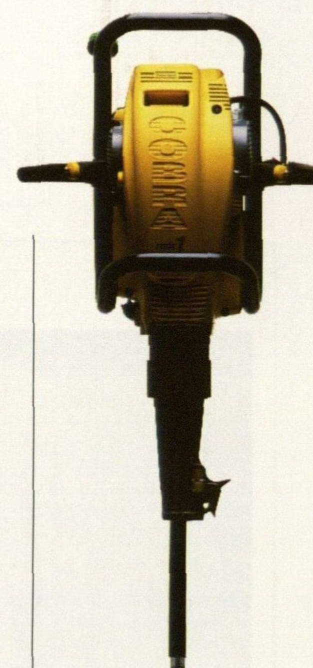
Products adapted to demands

As early as the product development phase, Atlas Copco takes into account environmental requirements. Hazardous substances should be replaced as far as is technically feasible by substances that are more environment-friendly. That is why a list of hazardous substances, such as cadmium and CFCs, becomes a key tool in the Group's environmental efforts.

Project groups are also working on analyzing the product lifecycles of a number of products. Although no standardized methods for such analyses currently exist, the most important environmental aspects will be analyzed as ISO 14001 is introduced.

A current example of lifecycle analysis in product development is Cobra, the new motorized breaker introduced in 1997. By paying attention to ergonomic and environmental factors from the product's inception, the designers at Atlas Copco Construction Tools developed a breaker that meets exacting demands on performance and environmental impact. The engine runs on unleaded fuel, and exhaust emissions are extremely clean. The components are also easy to disassemble, recover, and recycle. The ergonomics of the breaker are better thanks to ingenious solutions that reduce the levels of vibration and noise.

In Compressor Technique, Industrial Air introduced a new generation of drying equipment used to avoid condensation in pressurized air systems. CFCs used to be common cooling agents, but nowadays dryers contain more environmentally friendly chlorine-free cooling agent that do not damage the ozone layer.



The new breaker meets exacting demands on performance and environmental impact.

Salesmen of the year

Every year, the Atlas Copco Group appoints salesmen of the year. In 1997, many significant efforts were made in sales companies around the world.

The following people have been selected:

Mark Larkin, Prime Service, U.S., works in a sales district south of Dallas and has boosted revenues more than 30 percent in 1997. He made major advances by marketing service and sales of new products. He organized safety seminars involving 300 operators and sold 25 new booms, scissors, and forklifts.

Claude Roy, district manager at Secoroc in Canada, increased sales more than 50 percent in one year. One of the biggest contributions he made was entering a partnership for rock tools with Brunswick Mining and Smelting Co.

Garth Milton, sales manager for Atlas Copco Wagner in Australia, achieved great success with a new mining truck. The high point of the year was an order for two trucks to the Kanowna Belle gold mine. He has built up a long-term relationship with the mining company, which now has yielded fruit in this prestigious order.

Boeric Andersson, manager for construction and mining equipment in the Russian market, received a strategic order after two years of cultivating his territory. The Norilsk Mine, largest nickel mine in the world, ordered a large number of drilling rigs and loading equipment.

Marek Szafirski, compressor salesman in Poland, brought home large orders in 1997. Against tough competition, he sold standardized turbo-compressors to large petrochemical companies and customized compressors to chemicals firms.

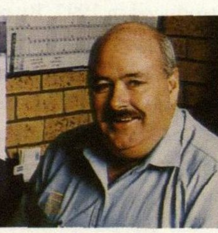
Ted Beasley, compressor salesman in the U.S., sold a large number of oil-injected compressors with additional drying equipment to the U.S. textile company Unifi, which has plants in Ireland as well as in the U.S. The order was a result of close cooperation with representatives from Atlas Copco's Irish sales company, which has worked with this customer for many years.

Ye Chun, sales engineer for compressors in China, was very successful in selling oil-free compressors. Thanks to thorough knowledge of compressor technique, he won the deep trust of his customers.

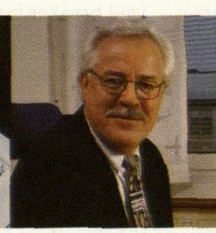
Tadashi Kinouchi, Oil-free Rental manager in Japan, succeeded in establishing the rental operation in the Japanese market. He also sold a large number of oil-free compressors.

Mark Larkin

Claude Roy



Garth Milton



Boeric Andersson

Marek Szafirski

Ted Beasley

Ye Chun

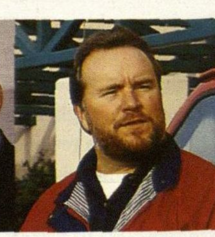
Tadashi Kinouchi

Lois Blot

Philippe Artzet

Carlos Maia

Rodrigo M Vincentini



Lyle Haley

Lois Blot, marketing manager for electric power tools in France, successfully contributed to much stronger sales of AEG tools. Listening to his distributors' requests and customer needs, he developed a special shop concept to position products with a distinct profile in home centers.

Philippe Artzet, France; *Carlos Maia,* Brazil; and *Rodrigo M. Vincentini,* Brazil, together customized a solution of assembly equipment for Renault's plant in Curitiba, Brazil. Thanks to Atlas Copco's worldwide sales organization, the team formed quickly and worked out the optimal customer solution which resulted in a significant order.

Lyle Haley, district manager for Milwaukee Electric Tool in San Francisco, boosted sales in his district in 1997 more than 20 percent. By working closely with customers, he developed customized sales programs based on the needs of each distributor. In addition, he is making a major contribution to provide distributor and company sales people with product and sales training.

Knowledge transfer enhances competencies

Atlas Copco's ability to bolster its competitive advantage depends on its personnel having opportunities to continuously develop their competencies.

That is why Atlas Copco has conducted more projects during the past year than in previous years to encourage and provide for knowledge transfer within the Group.

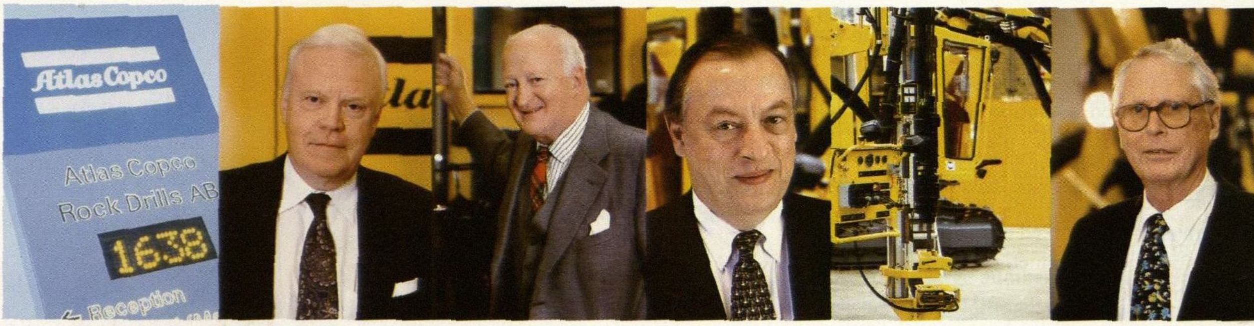
Atlas Copco Circles, introduced in 1996, has provided employees around the world the opportunity of learning more about their company. In small teams personnel have discussed the Group's various businesses and how their own, local work place fits into the overall organization.

The study circle project finished in 1997, having involved more than 21,000 employees in a total of 2,500 circles. Personnel expressed enthusiasm over the project, so the approach is certain to be applied for other purposes in the future. Next on the agenda is a project in which managers thoroughly discuss the strategic direction for achieving faster growth.

As part of its initiatives in Asia, Atlas Copco founded a company school in China. The aim of the school is to give the growing proportion of locally hired staff professional training and an understanding of their roles in the process. In 1997, experienced managers and specialists from Atlas Copco were on-site and trained in-house instructors who will conduct training in English and Mandarin Chinese.

Board of Directors and Auditors

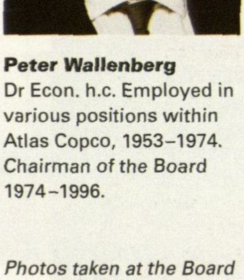
Board of Directors



Anders Scharp **Tom Wachtmeister** **Erik Belfrage** **Gösta Bystedt**

Sune Carlsson **Paul-Emmanuel Janssen** **Lennart Jeansson** **Hari Shankar Singhania**

Honorary Chairman



Peter Wallenberg
Dr Econ. h.c. Employed in various positions within Atlas Copco, 1953–1974. Chairman of the Board 1974–1996.

Photos taken at the Board of Directors' meeting at Atlas Copco Rock Drilling Equipment in Örebro, Sweden.

Board of Directors

Anders Scharp Chairman (1992). Born 1934. Chairman of the Boards of Electrolux, SKF, Saab, Scania, Incentive and Swedish Employers' Confederation. Vice Chairman of the Board of Investor. Board member of Email (Australia) and Federation of Swedish Industries. Stockholdings: 5,000 A.

Tom Wachtmeister Vice Chairman (1975). Born 1931. Employed by Atlas Copco 1959–1991. President and CEO 1975–1991. Member of the Boards of Norsk Hydro (Norway), North Atlantic National Resources, Scania, STORA and The Svenska Dagbladet Foundation. Chairman of Swedish Taxpayers' Association. Vice Chairman of the General Export Association. Stockholdings: 92,000 A.

Erik Belfrage (1991). Born 1946. Senior Vice President of S-E-Banken. Various positions in the Swedish Foreign Office 1970–1987. Chairman of the Boards of the Swedish Institute of Management, Centre for European Policy Studies and the Sigtuna School Foundation. Member of the Boards of Investor, Saab and SAS. Stockholdings: 0.

Gösta Bystedt (1987). Born 1929. Chairman of the Board of Kalmar Industries. Vice Chairman of the Boards of Electrolux and Axel Johnson. Member of the Boards of SKF and Federation of Swedish Industries. Stockholdings: 10,330 A; 1,665 B.

Sune Carlsson (1997). Born 1941. Executive Vice President ABB Asea Brown Boveri. Member of the Board of SKF. Stockholdings: 0.

Paul-Emmanuel Janssen (1994). Born 1931. Chairman of Générale de Banque, Brussels, Belgium. Director and Member of the Executive Committee of the Federation of Belgian Industry. Director of Union Financière Boël, Solvac (Solvay group) and Lhoist. Chairman of the Board of Directors of Atlas Copco Airpower, Belgium. Stockholdings: 1,125 B.

Lennart Jeansson (1997). Born 1941. Executive Vice President AB Volvo. Member of the Boards of AGA, Bilia and Storebrand ASA. Stockholdings: 1,000 A.

Michael Treschow **Giulio Mazzalupi** **Lars-Erik Soting** **Håkan Hagerius**

Bengt Lindgren **Sune Kjetselberg** **Tore Hedberg** **Per-Olov Olsson**

Hari Shankar Singhania (1996). Born 1932. President of J.K. Organization (India). Chairman of i.e. Atlas Copco (India), J.K. Corp, J.K. Industries, Central Pulp Mills and J.K. Udaipur Udyog. Former President of the International Chamber of Commerce. Stockholdings: 0.

Michael Treschow (1991). Born 1943. President and Chief Executive Officer of Electrolux. Chairman of Swedish Trade Council, Vice Chairman of Saab Automobile. Member of the Boards of e.g. Electrolux, Investor and Parker Hannifin (USA). Stockholdings: 27,555 A, 530 B.

Giulio Mazzalupi (1990). Born 1940. President and Chief Executive Officer of Atlas Copco. Employed by Atlas Copco since 1971. Member of the Board of Electrolux-Zanussi. Stockholdings: 1,000 A.

Employee representations

Tore Hedberg (1990). Born 1937. Chairman, Atlas Copco local of the Swedish Union of Clerical and Technical Employees in Industry (SIF), Stockholm. Stockholdings: 0.

Bengt Lindgren (1990). Born 1957. Chairman, Uniroc local of the Metal Workers' Union, Fagersta. Stockholdings: 0.

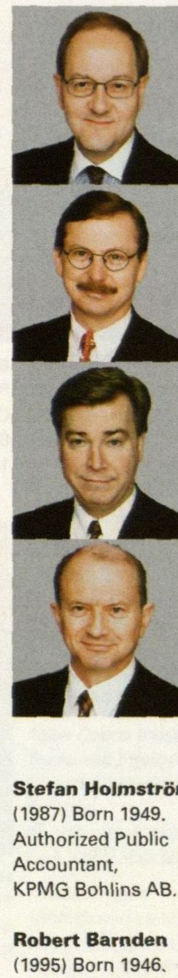
Lars-Erik Soting (1993). Born 1965. Chairman, Atlas Copco local of the Metal Workers' Union at Atlas Copco Rock Drills (Avos), Örebro. Stockholdings: 0.

Håkan Hagerius Deputy Member (1994). Born 1942. Chairman of the Swedish Union of Clerical and Technical Employees in Industry (SIF) at Atlas Copco Rock Drills (Avos), Örebro. Stockholdings: 0.

Sune Kjetselberg Deputy Member (1992). Born 1951. Chairman, Atlas Copco Tools local of the Metall Workers' Union, Tierp. Stockholdings: 0.

Per-Olov Olsson Deputy Member (1993). Born 1937. Chairman, Atlas Copco local Association of the Swedish Graduate Engineers, Nacka. Stockholdings: 1,000 B.

Auditors



Stefan Holmström (1987) Born 1949. Authorized Public Accountant, KPMG Bohlins AB.

Robert Barnden (1995) Born 1946. Authorized Public Accountant, Öhrlings Coopers & Lybrand AB.

Thomas Thiel (1993) Born 1947. Authorized Public Accountant, Deputy, KPMG Bohlins AB.

Sigvard Heurlin (1995) Born 1940. Authorized Public Accountant, Deputy, Öhrlings Coopers & Lybrand AB.

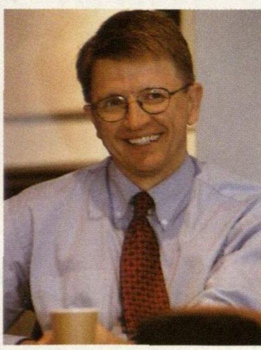
Group management and Group staffs

Giulio Mazzalupi
President and Chief Executive Officer. Employed since 1971. Born 1940. Stockholdings: 1,000 A.

Bengt Kvarnbäck
Senior Executive Vice President Compressor Technique. Employed since 1992. Born 1945. Stockholdings: 7,650 A; 50 B.

Freek Nijdam
Senior Executive Vice President Construction and Mining Technique. Employed since 1970. Born 1940. Stockholdings: 0.

Gunnar Palme
Senior Executive Vice President Industrial Technique. Employed since 1980. Born 1954. Stockholdings: 0.



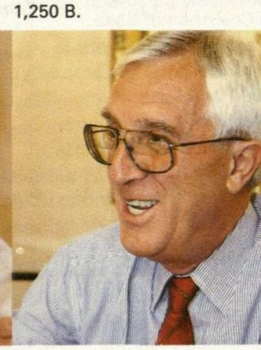
Hans Ola Meyer
Finance. Employed since 1991. Born 1955. Stockholdings: 500 A.

Lennart Johansson
Controlling, accounting and auditing. Employed since 1987. Born 1955. Stockholdings: 0.

Marianne Hamilton
Organization development and management resources. Employed since 1990. Born 1947. Stockholdings: 1,000 A; 1,250 B.

Hans Sandberg
Legal. Employed since 1975. Born 1946. Stockholdings: 0.

Arthur J. Droege
Regional Executive Asia Pacific and responsible for projects in Asia. Employed since 1976. Born 1948. Stockholdings: 0.



Romano Girardi
Regional Executive Latin America. Employed since 1962. Born 1930. Stockholdings: 0.

Paolo Duca
Regional Executive Middle East and northern Africa. Employed since 1962. Born 1940. Stockholdings: 0.

Directions

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Atlas Copco AB
A Public Company (publ)

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Atlas Copco Industrial Tools and Equipment
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Atlas Copco

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Atlas Copco

Annual Report

97

Extract in US dollars

All figures have been converted at the exchange rate of Dec. 31, 1997: USD 1.00 = SEK 7.90.

An English version of the complete Annual Report is available.

Atlas Copco

Five years in summary

Atlas Copco Group

USD millions unless otherwise noted	1993[12]	1994[12]	1995	1996	1997
Operating profit	155	239	337	371	483
Operating profit margin, %[1]	6.5	9.0	10.9	11.7	12.7
Profit after financial items	167	247	359	389	446
Profit margin, %[2]	7.0	9.3	11.6	12.2	11.7
Profit for the year	110	151	231	245	279
Return on capital employed, before tax, %[3]	13.2	18.4	22.4	21.2	21.1
Return on equity, after tax, %[4]	11.0	13.7	18.6	17.5	17.6
Equity/Assets ratio, %[5]	47.8	51.1	47.8	51.8	39.2
Orders received	2,430	2,747	3,145	3,185	3,884
Revenues	2,393	2,647	3,095	3,180	3,802
Percent change	+18	+11	+17	+3	+20
Sales outside Sweden, %	95	95	96	96	97
Net interest expense	5	7	16	16	–39
As percent of revenues	0.2	0.3	0.5	0.5	–1.0
Interest coverage ratio[6]	5.1	6.7	8.7	10.6	6.5
Cash flow from operations after financial items	165	174	194	243	491
Total assets	2,256	2,304	2,798	2,934	4,404
Ratio of assets to liabilities	1.9	2.0	1.9	2.1	1.6
Ratio of current assets to current liabilities	1.8	2.0	1.7	1.9	1.0
Debt/equity ratio[7]	20.9	3.8	29.9	15.8	74.9
Capital turnover ratio[8]	1.09	1.16	1.19	1.11	1.08
Investments in properties and machinery	50	80	90	104	106
As percent of revenues	2.1	3.0	2.9	3.3	2.8
Investments in rental equipment	29	21	29	43	116
As percent of revenues	1.2	0.8	0.9	1.3	3.1
Average number of employees	18,247	18,104	19,751	21,085	22,296
Revenues per employee, USD thousands	131	146	157	151	171

Per Share Data, USD unless otherwise noted	1993[12]	1994[12]	1995	1996	1997
Earnings[9]	0.60	0.82	1.26	1.34	1.52
Dividend	0.23	0.29	0.38	0.47	0.54[13]
Price quotation, Dec. 31, A share	10.51	12.03	12.91	20.89	30.00
Price quotation, Dec. 31, B share	10.38	12.03	12.66	21.01	30.00
Highest price quoted, A share	10.89	13.67	15.82	21.14	33.67
Lowest price quoted, A share	7.59	10.25	11.01	12.28	20.38
Average price quoted, A share	8.86	11.90	13.04	16.08	27.09
Direct yield, percent[10]	2.6	2.4	2.9	3.0	2.0
Price/Earnings[11]	14.9	14.5	10.4	12.0	17.8

Guidelines for foreign readers of Atlas Copco's financial statement

Accounting principles

General background

The underlying principles on which Swedish financial statements are based, are the universally accepted ones of historical cost, accrual accounting – i.e. matching income and expense on a correct inter-period allocation basis – and conversatism – recognizing a loss risk as soon as it is measurable but not taking credit for income items until actually earned. Certain exceptions from the consistent application of these principles are described below.

Effective from 1997, Atlas Copco has followed the new Swedish Annual Accounts Act, which conforms to EU requirements. The main effect of this change is a reordering of items in the income statement and balance sheet. The new Act has but a marginal effect on valuation principles previously applied. Income statements and balance sheets for previous years, provided for comparison, have been adjusted to comply with the new regulations.

Prior to the acquisition of Prime Service, the rental equipment was reported as inventory. The rental equipment has been reclassified and is now included in fixed assets. Previous years' figures have been restated accordingly.

The Company follows the recommendations of the Financial Accounting Standards Council with the exception of its principles for treatment of goodwill, as described below.

Consolidation

The Consolidated Income Statement and Balance Sheet of the Atlas Copco Group cover all companies in which the Parent Company, directly or indirectly, holds more than 50 percent of the voting rights, as well as those companies in which the Group in some other manner has a decisive influence and a substantial participation in the income from their operations.

The consolidated accounts have been prepared in accordance with the purchase method, which means that assets and liabilities are reported at market value including deferred taxes according to the acquisition plan. If the acquisition cost exceeds the market value of the company's net assets, calculated as above, the difference is reported as goodwill, see below.

Companies acquired during the year have been reported in the Consolidated Income Statement, with the amounts relating to the period following the date of acquisition.

Earnings of companies divested during the year have been deducted from consolidated earnings on the basis of the Group's reported net assets in these companies at the time of the divestment.

Goodwill

The acquisition of well-established companies active in an international environment, normally means that the acquisition price substantially exceeds tangible net worth. The market price is determined primarily by future expectations, which are based on the company's market position and know-how.

A company acquisition, in which the acquisition price exceeds the company's net assets valued at market prices, results in intangible assets which are capitalized and amortized over a certain period.

Goodwill is normally amortized over ten years, while goodwill arising from strategic acquisition is amortized over a period of 20-40 years.

The economic life of assets is appraised annually to determine whether the selected amortization plan is sufficient.

Notes

1 Operating profit (EBIT) as a percentage of revenues.

2 Profit after financial items as a percentage of revenues.

3 Profit after financial items plus interest paid and foreign exchange differences as a percentage of average total assets less non-interest-bearing liabilities.

4 Profit after financial items less tax and minority interest, as a percentage of average shareholders' equity.

5 Shareholders' equity and minority interest as a percentage of total capital.

6 Profit after financial items plus interest paid and foreign exchange differences divided by interest paid and foreign exchange differences.

7 Difference between interest-bearing liabilities and liquid assets in relation to shareholders' equity including minority interest.

8 Revenues divided by average total assets.

9 Profit after financial items less tax and minority interest, divided by the number of shares outstanding.

10 Dividend as percent of average quoted price during the year.

11 Average quoted price during the year in relation to earnings per share as defined in note 9.

12 Values and key ratios have been recalculated in accordance with change in accounting principles.

13 According to the Board of Directors' proposal.

Associated companies

Companies in which the Atlas Copco Group has between 20 and 50 percent of the voting rights, and in which it has a substantial ownership involvement, are reported as associated companies.

Holdings in associated companies are reported in the Consolidated Income Statement and Balance Sheet in accordance with the equity method.

Atlas Copco's share of income after net financial items in associated companies is reported in the Income Statement under the heading Other operating income.

Shares of taxes in associated companies are reported in consolidated tax expense.

The related acquisition costs are reported under Financial assets in the Balance Sheet, increased or reduced by the shares of income and less dividend received. Undistributed income in these companies is reported among restricted reserves in consolidated shareholders' equity.

Internal profits have been eliminated in appropriate cases.

Translation of accounts of foreign subsidiaries

Atlas Copco applies the current-rate method in translating the accounts of foreign subsidiaries, in accordance with the suggested recommendations of the Swedish Institute of Authorized Public Accountants FAR. In applying this method, the subsidiaries are primarily reported as independent units with operations conducted in foreign currencies, and in which the Parent Company has a net investment. The exceptions to this approach are those subsidiaries which are located in high-inflationary countries and so called integrated companies. The accounts of such subsidiaries are translated according to the monetary/non-monetary method. In accordance with this suggested recommendation, such a procedure is regarded as providing a more accurate picture of the earnings and financial positions of these companies.

In accordance with the current-rate method, all assets and liabilities in the balance sheets of subsidiaries are translated at year-end rates, and all items in the income statements at the average exchange rate for the year. Translation differences that arise are a result of the fact that net investments are translated at year-end at a rate different from that used at the beginning of the year. This does not affect earnings, but is instead transferred directly to shareholders' equity.

For those subsidiaries treated according to the monetary/non-monetary method, all non-monetary items, real estate (land and buildings), machinery and equipment, inventories, shareholders' equity, and deferred tax, are translated at the acquisition date rates. Other items, monetary items, are translated at year-end rates. The income statement items have been translated at the average rate for the year, except for the cost of goods sold, depreciation and deferred taxes, which have been translated at the investment rate. Exchange differences arising in connection with the translation of the accounts, and which accordingly relate to companies in countries with high inflation have been included in the Income Statement.

The accounts of all subsidiaries of the Atlas Copco Group are translated according to the current-rate method, except for the companies in high-inflationary countries, primarily Latin America. The operational currency of these companies is regarded as being the USD, and is therefore translated in two stages.

In the first stage, translation is made to USD in accordance with the monetary/non-monetary method, whereby translation differences arising are charged to consolidated income.

In the second stage, the company's balance sheet items are translated to SEK according to the year-end rate and the income statement items according to the average rate for the year. The resulting translation differences are transferred directly to shareholders' equity.

Receivables and liabilities in foreign currencies

Receivables and liabilities in foreign currencies are translated at the year-end rate.

Hedging of net investments

Forward contracts, currency swaps, and loans in foreign currencies have been arranged in order to hedge the Group's net assets in foreign subsidiaries. Foreign exchange gains and losses on such contracts, less current and deferred tax, are not included in income for the year but are offset against translation differences arising in connection with the translation of the foreign subsidiaries' net assets. In the individual subsidiaries, such contracts are valued in accordance with the lowest-value principle for receivables and with the highest-value principle for liabilities.

Interest-rate differences arising between currencies are included in the net interest items and distributed evenly over the term of each contract.

Hedging of commercial flows

When calculating the value of the forward contracts outstanding, provision is made for unrealized losses to the extent these exceed unrealized gains. Unrealized gains which exceed unrealized losses are not recognized as revenue. When calculating unrealized exchange-rate differences, that portion of the hedged amounts is excluded for which currency flows, through currency transactions, are most likely to cover the forward contracts.

Financial investments

Financial and other investments, that are to be held to maturity are valued at acquisition cost.

Investments intended for trading are valued at the lower of cost or market.

Inventories

Inventories are valued at the lower of cost or market, in accordance with the first in/first out principle and the net sales value.

Group inventories are shown after deductions for obsolescence and for internal profits arising in connection with deliveries from the product companies to the sales companies. Deferred tax has been taken into account in connection with these transactions.

Transfer pricing between the companies is based on market price setting.

Depreciation

Cost depreciation is based on original cost and is applied according to the straight-line method over the economic life of the asset.

The following economic lives are used for cost depreciation and current cost depreciation:

Goodwill and other intangible assets	5 to 40 years
Buildings	25 to 50 years
Machinery and equipment	3 to 10 years
Vehicles	4 to 5 years
Computer equipment	3 to 4 years
Rental equipment	3 to 10 years

Research and development costs

Atlas Copco's own research and development costs are expensed as incurred.

Product development costs and warranty costs

Product development costs are charged against operations when they are incurred.

Estimated costs of product warranties are charged against cost of sales at the time the products are sold.

Taxes

The Company calculates deferred tax based on the differences between reported values in the balance sheet and residual value available for tax purposes. Those tax-loss carryforwards arising are anticipated in instances where it is more likely than not that they will result in lower tax payments in the future. When calculating deferred tax, the nominal tax rates prevailing in each country have been used individually for each company. Deferred tax relating to 1997 operations is shown under the entry Taxes in the Income Statement and is specified in note 8 and under Fixed assets note 13 and Non-interest-bearing provisions in the Balance Sheet.

International accounting principles

The consolidated accounts for the Atlas Copco Group follow Swedish accounting practices. Swedish accounting practices, however, diverge from international practices on certain points. A calculation of the income for the year and financial position, taking into account the major differences between Swedish accounting practice and the U.S. GAAP.

Application of U.S. GAAP would have the following approximate effect on consolidated net income and shareholders' equity for the Group:

U.S. GAAP	1997	1996
Income as reported in the Consolidated Income Statement	279	245
Items increasing/decreasing reported net income:		
Depreciation/sales of revaluations	0	0
Capitalization of interest expenses	–1	0
Amortization of goodwill	–1	–2
Deferred taxes	1	0
Calculated net profit	278	243
Calculated earnings per share, USD	1.51	1.33
Total assets	4,461	3,003
Total liabilities	2,707	1,449
Shareholders' equity as reported in the Consolidated Balance Sheet	1,703	1,500
Net adjustments in reported shareholders' equity	51	54
Approximate shareholders' equity	1,754	1,554

Consolidated Income Statement

Amounts in USD m.	1997	1996
Revenues	3,802	3,180
Cost of goods sold	–2,485	–2,112
Gross profit	1,317	1,068
Cost of marketing, administration, research and development	–824	–716
Amortization on goodwill	–35	–20
Other income and expenses from operations	25	39
Operating profit	483	371
Financial income and expenses	–37	18
Profit after financial items	446	389
Taxes	–163	–141
Minority interest	–4	–3
Profit for the year	279	245
Earnings per share, USD	1.52	1.34

Consolidated Balance Sheet

Amounts in USD m.		Dec. 31, 1997		Dec. 31, 1996	
ASSETS					
Fixed assets	Intangible assets	1,399		479	
	Tangible assets	1,116		645	
	Financial assets	124	2,639	166	1,290
Current assets	Inventories	662		566	
	Current receivables	899		763	
	Investments	28		139	
	Cash and bank	176	1,765	176	1,644
Total assets			4,404		2,934
SHAREHOLDERS' EQUITY AND LIABILITIES					
Shareholders' equity	**Restricted equity**				
	Share capital	116		116	
	Restricted reserves	615		604	
	Non-restricted equity				
	Retained earnings	693		535	
	Profit for the year	279	1,703	245	1,500
Minority interest			23		19
Provisions	**Interest-bearing provisions**				
	Pensions and similar commitments	256		244	
	Non-interest-bearing provisions				
	Deferred taxes	207		147	
	Other provision	88	551	66	457
Long-term liabilities	**Interest-bearing liabilities**				
	Liabilities to credit institutions	279		72	
	Non-interest-bearing liabilities				
	Other liabilities	41	320	36	108
Current liabilities	**Interest-bearing liabilities**				
	Liabilities to credit institutions	963		239	
	Non-interest-bearing liabilities				
	Operating liabilities	844	1,807	611	850
Total shareholders' equity and liabilities			4,404		2,934
Assets pledged			25		21
Contingent liabilities			174		139

ATLAS COPCO GROUP

	1997	1996
Revenues, USD m.	3,802	3,180
Operating profit, USD m.	483	371
Profit after financial items, USD m.	446	389
Return on capital employed, %	21	21
Investments, USD m.	106	104
Number of employees	22,296	21,085

Atlas Copco is an international group of industrial companies, with its head office in Stockholm, Sweden. Operations are conducted in three business areas – Compressor Technique, Construction and Mining Technique and Industrial Technique – through 15 divisions. Each division is specialized within a specific area and has total responsibility for product development, manufacturing, and sales and service operations. 97 percent of the Group's revenues are attributable to countries outside Sweden. Products are manufactured at 58 plants in 14 countries.

COMPRESSOR TECHNIQUE

	1997	1996
Revenues, USD m.	1,806	1,402
Operating profit, USD m.	321	229
Return on capital employed, %	28	33
Investments, USD m.	44	36
Number of employees	9,235	7,698

The Compressor Technique business area is a leading manufacturer of industrial, oil-free and portable compressors, generators, air dryers, after coolers, control systems, filters and specially built gas and process compressors, expansion turbines and pumps.

The products are developed, manufactured and marketed by the following divisions: Airtec, Portable Air, Industrial Air, Oil-free Air, Atlas Copco Applied Compressor and Expander Technique (ACT) and Prime Service.

CONSTRUCTION AND MINING TECHNIQUE

	1997	1996
Revenues, USD m.	817	749
Operating profit, USD m.	49	50
Return on capital employed, %	12	14
Investments, USD m.	26	27
Number of employees	5,058	5,143

The Construction and Mining Technique business area is a leading manufacturer of rock drilling tools, tunneling and mining equipment, surface drilling equipment, construction tools, loading equipment and geotechnical drilling equipment.

The products are developed, manufactured and marketed by the following divisions: Atlas Copco Rock Drilling Equipment, Atlas Copco Craelius, Uniroc, Atlas Copco Construction Tools and Atlas Copco Wagner.

INDUSTRIAL TECHNIQUE

	1997	1996
Revenues, USD m.	1,179	1,029
Operating profit, USD m.	119	106
Return on capital employed, %	13	12
Investments, USD m.	35	39
Number of employees	7,898	8,119

The Industrial Technique business area is one of the world's largest manufacturers of power tools. The product range also covers assembly systems and motion control products.

The products are developed, manufactured and marketed by the following divisions: Milwaukee Electric Tool, Atlas Copco Electric Tools, Atlas Copco Industrial Tools and Equipment and Alliance Tools.

Atlas Copco

Atlas Copco AB, S-105 23 Stockholm, Sweden