

## 2017 Registration Document

Including the Annual Financial Report



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# 2017 REGISTRATION DOCUMENT

INCLUDING THE ANNUAL FINANCIAL REPORT

AMF

AUTORITÉ  
DES MARCHÉS FINANCIERS

This Registration Document was filed with the French financial markets authority (*Autorité des marchés financiers*, AMF) on 30 March 2018, in accordance with Article 212-13 of the AMF General Regulations. It may only be used in support of a financial transaction if accompanied by an offering circular authorised by the AMF. It was drawn up by the issuer and its signatories accept liability.

The English language version of this report is a free translation from the original, which was prepared and filed with the AMF in French. All possible care has been taken to ensure that the translation is an accurate presentation of the original. However, in all matters of interpretation, views or opinions expressed in the original language version of the document in French take precedence over the translation.

In accordance with Article 28 of Commission Regulation (EC) No. 809/2004, the following information is incorporated by reference in this Registration Document:

- the consolidated financial statements and corresponding audit reports presented on pages 29 to 80 of the 2015 Registration Document filed with the AMF on 31 March 2016;
- the Group's financial information, key figures and management report, presented respectively on pages 5 and 8 to 28 of the 2015 Registration Document filed with the AMF on 31 March 2016;
- the consolidated financial statements and corresponding audit reports presented on pages 27 to 71 of the 2016 Registration Document filed with the AMF on 5 April 2017;
- the Group's financial information, key figures and management report, presented respectively on pages 4, 5 and 8 to 25 of the 2016 Registration Document filed with the AMF on 5 April 2017.

The omitted sections of these documents are either irrelevant to the investor, or addressed elsewhere in this Registration Document.



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# CHAIRMAN'S FOREWORD



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## "ANOTHER RECORD YEAR FOR THALES"

"2017 was another record-breaking year for Thales. The Group exceeded all its annual financial targets. As expected, order intake remained high. It was comparable to the 2016 level if we remove the exceptional Rafale contract for India that was booked in September 2016. The Group enjoyed significant commercial successes. In the transport segment, they include the modernisation of the signalling for one of the main railways in Egypt as well as the signalling of the future regional express train that will link Dakar to its airport. In the defence and security segment, the Group booked several major projects for both the French and UK armed forces. Space was the only activity that experienced a slowdown in order intake reflecting the impact of the telecommunication satellite operators' wait-and-see attitude and a high basis of comparison in the institutional market.

For the second year in a row, organic sales growth exceeded 5%, powered by all our businesses. This solid performance reflects both our continued strong growth in emerging markets and stepped-up organic growth in mature markets, which reached almost 6% in 2017.

At 9.8%, the highest level ever achieved by our Group, operating profitability was at the top end of the range of the targets set in 2014.

This financial performance is the result of the momentum in sales, our continued efforts to improve our competitiveness and the strengthening of our technological leadership in our technological innovations. It would not have been possible without the dedication of the Group's 65,000 employees, all of whom I would like to thank on behalf of the Board of Directors.

At the same time, Thales is preparing for the future and stepping up its growth strategy: in 2017, we increased our investments in R&D by 9% and bolstered our expertise in artificial intelligence, with the creation of a new research centre in that field and, in the field of big data, through the acquisition of Guavus, a pioneer in real-time big data analytics. We are investing €150 million over three years to set up a cross-functional 'digital factory' in order to capitalise on our unique portfolio of digital technologies.

We are actively preparing for the acquisition of Gemalto, which is expected to close in the second half of 2018. This acquisition marks a key step in the implementation of our strategy. Together with the Gemalto management team, we have big ambitions based on a shared vision of the digital transformation of our businesses and our customers. By bringing together our talents, Thales and Gemalto will create a global leader in digital security.

I am confident that this strategy will allow us to further drive profitable and sustainable growth."

### **Patrice Caine**

Chairman & Chief Executive Officer

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# OVERVIEW OF THE GROUP

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## HELPING CUSTOMERS MASTERING EVERY DECISIVE MOMENT

The companies, governments and institutions that make the world go round – they rely on Thales.

In a world that is increasingly fast moving, unpredictable – and full of opportunities, they have big ambitions: to make life better, to keep us safer.

Combining a unique diversity of expertise, talents and cultures, Thales's 65,000 architects design and deliver extraordinary high technology solutions. Solutions that make tomorrow possible, today.

From the bottom of the oceans to the depths of space and cyberspace, we help our customers across five key markets – Aeronautics, Space, Ground Transportation, Defence and Security – to think smarter and act faster, mastering ever greater complexity and every decisive moment along the way.

Whatever it takes.

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### AERONAUTICS

In Aeronautics, governments, airports, airlines, pilots, crews and passengers rely on Thales to make flight safer, easier and more efficient.

We do this by designing, delivering and supporting the systems that keep our skies running. From air traffic management, training and simulation solutions, to nose-to-tail aircraft connectivity and in-flight services, we enable and connect all parts of the Aeronautics ecosystem in the air, on the ground, and in between.

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### SPACE

In Space, we design, operate and deliver the satellite-based systems that help our customers to position and connect anyone or anything, everywhere. We help them

observe our planet, and help them optimize the use of our planet's – and our solar system's – resources. We believe space is humankind's new horizon, which will enable us to build a better, more sustainable life on Earth.

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### GROUND TRANSPORTATION

In Ground Transportation, countries, cities and transport operators rely on Thales to adapt to rapid urbanisation and meet new mobility demands – locally, between cities and across national frontiers.

Our expertise in signalling, communications, fare collection and cybersecurity gives people and goods the connected journey to move safely and efficiently. And no matter how challenging the project, we stay by our customer's side until the job is done.

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### DEFENCE

In Defence, we are trusted at the highest levels to help armed forces prepare for, achieve and maintain tactical superiority and strategic independence over any form of threat.

Governments rely on Thales to protect citizens, and make the world safer.

From designing smart sensors and advanced defence systems, to developing collaborative combat, and connecting and equipping soldiers on the digital battlefield, our systems deliver information superiority and give joint forces mastery of action whenever they face their decisive moments.

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### SECURITY

In Security, governments, institutions and large global companies rely on Thales to design and deliver solutions that protect states, cities and critical infrastructures in an

increasingly unpredictable world, with emerging cyber threats.

From helping cities and critical infrastructures become safer and smarter, to securing global financial markets and protecting sensitive data, to keeping security forces connected on critical missions, we ensure integrity of the technologies that keep our world moving, staying one step ahead of all forms of digital threat and enhancing life for all.

# KEY FIGURES

## SALES



\* Organic growth.

## ORDER INTAKE (BOOK-TO-BILL RATIO)



## EBIT (EBIT MARGIN)



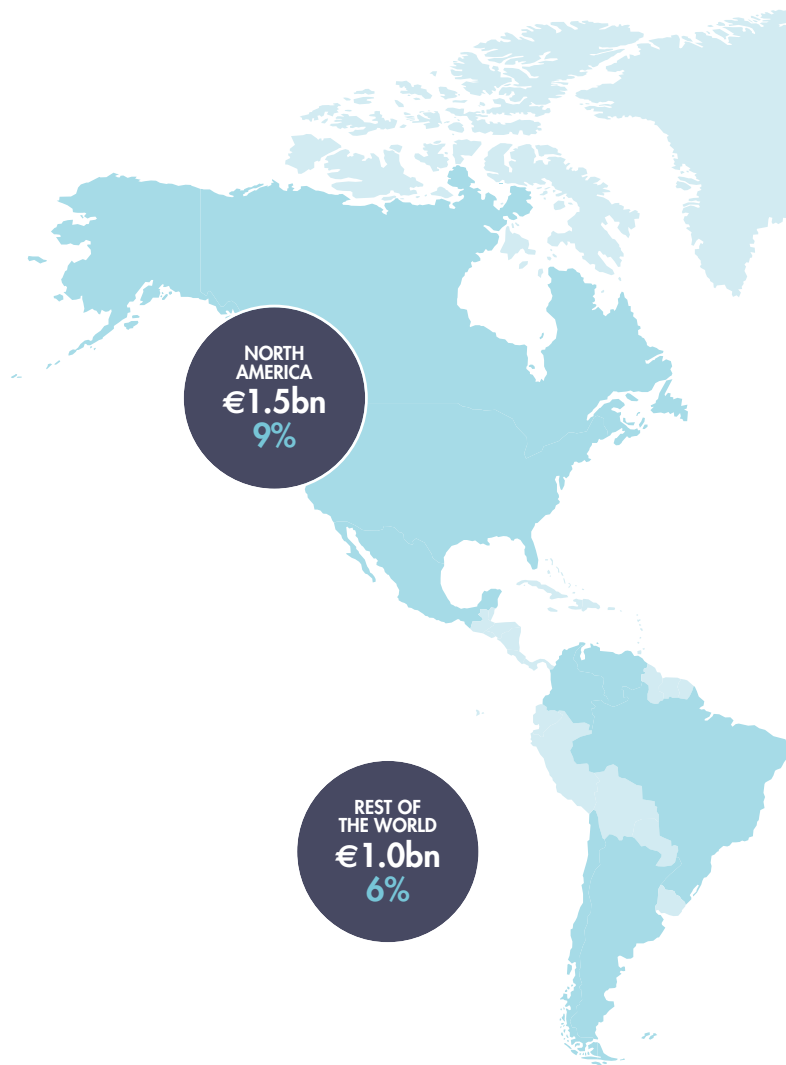
\* Organic growth.

## DIVIDEND PER SHARE



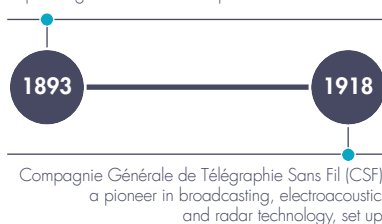
\* Proposed to the Shareholders' Meeting on 23 May 2018.

## BREAKDOWN OF 2017 SALES BY REGION

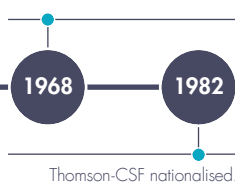


# HISTORY

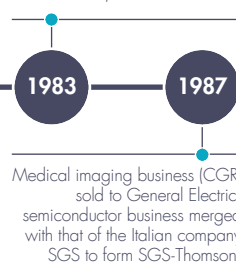
Compagnie Française Thomson-Houston (CFTH) established to exploit the patents of the US company Thomson-Houston Electric Corp. in France, in the field of power generation and transport.



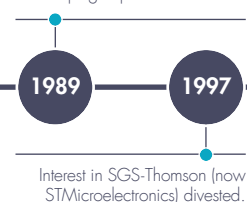
CSF and the professional electronics businesses of Thomson-Brandt merge to form Thomson-CSF.



Civil telecommunications businesses sold to Compagnie Générale d'Électricité (now Alcatel-Lucent).



Acquisition of the defence electronics business of the Philips group.



**WORKFORCE**  
(EMPLOYEES MANAGED)

**65,100**

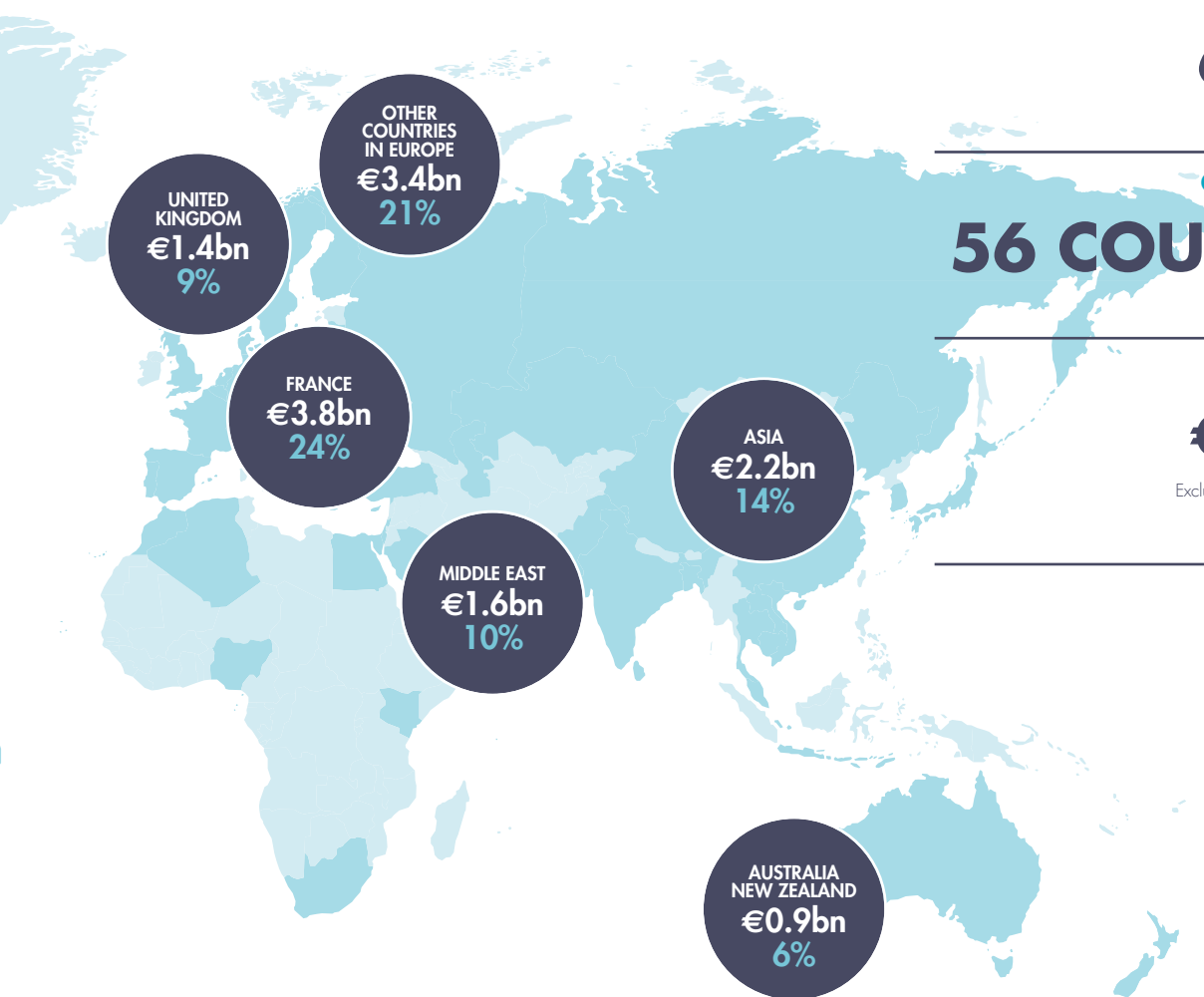
**GLOBAL PRESENCE**

**56 COUNTRIES**

**SELF-FUNDED R&D**

**€797m**

Excluding R&D using external funding



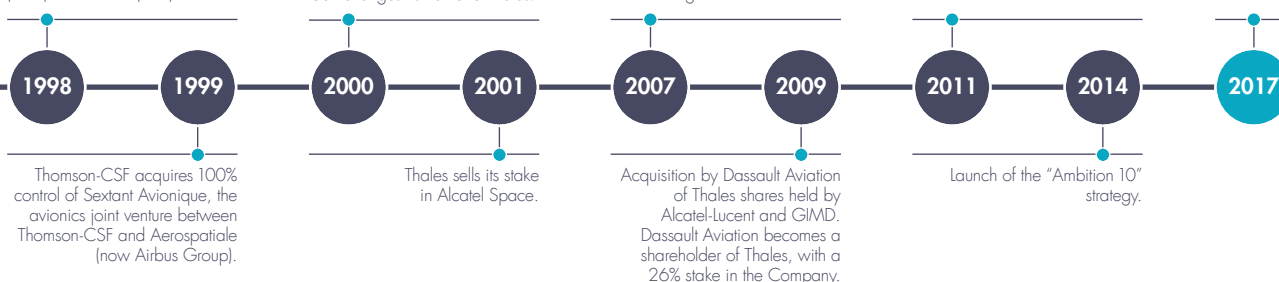
Thomson-CSF privatised; Alcatel and Groupe Industriel Marcel Dassault (GIMD) contribute assets and become shareholders. Satellite businesses of Alcatel, Aerospatiale and Thomson-CSF merge to form Alcatel Space, jointly owned by Thomson-CSF (49%) and Alcatel (51%).

Takeover of Racal electronics in the United Kingdom. Thomson CSF changes its name to Thales.

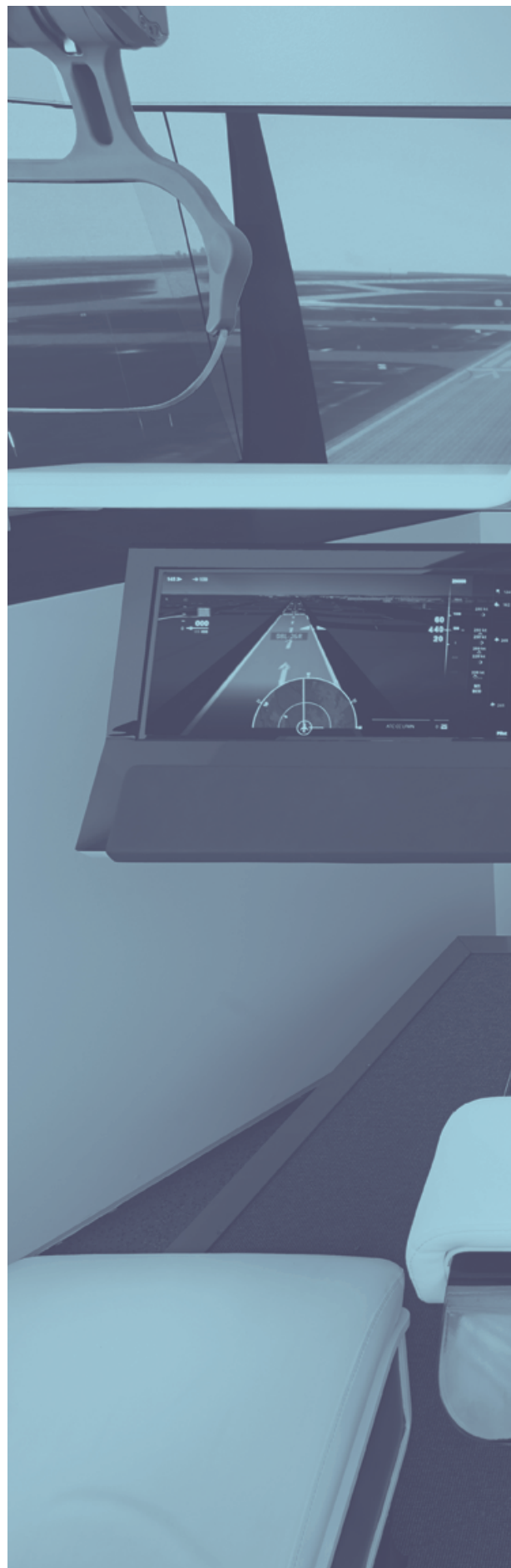
Thales acquires the transport, security and space businesses of Alcatel-Lucent and sells its French naval surface business to DCNS. At the same time, acquisition of a 25% stake in DCNS from the French government.

Thales increases its interest in DCNS to 35%.

Thales intended offer for Gemalto



# 2017 FINANCIAL INFORMATION





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# 1.1 2017 MANAGEMENT REPORT

## 1.1.1 Report on operations and results

### 1.1.1.1 Key figures (adjusted)

(in € millions, except earnings per share and dividend in €)	2017	2016	Total change	Organic change
Order intake	14,920	16,514	-10%	-9%
Order book at end of period	31,914	33,530	-5%	-3%
Sales	15,795	14,885	+6.1%	+7.2%
EBIT <sup>(a)</sup>	1,543	1,354	+14%	+16%
<i>In % of sales</i>	<i>9.8%</i>	<i>9.1%</i>	<i>+0.7 pt</i>	<i>+0.8 pt</i>
Adjusted net income, Group share <sup>(a)</sup>	982	897	+9%	
Consolidated net income, Group share	822	946	-13%	
Adjusted net income, Group share, per share <sup>(b)</sup>	4.64	4.25	+9%	
Dividend per share <sup>(b)</sup>	1.75	1.60	+9%	
Free operating cash flow <sup>(b)</sup>	1,365	954	+43%	
Net cash at end of period	2,971	2,366	+26%	

(a) Non-GAAP measures, see definitions in the appendices, pages 8 and 9.

(b) Proposed to the Shareholders' Meeting on 23 May 2018.

New orders in 2017 amounted to €14,920 million, down 10% compared to the high level recorded in 2016, which was boosted by the Q3 2016 booking of the 36 Rafale fighter aircraft contract ordered by the Indian government. The Group has therefore exceeded the €14 billion order intake target set at the start of 2017. The strong order momentum in Transport and Defence & Security enabled the Group to offset the slowdown of orders in Space. At 31 December 2017, the Group's order book stood at €31,914 million, which represents almost 2 years' worth of sales.

Sales came in at €15,795 million, up 6.1% on a reported basis, and up 7.2% at constant scope and currency ("organic" change). Sales benefitted from both a high rate of growth in emerging markets<sup>(1)</sup> organic growth of +10.3%, running at more than 10% for the fourth consecutive year) and a marked upturn in organic growth in mature markets<sup>(1)</sup> (+5.8%, after +3.9% in 2016 and +0.5% in 2015).

In 2017, consolidated EBIT was €1,543 million (9.8% of sales) compared to €1,354 million (9.1% of sales) in 2016, up 14%. All operating segments contributed to this increase and improved their EBIT margin.

As such, the Group noticeably exceeded all the financial objectives it had set for 2017: an order intake of around €14 billion, a mid-single digit organic sales growth, and an EBIT of between €1,480 million and €1,500 million, up 9% to 11% on 2016, based on February 2017 scope and exchange rates.

At €982 million, adjusted net income, Group share rose 9%. Its increase was held back by one-off items relating to tax reforms in France and the United States.

Consolidated net income, Group share was €822 million. It posted a fall of 13%, affected by the sharp fall in capital gains on disposal of assets.

At €1,365 million compared to €954 million in 2016, free operating cash flow reached a record level, benefiting from the rise in adjusted net income, from a slight reduction in operating investments (€431 million

compared to €472 million in 2016) and from a combination of items that improved the change in working capital requirement. At 31 December 2017, net cash was €2,971 million, up more than €600 million compared to 31 December 2016.

### 1.1.1.2 Presentation of financial information

#### Accounting policies

The Thales group's consolidated financial statements are prepared in accordance with IFRS (International Financial Reporting Standards) as approved by the European Union at 31 December 2017.

These principles, described in Note 13, are consistent with those applied for the year ended 31 December 2016. In particular, the new mandatory standards applicable as from 1 January 2017 (amendments to IAS 12 – Income Tax and annual improvements 2013-2016), have no impact on the Group's financial statements.

#### Non-GAAP financial indicators

In order to facilitate monitoring and benchmarking of its financial and operating performance, the Group presents three key non-GAAP indicators, which exclude non-operating and/or non-recurring items. They are determined as follows:

- **EBIT**, an adjusted operating indicator, corresponds to income from operations plus the share in the net income of equity-accounted companies, before the impact of entries relating to the amortisation of intangible assets acquired (purchase price allocation – PPA) recorded as part of business combinations. From 1 January 2016, it also excludes the other expenses recorded in income from operations that are directly related to business combinations, which are unusual by nature.

(1) "Mature markets" include Europe, North America, Australia and New Zealand; "emerging markets" include all other countries.

This definition drives the definition of other operating indicator on the adjusted P&L:

- **adjusted gross margin** corresponds to the difference between sales and the cost of sales, less expenses recorded in cost of sales that are directly related to business combinations, which are unusual by nature;
- **adjusted indirect costs** correspond to the indirect costs on the consolidated profit and loss account (research and development expenses, marketing and selling expenses, general and administrative expenses), less expenses recorded as part of these expenses and that are directly related to business combinations, which are unusual by nature;
- **adjusted net income** corresponds to net income, excluding the following items and net of the corresponding tax effects:
  - amortisation of acquired intangible assets (PPA) recorded as part of business combinations,
  - expenses recognised in income from operations, that are directly related to business combinations, which are unusual by nature,
  - gains and losses on disposals of assets, changes in scope of consolidation and other,
  - changes in the fair value of derivative foreign exchange instruments (recognised under “Other financial income and expenses” in the consolidated financial statements),
  - actuarial gains (losses) on long-term benefits (recognised under “Finance costs on pensions and other long-term employee benefits” in the consolidated financial statements);

- **free operating cash flow** corresponds to the net cash flow from operating activities before contributions to reduce the pension deficit in the United Kingdom, and after deducting net operating investments.

Readers are reminded that only the consolidated financial statements at 31 December were audited by the statutory auditors, including the calculation of EBIT, which is described in Note 2 “Segment Information” to the consolidated financial statements, and free operating cash flow, which is described and computed in Note 6.4. Adjusted financial information other than that provided in the notes to the consolidated financial statements is subject to the verification procedures applicable to all information included in this press release.

In this management report, amounts expressed in millions of euros are rounded to the nearest million. As a result, the sums of the rounded amounts may differ very slightly from the reported totals. All ratios and changes are calculated based on underlying amounts, which feature in the consolidated financial statements.

“Organic change” measures the movement in monetary indicators excluding the effects of changes in exchange rates and scope of consolidation. It is defined as the difference between (i) the indicator for the prior period, recomputed at the exchange rates applicable for the current period to entities whose reporting currency is not the euro, less the contribution of entities divested during the current period, and (ii) the value of the indicator for the current period less the contribution of entities acquired during the current period.

The impact of these adjustment entries on the income statements at 31 December 2017 and 31 December 2016 is shown in the tables on pages 4 and 5. Calculation of free operating cash flow is outlined on page 6.

## ➤ CALCULATION OF EBIT AND ADJUSTED NET INCOME – 2017

(in € millions)	Adjustments					2017 adjusted P&L
	2017 consolidated profit and loss account	Amortisation of intangible assets (PPA), related charges <sup>(a)</sup>	Gains (losses) on disposals and other	Change in fair value of foreign exchange derivatives	Actuarial differences on long-term employee benefits	
<b>Sales</b>	<b>15,795</b>					<b>15,795</b>
Cost of sales	(11,951)	1				(11,951)
Research and development expenses	(802)	5				(797)
Marketing and selling expenses	(1,041)	5				(1,036)
General and administrative expenses	(550)	7				(542)
Restructuring costs	(81)					(81)
Amortisation of acquisition-related intangible assets (PPA)	(113)	113				0
<b>Income from operations</b>	<b>1,258</b>					<b>N/A</b>
Impairment of non-current assets <sup>(b)</sup>	0					0
Disposal of assets, changes in scope and other	(82)		82			0
Share in net income of equity affiliates	135	19				154
<b>EBIT</b>	<b>N/A</b>					<b>1,543</b>
Impairment of non-current assets <sup>(b)</sup>	0					0
Cost of net debt	5					5
Other financial income and expenses	(99)			70		(29)
Finance costs on pensions and other long-term employee benefits	(66)				3	(63)
Income tax	(264)	(85)	(29)	(24)	(1)	(403)
Net income	887	65	53	46	2	1,052
Non-controlling interests	(65)	(5)		(1)		(71)
<b>NET INCOME, GROUP SHARE</b>	<b>822</b>	<b>60</b>	<b>53</b>	<b>46</b>	<b>2</b>	<b>982</b>
Average number of shares (thousands)	211,661					211,661
<b>NET INCOME, GROUP SHARE, PER SHARE (in €)</b>	<b>3.88</b>					<b>4.64</b>

(a) Including expenses related to acquisitions recorded in income from operations. See definitions of EBIT and adjusted net income on pages 8 and 9.

(b) Included in "Share in net income of equity-accounted companies" in the consolidated income statement and in "Net income" in the adjusted income statement.

## ➤ CALCULATION OF EBIT AND ADJUSTED NET INCOME – 2016

(in € millions)	Adjustments					2016 adjusted P&L
	2016 consolidated profit and loss account	Amortisation of intangible assets (PPA), related charges <sup>(a)</sup>	Gains (losses) on disposals and other	Change in fair value of foreign exchange derivatives	Actuarial differences on long-term employee benefits	
<b>Sales</b>	<b>14,885</b>					<b>14,885</b>
Cost of sales	(11,277)	1				(11,276)
Research and development expenses	(736)	6				(731)
Marketing and selling expenses	(1,023)	6				(1,017)
General and administrative expenses	(544)	7				(537)
Restructuring costs	(101)					(101)
Amortisation of acquisition-related intangible assets (PPA)	(107)	107				0
<b>Income from operations</b>	<b>1,097</b>					<b>N/A</b>
Impairment of non-current assets <sup>(b)</sup>	0					0
Disposal of assets, changes in scope and other	205		(205)			0
Share in net income of equity affiliates	120	11				131
<b>EBIT</b>	<b>N/A</b>					<b>1,354</b>
Impairment of non-current assets <sup>(b)</sup>	0					0
Cost of net debt	6					6
Other financial income and expenses	(81)			70		(10)
Finance costs on pensions and other long-term employee benefits	(78)				12	(66)
Income tax	(256)	(58)	28	(24)	(4)	(314)
Net income	1,015	79	(177)	46	8	970
Non-controlling interests	(68)	(4)		(1)		(74)
<b>NET INCOME, GROUP SHARE</b>	<b>946</b>	<b>75</b>	<b>(177)</b>	<b>45</b>	<b>8</b>	<b>897</b>
Average number of shares (thousands)	210,872					210,872
<b>NET INCOME, GROUP SHARE, PER SHARE (in €)</b>	<b>4.49</b>					<b>4.25</b>

(a) Including expenses related to acquisitions recorded in income from operations. See definitions of EBIT and adjusted net income on pages 8 and 9.

(b) Included in "Share in net income of equity-accounted companies" in the consolidated income statement and in "Net income" in the adjusted income statement.

(1) Compte tenu d'un effet change négatif de 316 M€ et d'un effet de périmètre net positif de 81 M€, principalement lié à la consolidation de la société Vormetric à compter de mars 2017 (secteur Défense & Sécurité).

### ➤ CALCULATION OF FREE OPERATING CASH FLOW

(in € millions)	2017	2016	Change
<b>Operating cash flow before interest and tax</b>	<b>1,776</b>	<b>1,698</b>	<b>+78</b>
Change in working capital and reserves for contingencies	223	(63)	+286
Pension expense, excluding contributions related to the reduction of the UK pension deficit	(121)	(102)	-19
Net interest (paid)/received	8	(8)	+16
Income tax paid	(91)	(99)	+9
<b>Net cash flow from operating activities, excluding contributions related to the reduction of the UK pension deficit</b>	<b>1,796</b>	<b>1,426</b>	<b>+369</b>
Net operating investments	(431)	(472)	+41
<b>FREE OPERATING CASH FLOW</b>	<b>1,365</b>	<b>954</b>	<b>+411</b>
Net (acquisitions)/disposals	(80)	(94)	+15
Contributions related to the reduction of the UK pension deficit	(82)	(88)	+6
Dividends paid	(349)	(297)	-52
Changes in exchange rates and other	(248)	(87)	-162
<b>CHANGE IN NET CASH</b>	<b>606</b>	<b>388</b>	<b>+218</b>

### 1.1.1.3 Order intake

2017 **order intake** amounted to **€14,920 million, down 10%** on 2016 (-9% at constant scope and currency<sup>(1)</sup>). The **book-to-bill** ratio was **0.94** for the year, compared to **1.11** in 2016 and **1.34** in 2015, both years marked by an exceptional intake of large contracts, notably with the booking of 6 major orders<sup>(2)</sup>.

(in € millions)	2017	2016	Total change	Organic change
Aerospace	5,200	5,872	-11%	-11%
Transport	1,780	1,504	+18%	+20%
Defence & Security	7,883	9,063	-13%	-12%
<b>Total – operating segments</b>	<b>14,863</b>	<b>16,439</b>	<b>-10%</b>	<b>-9%</b>
Other	57	75		
<b>TOTAL</b>	<b>14,920</b>	<b>16,514</b>	<b>-10%</b>	<b>-9%</b>
Of which mature markets <sup>(a)</sup>	10,824	10,138	+7%	+7%
Of which emerging markets <sup>(a)</sup>	4,095	6,376	-36%	-35%

(a) Mature markets: Europe, North America, Australia, New Zealand. Emerging markets: all other countries.

The consolidated **order book** remained at a high level: **€31.91 billion** at 31 December 2017, an increase of €7.4 billion (30%) since the launch of Ambition 10 (€24.47 billion at 31 December 2013).

Thales received **19 large orders with a unit value of over €100 million**, representing a total amount of €2,915 million:

- one contract booked in Q1 2017, for the provision of a telecommunications satellite to the Russian operator Gazprom Space System;
- seven large orders booked in Q2 2017:
  - the supply of in-flight entertainment (IFE) systems to a major carrier,
  - the construction for Inmarsat of a very high throughput satellite (V-HTS),

- the operation and maintenance of critical security, information and communication systems at the French Ministry of Defence's new headquarters,
- a contract in the framework of the development and construction of five intermediate-sized frigates (FTIs) for the French Navy,
- Thales's stake in the manufacturing of the first armoured vehicles for the Scorpion programme, for the French Ministry of Defence,
- the supply of AREOS reconnaissance pods to a military customer,
- the delivery of several systems and sensors to an emerging-market Navy;

(1) Taking into account a negative exchange rate effect of €142 million and a net positive scope effect of €5 million, mainly linked to the consolidation of RUAG's opto-electronic business as at 1 January 2017 (Aerospace segment), Vormetric as at 16 March 2016 and Guavus as at 12 September 2017 (Defence & Security segment), off-set by the disposal of the identity management business, effective as at 9 May 2017 (Defence & Security segment).

(2) With a unit value of more than €500 million.

- three large orders booked in Q3 2017:
  - an additional contract in the framework of the development and construction of the intermediate-sized frigates (FTIs) for the French Navy,
  - the notification of an additional contract in the framework of the CONTACT tactical digital communications programme for the French Ministry of Defence,
  - The sale of an integrated air defence system to an Asian country;
- eight large orders booked in Q4 2017:
  - a new tranche of the construction programme for 6 meteorological observation satellites “Meteosat Third Generation”, for ESA and EUMETSAT,
  - the modernisation of the signalling and telecommunication systems for one of the main railways in Egypt,
  - the extension of a signalling project for one of the world’s largest undergrounds,
  - a further contract related to the 36 Rafale fighter aircraft ordered by the Indian government,
  - an operational support contract for the European air defence systems on behalf of OCCAR, to be delivered through the Eurosam joint venture,
  - the support of the “Voyager” air-tanker programme for the United Kingdom’s air force,
  - the second part of the SSOP sensor support contract for the United Kingdom’s Royal Navy,
  - the first tranche of the Aerospace consumables logistics programme for the French armed forces (LORCA programme).

Orders with a unit value of less than €100 million grew by 1% compared to 2016.

From a geographical point of view, order intake was logically down in emerging markets (€4,095 million, -36%), Asia having benefited in 2016 from the order related to Indian Rafale fighter aircraft and the Middle East, of 2 large orders<sup>(1)</sup>. Order intake in mature markets recorded growth (€10,824 million, +7%), driven especially by France (+28%) and the United Kingdom (+15%).

At **€5,200 million** compared to €5,872 million in 2016, order intake in the **Aerospace** segment was down 11%. Avionics, both civil and military, was particularly robust. In-flight entertainment (IFE) maintained a solid commercial performance, in both the fields of traditional multimedia systems and in connectivity. Space order intake was however significantly down, affected by the wait-and-see attitude of telecommunications satellite operators and by a high basis of comparison in the institutional area (observation, exploration, navigation).

Order intake in the **Transport** segment totalled **€1,780 million**, up 18% on 2016, driven by robust growth in both urban and mainline signalling.

At **€7,883 million**, order intake in the **Defence & Security** segment posted a **13%** fall which can be explained by India’s 2016 booking for Rafale fighter aircraft. Excluding this “one-off” item, order intake in this segment was up, benefiting from robust bookings across almost all businesses.

### 1.1.1.4 Sales

(in € millions)	2017	2016	Total change	Organic change
Aerospace	5,985	5,812	+3.0%	+3.6%
Transport	1,761	1,603	+9.9%	+11.2%
Defence & Security	7,983	7,390	+8.0%	+9.4%
<b>Total – operating segments</b>	<b>15,729</b>	<b>14,805</b>	<b>+6.2%</b>	<b>+7.3%</b>
Other	66	80		
<b>TOTAL</b>	<b>15,795</b>	<b>14,885</b>	<b>+6.1%</b>	<b>+7.2%</b>
Of which mature markets <sup>(a)</sup>	10,913	10,395	+5.0%	+5.8%
Of which emerging markets <sup>(a)</sup>	4,882	4,490	+8.7%	+10.3%

(a) Mature markets: Europe, North America, Australia, New Zealand. Emerging markets: all other countries.

**Sales** for 2017 stood at **€15,795 million**, compared to €14,885 million for 2016, up 6.1% on a reported basis, and up **7.2% at constant scope and exchange rates<sup>(2)</sup>** (“organic” change), driven by very good momentum across virtually all segments.

As expected, sales saw a marked acceleration in the fourth quarter (+12.5% on reported basis, +14.8% in organic terms), driven by a weak basis of comparison and by phasing effects between Q3 and Q4 2017.

From a geographical perspective, this good performance reflects both continued strong growth in emerging markets, running at more than 10% for the fourth consecutive year (+10.3%), and increased organic growth in mature markets (+5.8%, after +3.9% in 2016 and +0.5% in 2015). Emerging markets accounted for 31% of Group sales, up from 30% in 2016 and 23% in 2013, the year prior to the launch of Ambition 10.

Sales in the **Aerospace** segment came in at **€5,985 million**, up 3.0% compared to 2016 (up +3.6% at constant scope and currency). The commercial avionics business remained robust, driven in particular by the growth in deliveries of avionic systems to Airbus. In-Flight Entertainment was affected by a high basis of comparison and posted a slight drop in sales as a result. Space sales experienced strong growth, lifted by the ramp-up of contracts signed in 2014 and 2015 in both observation and telecommunications activities. Sales in other segment businesses fell, as the growth in the training and simulation business was insufficient to offset the declining sales of microwave tubes, affected by the slowdown of the global satellite market.

(1) In-flight entertainment systems for Emirates’ future Boeing 777X as well as the signalling systems for the Dubai metro extension.

(2) Taking into account a negative exchange rate effect of €145 million and a net positive scope effect of €2 million, mainly linked to the consolidation of RUAG’s opto-electronic business as at 1 January 2017 (Aerospace segment), Vormetric as at 16 March 2016 and Guavus as at 12 September 2017 (Defence & Security segment), off-set by the disposal of the identity management business, effective as at 9 May 2017 (Defence & Security segment).

In the **Transport** segment, sales totalled **€1,761 million**, up 9.9% compared to 2016 (up +11.2% at constant scope and currency). This growth reflected the progress on the major urban signalling projects won in 2015 and 2016 (Doha, Dubai, Hong Kong, London). The strong rise in sales in the fourth quarter is not representative of the trend in this business activity; it reflects a low basis of comparison and phasing effects between quarters.

Sales in the **Defence & Security** segment were **€7,983 million**, up 8.0% compared to 2016 (up +9.4% at constant scope and currency). Almost all businesses contributed to this momentum. The Land and Air Systems business recorded particularly acute growth in optonics, missile electronics, Air Traffic Management and protected vehicles, with

the ramping-up of the Hawkei vehicle supply contract for the Australian Defence Force. The Defence Mission Systems business posted strong growth for combat aircraft systems, driven by the 3 major Rafale contracts in Egypt, Qatar and India. Despite favourable dynamics in cybersecurity and military network and infrastructure systems, the Secure Information Systems and Communication business posted a more modest growth, especially as several major critical infrastructure protection contracts came to an end.

As expected, sales in the Defence & Security segment recorded strong growth in the fourth quarter (+19.4% based on reported figures, +22.1% on an organic basis), owing to contract phasing effects and a favourable prior-year basis of comparison.

### 1.1.1.5 Adjusted results

#### EBIT

In 2017, consolidated **EBIT<sup>(1)</sup>** was **€1,543 million**, or **9.8%** of sales, compared to €1,354 million (9.1% of revenues) for the same period in 2016. EBIT advanced by 14% based on reported figures, and by 16% on an organic basis. Compared to 2013, the year before the launch of Ambition 10, it is up 53% (+50% on an organic basis).

(in € millions)	2017	2016	Total change	Organic change
<b>Aerospace</b>	<b>601</b>	<b>571</b>	<b>+5%</b>	<b>+7%</b>
<i>In % of sales</i>	<i>10.0%</i>	<i>9.8%</i>	<i>+0.2 pt</i>	<i>+0.3 pt</i>
<b>Transport</b>	<b>72</b>	<b>11</b>	<b>x6.3</b>	<b>x6.3</b>
<i>In % of sales</i>	<i>4.1%</i>	<i>0.7%</i>	<i>+3.4 pt</i>	<i>+3.3 pt</i>
<b>Defence &amp; Security</b>	<b>869</b>	<b>787</b>	<b>+10%</b>	<b>+13%</b>
<i>In % of sales</i>	<i>10.9%</i>	<i>10.7%</i>	<i>+0.2 pt</i>	<i>+0.3 pt</i>
<b>Total – operating segments</b>	<b>1,542</b>	<b>1,370</b>	<b>+13%</b>	<b>+15%</b>
<i>In % of sales</i>	<i>9.8%</i>	<i>9.3%</i>	<i>+0.5 pt</i>	<i>+0.6 pt</i>
Other – excluding Naval Group	(47)	(49)		
<b>Total – excluding Naval Group</b>	<b>1,495</b>	<b>1,321</b>	<b>+13%</b>	<b>+15%</b>
<i>In % of sales</i>	<i>9.5%</i>	<i>8.9%</i>	<i>+0.6 pt</i>	<i>+0.7 pt</i>
Naval Group (35% share)	48	34		
<b>TOTAL</b>	<b>1,543</b>	<b>1,354</b>	<b>+14%</b>	<b>+16%</b>
<i>In % of sales</i>	<i>9.8%</i>	<i>9.1%</i>	<i>+0.7 pt</i>	<i>+0.8 pt</i>

The **Aerospace** segment posted EBIT of **€601 million (10.0%** of sales), versus €571 million (9.8% of sales) in 2016. The EBIT margin rose in particular in the Space and cockpit avionics businesses, even as the Group implemented a sharp upturn in R&D investments. Profitability remained however under pressure within the microwave and imaging systems activities, affected by the slowdown in the global satellite construction market.

EBIT for the **Transport** segment continued to grow sharply, at **€72 million (4.1%** of sales), compared to €11 million (0.7% of sales) in 2016. This improvement is fully in line with the recovery plan that has been implemented since mid-2015, but low or zero margin contracts continued to weigh down on profitability. Ongoing transformation efforts and the gradual phasing-out of low-margin contracts should help this business regain its past profitability levels by 2018/2019.

EBIT for the **Defence & Security** segment was **€869 million (10.9%** of sales), compared to €787 million (10.7% of sales) in 2016. Just as in 2016, the EBIT margin for this segment improved organically by 0.3 points, driven by sales growth, good cost control and a drop in restructuring costs.

**Naval Group's** contribution to EBIT totalled **€48 million** in 2017, compared to €34 million in 2016, buoyed by the improved operating profitability in naval defence (which nevertheless included a few one-time items), partially offset by the depreciation of some assets in renewable marine energies.

**Naval Group's** contribution to EBIT totalled **€48 million** in 2017, compared to €34 million in 2016, the improved operating profitability being partially offset by the depreciation of some assets in renewable marine energies.

#### Adjusted financial result

At **€5 million** in 2017 compared to €6 million in 2016, the amount of **net financial interest** remained low. **Other adjusted financial results (expense)** amounted to a net expense of **-€29 million**, compared to a net expense of -€10 million in 2016, primarily due to a less favourable foreign exchange performance. **Adjusted finance costs on pensions and other employee benefits** remained stable (**-€63 million**, versus -€66 million in 2016), with the rise in pension obligations between 1 January 2016 and 1 January 2017 offset by a decline in discount rates.

(1) Non-GAAP measures, see definitions on pages 8 and 9.

## Adjusted tax expense

**Adjusted tax expense** amounted to a net of -€403 million in 2017 compared to -€314 million in 2016, representing 31.0% of adjusted net income before tax and Thales's share in the net income of equity affiliates. This rise in the effective tax rate can be explained by 3 one-off non-cash items representing a negative amount of €66 million:

- the benefit from the cancellation by France of the 3% tax payable on dividends, which was offset in 2017 by the one-off tax contribution implemented by the government;
- the estimated impact of the French parliament approving a gradual reduction of corporate income tax, which will drop from 34.43% in 2018 to 25.83% in 2022; and
- the estimated impact of the drop in the United States federal tax rate, which moves from 35% to 21% as of 1 January 2018, following the approval of the "Tax Cuts and Jobs Act".

Excluding these 3 one-off items, the effective tax rate would have been 26%, the same rate as in 2016.

## Adjusted net income

**Adjusted net income, Group share<sup>(1)</sup>** totalled **€982 million**, compared to €897 million in 2016, up **9%**.

**Adjusted net income, Group share, per share<sup>(1)</sup>** came out at **€4.64**, also up **9%** on 2016 (€4.25). Without the 3 one-off tax items mentioned above, the adjusted net income, Group share, would have come out at **€4.96**, up **14%** compared to 2016.

## 1.1.1.6 Consolidated results

### Income from operations

**Income from operations** amounted to **€1,258 million** versus €1,097 million in 2016, up around 15%. This increase reflects the improvement in gross margin and great discipline over indirect costs, which were up just 4%. General and administrative expenses increased by 1% from 2016 to 2017.

### Income from operations after share in net income of equity-accounted companies

**Income from operations after share in net income of equity-accounted companies** amounted to **€1,311 million** versus €1,422 million in 2016, down 8%, affected by changes to the "disposal of assets, changes in scope of consolidation and other" line, which had benefited in 2016 from capital gains on the disposal of shareholdings, in Hanwha Thales and Thales-Raytheon Systems LLC. Share in net income of equity affiliates amounted to €135 million, up 12%.

### Net income

**Consolidated net income, Group share**, came out at **€822 million** versus €946 million, down **13%**.

## 1.1.1.7 Financial position at 31 December 2017

At **€1,365 million** versus €954 million in 2016, **free operating cash flow<sup>(1)</sup>** reached a record level, benefiting from the rise in adjusted net income, from a good control of operating investments (€431 million compared to €472 million in 2016) and from a combination of items that improved the change in working capital requirement. The cash conversion rate from adjusted net income into free operating cash flow reached 139%.

The net balance of acquisitions and disposals amounted to -€80 million. It primarily included the net cash outflow of €91 million incurred when finalising the acquisition of Guavus, one of the pioneers in real-time "big data" analytics, and the proceeds from the disposal of the identity management business finalised in May 2017.

At 31 December 2017, **net cash** totalled **€2,971 million** compared to €2,366 million at 31 December 2016, after the distribution of €349 million in dividends (€297 million in 2016).

At **€5,326 million** versus €4,640 million at 31 December 2016, **equity, Group share** was up, driven by the consolidated net income, Group share, a fall in net pension provisions, and a higher valuation of the currency derivatives portfolio.

## 1.1.1.8 Proposed dividend

At the Annual General Meeting on 23 May 2018, the Board of Directors will propose the distribution of a **dividend** of **€1.75** per share, an increase of 9% on 2016.

If approved, the ex-dividend date will be 30 May 2018 and the payment date will be 1 June 2018. The dividend will be paid fully in cash and will amount to € 1.30 per share, after deducting the interim dividend of € 0.45 per share paid in December 2017.

## 1.1.1.9 IFRS 15 implementation

In 2017, the Group continued to work on the implementation of the IFRS 15 standard "Revenue from contracts with customers". This standard, the application of which has been mandatory since 1 January 2018, provides for:

- new criteria to demonstrate the continuous transfer of control of goods to the customer and enable the recognition of revenue over time;
- the unbundling of multiple performance obligations within a single contract;
- measurement of progress towards completion of a contract (or performance obligation for unbundled contracts) based on costs incurred.

With regard to **sales** and **adjusted gross margin**, the differences are primarily due to the change in the percentage-of-completion method for long-term contracts. Currently, contract sales and margins are recognised as and when technical milestones are reached, which attest to the effective stage of completion of a portion of the work or the performance of services provided for in the contract. Under IFRS 15, the percentage-of-completion method used is the cost-to-cost method, whereby revenue is recognised based on costs incurred at a given date divided by total costs expected at completion. For each contract, depending on the stage of completion and the type of milestones reached and costs incurred during the period, this change of method may lead to the recognition of revenue and margins being deferred from one period to another.

To a lesser degree, these differences are due to certain contracts being unbundled into performance obligations with differentiated margins (particularly for contracts combining construction and operation, or the construction and launch of a satellite), which may also lead to the deferral of the recognition of revenue and margins.

Finally, the impact of the requalification of contracts no longer fulfilling over time recognition criteria is very limited. A detailed analysis of the contract portfolio found that this requalification, which could have generated very significant deferrals in the recognition of revenue and margins if it had applied to a large number of contracts, only concerns a small number, the total revenue of which represents less than 1% of the order book at 31 December 2016.

(1) Non-GAAP measures, see definitions pages 8 and 9.

Had this standard been applicable as of 1st January 2017, these impacts taken together would have led to a negative restatement of €568 million on **2017 sales**, and of €133 million on **2017 adjusted gross margin**, which would in turn amount to 24.4% of sales (+0.0 points). As the new standard affects neither the total revenue nor the overall profitability of each contract, this restatement corresponds solely to timing differences.

The impact of the standard on **2017 adjusted indirect costs** would have amounted to -€29 million, corresponding solely to the derecognition of bid costs from costs at completion and their subsequent recognition under indirect costs for the period.

The impact on the 2017 **share in net income of equity affiliates** would have been negative by €15 million, exclusively linked to Naval Group.

As a result, **restated 2017 EBIT** would have been €1,365 million, €177 million lower than the EBIT reported for the same period. The fall in **EBIT margin** (9.0% under IFRS 15 versus 9.8% under current standards) corresponds primarily to the negative operating leverage due to lower sales, with the gross margin remaining stable in percentage, and indirect costs virtually unchanged by the standard.

These amounts reflect the impact on the aggregate sales and margin of several thousand contracts; they are not representative of the standard's impact on the financial statements of future periods.

After restatement, the **adjusted net income, Group share** would have amounted to €840 million, €142 million lower than the reported amount, reflecting the shifts in the timing of sales recognition resulting from the new standard.

The application of the standard would have had a similar negative impact, €142 million, on the **consolidated net income, Group share**.

## ➤ RESTATED KEY 2017 FIGURES

2017	Restated for IFRS 15	Reported	Difference	
			€m	%
(in € millions, except earnings per share (in €))				
Order intake	14,931	14,920	+12	+0%
Order book at end of period	32,064	31,914	+150	+0%
Sales	15,228	15,795	(568)	-4%
Adjusted gross margin <sup>(a)</sup> In % of sales	3,711 24.4%	3,845 24.3%	(133)	-3% +0.0 pt
Adjusted indirect costs <sup>(a)</sup>	(2,404)	(2,375)	(29)	+1%
Restructuring costs	(81)	(81)	-	+0%
Share in net income of equity affiliates	139	154	(15)	-10%
EBIT <sup>(a)</sup> In % of sales	1,365 9.0%	1,543 9.8%	(177)	-11% -0.8 pt
Adjusted net income, Group share <sup>(a)</sup>	840	982	(142)	-14%
Adjusted net income, Group share, per share <sup>(a)</sup>	3.97	4.64	(0.67)	-14%
Consolidated net income, Group share	680	822	(142)	-17%
Free operating cash flow <sup>(a)</sup>	1,365	1,365	0	+0%

(a) Non-GAAP measures, see definitions on pages 8 and 9.

## ➤ RESTATED 2017 SALES AND EBIT BY OPERATING SEGMENT

2017	Restated for IFRS 15			Reported			Difference		
	Sales	EBIT	EBIT margin	Sales	EBIT	EBIT margin	Sales	EBIT	EBIT margin
(in € millions)									
Aerospace	5,747	567	9.9%	5,985	602	10.0%	-4%	-6%	-0.1 pt
Transport	1,723	57	3.3%	1,761	72	4.1%	-2%	-21%	-0.8 pt
Defence & Security	7,690	757	9.8%	7,983	869	10.9%	-4%	-13%	-1.1 pt
<b>Total – operating segments</b>	<b>15,160</b>	<b>1,380</b>	<b>9.1%</b>	<b>15,729</b>	<b>1,542</b>	<b>9.8%</b>	<b>-4%</b>	<b>-10%</b>	<b>-0.7 pt</b>
Other	67	-15		66	1				-
<b>TOTAL</b>	<b>15,228</b>	<b>1,365</b>	<b>9.0%</b>	<b>15,795</b>	<b>1,543</b>	<b>9.8%</b>	<b>-4%</b>	<b>-11%</b>	<b>-0.8 PT</b>

### 1.1.1.10 Update on the projected Gemalto acquisition

On 17 December 2017, Thales and Gemalto (Euronext Amsterdam and Paris: GTO) announced the signing of a merger agreement including an all-cash offer for all issued and outstanding ordinary shares of Gemalto, for a price of €51 per share cum dividend<sup>(1)</sup>. This offer was unanimously recommended by Gemalto's Board of Directors.

Preparations for this offer are proceeding as planned. The draft offer document is under review by the Dutch Financial Markets Authority (AFM). The process of obtaining the necessary regulatory authorisations is also underway. The transaction is expected to close shortly after all of the usual regulatory approvals have been secured, which is expected in the second half of 2018.

All charges directly related to this transaction will be excluded from the 2018 EBIT and adjusted net income.

### 1.1.1.11 2018 Outlook

As of 1 January 2018, the Group applies the IFRS 15 standard "Revenue from contracts with customers". To provide a basis for understanding the 2018 financial targets, the 2017 results restated for the application of this standard are presented on page 16.

In 2018, Thales should continue to benefit from positive trends in the majority of its markets. The acceleration of the commercial momentum in

the defence businesses should offset the slowdown of the telecom satellite market. In this context, 2018 order intake is expected to be around €15.5 billion.

In spite of a more moderate growth in the Aerospace segment, sales should see an organic growth of between 4 and 5% compared to 2017 sales restated for the application of the IFRS 15 standard (€15,228 million).

The Group will continue to significantly increase its R&D investments, particularly in digital technologies. The self-funded R&D expenses should therefore increase by around 10% compared to 2017.

The growth in sales, combined with the impact of the Ambition 10 strategy on product competitiveness and differentiation, should result in Thales delivering an EBIT of between €1,620 and €1,660 million in 2018 (based on February 2018 scope and exchange rates), representing an increase of 19% to 22% compared to 2017 EBIT restated for the application of the IFRS 15 standard (€1,365 million).

Therefore, the Group expects to exceed its two mid-term objectives: the average organic sales growth in the 2016-2018 period should be over 5%, and the 2018 EBIT margin should be above the top end of the range set in April 2014 (9.5% to 10% in 2017/2018).

This outlook does not take into account the projected acquisition of Gemalto. The Group may need to update its outlook depending on the effective conclusion date of this transaction.

The Group will provide a detailed update on its strategy and set medium-term financial targets at a Capital Markets Day to be held on 6th June 2018, at its Gennevilliers site, in the Paris area.

## 1.1.2 Risk factors

Thales is exposed to numerous risks and uncertainties which could materially affect its business, reputation, financial position, results or ability to achieve its objectives. The risks described below are not the only ones that Thales faces. Other risks, currently unknown to Thales, or which presently appear to be non-significant, could also have an unfavourable impact on the business, profitability and financial position of the Group or its ability to achieve its objectives.

Generally, Thales may be faced with a number of operational and strategic risks (Section 1.1.2.1), legal and compliance risks (Section 1.1.2.2) and financial risks (Section 1.1.2.3).

See also Section 1.1.3 "Internal control and risk management".

### 1.1.2.1 Operational and strategic risks

#### 1.1.2.1.1 Control of bids and projects

Many of Thales's products and systems are highly complex due to their advanced technology content, the rigorous operational constraints and harsh environments in which they operate (which require them to be extremely reliable), and the contractual arrangements surrounding their sale (comprehensive prime contractorships for large-scale systems, public-private partnerships or their equivalent, local shares, compensation commitments (see Section 1.1.2.1.10), etc.).

The actual cost of development and manufacture may therefore exceed initial cost estimates, which in turn may adversely impact Thales's results and financial position, especially considering that the associated contracts are generally based on a fixed, all-inclusive price. In addition, many contracts include stringent performance levels and/or tight delivery schedules for the products or systems sold, particularly given the strong competition. If Thales is unable to deliver these products or systems in line with the required level of performance and/or delivery schedule, customers may demand penalty payments or even decide to terminate the contract.

Bid and project management is therefore subject to a detailed risk assessment and management process. Thales ranks the various levels of criticality. Critical bids and projects are specifically monitored at the management level of the operating entities (Business Lines and Global Business Units) and, as needed, by Group management.

Contractual risk assessment is an integral part of the tendering process. Depending on the complexity of the bid, this procedure involves a number of steps which progressively sharpen the estimated level of profitability and the associated risks to be assessed.

Numerous Thales contracts, particularly those that involve the most complex products and services, run for several years. Their economic contribution to the Group's result over a given period is therefore assessed, in accordance with applicable accounting standards, based on an estimate of their cost to completion.

These assessments can result in uncertainties that require subsequent correction despite the careful attention that is paid to estimates for each project through regular reviews to measure the technical, contractual and financial progress made.

<sup>(1)</sup> Valuing the equity capital of Gemalto at approximately €4.8 billion.

The Group pays special attention to analyses and action plans for efficiently managing bids and projects by measuring and monitoring financial variance on the projects as well as appropriately applying corrective actions.

As part of the Ambition Boost performance programme (see also Section 1.1.2.1.8 “Risk of lower impact of performance improvement measures”), the Group has also implemented action plans to improve the management of bids and projects, engineering and the supply chain. These actions aim in particular to:

- improve product policy and ensure it is better adapted to customer needs in order to streamline new developments and thus reduce risks;
- improve the management of commitments in both the bidding phase and the project phase, with the widespread use of independent peer reviews, closer involvement of Engineering, Purchasing, Production, Legal and Quality Control, and the introduction of Product and Project Design Authorities responsible for developing the technical solutions for products and projects (during the bid or project implementation phase);
- Improve the supply chain, by increasing its global dimension and enhance the increasing maturity of emerging countries in project implementation;
- improve methods, practices and tools to make them more relevant to international products/projects, in particular, through the implementation of a project management tool adapted to emerging countries, SAP by Design;
- introduce advanced training for project managers to obtain certification issued jointly with the International Project Management Association (IPMA). At the end of 2017, nearly 1,353 bid and project managers and project management officers (PMO) within the Group had gained IPMA certification, with approximately 187 certified during the year. The role of these project managers will be further increased within the PMO organizations and teams.

### 1.1.2.1.2 Supplier risk

Purchases constitute a very significant proportion of Thales’s business, representing nearly half its sales with purchases ranging from industrials to services, equipment and sub-systems. Thales is therefore exposed to the risk of the industrial, technical or financial default of any of its suppliers, which could affect its performance and, hence, profitability.

There are two major types of supplier risk:

- legal or regulatory non-compliance (ethics, export control, intellectual property, etc.); each of these risks is handled by the departments concerned using the Group Risk Management system with the support of the Purchasing department;
- structural and operational risks that could disrupt supply, which are dealt with in the Purchasing department using the Group Risk Management system. The Purchasing department has identified two key triggers: supplier default and economic dependence.

#### Risk of supplier default

Supplier default could be caused by a major incident at one of its sites, by its external environment (shortage of raw materials or components, major political instability, natural disasters, etc.) or through mismanagement. The supplier’s management performance is monitored both in operating terms (poor procurement planning, failure to manage tier 2 suppliers, loss of control over industrial processes, plant obsolescence, etc.) and in cross-disciplinary and financial terms (poor skills management, loss of know-how, fall in sales, mismanagement of working capital requirement, cash flow problems, administration or bankruptcy protection, etc.). A combination of problems could lead to

the disappearance of a company or its takeover by investors with different interests from those of Thales.

Faced with this risk of a supply shortage, Thales implements a dual sourcing (or alternative-source) policy as frequently as possible for each technology family, regularly updated and accompanied by buffer inventories that cover its requirements until customer contracts have been fulfilled.

In addition, given the increased risk of fragility of certain suppliers in the current economic climate, Thales has introduced a special approach. Based on close cooperation between buyers and financial teams, this is aimed at identifying, from among its critical suppliers, those that would be particularly susceptible financially and implementing appropriate action plans to ensure continuity of supply. Apart from individual monitoring, an analysis is also carried out by technology field in conjunction with the professional bodies concerned, to identify the most appropriate solutions.

Alongside these financial supervision measures, Purchasing and Quality Control have stepped up their appraisal, accreditation and management of supplier performance to better identify structural risks. Supplier performance audits are broad-based (covering quality control, industrial maturity, flow optimisation, compliance with environmental regulations, expertise in technical and technological processes, financial strength, etc.) and therefore allow a complete risk analysis to be carried out. When performing a purchasing contract, Thales closely monitors the implementation by the supplier of measures aimed at addressing the risks identified during the selection process.

#### Risk of economic dependence

The economic dependence of small and medium-sized enterprises (SMEs) towards Thales is considered a risk in its own right.

In order to mitigate this risk, the commitment rate (orders placed by Thales as a percentage of the supplier’s annual sales) is measured for each panel of suppliers by market segment (vertical approach) and for the main countries where the Group is established (France, the UK, the Netherlands, etc.).

If the commitment rate exceeds 50% for more than two consecutive years, an action plan coordinated with internal specifiers and internal users is created in order to return to a commitment rate of 25%.

The purchasing policy, supplier selection and performance monitoring processes, and the supplier monitoring systems are designed to reduce these risks, during both the bidding phase and the project implementation phase.

### 1.1.2.1.3 Human resources risk

#### a) Workplace health and safety

One of the Group’s key priorities is to provide a safe and healthy work environment for all employees, in compliance with applicable law, by monitoring procedures, preventing health and occupational risks and training employees.

These principles are reflected in a structure designed to prevent risks related to health and safety in the workplace, whether on Thales sites or external sites, and to manage major health crises that could occur internationally.

Regular monitoring of the risks to which the Group’s employees may be exposed is performed each year.

Tangible measures are also implemented in relation to the prevention of risks related to the health and safety of employees in the workplace by the Group’s Human Resources and Health, Safety and Environment Departments. For many years, Thales has also been committed to improving the quality of life in the workplace. In France, a third Group

agreement on “quality of life in the workplace” is under negotiation to increase the Group’s commitments and actions relating specifically to protecting the health of employees, improving well-being at work, preventing psychosocial risk situations and the right to disconnect to ensure a good work-life balance.

Proof of the Group’s continuing commitment to certification, 107 Thales entities (representing 82% of the workforce) had obtained OHSAS 18001 certification by the end of 2017.

## b) Talent development

If Thales is not attractive enough compared to its competitors to recruit the qualified staff it needs in a timely manner and to retain and motivate its employees, sales and operating profitability could be negatively affected.

Thales’s success and performance effectively depend on:

- its capacity to recruit employees in the different employment markets, in France and abroad;
- the quality of the key skills and the commitment of its employees; and
- its capacity to globally manage the talent required for the development of its activity worldwide.

Thales therefore attaches great importance to its attractiveness and positioning as a top employer, ensuring a positive external image which will boost recruitment and an internal work environment that will contribute to retaining employees.

As an attractive and recognised employer in France, Thales is also building up its image in all the countries where the Group is already present and in the countries in which Thales plans to expand, notably through communication campaigns and partnerships with leading universities. In addition, a global recruitment role, reporting to the corporate HR department has been created to help the Group expand in these geographical zones.

Thales works constantly to support its employer brand. The Group recently updated its brochures, booths, posters, web visuals and all other communication materials used at the various recruitment events worldwide and on Thales’s social media pages. The Group currently has more than 230,000 followers on LinkedIn.

Thales has also developed innovative initiatives to attract rare skills in fields such as in electronics and cyber-security, by organising challenges for students and young engineers such as cyber-security week and the Arduino project, a university competition held in 10 countries. This project gives more than 100 teams of young engineers the opportunity to develop innovative projects on subjects defined by the Group. These events give young engineers from across the world an insight into the Group and its business activities.

In recent years, Thales has also contributed to the integration of young people into business through the signature of close to 1,500 work-study contracts each year. Thales maintains active relations with schools and universities in all the countries where it intends to increase its presence. Many partnerships have been signed with these schools, which employees sometimes visit to provide training. Thales also has a presence on campuses through young employees who are alumni of these schools, and form a network of contacts. In France, Thales is regularly recognised as one of the top three companies by students of engineering schools.

The global process of identifying and developing talent within the Group has also been reinforced by encouraging interaction between management teams in different parts of the organisation.

Thales is also continuing its proactive skills management policy for the Group’s main professional families. A Steering Committee per family, composed of operational and HR managers, conducts a yearly analysis

of changes in jobs, expertise, and the needs of the Company, and creates action plans (for training, anticipated management of internal mobility, external recruitment, etc.). To complement this tool, each year the Group’s internal university updates key training programmes in response to changing needs. Significant work was carried out from 2014 to 2016 to pinpoint employee soft skills, namely for those employees reporting to the R&D Systems, R&D Hardware, R&D Software, Purchasing and Project Management job families. This work helps to more precisely identify training and recruitment requirements. In July 2017, Thales University, renamed Learning Hub, was completely overhauled to adapt its training tools to the digital era and to better integrate the training into employees’ professional life.

Lastly, in 2013, the Group signed a series of agreements with the unanimous support of the trade union organisations in France that encourage the integration of young people, either on work-study training schemes or post-qualification, and the transfer of knowledge (the Intergenerational Agreement); that develop diversity (the Gender Equality Agreement); and that take a forward-looking approach to jobs and skills. In 2017, the number of young people on work-study contracts in Thales’s workforce in France represented close to 5%, in line with the agreement signed in 2013.

## 1.1.2.1.4 Environmental risks

For many years, Thales has conducted a regular analysis and update of environmental risks in accordance with its business activities, scientific and technical developments as well as with current regulatory change.

This analysis is aimed at:

- regularly ensuring that employees and neighbouring residents are not exposed to health and environmental risks (hazardous substances, pollution, asbestos, etc.) through their activities or work environment, whether on Thales or external sites;
- ensuring the compliance of activities and products used and/or marketed (substances, waste, etc.);
- analysing the impact of new regulations (e.g. REACH in Europe) on the supply chain and on product design;
- analysing the impact of the environment on activities (water stress, climatic events, etc.);
- identifying an appropriate organisational structure and associated action plans, either at Group level or locally, based on the results of this analysis to reduce and manage the associated risks.

To support this analysis, an environmental management system designed to ensure control and limitation of the environmental impacts of activities and products is implemented on all sites. This management system, which forms an integral part of the Group’s framework, encompasses the different functions of the Group (engineering, manufacturing, supply chain, etc.) and is based on frameworks, special training, communication tools and sharing experience.

At the end of 2017, 124 entities had been ISO 14001 certified, representing 89% of the Group’s workforce, 33 had been ISO 50001 certified, representing 26% of the Group’s workforce and 107 had been OHSAS 18001 certified, representing 82% of the Group’s workforce.

Thales also regularly assesses the risks linked to climate change in order to evaluate their impact on activity and costs. The main risks identified are:

- regulatory change (reporting, carbon taxes, etc.) which has a very limited impact for Thales (not affected by the EU Emissions Trading Scheme). Nevertheless, Thales closely monitors current and future laws and regulations in order to analyse and anticipate their impact and set in place the requisite measures;

- changes in the regulations on substances and products (REACH in Europe and elsewhere in the world) in order to anticipate obsolescence issues to secure its supplies, reduce and control the impacts on the products and services it delivers through the required avoidance and replacement measures; but also to control the risks related to the handling of hazardous substances, for both people and the natural environment;
- financial risks related to the effects of climate change (floods, hurricanes, fires, water stress, etc.) that can result in damages and a continuous disruption in activity at Thales sites as well as the sites of its subcontractors and partners.

To manage this risk and reduce its vulnerability, Thales has carried out regular assessments of the exposure of its different sites to natural disasters and their consequences for several years now. Action plans linked to these assessments have been defined in order to attenuate this risk (see Section 5.2.4), and the Group's insurance policy (see Section 1.1.2.4 "Insurance") is also based on these assessments;

- risks related to water shortages. The majority of Group sites in vulnerable areas are offices that have very limited risk exposure given their low water consumption.

An analysis of "natural disaster" and "water stress" risks is now included in the regular prevention visits at Thales' sites and those of our critical subcontractors and suppliers;

- image risk: any failure by Thales to implement adequate measures in the fight against climate change could have a specific negative impact on its corporate image. Thales publishes information on the measures it has put in place to combat climate change and the results it obtains (see also Section 5.2.4) for its stakeholders (customers, investors, civil society, etc.). In 2017, it was awarded a rating of A- for "climate change" in the CDP (Carbon Disclosure Project), placing it in the top 20% of best-performing companies listed. In keeping with the commitments made in 2015, in December 2017 Thales signed the Paris "French Business Pledge"<sup>(1)</sup>.

At 31 December 2017, provisions for environmental risks amounted to €5.7 million.

#### 1.1.2.1.5 Security breaches in respect of sites and employees

Thales is exposed to attempts to breach the security of its sites: attempts by unauthorised persons to access confidential information, cyber-attacks, threats to the physical security of facilities and persons, etc. The occurrence of such events could affect the Group's intellectual, economic or human capital, the rollout of the Group's activities and its reputation and, consequently, its results and financial position.

In order to minimise these risk, the Group Security department has put in place a policy for regulating access to and movement around all sites. This policy, applied by the Group's network of security officers, is in keeping with the Group's defence businesses and the different national regulations requiring it to implement measures to protect its employees and industrial assets. The Group is therefore required to undergo a large number of audits and inspections by the national supervisory authorities.

It has also implemented a global procedure for employee safety and protection in all of the countries in which they perform their work. In certain countries, this global procedure runs alongside a local intervention system, which ensures a quick response to incidents.

Faced with the current heightened terrorist threat, the Group has increased the level of security and protection for its most sensitive sites.

Finally, in close collaboration with the other major functions concerned, the Group Security department is working to improve crisis management processes, put in place rules and define a policy to raise awareness on information protection.

#### 1.1.2.1.6 Risk of IT system failure

The Group operates – whether directly or through service providers – complex IT systems and infrastructures that are essential to the smooth running of its commercial, industrial and financial processes. These information systems include management, development and engineering systems as well as platforms operated on behalf of our customers and must be protected against any malfunctions, natural disasters, malicious acts or human error at all costs. The malfunction or failure of these systems may have external causes (viruses or hacking, network failures, natural disasters, etc.) or internal causes (malicious acts, breaches of data confidentiality, human error or obsolescence). Any such malfunction or failure can have an impact on the Group's operations and its financial results.

To guard against these risks, the Group has implemented multi-year plans to develop its protection measures in order to deal with part of its IT systems being temporarily or permanently unavailable, as well as any cyber-security threats to these systems.

#### Business continuity

A Disaster Recovery Plan is adapted to the different countries to deal with failures of part of Thales's IT systems; a methodology to prevent the risk of a failure of the Group's IT systems is applied to ensure disaster recovery solutions are adapted to the degree of the risk and its operational impact. The plan is based on an analysis of the criticality of the different services given their impact on the Group's operations and undergoes regular test runs.

#### Cybersecurity

A plan to protect against risks related to cyber-security has been defined and implemented in countries where the Group currently operates. As well as adapting the means of protection already in place, the plan includes the introduction of new measures to heighten protection against cyber sabotage attacks (e.g. Wannacry) to identify and correct any non-compliance. It is adapted to new regulations (military programming law in France, general regulations on data protection) and to technological developments (e.g. cloud computing).

This plan also includes the implementation of "CyberSecurity Operation Centres" coordinated at global level, so that anomalies and incidents that could affect the security of systems are identified as early as possible and the appropriate solutions put in place. These measures for monitoring and sharing information in relation to vectors of attack were further developed throughout 2017.

A number of "Key rules" on the security of Thales's information systems ensure the convergence and coherence of cyber-security and defence measures throughout the Group. Their effective application is regularly monitored and reporting submitted to the Group Information Systems Security department.

#### Awareness and know-how

The plan is completed by ongoing efforts to raise employee awareness of these threats: communication campaigns and training are rolled out to help users ensure the security of their IT systems and remind them of the best practices when using them. Regular forums for discussion attended by all employees are also held on site. Since 2017 new employees have also been made aware of cyber security issues.

<sup>(1)</sup> French Business Pledge: on the eve of the One Planet Summit on 12 December 2017, 91 French companies of all sizes and from all sectors announced the signature of a shared commitment to climate. Each of these companies put forward its actions as a committed player in the fight against global warming.

### 1.1.2.1.7 Risk related to failure of equipment or technology

Thales systems and equipment are highly complex and technical and are likely to be integrated within high-value commercial or military platforms. A malfunction of any such systems, equipment or technologies could result in client claims or third-party litigation. Thales could therefore be held liable, notably in the event of damage to property or personal injury, or in the event that they result in a disruption in the business and activities of its customers. Were they to occur, such events would be liable to impact Thales's results and financial position, as well as its reputation.

In order to limit the impact, Thales has put Group-wide standards in place (Design Authority, quality, documentation, contractual arrangements and risk management). In addition, Thales follows a policy of maintaining appropriate insurance coverage (see Section 1.1.2.4 "Insurance").

### 1.1.2.1.8 Risk of lower impact of performance improvement measures

In 2014, to support its medium-term financial targets, Thales launched the "Ambition Boost" performance plan to increase the entire Group's performance.

This global performance plan provides a common framework within which the units can implement plans and initiatives adapted to their own issues in terms of performance improvements. Five new cross-disciplinary initiatives are also now in place to complete and strengthen the performance plans: Going Global, Digital Transformation, Competitiveness, Diversity & Inclusion and Leadership & Governance.

The earnings and financial position of Thales could be negatively impacted if the initiatives planned under the Ambition Boost framework could not be fully implemented or if they failed to generate the expected results according to the original timetable. Moreover, the cost of implementing these initiatives could end up being higher than expected.

Thales has introduced specific monitoring for performance improvement initiatives and the Group's corporate management regularly reviews the progress of the main initiatives.

### 1.1.2.1.9 Competitive environment

Thales operates in highly competitive markets, both in terms of international groups and in terms of local or niche companies in certain market segments. This competitive pressure could negatively impact Thales's commercial position, sales and profits.

It could also intensify in a less favourable economic environment and there is no guarantee that Thales will be able to position itself successfully against its current or future competitors.

In order to limit the impact of this risk, Thales continues its research and development investments in order to provide more competitive and differentiating elements, and it also works to structure and upgrade its product offer in order to always best meet the needs of its customers in both the defence and commercial markets.

The Group's success and performance in relation to its competitors also depends on its capacity to recruit and retain quality employees with the requisite skills and commitment. Thales therefore attaches great importance to its attractiveness and positioning as a top employer, ensuring a positive external image which will boost recruitment and an internal work environment that will help retain employees (see Section 1.1.2.1.3-b) "Talent development").

### 1.1.2.1.10 Offsets

In some countries, the awarding of major contracts, particularly defence contracts, may be dependent on a legal or regulatory requirement to fulfil a direct, semi-direct or indirect offset requirement. The Group's ability to factor this into a proposal can be a major source of differentiation and, as such, have a decisive impact on its commercial success or failure.

The non-fulfilment of contractual offset obligations within the requisite deadlines can result in penalties, the payment of which does not always release the obligor from its obligations. It can also compromise the Group's capacity to expand its activities in a given country.

Thales's order intake in recent years (particularly the order for the Rafale fighter aircraft placed by the Indian authorities in the third quarter of 2016) has led to a substantial increase in its offset obligations.

Faced with these risks, Thales has set in place a dedicated structure, both at a central level and for its exporting units and destination countries, which is responsible for integrating and overseeing these obligations as early as the bid phase. The Group also has a specific unit that is entirely devoted to the management of indirect offsets, Thales International Offsets (TIO).

### 1.1.2.1.11 Market trends

The markets on which Thales operates are broadly correlated to the current economic backdrop, but can also be impacted by specific factors: technological breakthroughs, the impact of digitalisation, drastic changes in Business Models, deregulation, new standards, real or perceived increase in the threat of terrorism, changes in oil prices, conflicts or major political change, epidemics and disasters that could have an impact, however temporary, on these markets. This is particularly true of the civil aviation market.

As part of the development of its activities related to in-flight broadband, Thales entered into a strategic agreement with SES in 2016 to secure bandwidth over the Americas. Under this agreement, Thales committed to an annual bandwidth purchasing programme over the 2016 to 2028 period and the payment to SES of a set minimum fee. The profitability of this business could therefore be affected if the sale of the broadband services was lower than forecast for several consecutive years.

The main risk mitigation factors are Thales' efforts to bolster and promote the offer to airlines and the flexibility built into the agreement.

In the space sector, the telecommunications satellite market is affected by constant technological developments resulting in a decrease in the Megabyte transmission cost. Some operators face complex technological challenges which force them to postpone their investments. In particular, uncertainties remain in the articulation between new constellation models and the more traditional satellites in high orbit which are becoming increasingly technologically advanced, allowing for the development of higher capacity solutions. Thales is developing its offer and investing in breakthrough technologies to embrace these developments.

More generally, to limit the impact of market risk, Thales constantly seeks (i) to adapt its product lines to foreseeable changes in demand and to improve their competitive performance and industrial flexibility in line with fluctuations in activity, and (ii) a comprehensive strategy to balance its business portfolio.

### 1.1.2.1.12 Dependence on public procurement

Thales generates a significant share of its business from governments, particularly in the defence markets in many countries. In these markets, public spending is dependent on political and economic factors and is therefore likely to fluctuate from one year to the next. A reduction in the budget resources of government customers could, for example, generate delays in order booking, contract execution and payments, or mean a cut in funding for research and development programmes.

Thales has based its strategy on a balanced portfolio of defence operations and civil operations, each accounting for approximately 50% of sales. The overall solidity of the portfolio is underpinned by a diversified order base with a unit value of less than €100 million. Finally, the broad geographic spread of Thales's business, particularly through its international operations, ensures further diversification of its customer base.

### 1.1.2.1.13 Political risks

A significant proportion of Thales's sales is subject to the risk of economic and/or political instability in the countries in which the Group operates. The materialisation of these risks may affect the Group's financial position and profitability.

In particular, a change in government, major political event, armed conflict, act of terrorism, sharp deterioration in the balance of payments, industrial action, strike or protest could lead to various types of risks. These include:

- more restrictive currency control, with limitations or exclusions on withdrawing currency from a customer country, preventing it from honouring its financial commitments to Thales;
- impairment of assets because of devaluations of the local currency or other measures taken by public authorities that significantly affect the value of operations;
- expropriation (by confiscation, nationalisation, requisition, etc.) or the forced sale of Thales' interest in a local company, or, more broadly, discriminatory measures that compromise Thales's operations in a country;
- a security situation entailing a risk of bodily harm for its employees and/or security breaches at its facilities, which severely limit or prevent Thales from assuming its performance obligations under a contract, or reduce or prohibit the use of its local industrial assets;
- an unexpected breach of a contract or commitment;
- an unfair call of a bond or a guarantee;
- the non-certification of documents eligible for payment, or non-payment on the due dates stipulated in a contract, that prevent the anticipated progress of that contract.

To limit the financial impact of the risks listed above, Thales has put in place a methodology to identify and analyse the risks, determine measures to reduce them and define roles and responsibilities, within Thales, for the teams involved in the financial engineering of contracts. This enables Thales to use public or private insurers to cover the risk of contract interruption, credit risk or the risk of unfair calling of sureties. It can also make use of financial instruments such as notified or confirmed letters of credit, receivables discounting without recourse or export credit facilities.

In June 2016, by referendum, the United Kingdom, which represents approximately 9% of Group sales and 6,400 employees, voted to leave the European Union. This decision could have a number of

consequences on the activities and financial performance of Thales. It could notably lead to a higher degree of volatility between the pound sterling and the euro, in interest rates and in the value of plan assets covering the Group's pension commitments in the United Kingdom. The management of these financial risks is part of the procedures set in place by the Group and described in Section 1.1.2.3 "Financial risks". The risk of an increase in tariff barriers is automatically reduced by Thales's predominant use of local country production resources a strategy which also tends to reduce the effects of greater volatility in the pound since sales and production costs are essentially denominated in the same currency.

### 1.1.2.1.14 Risks relating to strategic acquisitions and investments

Thales regularly looks to acquire new companies (as well as making strategic investments and combining business activities through joint ventures, etc.) in order to round out its technological portfolio and strengthen its presence in certain markets. Integrating these businesses into Thales could prove more difficult and take longer than envisaged, requiring more significant involvement by senior managers and the teams concerned and, in turn, negatively impacting the Group's results and financial position.

In addition, there are no guarantees that the newly acquired companies will perform as well as expected in accordance with the assumptions which form the basis of their valuation and the investment decision. Significant variance could lead to the amortisation of goodwill and other intangible assets, thereby negatively impacting Thales's results and financial position.

In addition, the integration of a newly acquired company into the Group may prove difficult or fail to generate all the expected synergies and other benefits. Such events could have a negative impact on the Group's results.

The significance of these risks and their impact varies depending on the target company's size.

Before any planned acquisitions, Thales conducts audits and due diligence with the assistance of external consultants where necessary, in order to analyse the fundamentals of the target company. This due diligence is more limited when the target company is listed, due to the applicable regulations.

A review is also conducted at each key stage in the acquisition process to confirm Thales's interest and set the necessary conditions and parameters to ensure a successful outcome. The newly acquired company is then integrated into Thales's financial reporting system so that its performance can be monitored.

An internal audit is carried out for all major acquisitions within 18 months of the finalisation of the acquisition. These audits assess the strength of the business plans that led to the decision, the integration of the newly acquired company into the Group, the implementation of synergies and the level of performance in relation to the assumptions made. The audit reports are sent to the Group's corporate management and are summarised for the Audit and Accounts Committee.

### 1.1.2.1.15 Risks related to minority investments

Thales generates part of its sales from companies in which control is shared with, or exercised by, other partners; in accordance with the accounting principles in force on 1 January 2017, these companies are consolidated using the equity method<sup>(1)</sup>.

(1) See the list of companies accounted for under the equity method on pages 79 and 80.

By definition, the share in net income of equity-accounted companies is included in Thales's EBIT<sup>(1)</sup> and adjusted net income<sup>(1)</sup>. A deterioration in the performance of these companies may therefore impact on the Group's income, financial position and achievement of EBIT objectives.

Since Thales's influence over these minority investments varies, decisions that are detrimental to the interests of Thales may be taken, without Thales necessarily having the means to oppose them.

In addition, the risk of disagreement or deadlock, inherent in any jointly-controlled entity, exists, particularly in those where important decisions require the unanimity of members or where there are limited exit rights.

Lastly, the application of management rules and principles in these entities may differ from those adopted by Thales for entities over which it exerts exclusive control. This also means that the ability to carry out analyses and give instructions regarding financial or operational data, or even to access this data, may be more limited than in the entities over which Thales exerts exclusive control.

As a result, the Group aims to define appropriate governance methods by seeking to be represented on the Board of Directors (or a similar decision-making body), and more generally, to negotiate contractual provisions that are in Thales's best interests.

## 1.1.2.2 Legal and compliance risks

### 1.1.2.2.1 Compliance with laws and regulations

The Group operates its business, both nationally and internationally, in a strict and evolving complex legal and regulatory environment. This environment encompasses various fields such as company law, stock exchange law, tax law, employment law, intellectual property, personal data protection, export control, economic sanction measures, anti-corruption, influence peddling and money laundering.

Despite the steps taken by Thales in the form of organisation and internal procedures to comply with all applicable legislation, risks still exist due to their inherent nature, the interpretative powers of regulatory agents, the extraterritorial REACH of certain regulations, and changes in legal/judicial precedent and sanctioning powers.

In most cases, regulators in conjunction with the judicial authorities have the right to initiate legal proceedings, which could expose the Group or its employees to civil, administrative or criminal rulings. Such rulings could, if applicable, involve a temporary ban on trading, which would in turn have an adverse impact on the Group's profitability and financial position.

Using a risk map approved by the Risk Management Committee, the Audit, Risks & Internal Control Department carries out assessments and audits of the implementation and improvement of compliance plans within the Group's units. Compliance measures rely for these needs on networks of compliance officers who may be specialists (in Trade Compliance, international trade, etc.) and on risk advisors responsible for the prevention of each of the major risks identified and monitored by the Risk Assessment Committee.

The Audit, Risks & Internal Control Department takes into account these compliance areas when preparing its audit plan.

### a) Business ethics

Thales's business encompasses a variety of sectors in more than 50 countries. Infringement of applicable laws and regulations may have severe legal and financial consequences and seriously harm the Group's reputation.

An integrity programme linked to corruption risk prevention has been in place in all Group entities for more than 15 years. It is based on a Code of Ethics for all Group employees that is regularly updated in line with external and internal reference systems and is posted on the Group intranet. With a preface by the Chairman and CEO, it reaffirms in particular the principle of zero tolerance for any act of corruption. Thales's integrity programme was certified by independent third parties Mazars and ADIT in 2014.

In 2017, the Group reviewed its integrity programme to bring it in line with French Law 2016-1691 of 9 December 2016 on transparency, the fight against corruption and the modernisation of the economy (known as the "Sapin II Law").

The various components of the integrity programme form an integral part of Thales's reference system (Chorus 2.0), particularly the processes which govern the management of bids and projects, purchases and subcontracting, and the use of agents and consultants. In addition to its internal control procedures, the Audit, Risks & Internal Control Department conducts regular compliance and integrity audits on the various components of the model.

The anti-corruption policy is outlined in Section 5.3.2.1 "Anti-corruption".

### b) Export control and economic sanctions

The export of many products, technologies and systems for military and dual use by Thales is subject to obtaining licences issued by the French and foreign authorities in advance.

In addition, the French, European and foreign regulations including the extraterritorial regulation issued by the Office of Foreign Assets Control (OFAC), establish a framework of embargoes and economic and criminal sanctions on any natural person or legal entity, or any state in breach of these provisions.

There are no guarantees that (i) the export controls to which Thales is subject will not be tightened; (ii) new-generation products or systems developed by Thales will not be subject to similar or tighter controls; (iii) geopolitical factors will not make it impossible for Thales or its suppliers to obtain export licences for certain customers or make it more difficult for Thales to execute previously signed contracts or will not give rise to economic sanctions (embargoes) which could prevent Thales from conducting or continuing to conduct business with certain countries or certain customers. Further limitations on access to certain international military markets could thus have a negative impact on Thales's business, financial position and profitability.

The Group has put in place an ISO 9100 certification process to ensure compliance with the regulations and controls applicable in terms of export and the economic sanctions in force. This process includes procedures, specific IT tools, employee awareness programmes, with, in particular, e-learning modules, an annual internal audit plan and a system to monitor changes in the legislation, regulations and restrictions following economic sanctions relevant to Thales's business activities.

Operating units have access to a network of specialists within the Group, who are responsible for monitoring the correct application of compliance rules decided at Group level as well as tracking requests for the required authorisations and the conformity of their implementation.

(1) Non-GAAP measures, see definition and computation in Section 1.1.1.2.

### c) Competition law

Thales's business activities are subject to a wide range of national and international regulations mainly aimed at combating anti-competitive practices, concerning suppliers, customers, partners and the competitors themselves.

Infringement of these rules could lead to severe sanctions, such as fines, payment of damages and interest, and statutory prohibitions and criminal penalties. Such sanctions could also have a serious impact on the Group's reputation.

To prevent these risks, a dedicated team of experts carries out competitive assessment on sensitive agreements and projects, notifying the competent regulatory authorities in Europe or abroad as required. In addition, the Group has initiated a programme to raise awareness of these rules, in particular through the drafting of directives, the implementation of online training tools and dedicated training programmes for the most exposed employees.

### d) Intellectual property

Thales is exposed to two main types of intellectual property risk: dependence on third-party technology and the infringement of intellectual property rights.

To reduce the risk of reliance on critical third-party technology, Thales has implemented a process to identify and manage each situation with a precise, strategic "Make/Team/Buy" (MTB) plan.

Given the nature of its activities and the specific features of its products, Thales conducts most of its research and development work in-house and focuses on controlling the key technology which is critical to the business. The size of Thales's internal intellectual property portfolio (over 16,500 patents, as well as software and know-how) and its presence throughout the value chain (equipment, systems and systems of systems) reduce its reliance on third-party technology. As a result, Thales's dependence on such technology can be considered low.

To reduce the risk of third-party actions for alleged infringement of their intellectual property rights by Thales entities, the Group identifies and analyses this risk in the context of its own patent filing procedures and/or when embarking on technical research or product development.

In the event of a third-party infringement claim against a Thales company, the legal and technical analysis of the allegedly infringing products and intellectual property rights are handled centrally by Thales experts, with the assistance of specialist external consultants where needed.

Thales may be exposed to the risk of infringement of its intellectual property rights by a third party. To limit this risk, Thales contractually protects its rights in its contracts and agreements, engages in an active policy for filing and maintaining its patents, carries out technological monitoring on the equipment and systems sold by third parties to ensure that its own intellectual property rights are not infringed and, where applicable, takes all necessary measures to ensure these rights are respected.

### e) Personal data protection

In the context of the application, effective 25 May 2018, of Regulation 2016/679 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, Thales has committed to bringing its policies into line with this European regulation.

A Data Protection Officer has been appointed to coordinate compliance with this new European regulation within the Thales group. The Data Protection Officer relies on a network of contacts in the different functions and entities both in France and the other countries where the group operates.

Initiatives are already under way within the Group to launch this compliance process, including insertion into contractual clauses on personal data protection, the drafting of factsheets, the acquisition of a tool to record Thales's processing of personal data.

### 1.1.2.2 Litigation

Due to the nature of its business, Thales is exposed to the risk of technical and commercial disputes.

To prevent disputes or limit their impact, Thales's policy is to systematically seek alternative dispute resolution mechanisms. This policy is reviewed on a regular basis to take into account changes in the Group's core areas of business and is backed by employee training programmes.

In addition, for several years now Thales has implemented a procedure to centralise all civil, commercial and criminal litigation and claims. These are handled by the Corporate Legal Affairs department, with the support of the Group companies concerned.

In October 2017, Thales was notified of an arbitration award in a commercial dispute between the Republic of China and a group of three French manufacturers, including Thales Systèmes Aéroportés, a Thales subsidiary. As a result of this arbitration award, which pertains to a contract signed in 1992, the manufacturers were ordered to pay a total sum of €227 million including interest, of which €64.2 million was payable by Thales Systèmes Aéroportés. The corresponding charge was recognised under "Disposal of assets, changes in scope of consolidation and other" in the financial statements as at 31 December 2017 (see Note 3.2 of the consolidated financial statements).

There are no other government, judicial or arbitration claims, of which the Group is aware, which are pending or threatened, which had, in the course of the last 12 months, or which could have a material impact on the financial position or the profitability of the Company and/or the Group.

## 1.1.2.3 Financial risks

### 1.1.2.3.1 Liquidity

The Group's liquidity risk is the risk of it being unable to meet its cash needs out of its financial resources. In particular, it relates to Thales's level of exposure to changes in the main market indicators that could lead to an increase in the cost of credit or even to a temporary limitation of access to external sources of financing.

The Group manages this risk by trying to anticipate its cash needs and ensures that these are covered by the Group's short-term and long-term financial resources, as follows:

- shareholders' equity, listed by caption in Note 8 to the consolidated financial statements;
- gross debt, listed by maturity in Note 6 to the consolidated financial statements;
- committed, undrawn bank credit facilities used as backup to the commercial paper programme and as a financial reserve. These are described in more detail in Note 6 to the consolidated financial statements. At 31 December 2017, the Group also had an undrawn bridge loan to finance its proposed offer for the acquisition of Gemalto.

The principle of centralising the entities' short-term assets and liabilities (cash pooling) is applied to the combination of entities in the same currency zone (eurozone, sterling zone, dollar zone and Australian dollar zone, etc.) and, in some cases, in the same country.

By consolidating and centralising the cash requirements and surpluses of its units, the Group is in a position to:

- simplify cash management and match the cash positions of units to produce a single consolidated position that is easier to manage;
- gain prime access to financial markets through the parent company's financing programmes, rated by S&P Global Ratings and Moody's (see below).

At 31 December 2017, cash recorded under consolidated assets amounted to €4,282.7 million (compared with €3,616.9 million at end-2016), including:

- €3,450.5 million held by the parent company and available for immediate use (€3,183.1 million in 2016);
- €832.2 million in the credit balances of subsidiaries (€433.8 million in 2016), most of them outside France. This figure includes payments received in the last days of the financial year and subsequently transferred to the cash pooling account.

Cash at bank and equivalents at year-end is invested solely in sight and term bank deposits or in money market funds. At the date of publication, Thales's risk ratings were as follows:

	Moody's	S&P Global Ratings
Medium & long-term loans	A2	A-
Outlook	Negative	Negative watch
Commercial paper & short-term loans	Prime-1	A2

Moody's and S&P Global ratings downgraded their outlook (from "stable" to "negative" and "negative watch" respectively) following the announcement on 17 December 2017 of the planned cash tender offer for Gemalto. If this acquisition, partly financed from the Group's own cash flow and partly through borrowings, goes ahead, it would in all

likelihood cause Thales's rating to be lowered, due mainly to the change in the Group's financing structure.

The decrease of Thales's credit risk rating would not trigger the financial covenants included in its financing contracts. The coming into effect of the unique clause providing for accelerated repayment of bank credit facilities would only apply in the event that the French government no longer held its golden share and, simultaneously, the ratio of consolidated net financial debt to EBITDA (earnings before interest, taxes, depreciation and amortisation) were to exceed 3.

A lower rating would result in an increase (capped) in the margins applicable to the committed credit facility of €1.5 billion (described in Note 6 to the consolidated financial statements); at the same time, these margins would be improved (with a minimum threshold) in the event of a rating upgrade.

### 1.1.2.3.2 Interest rates

Thales is exposed to interest-rate volatility and in particular its impact on the conditions associated with variable-rate financing. To limit this risk, Thales operates an active interest rate hedging policy.

The Corporate Financing and Treasury Department consolidates data on Thales's exposure to interest rate risk and uses appropriate financial instruments to hedge those risks.

Thales policy is to control interest rate and counterpart risks and to optimise its funding and banking operations.

The breakdown of Thales's debt by type of interest rate is described in Note 6 to the consolidated financial statements. The table below summarises the Group's exposure to interest rate risk before and after hedging. Based on the average net cash (taking into account hedging instruments), a 1% rise in interest rates would impact net financial interest by €27.4 million in 2017 (€21.6 million in 2016).

(31/12/2017, in € millions)	< 1 year		> 1 year		Total	
	Fixed rate	Variable rate	Fixed rate	Variable rate	Fixed rate	Variable rate
Financial liabilities	(512.1)	(192.1)	(891.8)	(47.3)	(1,403.9)	(239.4)
Financial assets	—	4,614.7	—	—	—	4,614.7
<b>Net exposure before impact of derivative instruments</b>	<b>(512.1)</b>	<b>4,422.6</b>	<b>(891.8)</b>	<b>(47.3)</b>	<b>(1,403.9)</b>	<b>4,375.3</b>
Derivatives	296.2	(296.2)	695.4	(695.4)	991.6	(991.6)
<b>Net exposure after impact of derivative instruments</b>	<b>(215.9)</b>	<b>4,126.4</b>	<b>(196.4)</b>	<b>(742.7)</b>	<b>(412.3)</b>	<b>3,383.7</b>

### 1.1.2.3.3 Foreign exchange

Due to the international nature of its business, Thales is exposed to the risk of exchange rate fluctuations.

#### a) Business-related currency risk

Business-related currency risk occurs when some of the business is billed in a currency other than that of the related costs.

- As a general rule, Thales is structurally immune to exchange rate fluctuations for a significant part of its business activity. Around 40% of Thales's sales are generated in the eurozone, where a significant portion of its industrial operations are located. More generally, the reinforcement of the Group's international industrial footprint allows it to produce and invoice in local currency, which helps to reduce exchange rate risk on local sales.

- The accounts of Thales's subsidiaries located in countries where the functional currency is not the euro are translated into euros in the Group's consolidated financial statements. A fall in these currencies against the euro is likely to have a negative impact on the accounts. Its impact on profitability is limited, however, since the cost base of these subsidiaries is essentially in the same currency as their sales. The main currencies concerned are the pound sterling, the US dollar, the Canadian dollar and the Australian dollar.

- For certain Group businesses (commercial avionics and microwave systems, commercial space, etc.), the US dollar ("\$" or "USD") is the reference transaction currency. For business activities outside the dollar zone (the in-flight entertainment and connectivity business is based essentially in the United States and is therefore naturally immune to this risk), a specific currency risk hedging policy is implemented:

- for equipment transactions (avionics and microwave systems), this policy is defined on the basis of sales forecasts in USD, after accounting for corresponding purchases in USD. For these transactions, net exposure to dollar risk represents around 3.5% of the Group's total sales for 2017,

- for longer-term programmes in markets traditionally denominated in USD (primarily commercial space activities), each bid is examined for profitability in light of the effect of currency fluctuations, after accounting for corresponding purchases in USD, and, if necessary, is specifically hedged through market transactions (forward exchange-rate contracts and options).

Where necessary, a similar approach is adopted for other Thales activities if a customer specifically requires a contract denominated in USD on an ad hoc basis.

Overall, net exposure amounted to around 2% of the Group's total sales for 2017;

- as well as this direct dollar risk, which concerned around 5.5% in total of consolidated sales at end-2017, the Group is also exposed to an "indirect" dollar risk on contracts denominated in currencies other than the dollar. This occurs when it is bidding against companies that benefit from a cost base in dollars. At least one quarter of total sales may be exposed to this "indirect" dollar risk.

The "dollar risk" is thus the main currency risk that Thales needs to manage. The figures corresponding to the management of business-related dollar risk are as follows:

- \$2,496 million, the amount of financial instruments hedging net firm commitments (US dollar risk against the euro, Canadian dollar and pound sterling) at 31 December 2017 compared with \$2,985 million at 31 December 2016;
- financial instruments (forward transactions) used to hedge bids in US dollars against the euro, Canadian dollar and pound sterling amounted to zero at 31 December 2017 versus \$310 million at 31 December 2016.

Operating receivables and payables denominated in foreign currency are exchange-rate hedged and therefore not exposed to currency risk.

The change in the value of financial instruments (forward transactions) used to hedge cash flows is recognised in equity for the spot rate component. A decrease (increase) of 5% in the dollar against the main

currencies (EUR, GBP and CAD), would have increased (decreased) shareholders' equity by approximately €104 million at 31 December 2017 (€153 million at 31 December 2016). The premium/discount component is not eligible for hedge accounting and is recognised through profit and loss. In 2017, the change in market value of the premium/discount was -€65.3 million (compared to -€54.0 million in 2016).

The change in value of financial instruments used to hedge commercial bids which are not eligible for hedge accounting is recognised in profit and loss. A decrease (increase) of 5% in the dollar against the main currencies (EUR, GBP and CAD) would have had no impact on profit or loss at 31 December 2017 or 31 December 2016.

Foreign currency-denominated financial debt does not generate any exposure in profit and loss, as it is either denominated in the functional currency of the entity in which it is recognised or is used as a net foreign investment hedge.

#### b) Management of risks relating to foreign currency-denominated assets

The Group may hedge a portion of its foreign currency-denominated assets, mainly those likely to be disposed of. The main criteria for determining whether or not a given foreign currency denominated asset should be hedged are as follows:

- the nature of the business operations involved;
- the structure of Thales's commitment with respect to jointly held companies, in particular the specific features of the shareholders' agreement in each joint venture.

The actual application of this policy also depends on:

- the objective of optimising hedges in light of market conditions (availability of foreign currency, interest rates, hedging rate, etc.);
- the risks inherent in the future value of the assets being hedged and the nature of the business of the corresponding subsidiaries.

### ➤ SUMMARY OF ASSET RISKS AT 31 DECEMBER 2017 FOR THE MAIN CURRENCIES

(in € millions)	GBP zone	USD zone	AUD zone	Other currencies & eliminations	Total
Assets	1,989.6	1,652.5	963.9	17,037.5	21,643.5
Liabilities	2,093.1	1,424.3	489.5	12,081.1	16,088.0
<b>Net position before hedging</b>	<b>(103.5)</b>	<b>228.2</b>	<b>474.4</b>	<b>4,956.4</b>	<b>5,555.5</b>
Hedge	–	–	–	–	–
<b>NET POSITION AFTER HEDGING</b>	<b>(103.5)</b>	<b>228.2</b>	<b>474.4</b>	<b>4,956.4</b>	<b>5,555.5</b>

#### 1.1.2.3.4 Shares

Thales was not exposed to any material equity risk at end-2017, excluding the risk on treasury shares.

At 31 December 2017, Thales held 568,739 treasury shares, representing 0.27% of the share capital.

#### 1.1.2.3.5 Pension commitments

Defined-benefit pension plans are in place for certain Group employees, mainly in the UK, which are financed by the Group under the provisions of the applicable domestic legislation. As such, at 31 December 2017,

Thales's pension commitments in the United Kingdom amounted to €4,431.8 million, hedged by €3,248.7 million in investments, representing an underlying shortfall of €1,183.1 million.

Changing market parameters can lead to a substantial increase or decrease in the amount of the shortfall and the annual costs of defined-benefit plans. At 31 December 2017, the main sensitivity factors were as follows:

- a decrease or increase in the discount rate applied to liabilities, which could increase or reduce the underlying shortfall; this variable is partly offset by changes in the value of fixed-rate hedging bonds held as plan assets and interest rate swaps;
- changes in the total return on investments in equities and other assets;

- changes in the forecast inflation rate;
- a substantial change in mortality tables;
- exchange rate fluctuations (mainly sterling against the euro).

Thales has introduced six-monthly reporting on its pension plan commitments and makes regular projections measuring the sensitivity of underlying shortfalls to possible market changes taking into account their correlations. In the UK, Thales plan assets are managed by trustees in accordance with the applicable regulations and in consultation with the Group. Plan assets are allocated with regard to the long-term maturity of the commitments they cover.

Additional information on the amount of commitments and the annual costs linked to pension and other employee benefits, as well as the valuation and allocation of plan assets and the sensitivity of net commitments to different actuarial assumptions is given in Note 9.3 of the consolidated financial statements at 31 December 2017.

#### 1.1.2.3.6 Sureties, endorsements and guarantees granted by Thales (parent company)

Thales (parent company) issues sureties, endorsements and guarantees, primarily in support of commitments undertaken by its subsidiaries through commercial contracts. The Group's Corporate Financing and Treasury Department centralises the issuance of these sureties, endorsements and guarantees.

They are issued out of an envelope of €4 billion, which is regularly delegated by the Board of Directors to the Chairman and CEO. Before each time the Chairman's authorisation is renewed, the extent of use of this envelope, which is monitored by the Corporate Financing and Treasury Department, is notified to the Board.

As of 31 December 2017, outstanding sureties, endorsements and guarantees granted by Thales (parent company) to its subsidiaries amounted to €12,760.4 million. These guarantees include all commitments given in relation to Thales Alenia Space, which are backed by a counter guarantee from Leonardo in proportion to its interest in the capital of Thales Alenia Space (33%).

Thales has initiated a programme to control risks related to these sureties, endorsements and guarantees through the parent company and to optimise the financial terms of transactions guaranteed using these instruments with the following main objectives:

- to limit the risks to those corresponding to normal commitments in commercial contracts, particularly in terms of volume and duration;
- to limit their issuance to commitments made by wholly owned subsidiaries, with guarantees commitments involving business combinations or joint ventures only being issued in proportion to the Group's interest or counter-guaranteed by the other shareholder in proportion to its interest;
- to allow its subsidiaries to benefit, where appropriate, from the credit quality of Thales (parent company), by controlling the financial terms of guaranteed transactions.

#### 1.1.2.3.7 Customer credit

Credit risk relates to the risk that a party to a contract will default on its commitments or fail to pay what it owes.

##### a) Risk of default by private sector customers

Non-governmental customers (aircraft manufacturers, airlines, private infrastructure operators and industry) account for approximately 25% of Thales's sales. These customers may encounter major and/or prolonged financial difficulties that could lead to payment defaults or order cancellations. Such occurrences could have a negative impact on the Group's sales, profitability and financial position.

To mitigate these risks, Thales conducts regular analyses of the ability of customers to meet their obligations. When necessary, Thales may request bank guarantees or corporate guarantees, or may use credit insurers.

##### b) Credit risk relating to public sector customers

Public, government and institutional customers account for around 75% of Thales's sales. Thales works with a large number of countries. Some of them could present a significant credit risk which could, for example, lead them to suspend an order in production, or render them unable to pay on delivery, as agreed under the terms of the contract. To limit its exposure to these risks, Thales takes out insurance with export credit agencies (such as BPIFrance) or private insurers.

At 31 December 2017, only three customers accounted for annual sales in excess of €500 million: the French government (around €2.8 billion), the UK government (around €1 billion) and the Australian government (around €0.7 billion). At 31 December 2017, these three countries had first-class or high-quality ratings (France was rated AA by S&P and Aa2 by Moody's, the United Kingdom was rated AA by S&P and Aa2 by Moody's, and Australia was rated AAA by S&P and Aaa by Moody's).

#### 1.1.2.4 Insurance

Thales's Insurance and Risk Management department, based at head office and reporting to the SEVP Finance & Information Systems, is responsible for insurance activities and insurable risk management. It is in charge of Group operations and oversees policy implementation by Group companies.

The Group is covered against the financial consequences of the risk of accidental damage suffered or caused by property or people using appropriate insurance policies with leading international insurance and reinsurance companies.

The insurance policies arranged by the Group to cover these major risks relate to areas such as:

- damage to property and consequent operating losses;
- transport;
- assembling and testing;
- aviation liability, including liability for aeronautical products and hull/test flight insurance;
- liability for space products;
- risks of damage to or by naval vessels by subsidiaries, as naval equipment suppliers;
- general third-party liability;
- environmental liability;
- liability of executive officers and directors;
- individual accident – repatriation assistance for employees on assignment;
- cyber liability.

The Group had no major loss in 2017.

The Group's policy is to arrange cover on the insurance market based on the rates and within the limits that it considers reasonable, in view of the conditions offered by the market. Insurance policies covering the major risks may be limited in terms of guarantee (application of limits), while general exclusions for the entire market (e.g. asbestos) also apply to Thales.

In 2017, the maximum coverage limit for insurance against damage to property and consequent operating losses was €1.3 billion. This limit takes into account the estimated maximum possible loss caused to an industrial site which the Group could incur in this regard. In 2017, the Group renewed a specific cover against cyber incidents (IT data attack) and damages that could compromise its internal IT systems.

Levels of liability cover depend on the quantification of a reasonable claim expectancy for Thales, as identified by the risk map of the main business activities and at Group level, and on cover capacity available on the insurance market. The insurance coverage for aviation liability commitments, which is covered by a specific programme, is capped at \$2 billion.

The insurance industry depends on the financial markets. There are therefore no guarantees that Thales will be able to maintain current levels of insurance under similar financial conditions in the future.

In order to reduce its exposure to insurance market volatility, Thales insures major risks on a two-tier basis:

- the Group's contribution, through captive insurance and reinsurance companies, towards the settlement of claims, to a maximum net retention of €12 million per year, for damage to property and consequent operating losses, transport, general third-party liability, assembling and testing, development and space risks;
- transfer to insurers of payment for catastrophic or high intensity losses.

In parallel, an active Prevention and Protection policy for industrial sites is designed to reduce the magnitude and frequency of the accidental risks of fire or explosion and to detect other exposures, such as environmental or natural disasters and the vulnerability of critical industrial facilities. In 2017, more than 70% of the assets insured were the subject of a "multi-peril" audit by the insurers during their visits to the

principal operating sites and infrared thermography inspections by an outside organisation specialised in the prevention of electrical damage.

In accordance with Group processes, measures were taken to minimise business interruption and the consequences of any unforeseen events. An organisational structure and crisis management tools are in place to deal as efficiently as possible with the immediate consequences of a catastrophic event and to take the necessary emergency measures.

A risk prevention policy for critical supplier sites was also pursued to reduce the risk of operating losses for Thales in the event of an accidental disaster at one of their sites.

Furthermore, Thales continues to roll out an insurance policy for its staff to cover them in the context of their professional activity. Lastly, specific and/or local cover has been arranged to comply with the regulations in force and to satisfy the specific requirements of certain business activities or projects, particularly public-private partnerships.

## 1.1.3 Internal control and risk management

This section was submitted to the Audit and Accounts Committee at its meeting of 15 February 2018, attended by the statutory auditors. It was prepared on the basis of the main conclusions from the internal audit, internal control and risk management work carried out by the Group in 2017. The results of this work were reviewed at the various meetings of the Risk Assessment Committee and the Risk Management Committee (see Section 1.1.3.5) during the year, and also at meetings of the Audit and Accounts Committee held in 2017.

This section is based on the AMF reference framework on risk management and internal control systems, updated on 22 July 2010.

It covers all the suggested items, albeit sometimes in a different order.

Risk management gives executives an objective and comprehensive vision of potential threats and opportunities to which the Group is exposed, enabling them to take measured and considered risks and guiding them in their decisions on the allocation of human and financial resources.

### • Promote the consistency of action with the values of the Group

The Group's approach to risk management is consistent with its values, particularly with regard to the strict compliance of its business activities with national and international rules and legislation.

### • Involve the Group's employees in a shared vision of the main risks and make them aware of the risks inherent in their work

### 1.1.3.1 Objectives and definitions

#### a) Objectives of risk management

Thales adheres to the risk management objectives formalised by the AMF in its reference framework. Risk management is a management tool that Thales uses to:

#### • Create and preserve the value, assets and reputation of the Group

Risk management identifies and analyses the main threats and potential opportunities to which the Group is exposed. By anticipating the potential impact of these risks, it is intended to more effectively preserve the value, assets and reputation of the Group.

#### • Secure the Group's decision-making and processes to help it achieve its objectives

Risk analysis is designed to identify the principal events and situations which could significantly impact the achievement of the Group's objectives. Controlling such risks helps to achieve those objectives.

Risk management is integral to the Group's decision-making and operational processes. It is one of the tools for steering and assisting in decision-making.

#### b) Definition of internal control at Thales

The Group uses as a reference the international standards of COSO 2013 (Committee of Sponsoring Organizations of the Treadway Commission) and IFACI.

According to the definition used by Thales, internal control is a process that the organisation implements with the intention of providing reasonable assurance as to the achievement of the Group's objectives, through:

- the effectiveness and efficiency of internal processes;
- accounting and financial internal control aimed at:
  - ensuring the reliability of the information used internally for management and monitoring purposes as well as for the preparation of the published accounting and financial information,
  - preventing the risk of fraud ;
- legal compliance, which is intended to ensure compliance with regulatory requirements.

#### c) Scope of application and limits

Thales implements its corporate risk management and internal control approach in the companies it controls.

These internal control and risk management processes contribute to the achievement of the Group's objectives without providing an absolute guarantee because of the limitations inherent in any system, such as the need to take into account the cost/benefit ratio leading to acceptance of a certain level of risk, and due to external uncertainties beyond the Group's control.

### 1.1.3.2 Control environment

For most of its operations, the Group is subject to a control environment imposed by its customers and regulatory authorities (Ministries of Defence and Industry, Authorities in its customers' countries, Commercial Aviation Authorities, etc.), which require strict certification and controls.

These specific constraints are in addition to its statutory obligations and are an integral part of the Group's control environment.

#### a) The main parties in risk management and internal control

Thales is organised according to a two-dimensional matrix structure comprising Global Business Units and countries.

- The Global Business Units are organised into business lines, which cover a coherent range of products, solutions and services.

For the products, solutions and services entrusted to them, the business lines have worldwide responsibility for strategy, product policy and marketing, competitiveness, customer access, contractual commitments, engineering, development, production, integration, quality and services, industrial organisations, optimisation of resources, and economic performance (contribution to EBIT and cash flow).

- In the region assigned to them, country managers are responsible for the successful implementation of every aspect of Group policy and handle relations with customers and local partners.

The main countries in which the Group operates (Australia, Canada, France, Germany, the Netherlands, the United Kingdom and the United States) share responsibility with the Global Business Units for local bids and projects. Country managers are involved in all decisions taken by the Global Business Units with regard to organisation and appointments, or relating to bids, projects and centres of excellence of any kind in their territories. They are responsible for HR development and the optimisation of industrial resources. They are also responsible for Thales's institutional relations as well as for communication.

The country manager of each of the six major industrial countries (excluding France) in which the Group operates (see list above) reports to a Non-Executive Chairman, appointed from among the Group's senior executives. The Non-Executive Chairman acts an interface between the country and head office and liaises between the Country Manager and Executive Committee.

For the other countries in Europe (apart from those with a Non-Executive Chairman, see above), the country or regional Manager reports to the Europe and International Operations department, which in turn reports to the Senior Executive Vice President, Operations & Performance.

In all other regions (Africa, Latin America, Asia and the Middle East), the country or regional manager reports to the Senior Executive Vice President, International Development.

The Group defines common processes and internal rules on delegation setting out the way in which responsibility is shared, provides entities with the corresponding tools and sets up umbrella departments.

The delegations are implemented in legal entities coordinated at national level.

#### The Group's managing bodies

These consist of Global Business Units, countries and functional departments and are ultimately responsible for the Group's entire internal control system, relying in particular on internal processes and the work of the Risk Management Committee and the Risk Assessment Committee.

The Group's governance is founded on the key principle of the responsibility of the directors of operational entities, who are responsible for establishing and maintaining the risk management and internal control system within their operational entities.

#### The corporate risk assessment function

Since 2007, the Audit, Risks & Internal Control Department has included a corporate risk analysis function. This is the responsibility of a dedicated team, separate from the audit team, which provides support to all operating and functional managers to help them identify and assess the risks to which their activities are exposed and to institute the means to manage or reduce these risks. It is also responsible for developing and updating internal control assessment tools, such as the yearly attestation letter and the internal control questionnaire, and collating and analysing the responses given by the operational entities in these annual questionnaires.

The internal audits conducted by the Audit, Risks & Internal Control Department are primarily chosen and planned based on this risk analysis.

#### Finance function

The Group's Finance Department oversees the Company's accounting and financial operations. Its central organisation comprises:

- an accounting and consolidation function, responsible for preparing and presenting the Group's consolidated financial statements;
- a management and budget control function, which analyses the Group's financial data and produces monthly reports comparing actual results with the budget and comparable prior-year periods. On this occasion, financial forecasts for the current half-year and financial year are reviewed and discussed so as to steer the business in order to achieve the objectives set;
- a tax function, which provides support to the operational entities on legislation and during tax audits. It also monitors tax consolidation within the Group and ensures their overall coherence;
- a risk and prevention insurance function, which manages all insurance policies taken out by the Group to guarantee all of its companies, optimises the costs of these policies, verifies that the companies are properly covered against insurable risks that they incur and issues recommendations to prevent them. It also monitors any significant claims;
- a treasury and financing function, which optimises financial resources and manages the Group's financial risks (foreign exchange, interest rates, pensions, etc.);
- a financial engineering function, in support of commercial contracts to offer customers suitable financing, secure payments to be received and hedge against the financial consequences of contract interruption which could arise in particular in the event of political risk or risk of customer default.

The Group's Finance department is represented in each Global Business Unit, each operational entity and each of the main countries by a Finance Director who functionally reports to it. The implementation of the accounting and financial internal control is carried out by these Finance Directors, who have local teams within their scope of responsibility to ensure that the financial information is prepared in compliance with the rules on internal control.

At the time of the annual and half-year financial statements, the Chief Executive Officers and the Finance Directors issue a letter of representation to the Group's Finance department, certifying the fair presentation and completeness of the financial data submitted for consolidation.

#### Legal function

The Group's Legal & Contracts Department, as well as the legal counsel in the various countries and Global Business Units, provide support to the operational entities with regard to local and international laws, in order to manage any potential legal risks that may be incurred in the various fields of the law.

The Group's Human Resources department also has a network of legal advisors who specialise in employment law and who provide support to the Group's entities. The Legal & Contracts Department and the Human Resources Department call upon outside law firms, where necessary.

### Operations and performance function

The Operations and Performance department is responsible for the operational resources necessary to carry out projects and ensure customer satisfaction and quality, thus contributing to risk management. It approves the most sensitive bids according to specific criteria and holds quarterly reviews of projects deemed critical. It manages skills development plans as well as bid and project manager certification plans. It rolls out and upgrades bid costing and project management tools and provides *ad hoc* support to any Global Business Units and countries requesting it. In each entity, the Director of Operations coordinates, in close collaboration with the Legal Director and the Finance Director, the management of all of the Company's risks.

The Operations and Performance department includes the Quality Assurance and Customer Satisfaction Department, which defines the quality assurance policy and objectives and drives improvements in customer satisfaction. It steers the process management framework (Chorus 2.0) applicable to all Group entities. Each process is entrusted to a manager who is responsible for defining rules and setting targets, as well as for implementing them and making sure that they are effective. This translates into process targets being achieved while reducing risk. Quality assurance procedures for offers, projects and products are carried out by the operational entities, in order to effectively meet customer demands and ensure customer satisfaction and secure the execution of operations.

In addition, the Quality Assurance and Customer Satisfaction function manages the policy in place for assessing the maturity of operational entities (see description in Section 1.1.3.4-a).

### b) The Group's operating principles and procedures

Thales's operating principles and procedures underpin the Group's internal control. This set of organisational rules, policies and procedures, which includes rules on ethical conduct and corporate responsibility, is available on the Group intranet and is provided to all new employees in their welcome pack.

### Reference system

Thales has created a process-based reference system called Chorus 2.0, which defines the organisation, rules, practices and methods to be implemented at each Group entity.

Thanks to its modular design, it can be adapted to the business context and can be augmented within each entity or country, by local rules and practices detailed in a technical reference system.

Chorus 2.0 is accessible via the intranet, making it easy to locate the policies, procedures, instructions, templates and forms which need to be used. Chorus 2.0 covers nine headline processes, sub-divided into 26 processes. These processes, which are closely interfaced – and identify activities that require attention with regard to the potential for risks to occur – precisely define how Thales works according to the roles, rules, practices and operating modes described.

This reference system gives all Group companies a shared language and a unified management process. Chorus 2.0 is also aimed at organisational alignment across the Group.

Chorus 2.0 is a vital tool to enable each entity to have its management systems certified – on a Group wide platform – in terms of quality, health, safety and environment and with regard to the norms and standards applicable to each business activity.

Chorus 2.0 is a crucial element of the Group's internal control and is a natural component of the reference systems used in the work of the Audit, Risks & Internal Control Department.

### Rules of procedure of the Board of Directors

Section 3.2.1 provides more details on the Board of Directors, its rules of procedure and its operation.

### Codes and guides of conduct

The code of Conduct defines the types of conduct that are prohibited as they may be construed as acts of corruption or influence peddling. The Code applies to all employees of the Group. It has been incorporated into the internal regulations of the Group's French companies and is in the process of being rolled out to its foreign subsidiaries.

It is supplemented by the Code of Ethics and a set of guides published in the Group's framework.

The Code of Ethics, published in eight languages, is the bedrock of Thales's culture of integrity. It sets out the rules of conduct and the values that the Group wants to develop. It covers relationships with customers and suppliers, partners, employees, shareholders and financial markets, as well as protection of the environment.

A business ethics reference guide is dedicated to the prevention of corruption. It describes the rules and regulations that must be respected internally.

Several business ethics conduct guides present the best practices expected from employees with regard to anti-corruption measures, gifts and hospitality, conflicts of interest, lobbying and the use of the professional whistleblowing system.

A reference guide entitled "Compliance with Export Control Regulations" describes the compliance requirements and the process of export control. It identifies stakeholders, defines their responsibilities, and sets out best practices in terms of compliance with export control regulations.

As part of its policy of preventing insider trading, the Group has adopted a Code on Insider Trading for directors, and regularly updates the list of insiders (see Section 3.2.1).

An e-learning platform also helps to educate the Group's employees on topics such as export controls, ethics and corporate responsibility.

### c) Group risk mapping

The Group has mapped its major operational, strategic, compliance and financial risks. It updates this risk map each year.

Each risk factor identified is set out in risk scenarios prioritised on the basis of two analysis criteria, before and after mitigation: likelihood of occurrence and financial impact.

The Group has assigned each of these risks to a risk advisor who is responsible for coordinating the management of this risk under the supervision of the Risk Assessment Committee. This consists of characterising the risk, monitoring major incidents, overseeing the deployment of the risk management system and continuously improving it.

### 1.1.3.3 Principal corporate risks and their management

The section on risk factors in the Group management report (see Section 1.1.2) describes the measures taken by the Group to address operational, strategic, legal and compliance and financial risks and risks related to insurance.

#### a) Centralised activities

Some complex or risky transactions are carried out solely by central departments, which ensure the sharing, consistency and coordination of the Group's practices. A specific internal control mechanism has been put in place to manage the risks associated with these transactions.

#### Investments and divestments

Total or partial acquisitions and disposals come under the exclusive remit of the Group's corporate management. The Global Business Units propose projects at periodic meetings of the Mergers and Acquisitions Committee, made up of the main central departments.

#### Financing, treasury management and foreign exchange risk

The Group's financial resources, liquidity risk and interest rate risk are managed centrally by the Group Treasury and Financing department. Except in special cases, the Group's subsidiaries are not authorised to undertake financing operations themselves. According to the policy of optimising and centralising the Group's financial resources, the Group Treasury and Financing department provides funding to the subsidiaries, manages surplus cash positions in all of the Group's currencies and matches surpluses with cash requirements. The Group Treasury and Financing department is also responsible for managing the Group's currency position and hedging the associated risks (in particular the foreign exchange risks to which the subsidiaries are exposed, which are closely monitored at the subsidiary level). Foreign currency transactions are analysed prior to any financial commitment and are hedged against foreign exchange risk as soon as the likelihood of being awarded the sales contract and/or signing a purchase order becomes significant, excluding special cases.

#### Customer financing and hedging of contract interruption and credit risks

The International Financial Affairs department coordinates and supervises the Group's financial engineering activities (establishment of advance market commitments, customer financing (buyer or supplier credit), documentary credits or more complex transactions such as project financing or PPP). These transactions are carried out in collaboration with those responsible for the financial engineering of international activities, who report to their Finance department and also to the International Financial Affairs department.

#### Real estate management

All real estate transactions come under the exclusive remit of the Group's Real Estate Department. It may delegate certain operations, especially outside France, to a national organisation, or to a local company, while ensuring proper supervision.

#### Disputes, litigation and legal compliance

With the exception of disputes concerning relationships with employees and trade unions, which are handled by the Human Resources Department, other disputes are monitored by the Legal and Contracts Department.

#### Insurance and prevention (of insurable risks)

All of the insurance policies taken out by the Group are managed by the Insurance and Prevention of Insurable Risks Department. It optimises

the coverage and cost of insurance for the Group, checks that the entities are guaranteed against the insurable risks they incur, and issues recommendations for their prevention. This Department also monitors any significant claims.

#### b) Development and processing of published financial and accounting information

##### Accounting and financial procedures

The Group has several procedural manuals applicable in all entities and reiterated in the processes defined in Chorus 2.0. The Finance Directors of each entity are accountable to the Group Finance department for compliance with these procedures.

##### Manual of accounting standards and policies

This manual provides a detailed description of the accounting standards and policies to be applied during the preparation of the consolidated financial statements in accordance with IFRS.

##### Budgetary control manual

This manual describes the hierarchy and reporting levels required by the Group, the financial cycles, the responsibilities of the Finance department in operational processes and the rules to be followed by all Group entities.

##### Reporting manual

This manual describes the content and format of periodic reports and contains a glossary to help standardise financial aggregates.

##### Cash management manual

This manual describes the respective roles of central teams and teams within each entity in respect of cash flow and financing operations.

It also details the procedures for short-term cash flow management, operation of the exchange risk hedging system and the related reporting rules.

##### Internal control questionnaire

The internal control questionnaire and the accompanying instructions provide an additional framework and help to improve the reliability of financial reporting while at the same time preventing the risk of fraud. These elements, which have gradually been incorporated into the process management framework and distributed to the entire Group, are effectively equivalent to an internal financial control manual.

##### Budget process

There are three stages in setting the annual budgetary targets:

- the Global Business Units draw up a strategic plan over a minimum period of four years, which can be adjusted depending on their business models; this is then presented to and approved by Group corporate management;
- each Global Business Unit, each major country, the Europe and International Operations Department and the International Development Department then present a detailed three-year budget plan to Group corporate management. This plan is based on the sales forecasts and assumptions prepared by the marketing and sales departments, in accordance with the strategic plans prepared by the Global Business Units;
- finally, Group corporate management sets targets for the Global Business Units, the main countries, the Europe and International Operations department and the International department, ensuring that they are consistent overall. The first year of the plan is then analysed monthly and is used as a reference for steering the Group.

## Financial reporting

The system includes some of the key factors described earlier in this report, such as accounting and financial procedures and a centralised consolidation process supported by a single tool.

Monthly results are analysed in order to identify any budget deviations and to update annual forecasts for orders, sales, profits and cash flow. This procedure is carried out by each entity and provides a consolidated view at Global Business Unit and Group level. It also makes it possible to identify any action plans necessary to achieve the objectives set.

## Consolidation of the financial statements

The teams in charge of consolidation ensure that changes in regulations and standards are taken into account. They use the same consolidation software throughout the Group, selected from those available on the market, which enables it to upload the accounting information from the Group's various entities with consistency checks carried out at source. Transfers of accounting entries to head office are authorised only after validation. Training sessions and personalised support on the tool within the Group's consolidation teams ensure that users operate the software effectively.

### 1.1.3.4 Ongoing improvement process

Thales has introduced internal and external assessments, based on international standards, enabling the Group to identify any areas requiring continuous improvement, to prioritise these and to monitor the associated action plans.

#### a) Assessment of the maturity of operational entities

Thales has developed an internal system for assessing the maturity of its operational entities, known as the Thales Integrated Maturity System. It is used for:

- bid, project and product management;
- development, production, facilities and deployment;
- purchasing, quality, support activities and services.

An assessment may cover an entire organisation or be restricted to a specific element of said organisation, such as a project or product. Whatever the scope, the system considers three components: organisation and management, resources and skills, and processes, practices and tools.

Maturity assessments are performed by experienced assessors who are recognised in their field as well as by the quality managers at each operational entity.

The maturity model covers all of the Chorus 2.0 management system processes and is fully compliant with international standards, such as:

- the international CMMI® (Capability Maturity Model Integration) model, which is recognised by many customers for its development, acquisition and services models;
- the international Supply Chain Operations Reference (SCOR®) model.

## Process management

Thales has obtained and maintains, in its different activities, certifications of compliance with applicable standards and regulations that attest to its ability to manage its processes to meet the needs of its customers.

For quality and for all Group activities, the certification standard is ISO 9001, and, depending on the business activities, the following standards are also used (non-exhaustive list):

- AQAP 2110, NATO quality standard for the defence sector;
- EN 9100, European standard describing a quality assurance system for the Aerospace industry;
- EASA Part 21 subpart G for production activities (Europe);
- EASA Part 145 (Europe) and FAR 145 (USA) for maintenance activities;

- EASA Part 147 for aeronautical training and maintenance;
- ISO 14001 and OHSAS 18001 for Environment, Health & Safety at work.

#### b) Self-assessment and ongoing improvement of corporate risk management

Since 2007, the Group has had a corporate risk management process in place for all the businesses and subsidiaries it controls.

In 2017, the Group's risk mapping process identified and measured the potential frequency and impact of 56 risk scenarios, with operational responsibility for each being specifically allocated to one of the following three management structures:

- local entities, segments or Country Business Units;
- Global Business Units or Business Lines;
- central functions.

The processes defined in Chorus 2.0, the insurance policy, the self-assessment and internal control tools, and the internal and external audits form part of the management of these risks.

Every year, the local entities report on the risk scenarios under their responsibility, in the form of a questionnaire (yearly attestation letter), updated annually and completed by the heads of the operational entities and their management teams. In 2017, 110 questionnaires were completed by the Group's operational entities. The responses to these questionnaires are analysed by the Audit, Risks & Internal Control Department, and by the network of risk advisors. A sample of questionnaires are checked for accuracy and compliance by the Audit, Risks & Internal Control Department: in 2017, 15 questionnaires were subject to an internal audit.

#### c) Self-assessment and ongoing improvement of internal financial control

Drawing in particular on the AMF recommendation entitled "Reference framework for risk management and internal control systems" and in collaboration with its statutory auditors, the Group asks its financial community to complete an internal control questionnaire (ICQ) focusing on the reliability of financial processes and the prevention of fraud.

The ICQ is based on internal control objectives linked to the Group's processes and accounting cycles (customers/suppliers/fixed assets, etc.) and is designed to enable the entities to identify areas of improvement, whether these are due to control objectives that have not yet been completely achieved, insufficient control in practice, or procedures that need to be improved. In 2017, 132 questionnaires were completed, representing all of the operational entities plus the shared services.

### 1.1.3.5 Oversight of the internal control and risk management system

#### a) Monitoring and control bodies

The Board of Directors exercises control over the management of the Group, either directly or through its committees. Detailed information on the organisation of the Board's work and, more generally, the performance of the Board and its committees is given in Section 3.2.1 of the corporate governance report.

#### Audit and Accounts Committee

At the meetings of this committee to the Board of Directors, the resources employed, actions taken to improve internal control and risk identification and management are reviewed. In 2017, this committee met six times.

Each year, the Audit, Risks & Internal Control Department submits an audit plan to the Audit and Accounts Committee covering various aspects relating to the Group in respect of compliance with legislation and regulations, assessment of internal control and risk identification and management.

At the time of the annual closing of the accounts, the Senior Executive Vice President, Finance and Information Systems presents a report on risk exposure and significant off-balance sheet commitments to the Audit and Accounts Committee.

### Risk Management Committee

This committee, chaired by the Chairman and CEO, is responsible for defining the level of risk deemed acceptable by the Group, allocating risk management and control responsibilities for these risks, defining the strategy for transferring certain risks to insurance, approving the Group's risk mapping, and more generally, ensuring that the risk assessment and management system is as comprehensive as possible in order to maximise risk mitigation. It is supported by the work of the Risk Assessment Committee. In 2017, this committee met once.

### Risk Assessment Committee

This committee is chaired by the Senior Vice President, Audit, Risks & Internal Control. It is responsible for analysing risks and evolving threats; it updates and prioritises risk scenarios, ensuring that responsibility for each risk scenario is allocated within the Group, prepares risk maps and formulates recommendations for the Risk Management Committee, with a view to improving the overall management and mitigation of Group risks. In 2017, the Risk Assessment Committee met five times.

### Ethics and Corporate Responsibility Committee

This committee, chaired by the Company Secretary, is composed of representatives of the functional departments and the main countries in which the Group is based. Its work is focused on three areas:

- Strategy:
  - contribute to the definition of Thales's policy on Ethics and Corporate Responsibility,
  - identifying and making recommendations with regard to the standards and procedures concerning sales, environmental, human-resource-related and social issues;
- Ownership:
  - ensuring that the internal Codes are kept up to date and implemented within Thales,
  - defining training objectives and suitable means of communication,
  - coordinating and monitoring the Country Ethics Committees and ethics officers;
- Sharing:
  - holding discussions amongst its members on good practices, experiences and the ethical issues submitted to it.

In 2017, this committee met three times.

The Ethics and Corporate Responsibility department is responsible for the Group's actions in terms of ethics and responsibility, coordinating the relevant people within the Group, and ensuring that the ethical issues submitted to it are handled and followed up correctly, through an *ad hoc* committee where necessary.

### Group Internal Audit, Risks & Internal Control Department

Reporting to the Group General Secretary, the Audit, Risks & Internal Control Department principally works with the Audit and Accounts Committee, the Risk Management Committee, the Risk Assessment Committees, Group corporate management and the statutory auditors.

It ensures proper risk management and the maintenance of adequate internal control by conducting audits or providing guidance. It may have involvement throughout the Group (Thales parent company and its controlled subsidiaries) as well as with its non-controlled subsidiaries, with the agreement of the co-owner companies. Its scope of involvement covers all areas and processes (governance, administrative, accounting and financial, functional and operational, etc.).

Since 2006, the Audit, Risks & Internal Control Department has been certified by IFACI<sup>(1)</sup>, which ensures that its practices comply with the international auditing standards. The last IIA/IFACI triennial certification was obtained by the Audit, Risks & Internal Control Department in March 2016. The annual progress visit made by IFACI in March 2017 confirmed the Department's capacity and that of its auditors to coordinate their activities and operate in accordance with the prerequisites and the core principles of the internal audit profession.

The actions of the Audit, Risks & Internal Control Department are governed by an Internal Audit charter (updated in June 2016) that defines the basic principles of internal control and internal audit, the scope and limits of its responsibilities and its interaction with the entities.

In 2017, 63 audits or advisory engagements, arising from the Group's risk analysis and planned according to the criteria set out and approved by the Audit and Accounts Committee, were conducted by teams from the Audit, Risks & Internal Control Department. These engagements focused on the following themes:

- Operations: bids and projects, product policy, engineering and industry;
- Compliance: ethics, export control, security of information systems, business continuity plans;
- Governance: organisation, shared services, joint ventures, monitoring of acquisition and divestment transactions;
- Internal control: auditing the accuracy of risk management and internal control questionnaires (yearly attestation letter, internal control questionnaire).

### b) Audit of financial information

Each year, the Finance department reviews the financial audit manual with the statutory auditors. This manual describes the phases for the use of external auditors.

Consolidated companies are placed in one of three categories, according to their size and the risks to which they may be exposed. They may be subject to an in-depth review, a limited review or a review for statutory requirements.

In the first two types of review, as well as assessing the financial statements, the statutory auditors recommend improvements in terms of internal control. These recommendations are presented to Group management as part of the closure of the accounts at 31 December.

## 1.1.4 Human resources, environmental and social information

### Table of reconciliation (Articles L. 225-102-1 and R. 225-105-1 of the French Commercial Code)

In accordance with the Articles L. 225-102-1 and R. 225-105-1 of the French Commercial Code on transparency obligations for companies on social and environmental matters, in its management report, Thales provides information on the Group's social, environmental and societal

issues. This information is set out in full in Chapter 5 "Corporate responsibility"; an independent third-party verifier has issued a statement of completeness and limited assurance report on the consolidated social, environmental and societal information (see pages 199 *et seq.*).

(1) Institut Français de l'Audit et du Contrôle Interne (French Institute of Audit and Internal Control).

## 1.1.5 Events since year-end

Thales and Gemalto announced, with the publication of the Offer Document on 27 March 2018, that Thales is launching its recommended all-cash offer to all holders of issued and outstanding shares in the capital of Gemalto for EUR 51.00 per share, cum dividend.

## 1.1.6 Summary statement of transactions referred to in Article L. 621-18-2 of the French Monetary and Financial Code carried out in 2017

Details of the transactions carried out are set out in Section 4.2.3.7.

## 1.2 CONSOLIDATED FINANCIAL STATEMENTS

### 1.2.1 Consolidated profit and loss account

(in € millions)	Notes	2017	2016
<b>Sales</b>	Note 2	<b>15,795.4</b>	<b>14,884.8</b>
Cost of sales <sup>(a)</sup>		(11,951.2)	(11,276.8)
Research and development expenses		(802.2)	(736.1)
Marketing and selling expenses <sup>(a)</sup>		(1,040.6)	(1,023.2)
General and administrative expenses		(549.5)	(543.5)
Restructuring costs	Note 10.2	(81.1)	(100.5)
Amortisation of intangible assets acquired (PPA) <sup>(b)</sup>	Note 4.2	(113.0)	(107.3)
<b>Income from operations</b>	Note 2	<b>1,257.8</b>	<b>1,097.4</b>
Disposal of assets, changes in scope of consolidation and other	Note 3.2	(81.5)	205.1
Impairment on non-current assets		—	—
<b>Income of operating activities before share in net income of equity affiliates</b>		<b>1,176.3</b>	<b>1,302.5</b>
<b>Share in net income of equity affiliates</b>		<b>134.8</b>	<b>119.6</b>
• of which, share in net income of joint ventures	Note 5.1	88.5	72.4
• of which, share in net income of associates	Note 5.2	46.3	47.2
<b>Income of operating activities after share in net income of equity affiliates</b>		<b>1,311.1</b>	<b>1,422.1</b>
Interest expense on gross debt		(16.3)	(11.3)
Interest income on cash and cash equivalents		21.3	17.6
Interest income, net	Note 6.1	5.0	6.3
Other financial income (expenses)	Note 6.1	(99.3)	(80.6)
Finance costs on pensions and other employee benefits	Note 9.3	(65.5)	(77.6)
Income tax	Note 7.1	(264.2)	(255.6)
<b>NET INCOME</b>		<b>887.1</b>	<b>1,014.6</b>
Attributable to:			
<b>Shareholders of the parent company</b>		<b>821.7</b>	<b>946.4</b>
Non-controlling interests		65.4	68.2
Basic earnings per share (in euros)	Note 8.2	3.88	4.49
Diluted earnings per share (in euros)	Note 8.2	3.85	4.44

(a) The depreciation of net costs related to customer accounts was reclassified from marketing and selling expenses to cost of sales (a negative amount of €2.2 million in 2016).

(b) This item corresponds to the amortisation of acquired intangible assets (Purchase Price Allocation: PPA) of fully consolidated entities. The amortisation of PPA related to equity affiliates is included in the share in net income of equity affiliates and detailed in Note 2.1.

## 1.2.2 Consolidated statement of comprehensive income

(in € millions)	2017			2016		
	Total attributable to:		Total	Total attributable to:		Total
	shareholders of the parent company	non-controlling interests		shareholders of the parent company	non-controlling interests	
<b>NET INCOME</b>	<b>821.7</b>	<b>65.4</b>	<b>887.1</b>	<b>946.4</b>	<b>68.2</b>	<b>1,014.6</b>
Translation adjustment: subsidiaries (Note 8.1)	(88.5)	(1.9)	(90.4)	32.2	(0.3)	31.9
Deferred tax (Note 7.2)	–	–	–	1.3	–	1.3
Joint ventures (Note 5.1)	(7.9)	–	(7.9)	(26.9)	–	(26.9)
Associates (Note 5.2)	(17.5)	–	(17.5)	(30.7)	–	(30.7)
<b>Net</b>	<b>(113.9)</b>	<b>(1.9)</b>	<b>(115.8)</b>	<b>(24.1)</b>	<b>(0.3)</b>	<b>(24.4)</b>
Cash flow hedge: subsidiaries (Note 8.1)	384.2	17.2	401.4	49.5	3.0	52.5
Deferred tax (Note 7.2)	(107.5)	(5.5)	(113.0)	(17.4)	(1.5)	(18.9)
Joint ventures (Note 5.1)	(3.5)	–	(3.5)	(0.5)	–	(0.5)
Associates (Note 5.2)	(2.3)	–	(2.3)	0.5	–	0.5
<b>Net</b>	<b>270.9</b>	<b>11.7</b>	<b>282.6</b>	<b>32.1</b>	<b>1.5</b>	<b>33.6</b>
Available for sale financial assets: subsidiaries	(1.0)	–	(1.0)	3.5	–	3.5
Joint ventures (Note 5.1)	(6.7)	–	(6.7)	6.7	–	6.7
<b>Net</b>	<b>(7.7)</b>	<b>–</b>	<b>(7.7)</b>	<b>10.2</b>	<b>–</b>	<b>10.2</b>
<b>Items that may be reclassified to income</b>	<b>149.3</b>	<b>9.8</b>	<b>159.1</b>	<b>18.2</b>	<b>1.2</b>	<b>19.4</b>
Actuarial gains (losses) on pensions: subsidiaries (Note 9.3)	52.8	(3.4)	49.4	(658.1)	(2.9)	(661.0)
Deferred tax (Note 7.2)	2.9	0.3	3.2	22.6	(0.3)	22.3
Joint ventures (Note 5.1)	1.9	–	1.9	(12.7)	–	(12.7)
Associates (Note 5.2)	(0.7)	–	(0.7)	0.4	–	0.4
<b>Items that will not be reclassified to income</b>	<b>56.9</b>	<b>(3.1)</b>	<b>53.8</b>	<b>(647.8)</b>	<b>(3.2)</b>	<b>(651.0)</b>
<b>Other comprehensive income (loss) for the year, net of tax</b>	<b>206.2</b>	<b>6.7</b>	<b>212.9</b>	<b>(629.6)</b>	<b>(2.0)</b>	<b>(631.6)</b>
<b>TOTAL COMPREHENSIVE INCOME FOR THE YEAR</b>	<b>1,027.9</b>	<b>72.1</b>	<b>1,100.0</b>	<b>316.8</b>	<b>66.2</b>	<b>383.0</b>

## 1.2.3 Consolidated statement of changes in equity

(in € millions)	Number of shares outstanding (thousands)	Share capital	Additional paid-in capital	Retained earnings	Cash flow hedge	AFS investments	Cumulative translation adjustment	Treasury shares	Total attributable to shareholders of the parent company	Non-controlling interests	Total equity
<b>AT 1 JANUARY 2016</b>	<b>210,122</b>	<b>632.9</b>	<b>3,995.4</b>	<b>404.6</b>	<b>(276.8)</b>	<b>2.2</b>	<b>(87.2)</b>	<b>(25.2)</b>	<b>4,645.9</b>	<b>295.9</b>	<b>4,941.8</b>
Net income	—	—	—	946.4	—	—	—	—	946.4	68.2	1,014.6
Other comprehensive income	—	—	—	(647.8)	32.1	10.2	(24.1)	—	(629.6)	(2.0)	(631.6)
<b>Total comprehensive income for 2016</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>298.6</b>	<b>32.1</b>	<b>10.2</b>	<b>(24.1)</b>	<b>—</b>	<b>316.8</b>	<b>66.2</b>	<b>383.0</b>
Employee share issues	1,233	3.7	41.5	—	—	—	—	—	45.2	—	45.2
Parent company dividend distribution (Note 8.1)	—	—	—	(296.8)	—	—	—	—	(296.8)	—	(296.8)
Third-party share in dividend distribution of subsidiaries	—	—	—	—	—	—	—	—	—	(48.3)	(48.3)
Share-based payments (Note 9.4)	—	—	—	16.7	—	—	—	—	16.7	—	16.7
Acquisitions/disposals of treasury shares (Note 8.1)	90	—	—	(13.8)	—	—	—	(36.4)	(50.2)	—	(50.2)
Purchase of Raytheon stake in TRS SAS	—	—	—	(52.8)	—	—	—	—	(52.8)	(85.8)	(138.6)
Other	—	—	—	12.2	(5.8)	—	—	—	6.4	(0.6)	5.8
Changes in scope of consolidation	—	—	—	7.8	(0.2)	—	1.3	—	8.9	(1.5)	7.4
<b>AT 31 DECEMBER 2016</b>	<b>211,445</b>	<b>636.6</b>	<b>4,036.9</b>	<b>376.5</b>	<b>(250.7)</b>	<b>12.4</b>	<b>(110.0)</b>	<b>(61.6)</b>	<b>4,640.1</b>	<b>225.9</b>	<b>4,866.0</b>
Net income	—	—	—	821.7	—	—	—	—	821.7	65.4	887.1
Other comprehensive income	—	—	—	56.9	270.9	(7.7)	(113.9)	—	206.2	6.7	212.9
<b>Total comprehensive income for 2017</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>878.6</b>	<b>270.9</b>	<b>(7.7)</b>	<b>(113.9)</b>	<b>—</b>	<b>1,027.9</b>	<b>72.1</b>	<b>1,100.0</b>
Employee share issues	464	1.4	16.3	—	—	—	—	—	17.7	—	17.7
Parent company dividend distribution (Note 8.1)	—	—	—	(348.9)	—	—	—	—	(348.9)	—	(348.9)
Third-party share in dividend distribution of subsidiaries	—	—	—	—	—	—	—	—	—	(68.1)	(68.1)
Share-based payments (Note 9.4)	—	—	—	21.8	—	—	—	—	21.8	—	21.8
Acquisitions/disposals of treasury shares (Note 8.1)	181	—	—	(65.4)	—	—	—	9.1	(56.3)	—	(56.3)
Other	—	—	—	23.4	—	—	0.2	—	23.6	(0.3)	23.3
Changes in scope of consolidation	—	—	—	—	—	—	—	—	—	—	—
<b>AT 31 DECEMBER 2017</b>	<b>212,090</b>	<b>638.0</b>	<b>4,053.2</b>	<b>886.0</b>	<b>20.2</b>	<b>4.7</b>	<b>(223.7)</b>	<b>(52.5)</b>	<b>5,325.9</b>	<b>229.6</b>	<b>5,555.5</b>

## 1.2.4 Consolidated balance sheet

### Assets

(in € millions)	Notes	31/12/2017	31/12/2016
Goodwill, net	Note 4.1	3,447.2	3,424.4
Other intangible assets, net	Note 4.2	877.5	958.8
Property, plant and equipment, net	Note 4.2	1,819.1	1,798.9
<b>Total non-current operating assets</b>		<b>6,143.8</b>	<b>6,182.1</b>
Investments in joint ventures	Note 5.1	1,027.8	997.5
Investments in associates	Note 5.2	210.1	219.5
Non-consolidated investments	Note 6.3	87.7	82.3
Other non-current financial assets	Note 6.3	166.5	138.3
<b>Total non-current financial assets</b>		<b>1,492.1</b>	<b>1,437.6</b>
Non-current derivatives – assets	Note 6.5	17.0	27.9
Deferred tax assets	Note 7.3	858.1	975.8
<b>NON-CURRENT ASSETS</b>		<b>8,511.0</b>	<b>8,623.4</b>
Inventories and work in progress	Note 10.1	2,803.4	2,734.6
Construction contracts: assets	Note 10.1	2,306.0	2,331.5
Advances to suppliers	Note 10.1	451.8	348.3
Accounts, notes and other current receivables	Note 10.1	4,351.1	4,547.5
Current derivatives – assets	Note 6.5	254.4	161.7
<b>Total current operating assets</b>		<b>10,166.7</b>	<b>10,123.6</b>
Current tax receivable		36.6	59.8
Current financial assets	Note 6.2	332.0	265.9
Current derivatives – assets	Note 6.5	3.1	–
Cash and cash equivalents	Note 6.2	4,282.7	3,616.9
<b>Total current financial assets</b>		<b>4,617.8</b>	<b>3,882.8</b>
<b>CURRENT ASSETS</b>		<b>14,821.1</b>	<b>14,066.2</b>
<b>TOTAL ASSETS</b>		<b>23,332.1</b>	<b>22,689.6</b>

## Equity and liabilities

(in € millions)	Notes	31/12/2017	31/12/2016
Capital, additional paid-in capital and other reserves		5,602.1	4,811.7
Cumulative translation adjustment		(223.7)	(110.0)
Treasury shares		(52.5)	(61.6)
<b>Total attributable to shareholders of the parent company</b>		<b>5,325.9</b>	<b>4,640.1</b>
Non-controlling interests		229.6	225.9
<b>TOTAL EQUITY</b>	Note 8.1	<b>5,555.5</b>	<b>4,866.0</b>
Long-term loans and borrowings	Note 6.2	953.5	1,433.7
Non-current derivatives-liabilities	Note 6.5	2.6	–
Pensions and other long-term employee benefits	Note 9.3	2,674.3	2,785.8
Deferred tax liabilities	Note 7.3	237.6	294.6
<b>NON-CURRENT LIABILITIES</b>		<b>3,868.0</b>	<b>4,514.1</b>
Advances received from customers on contracts	Note 10.1	4,162.6	4,478.4
Refundable grants	Note 10.1	127.7	133.4
Construction contracts: liabilities	Note 10.1	1,278.3	1,139.4
Reserves for contingencies	Note 10.2	1,134.7	1,037.0
Accounts, notes and other current payables	Note 10.1	6,264.3	5,872.6
Current derivatives – liabilities	Note 6.5	179.7	478.3
<b>Total current operating liabilities</b>		<b>13,147.3</b>	<b>13,139.1</b>
Current tax payable		54.0	59.0
Short-term loans and borrowings	Note 6.2	707.3	111.4
<b>CURRENT LIABILITIES</b>		<b>13,908.6</b>	<b>13,309.5</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>23,332.1</b>	<b>22,689.6</b>

## 1.2.5 Consolidated statement of cash flows

(in € millions)	Notes	2017	2016
<b>Net income</b>		<b>887.1</b>	<b>1,014.6</b>
<b>Add (deduct):</b>			
Income tax expense (gain)		264.2	255.6
Net interest income		(5.0)	(6.3)
Share in net income of equity affiliates		(134.8)	(119.6)
Dividends received from equity accounted: joint ventures		38.5	43.6
Dividends received from equity accounted: associates		40.8	29.1
Depreciation and amortisation of property, plant and equipment and intangible assets	Note 4.2	391.1	384.6
Depreciation and amortisation of intangible assets acquired	Note 4.2	113.0	107.3
Provisions for pensions and other employee benefits	Note 9.3	191.7	170.5
Loss (gain) on disposal of assets, and other	Note 3.2	81.5	(205.1)
Provisions for restructuring, net	Note 10.2	(27.0)	(7.4)
Other items		(65.1)	31.4
<b>Operating cash flows before working capital changes, interest and tax</b>		<b>1,776.0</b>	<b>1,698.3</b>
Change in working capital and reserves for contingencies	Note 10.1	222.5	(63.4)
Cash contributions to pension plans and other long-term employee benefits	Note 9.3	(202.9)	(190.1)
• UK deficit payment		(82.3)	(88.3)
• recurring contributions/benefits		(120.6)	(101.8)
Interest paid		(14.0)	(21.1)
Interest received		22.3	13.6
Income tax paid		(90.6)	(99.4)
<b>NET CASH FLOW FROM OPERATING ACTIVITIES</b>	<b>- I -</b>	<b>1,713.3</b>	<b>1,337.9</b>
Acquisitions of property, plant and equipment and intangible assets		(438.9)	(480.3)
Disposals of property, plant and equipment and intangible assets		8.2	8.3
<b>Net operating investments</b>		<b>(430.7)</b>	<b>(472.0)</b>
Acquisitions of subsidiaries and affiliates, net	Note 6.4	(121.4)	(391.2)
Disposals of subsidiaries and affiliates, net	Note 6.4	41.9	296.9
Decrease (increase) in loans and non-current financial assets		(26.7)	(26.5)
Decrease (increase) in current financial assets		(70.8)	(235.6)
<b>Net financial investments</b>		<b>(177.0)</b>	<b>(356.4)</b>
<b>NET CASH FLOW USED IN INVESTING ACTIVITIES</b>	<b>- II -</b>	<b>(607.7)</b>	<b>(828.4)</b>
Parent company dividend distribution		(348.9)	(296.8)
Third party share in dividend distribution of subsidiaries		(68.1)	(48.3)
Capital increase (options exercised)		18.0	45.7
Purchase/sale of treasury shares		(56.3)	(40.8)
Issuance of debt		107.0	641.1
Repayment of debt		(32.9)	(643.7)
<b>Net financial debts</b>		<b>74.1</b>	<b>(2.6)</b>
<b>NET CASH FLOW USED IN FINANCING ACTIVITIES</b>	<b>- III -</b>	<b>(381.2)</b>	<b>(342.8)</b>
Effect of exchange rate variations and other	- IV -	(58.6)	-
<b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>I + II + III + IV</b>	<b>665.8</b>	<b>166.7</b>
Cash and cash equivalents at beginning of period		3,616.9	3,450.2
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>		<b>4,282.7</b>	<b>3,616.9</b>

The Group's net cash position and the changes from one period to the next are presented in Note 6.2.

## 1.2.6 Notes to the consolidated financial statements

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All monetary amounts included in these notes are expressed in millions of euros.

# NOTE 1. ACCOUNTING STANDARDS FRAMEWORK

Thales's consolidated financial statements for the year ended 31 December 2017 were approved and authorised for issue by its Board of Directors on 5 March 2018. In accordance with French legislation, the financial statements will be deemed to be definitive once they have been adopted by the shareholders of the Group at the Annual General Meeting to be held on 23 May 2018.

Thales (parent company) is a French joint-stock company (*société anonyme*) registered with the Nanterre Trade and Companies' Register under number 552 059 024.

## 1.1 Basis of preparation for the 2017 consolidated financial statements

Thales's consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS) approved by the European Union at 31 December 2017<sup>(1)</sup>.

These accounting policies, described in Note 13, are consistent with those applied by the Group for the year ended 31 December 2016. Furthermore, the new standards that were mandatory from 1 January 2017 (Amendments to IAS 12 – Income tax and Annual Improvements Cycle 2013-2016) have no impact on the Group's financial statements. The reconciliation for the changes in financial debts of balance sheet, and cash flow from financial activities as required in the amendments to IAS 7 (Cash Flow statement), is provided in Note 6.2-c.

## 1.2 New standards effective from 31 december 2017

The following standards have been adopted by the IASB and will be effective for the periods indicated below pending their adoption by the European Union:

Accounting standard	Description	First-time application	EU endorsement
IFRS 15 (Revenue from Contracts with Customers)	Supersedes standards IAS 18 (Revenue) and IAS 11 (Construction contracts) and the related interpretations	1 January 2018	Yes
IFRS 9 (Financial Instruments)	Supersedes all existing standards related to Financial instruments	1 January 2018	Yes
IFRS 16 (Leases)	Supersedes IAS 17. Removes the distinction between operating leases and finance leases, all contracts now being recognised on the balance sheet	1 January 2019	Yes
IFRIC 22 (Foreign Currency Transactions and Advance Consideration)	Clarifies the accounting for transactions that include the receipt or payment of advance consideration in a foreign currency	1 January 2018	In progress
IFRIC 23 (Uncertainty over Income Tax Treatments)	Refers to the recognition and measurement of financial risks related to income tax expense	1 January 2019	In progress
IFRS 2 amendments (Share-based Payments)	Provides a narrow-scope amendment for the classification and measurement of share-based payment transactions	1 January 2018	In progress
IAS 28 amendments (Long-term interests in associates and Joint Ventures)	Clarifies the rules applicable (particularly as regards depreciation and amortisation) to long-term investments in an associate	1 January 2019	In progress

(1) Available from: [https://ec.europa.eu/info/law/international-accounting-standards-regulation-ec-no-1606-2002\\_en](https://ec.europa.eu/info/law/international-accounting-standards-regulation-ec-no-1606-2002_en).

## Implementation of IFRS 15

The Group continued to work on the implementation of IFRS 15, which became mandatory as of 1 January 2018.

Thales has opted for the full retrospective approach; the financial statements for the first half of 2018 and for the full year 2018 will include the 2017 comparative financial statements adjusted for the

impact of applying the new standard. The opening balance sheet at 1 January 2017 will be presented, as adjusted.

In this context, the Group has estimated the impact of the new standard on the key indicators for 2017:

Group's key indicators	2017 Reported	Expected impacts IFRS 15	2017 Restated for IFRS 15
Order backlog	31,914.2	150.0	32,064.2
Order intake	14,919.6	11.6	14,931.2
Sales	15,795.4	(567.9)	15,227.5
Income from operations	1,257.8	(162.3)	1,095.5
Share in net income of equity affiliates	134.8	(14.9)	119.9
Net income, attributable to shareholders of the parent company	821.7	(141.9)	679.8

Segment information	2017 Reported	Expected impacts IFRS 15	2017 Restated for IFRS 15
<b>Aerospace</b>			
Sales	5,985.2	(237.9)	5,747.3
EBIT	601.5	(34.5)	567.0
<b>Transport</b>			
Sales	1,760.9	(37.6)	1,723.3
EBIT	71.6	(15.0)	56.6
<b>Defence &amp; Security</b>			
Sales	7,983.2	(293.5)	7,689.7
EBIT	868.5	(111.9)	756.6
<b>Other</b>			
Sales	66.1	1.1	67.2
EBIT	1.0	(15.8)	(14.8)
<b>Thales</b>			
<b>Sales</b>	<b>15,795.4</b>	<b>(567.9)</b>	<b>15,227.5</b>
<b>EBIT</b>	<b>1,542.6</b>	<b>(177.2)</b>	<b>1,365.4</b>

The main sources of differences between the current rules and IFRS 15 are the following:

### Order Backlog

IFRS 15 introduces the concept of accounting **order backlog** ("transaction price allocated to the remaining performance obligation"). This accounting definition compared to Thales current definition, does not lead to significant impact.

### Unbundling of multiple performance obligations within a single contract

In certain situations, IFRS 15 requires the unbundling of multiple performance obligations within a single contract, with differentiated margin rates. This is the case for some contracts combining construction and maintenance services, or construction and launch of a satellite. However, the impact of this restatement on the 2017 financial statements is limited.

### Recognition of revenue under the percentage of completion method

Under the current rules, revenue from construction contracts (representing over half the Group's revenue) is recognised according to the percentage of completion method.

IFRS 15 now provides for criteria proving the transfer of control over goods and services to the customer over time and allowing for the recognition of revenue under the percentage of completion method.

For complex sales of goods, it is necessary to demonstrate that the good sold has no alternative use and that the Group has an irrevocable right to payment for the work performed to date (corresponding to the costs incurred to date, plus a reasonable margin), in the event of termination for any reason other than Thales's failure to perform. Detailed analysis of the Group's contract portfolio has confirmed that, for the vast majority of contracts in progress, the criteria defined in IFRS 15 have been met.

In addition, as was the case before, revenue from services contracts will be recognised according to the percentage of completion method, with the customer receiving services as they are provided by Thales.

### Percentage of completion method

Currently, the revenue and margin of construction contracts are recognised as and when the technical milestones, which confirm effective progress of a part of the works or completion of the services specified in the contract, are achieved. Under IFRS 15, the percentage of completion method used is expense based: revenue is recognised based on costs incurred to date in relation to all the costs expected upon completion. For each contract, depending on the pace of performance and the

nature of the milestones achieved and costs incurred over the period, this change in method may cause shifts in revenue and margin recognition from one period to another.

### Bid cost

Bid cost which were previously included in contract costs, in accordance with IAS 11, are now expensed as incurred as a line item under "marketing and selling expenses".

### Other standards

The assessment of the potential impacts of these new standards for the Group's consolidated financial statements is underway.

The new IFRS 9 on financial instruments introduces:

- a new classification of financial assets based on the Group's management intention and the nature of expected flows;
- a dynamic impairment model for financial assets on expected losses;

- changes in rules relating to hedge accounting (and especially the treatment of the time value of options as a cost of hedging, which limits net income volatility).

This standard will come into effect on 1 January 2018. The review and analysis of the text is still in progress, but the Group does not at this stage anticipate any material impact on its consolidated financial statements.

The Group is also reviewing the new IFRS 16 "Leases", which is effective as from on 1 January 2019. This text, which replaces IAS 17 and the associated IFRIC and SIC interpretations, removes the distinction previously made between operating leases and finance leases. Under IFRS 16, a lessee recognises a right-of-use asset and a financial liability representative of the lease obligation. The right-of-use asset is amortised and the lease obligation is measured initially at the present value of the lease payments over the lease term, discounted at the rate implicit in the lease if that can be readily determined or at the incremental borrowing rate otherwise.

Work is under way to apply these new provisions, with most contracts concerning property leases.

## 1.3 Translation

The principal exchange rates used to translate financial statements of entities with a functional currency different from the euro are as follows:

Euro	31 December 2017		31 December 2016		31 December 2015	
	Closing rate	Average rate	Closing rate	Average rate	Closing rate	Average rate
Australian Dollar	1.5346	1.4795	1.4596	1.4852	1.4897	1.4837
Pound Sterling	0.8872	0.8757	0.8562	0.8227	0.7340	0.7242
U.S. Dollar	1.1993	1.1370	1.0541	1.1032	1.0887	1.1046

## 1.4 Main sources of estimates

The preparation of the Group's consolidated financial statements involves making estimates and assumptions, which have an impact on the valuation of the Group's performance and its consolidated assets and liabilities. These estimates are based on past experience and factor in the economic conditions prevailing at the end of the reporting period and any information available as of the date on which the financial statements are prepared.

In today's global economic environment, the degree of volatility and subsequent lack of visibility are particularly high. Future facts and circumstances could lead to changes in these estimates or assumptions which would affect the Group's financial situation, profit and loss and cash flows, notably with regard to:

### Construction contracts (Note 10.1)

A significant part of the Group's revenue and current operating income stems from construction contracts recognised according to the technical percentage of completion method. These contracts often span several financial years. In the accounting closing process, the recognition of income and expenses relating to these contracts depends mainly:

- on estimates of revenue and margin upon completion, including provisions for technical and commercial risks;
- technical milestones achieved in the performance of these contracts.

Estimates of figures upon completion, and the achievement of technical milestones, are based, for each contract, on the Group's internal systems and procedures, with the project managers playing a key role. These estimates are reviewed regularly by the Operations department and the Finance department, under the supervision of the Group's Corporate Management, particularly at each reporting period-end.

### Litigation (Note 11)

The Group conducts its business in France and abroad in complex, evolving legal and regulatory environments. As a result, it is exposed to legal, technical and commercial disputes.

The Group regularly identifies and reviews litigation in progress and recognises the accounting provisions that it considers to be reasonable in light of the circumstances. Any uncertainties concerning litigation in progress are described in Note 11.

### Business combinations

Business combinations are accounted for in accordance with the purchase accounting method described in Note 13-b: on the date of the takeover of a company, the acquiree's identifiable assets, liabilities and contingent liabilities are measured at their fair value. These valuations are performed by independent experts who base their work on assumptions and estimate the effects of future events, which are uncertain at the acquisition date.

### Goodwill (Note 4.1)

Goodwill is subject to impairment tests. The recoverable amount of goodwill is assessed based on forecast data from the strategic plans prepared in accordance with Group procedures. Sensitivity tests are carried out on key assumptions which lend greater weight to the conclusions reached.

### Pensions and other long-term employee benefits (Note 9.3)

Pensions and other long-term employee benefit commitments are estimated on statistical and actuarial bases in accordance with the policies outlined in the Note 13-j. Actuarial assumptions made by the Group (discount rates, inflation rate, mortality tables, etc.) are reviewed each year with the Group's actuaries.

### Deferred tax assets (Note 7)

Deferred tax assets are recognised for tax loss carryforwards and temporary differences between the book value and the tax value of assets and liabilities. Recovery of these assets is assessed on the basis of the forecast data in the strategic plans of each of the tax groups considered, and generally over a period of five years.

## NOTE 2. SEGMENT INFORMATION

### 2.1 Information by business segment

The operational segments presented by the Group are as follows:

- the **Aerospace** segment, which combines the “Avionics” and “Space” Global Business Units that develop on-board systems, solutions and services, mainly for private sector customers (aircraft manufacturers, airlines, satellite operators, etc.) but also to a lesser extent for government/defence customers (states, space agencies and other semi-public organisations);
- the **Transport** segment, which comprises the “Ground Transportation Systems” Global Business Unit that develops systems and services for an exclusively civilian customer base of ground transportation infrastructure operators;

- the **Defence and Security** segment, which combines the “Secure Communications and Information Systems”, “Land and Air Systems” and “Defence Mission Systems” Global Business Units that develop equipment, systems and services for the armed and security forces and for the protection of networks and infrastructures, mainly for a government/defence customer base.

In order to monitor the operating and financial performance of the Group entities, the Group’s executives regularly consider certain key non-GAAP indicators as defined in Note 13-a, which enable them to exclude certain non-operating and non-recurring items.

In particular, EBIT, presented by business segment below, corresponds to income from operations plus the share in net income of equity affiliates, excluding amortisation of acquisition-related intangible assets (purchase price allocation – PPA) reported under business combinations. It also excludes other expenses booked to income from operations that are directly linked to business combinations, which are unusual by nature.

2017	Aerospace	Transport	Defence & Security	Other, elim., and unallocated <sup>(a)</sup>	Thales
Order backlog – non-Group	8,850.0	4,390.5	18,605.3	68.3	31,914.2
Order intake – non-Group	5,199.9	1,780.3	7,882.8	56.6	14,919.6
Sales – non-Group	5,985.2	1,760.9	7,983.2	66.1	15,795.4
Sales – intersegment	91.9	8.6	306.3	(406.8)	–
<b>Total sales</b>	<b>6,077.1</b>	<b>1,769.5</b>	<b>8,289.5</b>	<b>(340.7)</b>	<b>15,795.4</b>
EBIT	601.5	71.6	868.5	1.0	1,542.6
Of which, Naval Group	–	–	–	47.9	47.9
Of which, excluding Naval Group	601.5	71.6	868.5	(46.9)	1,494.7
Capital expenditures	137.7	7.5	140.3	153.4	438.9
Dep. and amort. of property, plant and equipment and intangible assets	166.4	10.0	103.8	110.9	391.1

2016	Aerospace	Transport	Defence & Security	Other, elim., and unallocated <sup>(a)</sup>	Thales
Order backlog – non-Group	9,913.6	4,567.1	18,972.7	76.8	33,530.2
Order intake – non-Group	5,872.3	1,503.5	9,063.1	75.4	16,514.3
Sales – non-Group	5,812.0	1,602.8	7,390.2	79.8	14,884.8
Sales – intersegment	93.9	5.6	295.0	(394.5)	–
<b>Total sales</b>	<b>5,905.9</b>	<b>1,608.4</b>	<b>7,685.2</b>	<b>(314.7)</b>	<b>14,884.8</b>
EBIT	571.3	11.3	787.4	(15.5)	1,354.5
Of which, Naval Group	–	–	–	33.8	33.8
Of which, excluding Naval Group	571.3	11.3	787.4	(49.3)	1,320.7
Capital expenditures	147.0	10.3	126.4	196.6	480.3
Dep. and amort. of property, plant and equipment and intangible assets	182.5	8.3	95.3	98.5	384.6

(a) Data related to order backlog, order intake and sales included in the “Other, elim and non-allocated” column relate to Corporate activities (Thales parent company, Thales Global Services, Group R&D centers, facilities management) and the elimination of transactions between the business segments.

Non-allocated EBIT includes the Group’s share (35%) in the net income of Naval Group (ex DCNS), corporate income from operations not assigned to the segments and the cost of vacant premises. Other costs (mainly the costs of foreign holding companies not invoiced and expenses related to share-based payments) are reallocated to the business segments proportionally to their respective sales (excluding Group).

The reconciliation between income from operations and EBIT is analysed as follow:

	2017	2016
Income from operations	1,257.8	1,097.4
Share in net income of equity affiliates	134.8	119.6
<b>Sub-total</b>	<b>1,392.6</b>	<b>1,217.0</b>
PPA amortisation related to fully consolidated entities	113.0	107.3
PPA amortisation related to equity affiliates	19.2	11.2
Expenses linked directly to business combinations	17.8	19.0
<b>EBIT</b>	<b>1,542.6</b>	<b>1,354.5</b>

## 2.2 Information by destination

Consolidated order intake (direct and indirect) by destination	2017	2016
France	4,502.6	3,509.2
United Kingdom	1,153.3	1,003.2
Rest of Europe	2,918.5	3,646.3
<b>Europe</b>	<b>8,574.4</b>	<b>8,158.7</b>
<b>United States and Canada</b>	<b>1,579.2</b>	<b>1,215.6</b>
<b>Australia and New Zealand</b>	<b>670.8</b>	<b>763.7</b>
Asia	2,097.0	3,708.5
Middle East <sup>(a)</sup>	1,206.0	1,673.9
Rest of the world <sup>(a)</sup>	792.2	993.9
<b>Emerging markets</b>	<b>4,095.2</b>	<b>6,376.3</b>
<b>TOTAL</b>	<b>14,919.6</b>	<b>16,514.3</b>

Sales (direct and indirect) by destination	2017	2016
France	3,840.0	3,580.6
United Kingdom	1,351.9	1,272.3
Rest of Europe	3,386.9	3,227.1
<b>Europe</b>	<b>8,578.8</b>	<b>8,080.0</b>
<b>United States and Canada</b>	<b>1,459.6</b>	<b>1,555.9</b>
<b>Australia and New Zealand</b>	<b>875.0</b>	<b>759.2</b>
Asia	2,218.8	2,047.9
Middle East <sup>(a)</sup>	1,641.5	1,515.0
Rest of the world <sup>(a)</sup>	1,021.7	926.8
<b>Emerging markets</b>	<b>4,882.0</b>	<b>4,489.7</b>
<b>TOTAL</b>	<b>15,795.4</b>	<b>14,884.8</b>

(a) The 2016 figures have been adjusted to reflect the transfer of some countries out to the "Near and Middle East" region into the "Rest of the world" region within the Group's organisation.

## 2.3 Sales by category of contracts

More than half of the Group's sales come from contracts specifically negotiated with the customer, who draws up the technical specifications and defines the specific provisions linked to the contract. These contracts meet different needs depending on the customer, and are generally long-term contracts.

	2017	2016
Construction contracts	8,089.6	7,312.7
Sales of goods and equipment	3,523.8	3,549.3
Services	4,110.7	3,951.3
Other	71.3	71.5
<b>TOTAL</b>	<b>15,795.4</b>	<b>14,884.8</b>

## NOTE 3. IMPACT OF CHANGES IN SCOPE OF CONSOLIDATION

### 3.1 Main changes in scope of consolidation

#### In 2017:

In September 2017, Thales finalised the acquisition of the US company Guavus, one of the pioneers of real-time "big data" analytics, for a maximum enterprise value of \$215 million, subject to the achievement of significant sales growth targets. The net cash outflow reached \$109.1 million (€90.5 million) at the closing date. The purchase price was allocated to amortisable intangible assets in the amount of \$84.2 million (mainly technology acquired) and a deferred tax liability of \$32 million. Residual goodwill amounted to \$72.2 million (€60 million). The Company is fully consolidated.

In December 2017, Thales signed an agreement with the aim of acquiring Gemalto and creating a world leader in digital security. The offer, priced at €51 per share cum dividend (i.e. a total equity value of approximately €4.8bn) is subject to customary regulatory approvals. It is expected to be completed in the second half of 2018.

#### In 2016:

At the end of March 2016, Thales finalised the acquisition of Vormetric, a leading provider of data protection solutions for a total of \$408 million (€372.4 million). Vormetric has been consolidated since its acquisition.

As part of the transaction, Thales signed compensation agreements with key managers subject to their remaining with the company until 2020. The related amounts are being taken to income on a straight-line basis in tranches over the vesting period. These amounts are recognised in income from operations, but excluded from EBIT as they concern an event that is unusual nature (Note 2.1).

At the end of June 2016, Thales acquired Raytheon's non-controlling interest in French company TRS SAS and sold its stake in US company TRS LLC to Raytheon for a net gain of \$90 million (€81 million) in Thales' consolidated financial statements.

In Thales' consolidated financial statements, the acquisition of Raytheon's non-controlling interest in TRS SAS led to a reclassification in equity. The disposal of the interest in TRS LLC resulted in a disposal gain of €91.8 million. Thales-Raytheon Systems Air and Missile Defense Command remains jointly owned by the Group and is accounted for under the equity method.

In October 2016, Thales sold its interest in Hanwha Thales, a jointly-owned company that specialises in defence electronics in Korea, for €204.4 million. The disposal gain recognised in the consolidated financial statements amounted to €113.8 million.

### 3.2 Disposal of assets, changes in scope of consolidation and other

	2017	2016
<b>Disposal of investments</b>	<b>1.3</b>	<b>200.5</b>
Hanwha-Thales (50%)	—	113.8
Thales Raytheon Systems LLC (50%)	—	91.8
Other	1.3	(5.1)
<b>Disposal of real estate and movable assets</b>	<b>2.6</b>	<b>4.6</b>
<b>Impact of settlements/amendments to pensions plans (Note 9.3)</b>	<b>(21.2)</b>	<b>—</b>
<b>Litigation (Note 11)</b>	<b>(64.2)</b>	<b>—</b>
<b>TOTAL</b>	<b>(81.5)</b>	<b>205.1</b>

## NOTE 4. PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

### 4.1 Goodwill

#### a) Change in goodwill

Goodwill is allocated to cash-generating units (CGUs) or groups of CGUs corresponding to Thales' Global Business Units (GBU). The changes in goodwill attributable to fully consolidated subsidiaries is presented below.

	31/12/2016	Acquisitions	Disposals	Impairment	Changes in exchange rates and other	31/12/2017
Avionics	476.1	11.3	—	—	(15.2)	472.2
Space	481.8	8.6	—	—	(1.8)	488.6
<b>Aerospace</b>	<b>957.9</b>	<b>19.9</b>	<b>—</b>	<b>—</b>	<b>(17.0)</b>	<b>960.8</b>
<b>Transport</b>	<b>875.3</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>875.3</b>
Secure Communications & Information Systems	819.4	60.4 <sup>(a)</sup>	(7.0)	—	(30.8)	842.0
Land and Air Systems	309.8	—	—	—	(0.2)	309.6
Defence Mission Systems	462.0	—	—	—	(2.5)	459.5
<b>Defence and Security</b>	<b>1,591.2</b>	<b>60.4</b>	<b>(7.0)</b>	<b>—</b>	<b>(33.5)</b>	<b>1,611.1</b>
<b>TOTAL</b>	<b>3,424.4</b>	<b>80.3</b>	<b>(7.0)</b>	<b>—</b>	<b>(50.5)</b>	<b>3,447.2</b>

	31/12/2015	Acquisitions	Disposals	Impairment	Changes in exchange rates and other	31/12/2016
Avionics	472.0	—	—	—	4.1	476.1
Space	472.7	11.1	—	—	(2.0)	481.8
<b>Aerospace</b>	<b>944.7</b>	<b>11.1</b>	<b>—</b>	<b>—</b>	<b>2.1</b>	<b>957.9</b>
<b>Transport</b>	<b>875.3</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>875.3</b>
Secure Communications & Information Systems	625.1	189.9 <sup>(b)</sup>	—	—	4.4	819.4
Land and Air Systems	309.8	—	—	—	—	309.8
Defence Mission Systems	461.0	—	—	—	1.0	462.0
<b>Defence and Security</b>	<b>1,395.9</b>	<b>189.9</b>	<b>—</b>	<b>—</b>	<b>5.4</b>	<b>1,591.2</b>
<b>TOTAL</b>	<b>3,215.9</b>	<b>201.0</b>	<b>—</b>	<b>—</b>	<b>7.5</b>	<b>3,424.4</b>

(a) Goodwill on Guavus after purchase price allocation (may not be definitive).

(b) Goodwill on Vormetric after purchase price allocation.

#### b) Impairment tests

Goodwill is subject to annual impairment tests in accordance with the Group's budgetary timetable. Value in use is determined on the basis of discounted future operating cash flows over a three-year period and a terminal value. This calculation is based on data from the strategic plans prepared in accordance with Group procedures. In certain specific cases (recent acquisitions, non-typical annual results, etc.), the terminal value is determined based on forecasts over an appropriate period of time.

At end-2017 and end-2016, impairment tests were performed with the initial assumption of a 8.5% discount rate for all CGUs (each of which presented a similar degree of risk given that the specific CGU risks are factored into forecasts).

The assumptions used concern growth in sales and terminal values and are based on reasonable estimations in line with specific data available for each business sector (generally, terminal value is based on the average income from operations over the three years of the strategic plan, with growth capped at 2%).

At end-2017, the overall value in use of the group CGUs was higher than its carrying amount.

#### c) Sensitivity of values in use

The Group also tests the sensitivity of values in use based on reasonable key assumptions. At the end of 2017, a 1% increase in the discount rate, a 1% decrease in the growth rate or a 2% decrease in operating profitability of the group CGUs would not require any additional impairments.

## 4.2 Plant, property and equipment and other intangible assets

### a) Change in net assets

	Acquired intangible assets (PPA)	Development costs	Other intangible assets	Property, plant and equipment	Total
<b>Net value at 1 January 2016</b>	<b>649.2</b>	<b>123.3</b>	<b>90.4</b>	<b>1,696.7</b>	<b>2,559.6</b>
Acquisitions/increases	–	6.6	45.1	428.6	480.3
Disposals	–	–	–	(8.3)	(8.3)
Amortisation of acquisition-related intangible assets	(107.3)	–	–	–	(107.3)
Other depreciation and amortisation	–	(48.1)	(39.1)	(297.4)	(384.6)
Changes in scope, exchange rates and other	232.0	(2.5)	9.2	(20.7)	218.0
<b>Net value at 31 December 2016</b>	<b>773.9</b>	<b>79.3</b>	<b>105.6</b>	<b>1,798.9</b>	<b>2,757.7</b>
Acquisitions/increases	–	10.4	55.5	373.0	438.9
Disposals	–	–	–	(8.2)	(8.2)
Amortisation of acquisition-related intangible assets	(113.0)	–	–	–	(113.0)
Other depreciation and amortisation	–	(35.0)	(40.5)	(315.6)	(391.1)
Changes in scope, exchange rates and other	33.7	(2.5)	10.1	(29.0)	12.3
<b>NET VALUE AT 31 DECEMBER 2017</b>	<b>694.6</b>	<b>52.2</b>	<b>130.7</b>	<b>1,819.1</b>	<b>2,696.6</b>

### b) Breakdown by item

	31/12/2017		31/12/2016
	Gross	Depr., amort., and impairment	Net
Technologies acquired	849.7	(416.3)	433.4
Customer relationships acquired	555.8	(322.3)	233.5
Order backlog acquired	271.7	(253.7)	18.0
Other	71.3	(61.6)	9.7
<b>Intangible assets acquired (business combinations)</b>	<b>1,748.5</b>	<b>(1,053.9)</b>	<b>694.6</b>
Development costs	867.6	(815.4)	52.2
Other	780.5	(649.8)	130.7
<b>Intangible assets</b>	<b>3,396.6</b>	<b>(2,519.1)</b>	<b>877.5</b>
Land	52.6	(0.8)	51.8
Buildings	1,681.7	(924.1)	757.6
Technical facilities and industrial equipment and tooling	2,424.5	(1,809.1)	615.4
Other	1,135.8	(741.5)	394.3
<b>Property, plant and equipment</b>	<b>5,294.6</b>	<b>(3,475.5)</b>	<b>1,819.1</b>

## 4.3 Lease commitments

Irrevocable lease and rental commitments at 31 December 2017 and 2016 are as follows:

Irrevocable rental commitments	Total	Less than 1 year	1 to 5 years	More than 5 years
<b>31 December 2017</b>	<b>1,190.5</b>	201.7	566.1	422.7
31 December 2016	1,345.4	212.5	615.9	517.0

## NOTE 5. INVESTMENTS IN JOINT VENTURES AND ASSOCIATES

### 5.1 Joint ventures

#### a) Group share in net equity and net income of joint ventures

	Investments in joint ventures		Share in net income		Share in comprehensive income	
	31/12/2017	31/12/2016	2017	2016	2017	2016
Naval Group (35%)	730.7	713.9	29.1	23.9	18.0	26.9
Other joint ventures <sup>(a)</sup>	297.1	283.6	59.4	48.5	54.3	12.1
<b>TOTAL</b>	<b>1,027.8</b>	<b>997.5</b>	<b>88.5</b>	<b>72.4</b>	<b>72.3</b>	<b>39.0</b>

(a) Not individually material, the value of each investment representing less than 10% of the total.

#### b) Change in investments in joint ventures

	31/12/2017	31/12/2016
<b>Investment at 1 January</b>	<b>997.5</b>	<b>1,126.4</b>
Share in net income of joint ventures	88.5	72.4
Translation adjustment	(7.9)	(26.9)
Cash flow hedge	(3.5)	(0.5)
Available for sale financial assets	(6.7)	6.7
Actuarial gains (losses) on pensions	1.9	(12.7)
<b>Share in comprehensive income</b>	<b>72.3</b>	<b>39.0</b>
Dividends paid	(38.5)	(43.6)
Scope variation (Hanwha Thales Co., Ltd in 2016)	(2.6)	(112.3)
Other	(0.9)	(12.0)
<b>INVESTMENTS AT 31 DECEMBER</b>	<b>1,027.8</b>	<b>997.5</b>

#### c) Naval Group summary financial information

Thales has a 35% stake in the share capital of Naval Group, a subsidiary jointly controlled with the French State. Naval Group is a French industrial group specialised in naval defence and marine infrastructures.

The financial statements of Naval Group, after Thales restatements (mainly linked to acquisition-related intangible assets) are presented below:

<b>Summary balance sheet based on a 100% interest</b>	<b>31/12/2017</b>	<b>31/12/2016</b>
Non-current assets	2,057.3	2,359.9
Current assets	5,947.0	6,078.9
<b>Total assets</b>	<b>8,004.3</b>	<b>8,438.8</b>
Restated equity attributable to shareholders of the Company	1,253.5	1,205.3
Non-controlling interests	(13.0)	86.2
Non-current liabilities	601.2	649.6
Current liabilities	6,162.6	6,497.7
<b>Total equity and liabilities</b>	<b>8,004.3</b>	<b>8,438.8</b>

Consolidation by Thales	31/12/2017	31/12/2016
Restated equity attributable to shareholders of the Company	1,253.5	1,205.3
% of Thales' interests	35%	35%
Thales' share	438.7	421.9
Goodwill	292.0	292.0
<b>Share in net assets of the joint venture</b>	<b>730.7</b>	<b>713.9</b>

Summary profit and loss account based on a 100% interest	2017	2016
Sales	3,698.2	3,191.2
Income (loss) from operating activities after impact of equity affiliates <sup>(a)</sup>	56.5	4.3
Financial income	2.4	23.9
Tax	(85.9)	33.3
<b>Restated net income<sup>(a)</sup></b>	<b>(27.0)</b>	<b>61.5</b>
• of which, attributable to shareholders of the Company	83.2	68.3
• of which, non-controlling interests	(110.2)	(6.8)

(a) After Thales restatements (mainly linked to acquisition-related intangible assets).

Consolidation by Thales	2017	2016
Restated net income attributable to shareholders of the Company	83.2	68.3
% of Thales' interests	35%	35%
<b>Share in income of the joint venture</b>	<b>29.1</b>	<b>23.9</b>
• of which, impact of PPA	(18.8)	(9.9)
• of which, share in income before PPA	47.9	33.8
<b>Dividends received from the joint venture</b>	<b>—</b>	<b>—</b>

#### d) Commitments toward joint ventures

At 31 December 2017, outstanding sureties, endorsements and guarantees granted by Thales S.A. (parent company) to its joint ventures amounted to €321.9 million (€238.3 million at 31 December 2016).

The Group's policy is to issue guarantees on commitments by joint ventures in proportion to its equity interest, or to secure counter-guarantees from the other shareholders in proportion to their interest.

#### e) Transactions with joint ventures (related parties)

The volume of transactions with joint ventures and their joint shareholders is as follows:

	2017	2016
Sales	520.3	559.7
Purchases	202.9	189.7
Loans and current accounts receivable	45.8	47.5
Borrowings and current accounts payable	5.8	12.4

## 5.2 Associates

The main associates are listed in Note 16. None of these companies is individually material with regard to consolidated aggregates. The mandatory disclosures are therefore presented in aggregate form in the table below:

### a) Changes in investment in associates

	31/12/2017	31/12/2016
<b>Investments in associates at 1 January</b>	<b>219.5</b>	<b>359.5</b>
Share in net income of equity affiliates	46.3	47.2
Translation adjustment	(17.5)	(30.7)
Cash flow hedge	(2.3)	0.5
Actuarial gains (losses) on pensions	(0.7)	0.4
<b>Total comprehensive income</b>	<b>25.8</b>	<b>17.4</b>
Dividends paid	(40.8)	(29.1)
Changes in scope (TRS LLC in 2016)	—	(127.8)
Other	5.6	(0.5)
<b>INVESTMENTS IN ASSOCIATES AT 31 DECEMBER</b>	<b>210.1</b>	<b>219.5</b>

### b) Commitments towards associates

The Group has no material off-balance sheet commitments towards associates.

## NOTE 6. FINANCING AND FINANCIAL INSTRUMENTS

### 6.1 Financial income

#### a) Net interest income

	2017	2016
<b>Interest expense:</b>		
• on gross debt	(24.3)	(36.4)
• on interest rate swaps	8.0	25.1
	(16.3)	(11.3)
Interest income/cash and cash equivalents	21.3	17.6
<b>TOTAL</b>	<b>5.0</b>	<b>6.3</b>

#### b) Other financial income

	2017	2016
Foreign exchange gains (losses)	(17.4)	(2.4)
Cash flow hedge, ineffective portion	(10.9)	(5.9)
Change in fair value of currency derivatives <sup>(a)</sup>	(69.9)	(70.3)
<b>Foreign exchange gains (losses)</b>	<b>(98.2)</b>	<b>(78.6)</b>
Dividends received	2.6	2.8
Impairment of non consolidated investments, loans and other financial assets	(0.2)	(1.4)
Other	(3.5)	(3.4)
<b>TOTAL</b>	<b>(99.3)</b>	<b>(80.6)</b>

(a) Includes the change in the fair value of premiums/discounts (losses of €65.3 million in 2017 and €54.0 million in 2016), the time value of derivatives documented as future cash flow hedges (losses of €5.7 million in 2017 and €7.3 million in 2016), as well as changes in the fair value of derivatives not documented as hedges.

## 6.2 Net cash (net debt)

Group net cash is as follows:

	31/12/2017	31/12/2016
Current financial assets	332.0	265.9
Cash and cash equivalents	4,282.7	3,616.9
<b>Cash and other short-term investments (I)</b>	<b>4,614.7</b>	<b>3,882.8</b>
Borrowings and debt, long-term portion	953.5	1,433.7
Borrowings and debt, short-term portion	707.3	111.4
Fair value of interest rate derivatives <sup>(a)</sup>	(17.5)	(27.9)
<b>Gross debt (II)</b>	<b>1,643.3</b>	<b>1,517.2</b>
<b>NET CASH (I-II)</b>	<b>2,971.4</b>	<b>2,365.6</b>

(a) The value of borrowings documented as fair value hedges takes into account changes in the fair value of the hedged risk. This change in the value of the debt is offset by the remeasurement of interest-rate swaps used as hedges (Note 6.5).

### a) Current financial assets

	31/12/2017	31/12/2016
Current accounts receivable with related parties	3.1	8.5
Marketable securities	325.0	250.0
Accrued interest	3.9	7.4
<b>CURRENT FINANCIAL ASSETS</b>	<b>332.0</b>	<b>265.9</b>

Marketable securities consist of investments in short-term deposits (3 to 12 months) with tier-one banks.

### b) Cash and cash equivalents

At 31 December 2017, cash recorded under consolidated assets amounted to €4,282.7 million (€3,616.9 million in 2016) and included:

- €3,450.5 million held by the parent company and available for immediate use (€3,183.1 million in 2016). These amounts include €2,199.2 million (€2,886.2 million in 2016) in very short-term deposits with tier-one banks or money market funds;
- €832.2 million in the credit balances of subsidiaries (€433.8 million in 2016), most of them outside France. This figure includes payments received in the last days of the financial year and subsequently transferred to the cash pooling account.

### c) Borrowings and debt

	31/12/2017	31/12/2016
Bond maturing in 2023	593.9	595.6
Bond maturing in 2021	312.0	315.9
Bond maturing in 2018	500.6	502.8
Interest rate derivatives (Note 6.5)	(17.5)	(27.9)
Current accounts in credit with related parties <sup>(a)</sup>	115.2	48.7
Bank overdrafts	62.0	36.6
Subscription commitments	43.8	11.2
Other debt	33.3	34.3
<b>GROSS DEBT</b>	<b>1,643.3</b>	<b>1,517.2</b>

(a) Of which, at the end of 2017, €103.6 million toward Leonardo (€32.2 million at the end of 2016).

## Gross debt's evolution

	31/12/2016	Other changes				31/12/2017
		Cash flow	Scope	Exchange rates	Fair value and other	
<b>Gross debt</b>	<b>1,517.2</b>	74.1	51.7	(4.4)	4.7	<b>1,643.3</b>

Nature of bonds	Nominal value	Maturity	Nature	Nominal rate (excluding impact of hedging)	Effective rate (excluding impact of hedging)
Bond maturing in 2023	€600 million	June 2023	Fixed incl. €400 million swapped at variable rates	0.75%	0.84%
Bond maturing in 2021	€300 million	March 2021	Fixed incl. €300 million swapped at variable rates	2.25%	2.40%
Bond maturing in 2018	€500 million	March 2018	Fixed incl. €300 million swapped at variable rates	1.625%	1.74%

In January 2018, Thales issued a €500 million 0.75% fixed-rate bond maturing in 7 years. This issue will be used in particular to refinance the bond maturing in March 2018.

## Breakdown of gross debt by maturity

31/12/2017	Total	2018	2019	2020	2021	> 2021
<b>Gross debt<sup>(a)</sup></b>	<b>1,643.3</b>	704.2	45.3	1.4	295.5	596.9
<b>Contractual cash flows</b>	<b>1,684.6</b>	700.9	51.0	9.7	309.8	613.2

(a) After deduction of fair value of interest-rate derivatives.

31/12/2016	Total	2017	2018	2019	2020	> 2020
<b>Gross debt<sup>(a)</sup></b>	<b>1,517.2</b>	111.4	509.4	4.3	1.4	890.7
<b>Contractual cash flows</b>	<b>1,572.3</b>	106.9	523.4	11.1	8.9	922.0

(a) After deduction of fair value of interest-rate derivatives.

## Breakdown of gross debt by currency

	31/12/2017	31/12/2016
Euro	1,538.9	1,468.6
Livre sterling	9.4	13.7
US Dollar	38.6	11.6
Other	56.4	23.3
<b>TOTAL</b>	<b>1,643.3</b>	<b>1,517.2</b>

After impact of the related derivative instruments.

## 6.3 Non-current financial assets

### a) Non-consolidated investments

	%	31/12/2017	31/12/2016
Investments held by Thales International Offsets <sup>(a)</sup>	N/A	14.2	28.0
Other <sup>(b)</sup>		73.5	54.3
<b>TOTAL</b>		<b>87.7</b>	<b>82.3</b>

(a) Group subsidiary in charge of negotiating and implementing indirect offset obligations.

(b) Investments of less than €25 million, including Tronics Microsystems and Spaceflight Industries investments at 31 December 2017, and Aviovision, and Tronics Microsystems investments at 31 December 2016.

## b) Non-current financial assets

	31/12/2017	31/12/2016
Loans to related parties	88.2	86.6
Loans to employee shareholding	21.2	0.3
Loans and other financial assets at amortised cost	40.0	37.1
Loans and other financial assets at market value	22.0	19.3
<b>Gross value</b>	<b>171.4</b>	<b>143.3</b>
Impairment	(4.9)	(5.0)
<b>NET</b>	<b>166.5</b>	<b>138.3</b>

## 6.4 Changes in net cash

	2017	2016
<b>Net cash (debt) at 1 January</b>	<b>2,365.6</b>	<b>1,977.6</b>
Net cash flow from operating activities	1,713.3	1,337.9
Less, reduction in pension deficits	82.3	88.3
Net operating investments	(430.7)	(472.0)
<b>Free Operating cash-flow</b>	<b>1,364.9</b>	<b>954.2</b>
Acquisitions of subsidiaries and affiliates:	(121.4)	(391.2)
• including, Guavus	(90.5)	–
• including, Vormetric	–	(365.4)
Disposals of subsidiaries and affiliates	41.9	296.9
• including, Hanwha Thales Co. Ltd (50%)	–	204.4
• including, equalisation payment/Thales – Raytheon Systems	–	81.0
Less, reduction of U.K. pension deficits	(82.3)	(88.3)
Changes in loans	(26.7)	(26.5)
Dividends paid by the parent company	(348.9)	(296.8)
Third party share in dividend distributions of subsidiaries	(68.1)	(48.3)
Treasury shares and subscription options exercised	(38.3)	4.9
Changes in exchange rates: translation and financing operations	(63.6)	(19.8)
Other	(51.7)	2.9
<b>Total change</b>	<b>605.8</b>	<b>388.0</b>
<b>Net cash (debt) at 31 December</b>	<b>2,971.4</b>	<b>2,365.6</b>

## 6.5 Fair value of financial assets and liabilities

	31/12/2017					31/12/2016	
	At cost/ amortised cost	Fair value through: Equity	Profit or loss	Value in balance sheet	Fair value	Value in balance sheet	Fair value
<b>Non-current financial assets</b>							
Non-consolidated investments	–	87.7	–	87.7	87.7	82.3	82.3
Non-current loans and financial assets	144.5	–	22.0	166.5	166.5	138.3	138.3
Non-current derivatives documented as hedges	–	–	17.0	17.0	17.0	27.9	27.9
<b>Current financial assets</b>							
Derivative instruments documented as hedges	–	246.7	3.1	249.8	249.8	154.2	154.2
Derivative instruments not documented as hedges	–	–	7.7	7.7	7.7	7.5	7.5
Current financial assets	332.0	–	–	332.0	332.0	265.9	265.9
Cash and cash equivalents	3,259.1	–	1,023.6	4,282.7	4,282.7	3,616.9	3,616.9
<b>Non-current financial liabilities</b>							
Long-term debt	939.1	–	14.4	953.5	980.8	1,433.7	1,477.4
Non-current derivative instruments, liabilities	–	–	2.6	2.6	2.6	–	–
<b>Current financial liabilities</b>							
Derivative instruments documented as hedges	–	170.3	–	170.3	170.3	458.3	458.3
Derivative instruments not documented as hedges	–	–	9.4	9.4	9.4	20.0	20.0
Short-term debt	704.2	–	3.1	707.3	709.6	111.4	111.4

Receivables, payables and refundable grants are financial assets and liabilities within the meaning of IAS 32/39 and are measured at amortised cost. They are detailed in the Note 10.1.

IFRS 13 categorises valuation techniques for each financial asset and liability according to a fair value hierarchy with three levels:

- level 1: valuation is based on quoted (non adjusted) prices in active markets for identical assets or liabilities;
- level 2: valuation is based on information other than quoted market prices that is observable for the asset or liability, either directly or indirectly;
- level 3: valuation is based on unobservable information for an asset or liability.

The fair value of financial assets and liabilities recorded at amortised cost approximates their carrying amount, except for borrowings and debts.

The fair value of bond debt is based on quoted prices (level 1). The fair value of other borrowings and debt is determined for each loan by discounting the expected future cash flows at the Euribor interest rate at the closing date, adjusted for the Group's credit risk (level 2).

The fair value of monetary and non-monetary UCITS is measured based on the last known net asset value. The fair value of interest rate products (certificates of deposit, short-term deposits, negotiable medium-term notes, etc.) is based on the discounting of coupons flows (nominal and interest) over the remaining life of the product at the closing date. The discount rate used is the market rate corresponding to the maturity and product characteristics.

The fair value of derivatives is based on models commonly used to measure these financial instruments (models including observable market data). Counterparty default risk and credit risk have no material impact on the fair value of derivatives.

## 6.6 Financial risk

Thales' financial risk management policy is described in detail in the Group management report (chapter 1 of the 2017 Registration Document, see Section 1.1.2).

### a) Market risk

Thales hedges its foreign exchange and interest-rate risk using over-the-counter derivatives from tier-one banks. The book value of derivatives used to manage the Group's market risk is presented below:

	31/12/2017		31/12/2016	
	Assets	Liabilities	Assets	Liabilities
<b>Non-current derivatives:</b>				
• foreign exchange derivatives	—	—	—	—
• interest-rate derivatives	17.0	2.6	27.9	—
<b>Current derivatives:</b>				
• foreign exchange derivatives	252.8	178.7	160.4	476.8
• interest-rate derivatives	4.7	1.0	1.3	1.5
Foreign exchange derivatives, net	74.1		(316.4)	
Interest-rate derivatives, net	18.1		27.7	

### Foreign exchange risk

Thales hedges currency risks arising in connection with the negotiation of contracts denominated in currencies other than the main production currency, currency risks generated by ordinary commercial operations, risks relating to cash pooling and, in some cases, risks relating to its net investments in foreign operations.

At 31 December 2016 and 2017, the amount of derivatives in the portfolio can be analysed as follows:

Foreign exchange derivatives	31/12/2017				31/12/2016	
	Nominal value				Market value	Nominal value
	USD	GBP	Other	Total		Market value
<b>Negotiations and trade operations hedges</b>						
<b>Documented as hedges</b>						
Forward currency sales	3,650.1	878.4	2,384.4	6,912.9	(144.4)	7,710.7
Forward currency purchases	1,471.4	992.8	1,930.6	4,394.8		4,199.2
Currency sales (call and put options)	—	—	—	—	—	90.6
Currency purchases (call and put options)	—	—	—	—		14.8
<b>Not documented as hedges</b>						
Forward currency sales	—	—	—	—	—	—
Forward currency purchases	—	—	—	—	—	—
Currency sales (call and put options)	90.9	—	22.3	113.2	0.1	3.5
Currency purchases (call and put options)	111.1	—	1.8	112.8		11.2
<b>Hedges related to cash pooling</b>						
Currency sales: currency swaps	82.5	—	270.3	352.8	(3.1)	313.7
Currency purchases: currency swaps	1.3	37.1	71.9	110.3		924.9
<b>Hedges related to net investments in foreign operations (hedge accounting)</b>						
Currency sales: foreign exchange swaps	619.5	—	—	619.5	(67.3)	716.5
Currency purchases: foreign exchange swaps	—	532.5	—	532.5		561.0
<b>NET ASSET (LIABILITY)</b>					<b>74.1</b>	<b>(316.4)</b>

Nominal amounts are translated into euros at the closing rate.

The maturity of the derivatives used to hedge commercial contracts is consistent with the average maturities of these contracts, typically less than five years. Other derivatives have a maturity of less than one year.

The change in the value of financial instruments (forward transactions) used to hedge cash flow is recognised in equity for the spot rate component. A decrease (increase) of 5% in the dollar against the main currencies (EUR, GBP and CAD) would have had a positive (negative) impact on equity of approximately €104 million at 31 December 2017 and €153 million at 31 December 2016.

The change in value of derivative instruments matched with commercial tender portfolio, which are not eligible for hedge accounting, is recognised in profit and loss.

A decrease (increase) of 5% in the dollar against the main currencies (EUR, GBP and CAD) would have no impact on profit or loss at 31 December 2017, as at 31 December 2016.

## Interest-rate risk

Thales is exposed to interest-rate volatility and in particular its impact on the conditions associated with variable-rate financing. To limit this risk, Thales operates an active interest-rate hedging policy. At 31 December 2016 and 2017, the amount of derivatives in the portfolio was as follows:

Interest-rate derivatives	31/12/2017		31/12/2016	
	Nominal	Market value	Nominal	Market value
<b>Fair value hedge (swaps with variable rate payable):</b>				
• swaps related to bond maturing in 2023	400.0	(2.6)	400.0	0.1
• swaps related to bond maturing in 2021	300.0	17.0	300.0	21.6
• swaps related to bond maturing in 2018	300.0	3.1	300.0	6.2
	<b>17.5</b>		<b>27.9</b>	
<b>Cash flow hedge (financing of projects at variable-rate swapped to fixed-rate)</b>	<b>8.4</b>	<b>(0.7)</b>	<b>12.8</b>	<b>(1.3)</b>
<b>Swaps not documented as hedges:</b>				
• cross-currency swap with fixed-rate payable, hedging a loan	14.3	1.6	15.2	1.3
• swap with fixed-rate payable, hedging a loan	3.9	(0.3)	6.3	(0.2)
<b>NET ASSET</b>	<b>18.1</b>		<b>27.7</b>	

The table below summarises the Group's exposure to interest-rate risk before and after hedging.

31/12/2017	< 1 year		> 1 year		Total	
	Fixed-rate	Variable-rate	Fixed-rate	Variable-rate	Fixed-rate	Variable-rate
Gross debt <sup>(a)</sup>	(512.1)	(192.1)	(891.8)	(47.3)	(1,403.9)	(239.4)
Financial assets, cash and cash equivalents	—	4,614.7	—	—	—	4,614.7
<b>NET EXPOSURE BEFORE IMPACT OF DERIVATIVE INSTRUMENTS</b>	<b>(512.1)</b>	<b>4,422.6</b>	<b>(891.8)</b>	<b>(47.3)</b>	<b>(1,403.9)</b>	<b>4,375.3</b>
Hedging derivatives	296.2	(296.2)	695.4	(695.4)	991.6	(991.6)
<b>NET EXPOSURE AFTER IMPACT OF DERIVATIVE INSTRUMENTS</b>	<b>(215.9)</b>	<b>4,126.4</b>	<b>(196.4)</b>	<b>(742.7)</b>	<b>(412.3)</b>	<b>3,383.7</b>

31/12/2016	< 1 year		> 1 year		Total	
	Fixed-rate	Variable-rate	Fixed-rate	Variable-rate	Fixed-rate	Variable-rate
Gross debt <sup>(a)</sup>	(14.5)	(96.9)	(1,387.1)	(18.7)	(1,401.6)	(115.6)
Financial assets, cash and cash equivalents	—	3,882.8	—	—	—	3,882.8
<b>NET EXPOSURE BEFORE IMPACT OF DERIVATIVE INSTRUMENTS</b>	<b>(14.5)</b>	<b>3,785.9</b>	<b>(1,387.1)</b>	<b>(18.7)</b>	<b>(1,401.6)</b>	<b>3,767.2</b>
Hedging derivatives	(4.0)	4.0	991.2	(991.2)	987.2	(987.2)
<b>NET EXPOSURE AFTER IMPACT OF DERIVATIVE INSTRUMENTS</b>	<b>(18.5)</b>	<b>3,789.9</b>	<b>(395.9)</b>	<b>(1,009.9)</b>	<b>(414.4)</b>	<b>2,780.0</b>

(a) After deduction of the fair value of interest-rate derivatives.

Based on the Group's average net cash (taking into account hedging instruments), a 1 point rise in interest rates would increase net interest income by €25.9million in 2017 (€21.6 million in 2016).

## b) Customer credit risk

Credit risk relates to the risk that a party to a contract will default on its commitments or fail to pay what it owes.

### Risk of default by private sector customers

Non-governmental customers (aircraft manufacturers, airlines, private infrastructure operators and industry) account for approximately 25% of Thales' sales. These customers may encounter major and/or prolonged financial difficulties that could lead to payment defaults or order cancellations. Such occurrences could have a negative impact on Thales' sales, profitability and financial position.

To mitigate these risks, Thales conducts regular analyses of the ability of customers to meet their obligations. When necessary, Thales may request bank guarantees or corporate guarantees, or may use credit insurers.

The Group's Finance department consolidates all the information relating to the Group's exposure to credit risk, notably by identifying and analysing the ageing of overdue accounts and notes receivable that have not been impaired. At 31 December 2017 and 2016, the ageing of these accounts and notes receivable is as follows:

31/12/2017	Total	Accounts and notes receivables past due		
		Less than 3 months	3 to 6 months	More than 6 months
Overdue accounts and notes receivables not impaired				
State and similar	270.9	122.5	33.1	115.3
Other	378.3	172.9	68.5	136.9

31/12/2016	Total	Accounts and notes receivables past due		
		Less than 3 months	3 to 6 months	More than 6 months
Overdue accounts and notes receivables not impaired				
State and similar	158.0	80.1	10.3	67.6
Other	517.6	274.3	101.3	142.0

### Credit risk related to banking counterparties

Financial investments are diversified. They relate to first ranking debt and are negotiated with tier-one banks.

Thales Group trades over-the-counter derivatives with tier-one banks under agreements which provide for the offsetting of amounts payable

### Credit risk relating to public sector customers

Public, government and institutional customers account for around 75% of Thales' sales. Thales works with a large number of countries. Some of them could present a significant credit risk which could, for example, lead them to suspend an order in production, or render them unable to pay on delivery, as agreed under the terms of the contract. To limit its exposure to these risks, Thales takes out insurance with export credit agencies (such as BPIFrance) or private insurers.

At 31 December 2017, only three customers accounted for annual sales in excess of €500 million: the French State (around €2.8 billion), the UK government (around €1 billion) and the Australian government (around €0.7 billion). At 31 December 2017, these three countries had first-class or high-quality ratings (France: AA by S&P Global Ratings and Aa2 by Moody's, the United Kingdom: AA by S&P Global Ratings and Aa2 by Moody's, – Australia: AAA by S&P Global Ratings and Aaa by Moody's).

and receivable in the event of default by one of the contracting parties. These conditional offsetting agreements do not meet the eligibility criteria within the meaning of IAS 32 for offsetting derivative instruments recorded under assets and liabilities. However, they do fall within the scope of disclosures under IFRS 7 on offsetting.

31/12/2017	Gross value (before offset)	Offset amounts on balance sheet	Net presented in balance sheet	Impact of other offsetting agreements		Net
				Offsetting agreements	Financial collaterals	
Derivatives – Assets	274.5	–	274.5	(167.0)	–	107.5
Derivatives – Liabilities	182.3	–	182.3	(167.0)	–	15.3

31/12/2016	Gross value (before offset)	Offset amounts on balance sheet	Net presented in balance sheet	Impact of other offsetting agreements		Net
				Offsetting agreements	Financial collaterals	
Derivatives – Assets	189.6	–	189.6	(185.0)	–	4.6
Derivatives – Liabilities	478.3	–	478.3	(185.0)	–	293.3

## c) Liquidity risk

The Group's liquidity risk is the risk of it being unable to meet its cash needs out of its financial resources. In particular, it relates to Thales' level of exposure to changes in the main market indicators that could lead to an increase in the cost of credit or even to a temporary limitation of access to external sources of financing.

The Group manages this risk by trying to anticipate its cash needs and ensures that these are covered by the Group's short-term and long-term financial resources, as follows:

- shareholders' equity (Note 8.1);
- gross debt (listed by date of maturity in Note 6.2);
- committed, undrawn credit facilities granted by banks amounted to €1,500 million with maturing in 2021 as backup to the commercial paper programme and acting as a financing reserve.

At 31 December 2017, the Group also had an undrawn bridge loan to finance its proposed offer for the acquisition of Gemalto.

The parent company's financing programmes are rated by S&P Global Rating and Moody's. At the date of publication, Thales' credit risk ratings were as follows:

	Moody's	S&P Global Ratings
Medium and long-term loans Outlook	A2 Negative	A- Negative watch
Commercial paper and short-term loans	Prime-1	A-2

Moody's and S&P Global ratings downgraded their outlook (from "stable" to "negative" and "negative watch" respectively) following the announcement on 17 December 2017 of the planned cash tender offer for Gemalto. If this acquisition, partly financed from the Group's own cash flow and partly through borrowings, goes ahead, it would in all likelihood cause Thales's rating to be lowered, due mainly to the change in the Group's financing structure.

The decrease of Thales' credit risk rating would not trigger the financial covenants included in its financing contracts. The single accelerated repayment clause would apply only in the event that the French State ceased to hold its golden share and, simultaneously, the ratio of consolidated net debt to EBITDA<sup>(1)</sup> were to exceed 3x.

A lower rating would result in an increase (capped) in the margins applicable to the €1.5 billion committed credit facility. A higher rating would lead to a decrease in the applicable margin (with a minimum threshold). No other financing arrangements are subject to covenants based on financial ratios.

## NOTE 7. INCOME TAX

The income tax charge takes into account specific local tax rules, including the tax consolidation systems in France and the United States, group Relief in the United Kingdom and *Organschaft* rules in Germany.

### 7.1 Income tax expense

	2017	2016
Current tax	(288.8)	(262.4)
Deferred tax	24.6	6.8
<b>TOTAL</b>	<b>(264.2)</b>	<b>(255.6)</b>

(1) EBITDA, as defined in the financing agreements, is the sum of operating income, depreciation of non-current assets and impairment of intangible assets, net of goodwill amortisation. This indicator is calculated in accordance with French GAAP.

## Tax proof

	2017	2016
Net income	887.1	1,014.6
Less: income tax	264.2	255.6
Less: share in net income of equity affiliates	(134.8)	(119.6)
<b>Net income before tax and share in net income of equity affiliates</b>	<b>1,016.5</b>	<b>1,150.6</b>
Theoretical average tax rate	30.8%	29.6%
<b>Theoretical tax benefit (expense)</b>	<b>(312.5)</b>	<b>(340.9)</b>
<b>Reconciliation items:</b>		
• Impact of tax credits	74.0	76.9
• Taxes not taken into account in the theoretical rate	(63.8)	(29.2)
• Impact of dividends paid	54.3	(18.8)
• Impact of change in deferred tax rates	(28.2)	(7.7)
• Change in provision for deferred tax assets	(8.3)	38.7
• Adjustments in respect of prior periods	7.4	5.2
• Impact of partial or total exemption of disposals and other	12.9	20.2
<b>Income tax benefit (expense) recognised in profit and loss</b>	<b>(264.2)</b>	<b>(255.6)</b>
<b>Effective tax rate</b>	<b>26.0%</b>	<b>22.2%</b>

The theoretical average rate corresponds to the sum of theoretical taxes of consolidated companies, divided by the consolidated net income before tax and the share in net income of equity affiliates. The theoretical tax of each consolidated company corresponds to the application of the local tax rate to net income before tax. Accordingly, the theoretical average tax rate reflects the relative contribution of the different countries to consolidated net income. France, which has a tax rate of 34.43%, represented almost 70% of income before tax in both 2016 and 2017.

The impact of tax credits includes:

- the impact of tax exemption on research tax credits (€176 million in 2017, €176.2 million in 2016) and tax credits for competitiveness and jobs (*crédit d'impôt pour la compétitivité et l'emploi* – CICE) recognised in operating income;
- the tax advantages related to research, which are recognised in income tax (notably in United States, Australia and the Netherlands).

Taxes not taken into account in the theoretical rate mainly include state taxes in the United States, IRAP in Italy, taxes on foreign establishments, and the additional contribution in France in 2017 (a negative amount of €50.3 million).

In 2016, the impact of dividends paid mainly included the 3% tax introduced in France at the end of 2012 (a negative amount of €12.9 million). This tax, deemed unconstitutional, was repaid by the French government at the end of 2017 (net impact in 2017 of €48.5 million covering financial years 2013-2017).

The impact of changes in deferred tax rates mainly includes:

- in 2016, the impact of the decrease in tax rate enacted in France with effect from 2020 (to 28.92% from 34.43%);
- in 2017, the impact of the new gradual decrease in tax rate in France (a negative amount of €7.7 million) and the impact of the reduction in the federal tax rate in the USA from 35% to 21% (a negative amount of €22.0 million).

## 7.2 Deferred tax recognised in equity

		2017		2016
Fully consolidated entities	Base	Tax	Base	Tax
Translation of the financial statements of foreign subsidiaries	(90.4)	–	35.8	–
Net foreign investment hedges	–	–	(3.9)	1.3
Cash flow hedges	401.4	(113.0)	52.5	(18.9)
Available for sale financial assets	(1.0)	–	3.5	–
<b>Items reclassified to income</b>	<b>310.0</b>	<b>(113.0)</b>	<b>87.9</b>	<b>(17.6)</b>
Actuarial gains and losses/pensions – United Kingdom	98.7	6.5	(553.0)	11.5 <sup>(a)</sup>
Actuarial gains and losses/pensions – Other countries	(49.3)	(3.3) <sup>(b)</sup>	(108.0)	10.8 <sup>(b)</sup>
<b>Items not reclassified to income</b>	<b>49.4</b>	<b>3.2</b>	<b>(661.0)</b>	<b>22.3</b>
Treasury shares and share-based payment		6.4		7.1
<b>TOTAL DEFERRED TAX RECOGNISED IN EQUITY</b>		<b>(103.4)</b>		<b>11.8</b>

(a) Release of a portion of the provision for deferred taxes linked to pensions in the United Kingdom.

(b) Including, a negative amount of €18.6 million in 2017, and a negative amount of €16.5 million in 2016, due to the tax cut with future effect in France.

## 7.3 Tax assets and liabilities presented in the balance sheet

	01/01/2017	Income (expense)	Equity	Cash flow	Changes in exch. rates, scope	Other	31/12/2017
Current income tax assets	59.8	—	—	(23.2)	—	—	36.6
Current income tax liabilities	(59.0)	(288.8)	—	113.8	(1.3)	181.3	(54.0)
<b>Current income tax, net</b>	<b>0.8</b>	<b>(288.8)</b>	<b>—</b>	<b>90.6</b>	<b>(1.3)</b>	<b>181.3</b>	<b>(17.4)</b>
Deferred tax assets	975.8	(50.7)	(103.4)	—	14.3	22.1	858.1
Deferred tax liabilities	(294.6)	75.3	—	—	(18.3)	—	(237.6)
<b>Deferred tax, net</b>	<b>681.2</b>	<b>24.6</b>	<b>(103.4)</b>	<b>—</b>	<b>(4.0)</b>	<b>22.1</b>	<b>620.5</b>
<b>TOTAL</b>		<b>(264.2)</b>	<b>(103.4)</b>	<b>90.6</b>			

	01/01/2016	Income (expense)	Equity	Cash flow	Changes in exch. rates, scope	Other	31/12/2016
Current income tax assets	70.8	—	—	(11.0)	—	—	59.8
Current income tax liabilities	(63.7)	(262.4)	—	110.4	—	156.7	(59.0)
<b>Current income tax, net</b>	<b>7.1</b>	<b>(262.4)</b>	<b>—</b>	<b>99.4</b>	<b>—</b>	<b>156.7</b>	<b>0.8</b>
Deferred tax assets	967.0	(37.6)	11.8	—	28.0	6.6	975.8
Deferred tax liabilities	(257.9)	44.4	—	—	(81.1)	—	(294.6)
<b>Deferred tax, net</b>	<b>709.1</b>	<b>6.8</b>	<b>11.8</b>	<b>—</b>	<b>(53.1)</b>	<b>6.6</b>	<b>681.2</b>
<b>TOTAL</b>		<b>(255.6)</b>	<b>11.8</b>	<b>99.4</b>			

### a) Current income tax

Income tax paid is reported net of tax credits utilised. The allocation of tax credits is presented under “Other”.

### b) Deferred tax

#### Changes by nature

	01/01/2017	(Expense)/ Income for the period	Equity	Changes in exch. rates, scope and other	31/12/2017
<b>Temporary differences:</b>	<b>884.2</b>	<b>66.3</b>	<b>(133.4)</b>	<b>(4.3)</b>	<b>812.8</b>
• pensions and other employee benefits	593.3	(12.5)	(19.7)	50.8	611.9
• intangible assets	(310.1)	69.9	—	(4.8)	(245.0)
• reserve for losses at completion	141.5	(12.0)	—	3.4	132.9
• other	459.5	20.9	(113.7)	(53.7)	313.0
<b>Tax loss carry-forwards</b>	<b>192.4</b>	<b>(33.1)</b>	<b>—</b>	<b>15.2</b>	<b>174.5</b>
<b>Total</b>	<b>1,076.6</b>	<b>33.2</b>	<b>(133.4)</b>	<b>10.9</b>	<b>987.3</b>
<b>O/w not recognised in the balance sheet</b>	<b>(395.4)</b>	<b>(8.6)</b>	<b>30.0</b>	<b>7.2</b>	<b>(366.8)</b>
<b>Total net deferred tax assets</b>	<b>681.2</b>	<b>24.6</b>	<b>(103.4)</b>	<b>18.1</b>	<b>620.5</b>

	01/01/2016	(Expense)/ Income for the period	Equity	Changes in exch. rates, scope and other	31/12/2016
<b>Temporary differences:</b>	<b>846.7</b>	<b>35.8</b>	<b>80.5</b>	<b>(78.8)</b>	<b>884.2</b>
• pensions and other employee benefits	531.1	(21.3)	104.3	(20.7)	593.3
• intangible assets	(262.5)	32.8	—	(80.4)	(310.1)
• reserve for losses at completion	118.6	24.1	—	(1.2)	141.5
• other	459.5	0.2	(23.8)	23.6	459.5
<b>Tax loss carry-forwards</b>	<b>248.0</b>	<b>(67.7)</b>	<b>—</b>	<b>12.1</b>	<b>192.4</b>
<b>Total</b>	<b>1,094.7</b>	<b>(31.9)</b>	<b>80.5</b>	<b>(66.7)</b>	<b>1,076.6</b>
<b>O/w not recognised in the balance sheet</b>	<b>(385.6)</b>	<b>38.7</b>	<b>(68.7)</b>	<b>20.2</b>	<b>(395.4)</b>
<b>Total net deferred tax assets</b>	<b>709.1</b>	<b>6.8</b>	<b>11.8</b>	<b>(46.5)</b>	<b>681.2</b>

### Tax loss carry-forwards

Total tax loss carry-forwards represent a potential tax saving of €174.5 million at 31 December 2017 (€192.4 million at 31 December 2016). The corresponding expiry dates are as follows:

	31/12/2017		31/12/2016
2018	1.1	2017	1.0
2019-2022	0.2	2018-2021	0.8
Beyond 2022	44.8	Beyond 2021	47.5
Not time limited	128.4	Not time limited	143.1
<b>Total</b>	<b>174.5</b>	<b>Total</b>	<b>192.4</b>
O/w not recognised in the balance sheet	(112.0)	O/w not recognised in the balance sheet	(112.5)
<b>Net deferred tax asset</b>	<b>62.5</b>	<b>Net deferred tax asset</b>	<b>79.9</b>

As described in Note 13-i, only deferred tax assets related to tax losses which the Group expects to recover are recognised in the balance sheet. In particular, the Group takes into account any loss carry-forward limitations.

## NOTE 8. EQUITY AND EARNINGS PER SHARE

### 8.1 Equity

#### a) Share capital

At 31 December 2017, the share capital of Thales parent company, amounts to €637,976,175 and comprises 212,658,725 shares with a par value of €3, compared with 212,194,766 shares at 31 December 2016. This represents an increase of 463,959 shares resulting from the exercise of share subscription options.

#### b) Outstanding securities giving access to the share capital

At 31 December 2017, there are no securities that give access to the share capital of the Company, with the exception of the share subscription options described in Note 9.4.

### c) Treasury shares

Thales parent company held 568,739 of its own shares at 31 December 2017. They are accounted for as a deduction from equity in the amount of €52.5million.

In accordance with the authorisations given to the Board of Directors at the Annual General Meeting, the Company carried out the following transactions in 2016 and 2017:

	2017	2016
<b>Treasury shares at 1 January</b>	<b>749,559</b>	<b>839,254</b>
Purchases as part of a liquidity agreement	819,512	513,001
Sales as part of a liquidity agreement	(743,512)	(472,001)
Transfer to employees as part of the employee share purchase offering	(462,167)	(41,714)
Delivery of free shares	(606,653)	(607,381)
Market purchases	852,000	575,000
Exercise of share purchase options	(40,000)	(56,600)
<b>Treasury shares at 31 December</b>	<b>568,739</b>	<b>749,559</b>

At 31 December 2017 and 2016, as part of a liquidity agreement managed by Kepler Cheuvreux, the following numbers of shares were held in the liquidity account:

	2017	2016
Number of shares at 31 December	126,000	50,000
Value (€ million)	23.2	29.5

### d) Translation adjustments

Translation adjustments result from the translation of financial statements of companies whose functional currency is not the euro, offset as applicable by the impact of derivative instruments denominated in foreign currencies to hedge net investments in foreign operations.

Translation adjustments are recorded in equity as other comprehensive income, and are subsequently reclassified to income on disposal. They break down as follows:

	2017	2016
<b>Translation adjustment at 1 January</b>	<b>(110.0)</b>	<b>(87.2)</b>
Changes in value	(113.9)	21.4
Reclassified to profit and loss	—	(46.8)
Gross change	(113.9)	(25.4)
Deferred tax	—	1.3
Scope and other	0.2	1.3
<b>Translation adjustment at 31 December</b>	<b>(223.7)</b>	<b>(110.0)</b>
<b>Of which:</b>		
Hedge of net investments in foreign operations	—	—

## e) Reserves for cash flow hedge

The Group uses foreign exchange derivatives to hedge against changes in the value of future cash flows related to commercial cash flows in foreign currencies. In the consolidated financial statements, the effective portion of changes in fair value of these derivatives is recognised directly in equity, until such time as the hedged flows affect profit and loss.

	2017	2016
<b>Cash flow hedge at 1 January</b>	<b>(250.7)</b>	<b>(276.8)</b>
Changes in value of derivatives	252.2	17.6
Reclassified to operating (income)/expense	33.2	27.4
Reclassified to income tax (benefit)/expense	(14.5)	(9.9)
Changes in scope and exchange rates	—	(9.0)
<b>Cash flow hedge at 31 December<sup>(a)</sup></b>	<b>20.2</b>	<b>(250.7)</b>

(a) A negative balance at closing means that the exchange rates of the derivative instruments documented as hedges are generally less favorable than the exchange rates prevailing at the closing date.

## f) Parent company dividend distribution

The per share dividend amounted to €1.60 in 2016 and €1.36 in 2015.

The Board of Directors decided to propose to shareholders, who will be convened to a General Meeting on 23rd May 2018, the payment of a total amount of €1.75 per share.

If approved, the ex-dividend date will be 30 May 2018 and the payment date will be 1 June 2018. The dividend will be paid fully in cash and will amount to €1.30 per share, after deducting the interim dividend of €0.45 per share paid in December 2017.

Dividends paid in 2016 and 2017 are described below:

Year	Approved by	Description	Dividend per share	Payment date	Payment method	Total
2017	Board of Directors meeting on 28 September 2017	2017 interim dividend	€0.45	12/2017	Cash	€95.2 million
	General Meeting on 17 May 2017	Balance for 2016	€1.20	06/2017	Cash	€253.7 million
	<b>Total dividends paid in 2017</b>					<b>€348.9 million</b>
2016	Board of Directors meeting on 22 September 2016	2016 interim dividend	€0.40	12/2016	Cash	€84.6 million
	General Meeting on 18 May 2016	Balance for 2015	€1.01	05/2016	Cash	€212.2 million
	<b>Total dividends paid in 2016</b>					<b>€296.8 million</b>
2015	Board of Directors meeting on 17 September 2015	2015 interim dividend	€0.35	12/2015	Cash	€73.4 million

## g) Non-controlling interests

This item principally includes Leonardo's interest in sub-group Thales Alenia Space (33%), Siemens' and Philips Medical Systems International's interest in Trixell SAS (49%) and, up until 29 June 2016, Raytheon's interest in Thales-Raytheon Systems Company SAS (50%).

The individual contributions of these minority shareholders to the Group's key financial indicators are not material.

The cash of these three companies is unrestricted and is exclusively pooled with Thales' Corporate Treasury department.

## 8.2 Earnings per share

Basic earnings per share are calculated by dividing the attributable net income by the weighted average number of shares outstanding during the period, excluding treasury shares.

Diluted earnings per share take into account instruments with a dilutive effect on earnings per share and exclude non-dilutive instruments. The dilutive effect of share subscription and share purchase options, free share and unit allotments, is calculated using the treasury stock method, taking into account the average share price over the relevant period.

		2017	2016
<b>Numerator</b> (in € millions)			
Net income attributable to shareholders of the parent company	(A)	821.7	946.4
<b>Denominator</b> (in thousands)			
Average number of shares outstanding	(B)	211,661	210,872
Share subscription and share purchase options <sup>(a)</sup>		596	1,004
Free share and units plans <sup>(b)</sup>		984	1,432
Diluted average number of shares outstanding	(C)	213,241	213,308
<b>Basic earnings per share</b> (in euros)	<b>(A) / (B)</b>	<b>3.88</b>	<b>4.49</b>
<b>Diluted earnings per share</b> (in euros)	<b>(A) / (C)</b>	<b>3.85</b>	<b>4.44</b>
Average share price		€92.14	€77.59

(a) Only option plans with an exercise price that is lower than the average share price are taken into account in the calculation of diluted earnings per share.

(b) Performance shares/units are only taken into account when performance targets are achieved (for the portion deliverable in shares).

## NOTE 9. EMPLOYEE BENEFITS

### 9.1 Consolidated headcount

Consolidated headcount includes all employees of fully consolidated companies. It does not include employees of equity affiliates. At end-2017, Thales' headcount stood at 64,860 versus 63,783 at end-2016.

Headcount includes three-fourth of employment grade of engineer, specialist, manager or equivalent.

### 9.2 Personnel expenses

	2017	2016
Wages and salaries and payroll taxes <sup>(a)</sup>	(6,120.8)	(5,875.8)
Defined benefit pension expense: current service cost (Note 9.3)	(105.0)	(92.9)
Compensation subject to presence conditions related to business combinations	(17.8)	(19.0)
Share-based payment (Note 9.4)	(48.8)	(36.9)
<b>TOTAL</b>	<b>(6,292.4)</b>	<b>(6,024.6)</b>

(a) Including profit-sharing, incentive plans and defined contribution pension expenses.

### 9.3 Pensions and other employee benefits

The Group grants its employees post-employment benefits (pensions, end-of-career indemnities, medical care, etc.) and other long-term benefits (long-service and jubilee awards, etc.).

#### a) Description of the plans

The Group's existing plans are either defined contribution plans or defined benefit plans.

#### Defined contribution plans

In certain countries, the Group pays contributions based on salaries to state organisations in charge of basic pension schemes (e.g., *Sécurité Sociale* or compulsory supplementary schemes ARRCO and AGIRC in France). Beyond these basic pension schemes, Thales also contributes to other defined contribution plans (e.g., Netherlands and United Kingdom

since 2002). These plans do not impose any other obligations on the Group except for the payment of contributions: there is no related benefit obligation and contributions are expensed in the period they are incurred.

#### Defined benefit plans

Defined benefit plans relate to different types of advantages:

- pensions and end-of-career indemnities (legal or contractual), and other long-term benefits (jubilee awards, etc.), notably in France. In general, these commitments are not covered by any assets;
- supplementary pension schemes, mainly in the United Kingdom where the main scheme, "Thales UK Pension Scheme" provides a pension based on the beneficiary's average salary, indexed to inflation. This plan has been closed to new entrants since 2002, and is managed by a trust according to minimum local funding regulations.

The present value of the Group's obligations and the value of plan assets are measured independently. A provision is recognised if the value of the assets is insufficient to cover the obligations.

## b) Provisions recognised in the balance sheet

	2017	2016
<b>Provision at 1 January</b>	<b>(2,785.8)</b>	<b>(2,318.9)</b>
<b>Current service cost (income from operations)</b>	<b>(105.0)</b>	<b>(92.9)</b>
<b>Amendments and settlements (non-recurring operating income)</b>	<b>(21.2)</b>	<b>0.0</b>
Interest expense	(151.4)	(182.6)
Expected return on plan assets	94.2	122.0
Net interest cost	(57.2)	(60.6)
Pension fund management cost	(5.6)	(5.2)
Actuarial gains and losses on other long-term benefits	(2.7)	(11.8)
<b>Finance costs on pensions and other long-term employee benefits</b>	<b>(65.5)</b>	<b>(77.6)</b>
<b>Total expense for the period</b>	<b>(191.7)</b>	<b>(170.5)</b>
<b>Actuarial gains and losses (other comprehensive income)</b>	<b>49.4</b>	<b>(661.0)</b>
<b>Benefits and contributions</b>	<b>202.9</b>	<b>190.1</b>
• of which, deficit payment in the United Kingdom	82.3	88.3
• of which, other benefits and contributions	120.6	101.8
Translation adjustment	55.7	163.2
Changes in scope of consolidation and other	(4.8)	11.3
<b>Provision at 31 December</b>	<b>(2,674.3)</b>	<b>(2,785.8)</b>
<b>Of which:</b>		
• post-employment benefits	(2,468.0)	(2,586.9)
• other long-term benefits	(206.3)	(198.9)

## c) Changes in defined benefit obligations and plans assets

31/12/2017	UK	France	Other	Total
<b>Obligation at 1 January</b>	<b>(4,605.7)</b>	<b>(1,138.1)</b>	<b>(597.3)</b>	<b>(6,341.1)</b>
Current service cost	(24.0)	(57.6)	(23.4)	(105.0)
Interest cost	(123.7)	(16.9)	(10.8)	(151.4)
Plan participant contributions	(10.2)	—	(2.2)	(12.4)
Amendments/settlements	(2.8)	(18.4)	—	(21.2)
Experience gains (losses)	20.8	(28.7)	5.4	(2.5)
Actuarial gains (losses)/financial assumptions	(147.0)	(35.5)	(5.3)	(187.8)
Actuarial gains (losses)/demographic assumptions	137.8	—	1.1	138.9
Actuarial gains (losses) on long-term benefits	—	(1.1)	(1.6)	(2.7)
Benefits paid by plan assets	161.5	2.6	12.7	176.8
Benefits paid by employer	0.5	75.7	18.6	94.8
Changes in scope, exchange rates and other	161.0	5.5	0.1	166.6
<b>Obligation at 31 December</b>	<b>(4,431.8)</b>	<b>(1,212.5)</b>	<b>(602.7)</b>	<b>(6,247.0)</b>
<b>Plan assets at 1 January</b>	<b>3,246.2</b>	<b>141.5</b>	<b>167.6</b>	<b>3,555.3</b>
Expected return on plan assets	88.2	2.1	3.9	94.2
Employer's contribution	98.5	4.0	5.6	108.1
Plan participant contributions	10.2	—	2.2	12.4
Amendments/settlements	—	—	—	—
Benefits paid by plans assets	(161.5)	(2.6)	(12.7)	(176.8)
Experience gains (losses)	87.0	6.9	6.9	100.8
Changes in scope, exchange rates and other	(119.9)	(0.1)	(1.3)	(121.3)
<b>Plan assets at 31 December</b>	<b>3,248.7</b>	<b>151.8</b>	<b>172.2</b>	<b>3,572.7</b>
<b>PROVISIONS AT 31 DECEMBER</b>	<b>(1,183.1)</b>	<b>(1,060.7)</b>	<b>(430.5)</b>	<b>(2,674.3)</b>

31/12/2016	UK	France	Other	Total
<b>Obligations at 1 January</b>	<b>(4,294.5)</b>	<b>(1,042.2)</b>	<b>(555.0)</b>	<b>(5,891.7)</b>
Current service cost	(19.9)	(51.4)	(21.6)	(92.9)
Interest cost	(148.7)	(21.4)	(12.5)	(182.6)
Plan participant contribution	(11.4)	—	(1.8)	(13.2)
Amendments/settlements	—	—	—	—
Experience gains (losses)	8.1	(11.5)	2.9	(0.5)
Actuarial gains (losses)/financial assumptions	(1,011.8)	(17.3)	(28.3)	(1,057.4)
Actuarial gains (losses)/demographic assumptions	79.7	(56.8)	2.3	25.2
Actuarial gains (losses) on long-term benefits	—	(10.1)	(1.7)	(11.8)
Benefits paid by plan assets	141.7	2.4	5.1	149.2
Benefits paid by employer	0.5	58.5	18.7	77.7
Changes in scope, exchange rates and other	650.6	11.7	(5.4)	656.9
<b>Obligations at 31 December</b>	<b>(4,605.7)</b>	<b>(1,138.1)</b>	<b>(597.3)</b>	<b>(6,341.1)</b>
<b>Plan assets at 1 January</b>	<b>3,274.6</b>	<b>139.2</b>	<b>159.0</b>	<b>3,572.8</b>
Expected return on plans assets	115.0	2.9	4.1	122.0
Employer's contribution	106.1	2.0	4.3	112.4
Plan participant contribution	11.4	—	1.8	13.2
Amendments/settlements	—	—	—	—
Benefits paid by plan assets	(141.7)	(2.4)	(5.1)	(149.2)
Experience gains (losses)	371.0	0.0	0.7	371.7
Changes in scope, exchange rates and other	(490.2)	(0.2)	2.8	(487.6)
<b>Plan assets at 31 December</b>	<b>3,246.2</b>	<b>141.5</b>	<b>167.6</b>	<b>3,555.3</b>
<b>PROVISIONS AT 31 DECEMBER</b>	<b>(1,359.5)</b>	<b>(996.6)</b>	<b>(429.7)</b>	<b>(2,785.8)</b>

#### d) Actuarial assumptions used

The actuarial assumptions used are determined according to the economic environment and specific criteria of each country and each system. The most sensitive assumptions are as follows:

2017	UK	France	2016	UK	France
Inflation rate	3.19%	1.35%	Inflation rate	3.22%	1.40%
Discount rate	2.60%	1.20%	Discount rate	2.79%	1.50%
Average duration of the plans	17 years	10 years	Average duration of the plans	17 years	10 years

For each country, the discount rates are obtained by reference to the Iboxx Corporate AA index which reflects the rate of return of very high-quality corporate bonds, with maturity dates equivalent to the duration of the plans being measured, and in the same currency.

At 31 December 2017, the sensitivity of the net obligation to a change in the discount rate is as follows:

Sensitivity in basis points	+0.25%	−0.25%	+0.50%	−0.50%	+1%	−1%
Decrease (increase) in provision (in € millions)	249.6	(265.6)	483.7	(548.7)	910.5	(1,172.9)

In the United Kingdom, a 25-basis-point increase in the inflation rate would lead to a €117.1 million increase in the obligation. Conversely, a 25-basis-point decrease in the inflation rate would give rise to a €135.5 million decrease in the obligation.

#### e) Allocation and return on plan assets

Plan assets generated an actual average return of 5.5% in 2017, compared with 14% in 2016. At 31 December 2017, the allocation of assets, mainly invested in the United Kingdom, breaks down as follows:

	2017	2016
Fixed-rate bonds	34%	32%
Index-linked investments	12%	13%
Equities	28%	33%
Alternative liquid investments	10%	8%
Alternative non-liquid investments (property, etc.)	16%	14%
<b>TOTAL</b>	<b>100%</b>	<b>100%</b>

#### f) Funding

Thales is subject to funding obligations in respect of its defined benefit pension commitments in the United Kingdom.

In accordance with the regulations in force, the level of funding for its pension obligation is remeasured every three years, further to which the suitability of a new funding plan and/or the implementation of guarantees for the plan is decided in consultation with the trustees. The latest measurement, based on the situation at end-2014, was finalised in September 2016 and led to an annual contribution of £60 million to the main Thales UK Pension Scheme (£5 million for other schemes).

Depending on changes in the degree of deficit which will be determined based on the situation at the end of 2017, future contributions to the main scheme could change from 2018 and increase to £75 million.

Thales (parent company), in support of the contributions made by Thales UK Ltd to the British pension plans, has also guaranteed the future liabilities linked to the funding plans for the subsidiaries concerned.

At 31 December 2017, the balance of these guarantees was £825.8 million, partly reduced by any sums paid into the funding plans.

## 9.4 Share-based payment

At 31 December 2017, the following options, shares and units were outstanding:

- 850 share purchase options with a weighted average exercise price of €38.50;
- 783,204 share subscription options with a weighted average exercise price of €34.13, including 155,427 performance shares;
- 447,860 free shares, including 360,300 performance shares;

- 1,235,940 share units, including 480,150 performance units;
- 142,180 phantom shares, payable in cash at the end of a four-year vesting period, including 103,390 performance shares.

The terms of these plans are described in the Registration Document (see section on share capital and shareholders).

The Group also implemented an employee share purchase plan, the terms of which are described as below:

### a) Outstanding share purchase option plans

Date of Board decision	Exercise period	Exercise price	Number of options outstanding at 31/12/2016	Options exercised in 2017	Options cancelled in 2017	Number of options outstanding at 31/12/2017
25/11/2008	from 25/11/2012 to 24/11/2018	€38.50	850	—	—	850
04/07/2007	from 04/07/2011 to 03/07/2017	€44.77	40,000	(40,000)	—	—

### b) Outstanding share subscription option plans

Date of Board decision	Exercise period	Exercise price	Number of options outstanding at 31/12/2016	Options exercised in 2017	Options cancelled in 2017	Number of options outstanding at 31/12/2017
15/09/2011 <sup>(a)</sup>	from 15/09/2015 to 14/09/2021	€26.34	126,322	(40,945)	—	85,377
23/09/2010 <sup>(a)</sup>	from 23/09/2014 to 22/09/2020	€26.34	110,150	(40,100)	—	70,050
25/06/2009	from 25/06/2013 to 24/06/2019	€32.88	362,584	(84,342)	(5,490)	272,752
01/07/2008	from 01/07/2012 to 30/06/2018	€38.50	463,237	(96,732)	(11,480)	355,025
04/07/2007	from 04/07/2011 to 03/07/2017	€44.77	258,400	(201,840)	(56,560)	—

(a) Plans contingent upon the achievement of internal performance targets over the three financial years following the grant date.

### c) Allotment of free shares

Date of Board decision	Vesting period	Share price at grant date	Number of free shares at 31/12/2016	Shares allotted in 2017	Shares cancelled in 2017	Shares delivered in 2017	Number of free shares at 31/12/2017
28/09/2017	from 28/09/2017 to 28/09/2021	€94.66	—	212,540 <sup>(a)</sup>	—	—	212,540
27/10/2016	from 27/10/2016 to 27/10/2020	€83.10	87,860 148,070 <sup>(a)</sup>	— —	(300) (310)	— —	87,560 147,760
17/09/2013	from 17/09/2013 to 17/09/2017	€39.16	397,180 226,335 <sup>(a)</sup>	— —	(9,274) (7,638)	(387,906) (218,697)	— —
20/12/2012	from 20/12/2012 to 20/12/2016	€27.47	50 <sup>(b)</sup>	—	—	(50)	—

(a) Plans contingent upon the achievement of internal performance targets over the three financial years following the grant date.

(b) Adjustment after 2016.

**d) Allotment of share units indexed to the value of Thales shares**

Date of the allocation decision	Vesting period	Share price at grant date	Number of units at 31/12/2016	Units cancelled in 2017	Units delivered in 2017	Number of units at 31/12/2017
17/09/2015	from 17/09/2015 to 17/09/2019	€61.75	368,350 <sup>(b)</sup> 229,200 <sup>(a)</sup>	(9,050) (7,750)	(270) —	359,030 221,450
16/09/2014	from 16/09/2014 to 16/09/2018	€42.42	405,210 268,000 <sup>(a)</sup>	(8,210) (9,300)	(240) —	396,760 258,700

(a) Plans contingent upon the achievement of internal performance targets over the three financial years following the grant date.

(b) Adjustment of 620 shares after 2016.

**e) Allotment of phantom shares indexed to the value of Thales shares**

Date of the allocation decision	Vesting period	Number of phantom shares at 31/12/2016	Phantom shares delivered in 2017	Phantom shares cancelled in 2017	Number of phantom shares at 31/12/2017
28/09/2017	from 28/09/2017 to 28/09/2021	—	67,140 <sup>(a)</sup>	(140)	67,000
27/10/2016	from 27/10/2016 to 27/10/2020	39,430 37,910 <sup>(a)</sup>	— —	(640) (1,520)	38,790 36,390

(a) Plans contingent upon the achievement of internal performance targets over the three financial years following the grant date.

**f) Employee share purchase plan**

Following the decision of the Board of Directors on 27 February 2017, the Group implemented a Thales share purchase plan reserved to its employees with a discount compared to the average market price plus an employer contribution.

The subscription price of €75.93, set on 12 October 2017, corresponds to the average of the opening price of Thales shares on Euronext Paris over the twenty trading days preceding this date, discounted by 20%.

The employees also received an employer contribution corresponding to one free share for four acquired shares up to 40 shares purchased, within the limit of 10 matching shares.

This plan is part of the Group savings plan, subject to a five-year lockup period of the investment, except for the United Kingdom where the share offering is implemented in accordance with the Share Incentive Plan ("SIP").

Thus, in 2017, 377,989 shares were subscribed by employees at the subscription price of €75.93 and 84,178 bonus shares were received. The delivery of shares to UK based employees will be finalised in early 2018.

In the consolidated financial statements, the cost of this plan is measured according to the French CNC (Conseil National de la Comptabilité) recommendation, taking the five-year lock-up period into account. This approach measures the share according to a replication strategy in which the market participant would sell the share at the end of the five-year lockup period and would borrow the necessary amount to immediately buy a free share by financing the loan by the future sale and dividends paid out during the lock-up period.

**Accounting cost: hypothesis taken**

Five-year free risk interest rate	0.18%
Spread of the banking system (retail)	5.00%
Financing rate for an employee	5.18%
Cost of security loan (repo)	1.0%
Cost for the Group (M€)	€6.0 M <sup>(a)</sup>

(a) Before social contributions (€1.8 million) and administrative charges.

## g) Expenses related to share based payment

In the consolidated financial statements, the benefit granted to beneficiaries of the above-mentioned plans is recognised as an operating expense. These amounts break down as follows:

Plans	Residual fair value at the end of 2017	2017 expense	2016 expense
Free shares	27.0	(8.8)	(9.9)
Share units <sup>(a)</sup>	23.3	(20.7)	(19.0)
Phantom shares and others <sup>(b)</sup>	9.6	(2.0)	(0.3)
Employee share scheme	–	(6.0)	–
Social contributions related to the plans	15.4	(11.3)	(7.7)
<b>TOTAL</b>	<b>75.3</b>	<b>(48.8)</b>	<b>(36.9)</b>
<b>Of which, offsetting entries:</b>			
• Shareholders equity		21.8	16.6
• Debt		27.0	20.3

(a) The fair value of the plan, measured in accordance with the Monte Carlo model, takes into account the following assumptions respectively in 2014 and 2015: volatility rates of 22% and 23%, dividend payout rates of 2.7% and 2%, and free risk rates of 0.14% and 0.10%.

(b) In 2017, this line included the expense relating to the long-term incentive plan (LTIP) of the Chairman and CEO, consisting of a maximum of 5,000 performance units, the conditions of which are described in the 2016 Registration Document on page 153.

## 9.5 Compensation of directors and senior corporate officers

Expenses recognised in respect of compensation, benefits and social security contributions attributed to Directors and members of the Executive Committee are as follows:

	2017	2016
<b>Short-term benefits:</b>		
• Fixed compensation	5.2	4.8
• Variable compensation	4.5	3.9
• Retirement benefit	0.5	–
• Employer social security contributions	3.3	2.9
• Attendance fees	0.6	0.5
<b>Other benefits:</b>		
• Post-employment benefits	2.4	1.7
• Share-based payments	2.4	2.5

## NOTE 10. CURRENT OPERATING ASSETS AND LIABILITIES

Current operating assets and liabilities include working capital components and reserves for contingencies. The changes in these items are presented below.

Contracts falling within the scope of IAS 11 are subject to specific classification in the consolidated balance sheet: for each contract, the balance of unbilled receivables, work in progress and reserves for contingencies are presented in assets or liabilities under "Construction contracts" (Note 13-c).

The Group is authorised to assign trade receivables, mainly from the French State, and commercial paper. At 31 December 2017,

derecognised receivables amounted to €292.5million (€143.5 million at 31 December 2016). The organic change in derecognised receivables represents an increase of €149 million for 2017 (a decrease of €39.7 million in 2016).

As these assignments without recourse in case of default by the debtor involve the transfer of substantially all corresponding risks and rewards, they are derecognised. Thales' continued involvement (within the meaning of IFRS 7) in the related risks and rewards corresponds to the share of dilution risk not transferred to the bank and the remuneration received under the recovery mandate.

## 10.1 Change in current operating assets and liabilities

	01/01/2016	Change in WCR and reserves	Change in scope, exchange rates and reclassifications	31/12/2016	Change in WCR and reserves	Change in scope, exchange rates and reclassifications	31/12/2017
Inventories and work in progress	2,560.8	177.4	(3.6)	2,734.6	126.6	(57.8)	2,803.4
Construction contracts: assets	2,042.6	285.2	3.7	2,331.5	40.8	(66.3)	2,306.0
Advances to suppliers	383.0	(32.4)	(2.3)	348.3	110.3	(6.8)	451.8
Accounts, notes and other receivables	4,404.2	223.3	(80.0)	4,547.5	(103.1)	(93.3)	4,351.1
Current derivatives – assets	154.2	18.0	(10.5)	161.7	122.6	(29.9)	254.4
<b>Current operating assets</b>	<b>9,544.8</b>	<b>671.5</b>	<b>(92.7)</b>	<b>10,123.6</b>	<b>297.2</b>	<b>(254.1)</b>	<b>10,166.7</b>
Advances received from customers on contracts <sup>(a)</sup>	(4,317.2)	(193.0)	31.8	(4,478.4)	251.3	64.5	(4,162.6)
Refundable grants	(127.6)	(6.6)	0.8	(133.4)	5.0	0.7	(127.7)
Construction contracts: liabilities	(1,021.0)	(116.8)	(1.6)	(1,139.4)	(156.2)	17.3	(1,278.3)
Reserve for contingencies	(1,022.9)	5.6	(19.7)	(1,037.0)	(117.1)	19.4	(1,134.7)
Accounts, notes and other payables	(5,547.6)	(310.7)	(14.3)	(5,872.6)	(475.7)	84.0	(6,264.3)
Current derivatives – liabilities	(405.3)	21.0	(94.0)	(478.3)	–	298.6	(179.7)
<b>Current operating liabilities</b>	<b>(12,441.6)</b>	<b>(600.5)</b>	<b>(97.0)</b>	<b>(13,139.1)</b>	<b>(492.7)</b>	<b>484.5</b>	<b>(13,147.3)</b>
<b>Restructuring provision<sup>(b)</sup></b>	<b>116.3</b>	<b>(7.4)</b>	<b>5.4</b>	<b>114.3</b>	<b>(27.0)</b>	<b>(1.3)</b>	<b>86.0</b>
<b>INCREASE (DECREASE) IN WCR AND RESERVES FOR CONTINGENCIES</b>		<b>63.4</b>			<b>(222.5)</b>		

(a) Advances received on construction contracts respectively amount to €3,262.8 million, €3,302.7 million and €3,024.1 million at 1 January 2016, 31 December 2016 and 2017.

(b) Included in reserves for contingencies.

## 10.2 Reserves for contingencies (excluding construction contracts)

	31/12/2016	Additions	Utilisation	Reversal (surplus)	Exchange rates and other	31/12/2017
Restructuring <sup>(a)</sup>	114.3	42.8	(62.8)	(7.0)	(1.3)	86.0
Litigation	125.5	84.4	(21.2)	(29.2)	(1.0)	158.5
Guarantees	255.8	120.1	(40.4)	(12.9)	1.8	324.4
Losses at completion	96.3	55.9	(43.0)	(11.5)	(10.9)	86.8
Provisions on contracts	173.5	40.0	(32.5)	(8.8)	8.4	180.6
Other <sup>(b)</sup>	271.6	112.9	(68.7)	(13.4)	(4.0)	298.4
<b>TOTAL</b>	<b>1,037.0</b>	<b>456.1</b>	<b>(268.6)</b>	<b>(82.8)</b>	<b>(7.0)</b>	<b>1,134.7</b>

	01/01/2016	Additions	Utilisation	Reversal (surplus)	Exchange rates and other	31/12/2016
Restructuring <sup>(a)</sup>	116.3	72.4	(68.1)	(11.7)	5.4	114.3
Litigation	127.7	33.4	(18.9)	(24.4)	7.7	125.5
Guarantees	239.7	82.2	(51.8)	(10.4)	(3.9)	255.8
Losses at completion	76.1	52.9	(27.9)	(4.8)	—	96.3
Provisions on contracts	147.4	44.9	(12.7)	(4.8)	(1.3)	173.5
Other <sup>(b)</sup>	315.7	71.1	(58.4)	(23.0)	(33.8)	271.6
<b>TOTAL</b>	<b>1,022.9</b>	<b>356.9</b>	<b>(237.8)</b>	<b>(79.1)</b>	<b>(25.9)</b>	<b>1,037.0</b>

(a) Net restructuring costs break down as follows:

	2017	2016
Additions for the period	(42.8)	(72.4)
Reversals for the period	69.8	79.8
Expenses for the period	(108.1)	(107.9)
<b>Restructuring costs, net</b>	<b>(81.1)</b>	<b>(100.5)</b>

(b) Includes technical provisions of insurance companies, provisions for tax and labour-related risks, vendor warranties, environmental guarantees and other.

## 10.3 Maturity of current receivables and payable

The amounts presented in the balance sheet for this item break down as follows:

		31/12/2017	31/12/2016
	Total	< 1 year	> 1 year
Accounts and accrued receivables, gross	3,217.3	3,139.0	78.3
Provisions on accounts and notes receivable <sup>(a)</sup>	(91.6)	(53.4)	(38.2)
<b>Accounts and accrued receivables, net</b>	<b>3,125.7</b>	<b>3,085.6</b>	<b>40.1</b>
Tax receivables (excluding income tax)	893.1	753.2	139.9
Other receivables, gross	335.2	313.1	22.1
Provisions for other receivables	(2.9)	(2.9)	—
<b>Net</b>	<b>1,225.4</b>	<b>1,063.4</b>	<b>162.0</b>
<b>Accounts, notes and other receivables</b>	<b>4,351.1</b>	<b>4,149.0</b>	<b>202.1</b>
Accounts and notes payable	2,652.6	2,645.5	7.1
Accrued holiday pay and payroll taxes	1,564.4	1,541.1	23.3
Tax payables (excluding income tax)	698.6	698.1	0.5
Other creditors and accrued liabilities	1,348.7	1,260.5	88.2
<b>Accounts, notes and other payables</b>	<b>6,264.3</b>	<b>6,145.2</b>	<b>119.1</b>

(a) In 2017, additions to provisions for bad debts, net of reversals of surplus provision, amounted to €6.5 million (€2.1 million in 2016).

## 10.4 Bonds and warranties linked to commercial contracts

In the ordinary course of its activities, the Group regularly responds to invitations to tender. When requested by the customer, bid bonds are delivered in order to demonstrate the definitive nature of the bid and to indemnify the customer if the Group fails to meet its commitments. At 31 December 2017, bid bonds issued amounted to €33.6 million (€26.2 million at 31 December 2016).

From the signature of a contract up until its completion, the Group may also issue performance bonds for its customers, with a bank acting as an

intermediary, in order to cover the payment of damages to the customer in the event that the Group does not meet its contractual commitments. At 31 December 2017, performance bonds amounted to €1,812.5 million (€2,288.6 million at 31 December 2016).

Technical, operational and financial costs incurred by the Group in order to meet its obligations are valued, on a contract-by-contract basis, and are included in the cost to completion of the contract. Where this is not the case, a provision is set aside in the consolidated financial statements for any potential risk, estimated on a contract-by-contract basis.

In order to finance contract execution, the Group may receive advance payments from its customers, in accordance with contractual terms, which are recognised in liabilities in the balance sheet. In order to guarantee reimbursement of these advance payments if the contractual obligations

are not met, the Group may deliver, at the customer's request, an advance payment bond. At 31 December 2017, advance payment bonds amounted to €2,143.2million (€2,336.7 million at 31 December 2016).

The Group evaluates and sets aside provisions for warranty costs in order to guarantee the conformity of goods sold to the customer during

the contractual warranty period. In most cases, the provisional withholding of payment contractually applying during this period can be replaced by a warranty retention bond using a bank as intermediary. At 31 December 2017, warranty retention bonds amount to €90.4million (€114.9 million at 31 December 2016).

The maturity dates of these commitments are:

	< 1 year	1 to 5 years	> 5 years	31/12/2017	31/12/2016
Bid bonds	32.0	1.3	0.3	33.6	26.2
Performance bonds	741.8	832.4	238.3	1,812.5	2,288.6
Advance payment bonds	1,094.4	824.3	224.5	2,143.2	2,336.7
Warranty retention bonds	66.1	17.9	6.4	90.4	114.9
Other bank bonds	55.9	56.7	69.9	182.5	163.2
<b>TOTAL</b>	<b>1,990.2</b>	<b>1,732.6</b>	<b>539.4</b>	<b>4,262.2</b>	<b>4,929.6</b>

The awarding of major contracts, particularly within the defence sector, may be subject to local or regulatory offsetting obligations, which can take the form of direct offsetting, semi-direct offsetting or indirect offsetting. The associated risks are described under "risk factors" in the management report.

### Parent company guarantees

In addition, Thales may grant parent company guarantees to third parties on behalf of its subsidiaries without using a bank as an intermediary. At 31 December 2017, these guarantees amounted to €12,760.4million (€13,697.1 million at 31 December 2016).

These guarantees include all commitments given on behalf of Thales Alenia Space, which are backed by a counterguarantee from Leonardo in proportion to its interest in the capital of Thales Alenia Space (33%).

## NOTE 11. LITIGATION

Due to the nature of its business activities, Thales is exposed to the risk of technical and commercial litigation.

To prevent disputes or limit their impact, Thales' policy is to systematically seek alternative dispute resolution mechanisms. This policy is reviewed on a regular basis to take into account changes in the Group's core areas of business and is backed by employee training programmes.

In addition, Thales implemented a procedure several years ago to centralise all civil commercial and criminal litigation and claims. These are handled by the Corporate Legal Affairs department, with the support of the Group companies involved.

In October 2017, Thales was notified of an arbitration award in a commercial dispute between the Republic of China and a group of three French manufacturers, including Thales Systèmes Aéroportés, a Thales subsidiary.

As a result of this arbitration award, which pertains to a contract signed in 1992, the manufacturers were ordered to pay a total sum of €227 million including interest, of which €64 million was payable by Thales Systèmes Aéroportés. The corresponding charge was recognised under "Disposal of assets, changes in scope of consolidation and other" in the financial statements as at 31 December 2017 (see Note 3.2).

There are no other government, judicial or arbitration claims of which the Group is aware, which are pending or threatened and which could have or have had, any significant effect on the financial position or profitability of the Company and/or the Group in the last 12 months.

## NOTE 12. SUBSEQUENT EVENTS

To the best of the Group's knowledge, no significant events occurred after the end of the reporting period.

## NOTE 13. ACCOUNTING POLICIES

### a) Presentation of the financial statements

#### Consolidated profit and loss account

Expenses in the income statement are presented analytically by destination.

Income from operations is equal to income of operating activities before taking into account:

- gains and losses on disposal of disposals of property, plant and equipment and intangible assets, businesses or investments;
- the impact of changes in scope on consolidated net income (Note 13-b);
- the impact of the amendment, curtailment or liquidation of pension plans and other long-term benefits;
- the impairment of non-current operating assets;
- other operating income (expense) resulting from events that are unusual by their frequency, nature and amount.

#### Consolidated balance sheet

A significant portion of the Group's activities in its different business segments have long-term operating cycles. Accordingly, assets (liabilities) that are usually realised (settled) within the entities' operating cycles (inventory, accounts receivable and payable, advances, reserves, etc.) are classified in the consolidated balance sheet as current assets and liabilities, with no distinction between the amounts due within one year and those due after one year.

#### Consolidated statement of cash flows

The statement of cash flows provides an analysis of the change in cash and cash equivalents, as presented in the balance sheet and defined in Note 13-h. The statement of cash flows is prepared using the indirect method based on consolidated net income and is broken down into three categories:

- net cash flow from operating activities (including interest and taxes);
- net cash flow used in investing activities, including net operating investments (acquisition and disposal of property, plant and equipment and intangible assets, capitalisation of development costs) and net financial investments;
- net cash flow used in financing activities including dividends paid, from capital subscriptions (exercise of options by employees), the purchase/sale of treasury shares, the issuance and repayment of debt, and changes in bank overdrafts, etc.

The Group also presents the changes in its **net cash**, which is a non-GAAP measure and includes gross debt, net of cash and cash equivalents and liquid investments. Changes in net cash, presented in Note 6.4, notably reflect **Free operating cash flow**, defined as net cash flow from operating activities less net operating investments, plus the payment of the UK pension deficits.

#### Adjusted net income

In order to monitor and compare its operating and financial performances, the Group presents the following key indicators:

**EBIT**, corresponding to income from operations plus the share in net income of equity affiliates minus the amortisation of acquired intangible assets (purchase price allocation – PPA) recorded when significant businesses are combined. From 1 January 2016, it also excludes the other expenses recognised in current operational result that are directly related to business combinations, and which are unusual by nature.

**Adjusted net income** is regarded as pertinent by the Group as it excludes non-recurring items. It corresponds to consolidated net income attributable to shareholders of the parent company, less the following items, net of the corresponding tax impacts:

- amortisation of acquired intangible assets (PPA);
- other expenses recognised in current operational result that are directly related to business combinations, and which are unusual by nature;
- disposal of assets, changes in scope of consolidation and other;
- changes in the fair value of derivative foreign exchange instruments, recognised in "Other financial income";
- actuarial gains and losses on long-term employee benefits, included in "financial income on pensions and other employee benefits".

**Adjusted net income per share** corresponds to the adjusted net income attributable to shareholders of the parent company, divided by the average number of shares outstanding during the period concerned.

#### Off-balance sheet commitments

Disclosures regarding off-balance sheet commitments are presented in the following notes:

- Note 4.3: lease commitments;
- Note 9.3-f: funding obligations in respect of pensions;
- Note 10.4: commercial contract commitments.

#### Related parties

The Group has identified the following related parties: shareholders of Thales SA (parent company), notably the French State and Dassault Aviation, companies controlled by these shareholders, companies under joint control or significant influence, Directors and Senior Corporate Officers.

Section 4.3.3.3 of the 2017 Registration Document describes the main provisions concerning the shareholders' agreement governing relations between the French State ("public sector") and Dassault Aviation ("Industrial Partner") within Thales, the convention on the protection of national strategic interests and the specific convention binding the State and Thales.

Information related to transactions with related parties is presented in the following notes:

- sales with the French State (mainly with DGA: French defence procurement agency) in Note 6;
- transactions with companies under joint control and their joint shareholders in Note 5.1-e.

Transactions with other related parties are not material.

Expenses recognised in respect of compensation, benefits and social security contributions attributable to Directors and members of the Executive Committee are presented in Note 9.5.

### b) Scope of consolidation and changes in scope

#### Scope of consolidation

The financial statements of material subsidiaries directly or indirectly controlled by Thales are fully consolidated. The financial statements of material subsidiaries jointly controlled by Thales (Joint Ventures) or in which the Group has significant influence (associates) are accounted for under the equity method.

The main consolidated companies are listed in Note 16.

The full list of affiliates outside of France is available on the Group's website (<https://www.thalesgroup.com/en/corporate-responsibility#documents>).

#### Business combinations

Business combinations are accounted for under the acquisition method as described in IFRS 3. Under this method, the Group recognises identifiable assets acquired and liabilities assumed at fair value on their acquisition date. It also recognises non-controlling interests in an acquiree on their acquisition date.

Non-controlling interests are measured either at fair value or proportionate to the share of the identifiable net assets. This is determined on a case-by-case by the Group depending on the option it wishes to apply.

Acquisition-related costs (valuation fees, consulting fees, etc.) are recognised under “other operating expenses” as incurred.

Negative goodwill is immediately recognised in “other operating income (expenses)”. Positive goodwill related to controlled companies is recognised in balance sheet assets under intangible assets. Positive goodwill related to equity affiliates is recognised under “share in net income of equity affiliates”.

Goodwill is not amortised but is subject to impairment tests each year. Goodwill impairment is booked as an expense under “impairment of non-current operating assets” and may not be reversed. Goodwill impairment related to equity affiliates is recognised in “share in net income of equity affiliates” and may be reversed.

## c) Revenue recognition

The Group’s sales can be divided into two main accounting categories: sales of goods and services, and construction contracts.

Sales are measured at the fair value of the consideration received or receivable. When the deferral of payment has a material effect on the determination of fair value, the amount at which sales are recognised is adjusted to take the financial impact of the deferral of payment into account.

### Sales of goods and services

Income from the sales of goods and services together with royalty and licence income are recognised when future economic benefits are likely to flow to the Group and when the amount of sales can be measured reliably. The following specific criteria must also be satisfied in order for sales to be recognised:

- income from the sale of goods is recognised when the Company has transferred the principal risks and rewards inherent to ownership of the goods to the purchaser;
- income from services rendered is recognised according to the percentage-of-completion method.

The costs related to the service provided (sale of goods or services rendered) are recognised in the statement of income at the same time as the corresponding sales.

### Construction contracts

A construction contract is a contract specifically negotiated for the construction of an asset or group of assets that are closely linked or interrelated in terms of their design, technology, function, purpose or use.

According to its characteristics, a notified construction contract can either be accounted for separately, be segmented into several components which are each accounted for separately, or be combined with another construction contract in progress in order to form the scope of the contract for accounting purposes in respect of which sales and expenses will be recognised.

Sales and expenses on construction contracts are recognised in accordance with the technical percentage-of-completion method. However, when there is no significant time difference between technical percentage of completion and contractual dates of transfer of ownership, the percentage of completion is determined according to the contractual transfer of ownership.

Penalties for late payment or the improper execution of a contract are recognised as a deduction from sales. In the balance sheet, provisions for penalties are deducted from assets related to the contract.

Expected losses on contracts are fully recognised as soon as they are identified.

Selling, administrative and interest expenses are directly charged to the profit and loss account in the period in which they are incurred.

Estimates of work remaining on loss-making contracts do not include sales from claims made by the Group, except when it is highly probable that such claims will be accepted by the customer.

Progress payments received on construction contracts are deducted from contract assets as the contract is completed. Progress payments received before the corresponding work has been performed are classified in “advances received from customers on contracts” in balance sheet liabilities.

The cumulative amount of costs incurred and profit recognised, less any recognised losses and progress billings, is determined on a contract-by-contract basis. If this amount is positive, it is recognised under “Construction contracts: assets” in the balance sheet. If it is negative, it is recognised under “Construction contracts: liabilities”.

## d) Inventories and work in progress

In the consolidated balance sheet, work in progress related to construction contracts is included under “Construction contracts: assets” or “Construction contracts: liabilities”.

Inventories and work in progress are carried at their production cost (determined using the FIFO or weighted-average cost method) and written down when production cost exceeds their net realisable value. Work in progress, semi-finished and finished goods are stated at direct cost of raw materials, production labour and subcontractor costs incurred during production, plus an appropriate portion of production overheads and any other costs that can be directly allocated to contracts.

When material, the cost of debt incurred during the construction of a qualifying asset is incorporated in the value of the asset. When the funding is specific, the loan interest rate is used, otherwise the Group’s financing rate is used.

## e) Research and development expenses

A significant share of research and development expenses is funded by customers and government agencies. Internally funded research and development expenses are charged to the profit and loss account as incurred, except for project development costs which meet the criteria below. In this case, the development costs are capitalised in balance sheet assets:

- the product or process is clearly defined, and costs are separately identified and reliably measured;
- the technical feasibility of the product or project is clearly demonstrated, and the Group’s experience in this area is established;
- adequate resources are available to complete the project successfully;
- a potential market for the products exists or their usefulness, in case of internal use, is demonstrated;
- the Company intends to produce and market, or use the new product or process, and can demonstrate its profitability. Profitability is assessed on the basis of prudent commercial assumptions in order to reflect contingencies inherent to the long cycles of the Group’s activities, in particular Aerospace. Minimum internal rates of return are required in the case of projects deemed risky.

Capitalised development costs mainly relate to the Group’s Aerospace and Security activities, for which the products developed are relatively generic and can be sold to a larger number of potential customers. By contrast, development costs linked to Defence activities are for more specific and restricted markets with a more limited number of players: the specific features of the products developed make it harder to share development work and therefore harder to capitalise the associated costs.

Development costs are then amortised over the useful life of the product. The method of amortisation is generally determined by reference to expected future quantities over the period in which future economic benefits will be earned. If the method cannot be determined reliably, linear amortisation is adopted. The period of amortisation depends on the type of activity.

Assets are also subjected to impairment loss tests. The terms and assumptions taken into account to conduct these tests are described in Note 4. These impairment losses can be reversed. Impairment loss reversal criteria are identical to those retained when first capitalising development costs on a new project.

The Group receives tax credits related to research carried out by its subsidiaries. These tax credits are considered as operating grants and are therefore included in income from operations, when their award is not dependent on the generation of taxable income. Otherwise, they are recognised as a deduction from income tax expense.

## f) Restructuring costs

Provisions for restructuring costs are set aside when restructuring programs have been agreed and approved by Group management and have been announced before the balance sheet date, resulting in an obligating event of the Group to the third parties in question, as long as the Group does not expect consideration for these costs.

Such costs primarily relate to severance payments, costs for notice periods not worked and other costs linked to the closure of facilities such as write-offs of fixed assets. These costs and the costs directly linked to restructuring measures (removal costs, training costs of transferred employees, etc.) are recognised under "restructuring costs" in the profit and loss account.

## g) Property, plant and equipment and intangible assets

### Intangible assets

The Group's intangible assets mainly include:

- goodwill (Note 13-b);
- assets acquired in business combinations, primarily acquired technologies, customer relationships and the order backlog. These assets are recognised at fair value and amortised over their useful lives. The fair value of the assets is based on the market value. If no active market exists, the Group uses methods based on forecasts of the present value of the expected future operating cash flows (excess earnings method, royalty method, etc.);
- capitalised development costs (Note 13-e).

Intangible assets are submitted to impairment tests.

### Property, plant and equipment

Property, plant and equipment is stated at cost, net of any accumulated depreciation and accumulated impairment losses. Depreciation of property, plant and equipment is generally calculated on the basis of the following typical useful lives:

- 20 years for buildings;
- 1 to 10 years for technical facilities and industrial equipment and tooling;
- 5 to 10 years for other property, plant and equipment (vehicles, fixtures, etc.).

The depreciable amount takes into account the residual value of the asset. The different components of property, plant and equipment are recognised separately when their estimated useful lives or patterns of use, and thus the period over which they are depreciated or the depreciation methods applicable to them, are materially different.

Borrowing costs that are directly attributable to the acquisition or construction of an asset are capitalised as part of the cost of that asset.

## h) Financial assets, financial liabilities and derivatives

### Financial assets

Financial assets are initially recorded at fair value. They are subsequently measured at either fair value or amortised cost, depending on the category they fall into, as defined by IAS 39.

- Investments are designated as "available for sale" assets and measured at fair value. The fair value corresponds to the market price for shares quoted on a regulated market. For other shares, the fair value is usually determined using valuation models provided by independent third parties, or by reference to the share in net equity held by the Group. Changes in fair value are recognised directly in equity. If an impairment indicator is identified, impairment is recognised in "other financial income (expense)". Such impairments are only written back to profit and loss at the date of disposal of the security in question.
- Receivables and financial loans are recognised at amortised cost. They are subject to impairment if an impairment indicator is identified. Such impairment, recognised in "other financial income (expense)", may subsequently be reversed through profit and loss if the conditions which led to the impairment loss being recognised cease to exist.
- Deposits that Thales intends to hold until maturity are recognised at amortised cost.
- Other financial assets are estimated at fair value, with changes in fair value recognised in profit and loss. They include money market funds and other mutual funds, and interest rate products (certificates of deposit, term deposits, medium-term negotiable notes, etc.).
- "Cash and cash equivalents" includes cash at bank and in hand as well as cash equivalents (short-term and liquid investments that are easily converted into a known amount of cash and exposed to negligible risk of a change in value).

### Financial liabilities

Borrowings and other financial liabilities are measured at amortised cost using the effective interest rate. Upon initial recognition, premiums, redemption and issuance costs are included in the calculation of the effective interest rate and are recognised in the profit and loss account on an actuarial basis over the life of the loan.

### Derivatives

The Group uses financial instruments to manage and reduce its exposure to risks of changes in interest rates and foreign exchange rates.

**Foreign exchange derivatives** eligible for hedge accounting are accounted for as follows:

- the effective portion of the change in fair value of the hedging instrument is recognised directly in equity until such time as the hedged flows affect profit and loss. The ineffective portion is recognised in profit and loss;
- the amount of the foreign currency denominated transaction is subsequently translated at the exchange rate prevailing at the date of inception of the hedge.

Changes in the fair value of premiums or discounts related to forward foreign currency contracts, as well as the time value of foreign currency options, are recognised in "other financial income (expense)" as they are excluded from the hedging relationship.

**Interest-rate derivatives** are used either as fair value hedges or cash flow hedges:

- a fair value hedge is a hedge of the exposure to changes in the value of assets and liabilities;
- a cash flow hedge is a hedge of the exposure to changes in the value of future cash flows (unknown future interest flows payable on existing variable-rate borrowings or on highly probable future borrowing issues, for example).

In the case of fair value hedge relationships, particularly for the portion of fixed-rate bond debt swapped for a variable rate, the financial liabilities hedged by the interest-rate derivatives are remeasured to the extent of risk hedged. Changes in the value of hedged items are recognised in profit and loss for the period and are offset by symmetrical adjustments in interest-rate derivatives.

In the case of cash flow hedging relationships, the effective portion of changes in fair value of interest-rate derivatives shown in the balance sheet is recognised directly in equity until such time as the hedged flows affect profit and loss.

### i) Deferred taxation

Thales recognises deferred taxes when the tax value of an asset or liability differs from its book value.

Deferred tax assets are not recognised in the balance sheet if the company concerned does not reasonably expect to recover the tax asset. To assess its ability to recover deferred tax assets, the Group takes into account forecast taxable income of the tax entities concerned, generally over a five-year time-frame, non-recurring past events and tax strategies specific to each country.

### j) Pensions and other long-term employee benefits

The Group's defined benefit plan commitments are measured by independent actuaries using the projected unit credit method on the basis of estimated salaries at the date of retirement. The calculations mainly take into account assumptions concerning discounting as well as inflation, mortality and staff turnover rates, etc.

Changes in actuarial assumptions and experience adjustments – corresponding to the effects of differences between previous actuarial assumptions and what has actually occurred – give rise to actuarial gains and losses:

- actuarial gains and losses on post-employment benefits are recognised in full within other comprehensive income, and are not subsequently reclassified to profit and loss. Where appropriate, the same treatment is applied to adjustments linked to the ceiling on net assets for plans in surplus;
- actuarial gains and losses on other long-term benefits are recognised immediately in financial income (Note 9.3).

Past service cost, measured in cases of amendments or curtailments of plans, and plan settlements are recognised in full within non-recurring operating income in the period in which it is incurred.

Net interest expense, determined based on the discount rate of obligations, is recognised in financial income.

### k) Share-based payment

#### Free share plans

Between 2007 and 2013, and then again in 2016 and 2017, Thales granted free shares and/or performance shares to its employees. These allotments give rise to an expense representing the fair value of services received at the grant date. This payroll expense is recognised against equity.

The fair value of the services received is calculated by reference to the fair value of the shares at the grant date, less the present value of dividends forfeited by employees during the vesting period, taking into account the presence conditions.

Internal performance conditions are taken into account only by means of an adjustment in the projected number of instruments acquired by employees at the end of the vesting period. Therefore, they are not taken into account in the fair value estimate of the instruments granted, which is determined at the grant date.

The expense related to these plans is included in the current operating income with the consolidated reserves account as counterpart without impact on total equity. As the payment of compensation is subject to presence conditions, the corresponding expense is recorded over the vesting period on a straight-line basis. When appropriate, the expense is adjusted over the vesting period to reflect any losses of rights.

#### Share unit plans indexed to the value of the Thales share

A share unit plan indexed to the value of Thales shares, some of which are performance shares, was implemented in 2014 and in 2015. At the maturity date, the beneficiaries will receive the value, about half of which is in the form of shares and half in the form of cash-settled share-based payment.

The proportion delivered in shares follows the same accounting policies as those applied to free share plans. The accounting treatment applicable to cash-settled share-based payments is governed by IFRS 2. Under this policy, the services acquired and the liability incurred are measured at fair value. Until the liability is settled, debt is remeasured at each reporting date, with any changes in fair value recognised in income for the period. The remeasurement of the liability at the reporting date takes into account any changes in the value of the underlying shares, as well as whether or not the presence conditions and performance criteria have been met.

#### Phantom shares

Since this is a cash-settled plan, IFRS 2 requires an evaluation of vested services and the liability assumed at fair value. Until the payment of the liability, the debt is remeasured at the closing date and taken to profit and loss. The remeasurement of the debt takes into account the achievement of performance and/or presence conditions, as well as the change in value of the underlying shares.

#### Company savings plans

Employee share offerings with a discount to the market price proposed within Company savings plans do not include any vesting period for rights but are subject to a legal five-year lock-up period. The measurement of the advantages granted to employees takes into account the cost of the five-year lock-up period.

## NOTE 14. FEES PAID TO STATUTORY AUDITORS

The amounts of fees paid to the statutory auditors of Thales SA (parent company) and their networks recognised in profit and loss for 2016 and 2017 are presented below:

Other Services cover services required by law (e.g. interim dividend, capital increase) and other services compatible with the statutory auditor's role (certification of expenditures, agreed engagements, services of a tax-related nature without material impact, etc.).

(in € thousands)	Mazars		Ernst & Young Audit		Total	
	2017	2016	2017	2016	2017	2016
<b>Certification of accounts</b>	<b>6,221</b>	<b>5,427</b>	<b>5,052</b>	<b>4,627</b>	<b>11,273</b>	<b>10,054</b>
• Issuer	927	779	920	856	1,847	1,635
• Subsidiaries	5,294	4,648	4,132	3,771	9,426	8,419
<b>Other services</b>	<b>690</b>	<b>526</b>	<b>1,030</b>	<b>791</b>	<b>1,720</b>	<b>1,317</b>
• Issuer	197	190	193	31	390	221
• Subsidiaries	493	336	837	760	1,330	1,096
<b>TOTAL</b>	<b>6,911</b>	<b>5,953</b>	<b>6,082</b>	<b>5,418</b>	<b>12,993</b>	<b>11,371</b>

## NOTE 15. OTHER DISCLOSURES

The German group company Electronic Signalling Services (ESS) GmbH, located at 1 Thalesplatz, 71254 Ditzingen has claimed an exemption from their obligation to publish their respective German financial statements for the fiscal year 2017 by reference to Section 264 paragraph 3 of the German Commercial code.

## NOTE 16. LIST OF MAIN CONSOLIDATED COMPANIES

(excluding Thales SA, the parent company)

Company name	Country	% interest 31/12/2017	% interest 31/12/2016
<b>1. Consolidated subsidiaries<sup>(a)</sup></b>			
TDA Armements SAS <sup>(b)</sup>	France	—	100%
Thales Alenia Space SAS	France	67%	67%
Thales Alenia Space Italia SpA	Italy	67%	67%
Thales Air Operations SAS	France	—	100%
Thales Australia Ltd	Australia	100%	100%
Thales Avionics, Inc.	United States	100%	100%
Thales Avionics Electrical Systems SAS	France	100%	100%
Thales AVS France SAS (ex Thales Avionics SAS) <sup>(b)</sup>	France	100%	100%
Thales Canada Inc.	Canada	100%	100%
Thales Communications & Security SAS	France	100%	100%
Thales Defense & Security, Inc.	United States	100%	100%
Thales Deutschland GmbH (ex Thales Electronic Systems GmbH) <sup>(c)</sup>	Germany	100%	100%
Thales DMS France SAS (ex Thales Systèmes Aéroportés SAS) <sup>(b)</sup>	France	100%	100%
Thales Electron Devices SAS <sup>(b)</sup>	France	—	100%
Thales e-Security, Inc	United States	100%	100%
Thales Espana Grp, S.A.U.	Spain	100%	100%
Thales Ground Transportation Systems UK Ltd	United Kingdom	100%	100%
Thales Italia SpA	Italy	100%	100%
Thales IAS France SAS (ex Thales Air Systems SAS) <sup>(b)</sup>	France	100%	100%
Thales Nederland B.V.	Netherlands	99%	99%
Thales Norway AS	Norway	100%	100%

Company name	Country	% interest 31/12/2017	% interest 31/12/2016
Thales Optronique SAS <sup>(a)</sup>	France	—	100%
Thales Rail Signalling Solutions AG	Switzerland	100%	100%
Thales Services SAS	France	100%	100%
Thales Solutions Asia Pte Ltd	Singapor	100%	100%
Thales Training & Simulation SAS <sup>(b)</sup>	France	—	100%
Thales Transportation Systems GmbH <sup>(c)</sup>	Germany	—	100%
Thales Transport & Security (Hong-Kong) Ltd	Hong Kong	100%	100%
Thales Transport & Security Ltd	United Kingdom	100%	100%
Thales Underwater Systems SAS <sup>(b)</sup>	France	—	100%
Thales UK Ltd	United Kingdom	100%	100%
Trixell SAS	France	51%	51%
<b>2. Joint ventures (equity method)</b>			
Thales-Raytheon Systems Air and Missile Defense Command and Control SAS	France	50%	50%
Naval Group	France	35%	35%
Diehl Aerospace GmbH	Germany	49%	49%
Sofradir SAS	France	50%	50%
<b>3. Associates (equity method)</b>			
Aviation Communications & Surveillance Systems	United States	30%	30%
Airtanker Holdings Ltd	United Kingdom	13%	13%
Elettronica SpA	Italy	33%	33%
Telespazio SpA	Italy	33%	33%

(a) Companies with sales representing more than 0.5% of consolidated sales.

(b) In France, as at 31 December 2017, the main transactions carried out were as follows:

- Thales Air Systems SAS (now Thales IAS France SAS) absorbed the following companies: TDA Armements SAS, Thales Air Operations SAS, Thales Angénieux SAS, Thales Cryogénie SAS and Thales Optronique SAS,
- Thales Avionics SAS (now Thales AVS France SAS) absorbed the following companies: Thales Avionics LCD SAS, Thales Electron Devices SAS and Thales Training & Simulation SAS,
- Thales Systems Aéroportés SAS (now Thales DMS France SAS) absorbed the following companies: Thales Microelectronics SAS and Thales Underwater Systems SAS.

(c) Thales Transportation Systems GmbH merged into Thales Electronic Systems GmbH and was renamed Thales Deutschland GmbH.

## 1.2.7 Statutory auditors' report on the consolidated financial statements

*This is a translation into English of the statutory auditors' report on the consolidated financial statements of the Company issued in French and it is provided solely for the convenience of English-speaking users. This statutory auditors' report includes information required by European regulation and French law, such as information about the appointment of the statutory auditors or verification of the information concerning the Group presented in the management report. This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.*

To the Annual General Meeting of Thales,

### Opinion

In compliance with the engagement entrusted to us by your annual general meetings, we have audited the accompanying consolidated financial statements of Thales for the year ended December 31, 2017.

In our opinion, the consolidated financial statements give a true and fair view of the assets and liabilities and of the financial position of the Group as at December 31, 2017 and of the results of its operations for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

The audit opinion expressed above is consistent with our report to the Audit and Accounts Committee.

### Basis for opinion

#### • Audit framework

We conducted our audit in accordance with professional standards applicable in France. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the Statutory Auditors' Responsibilities for the Audit of the Consolidated Financial Statements section of our report.

#### • Independence

We conducted our audit engagement in compliance with independence rules applicable to us, for the period from January 1, 2017 to the date of our report and specifically we did not provide any prohibited non-audit services referred to in Article 5 (1) of Regulation (EU) No 537/2014 or in the French Code of Ethics (*Code de déontologie*) for statutory auditors.

## Justification of assessments – Key audit matters

In accordance with the requirements of Articles L. 823-9 and R. 823-7 of the French Commercial Code (*Code de commerce*) relating to the justification of our assessments, we inform you of the key audit matters relating to risks of material misstatement that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period, as well as how we addressed those risks.

These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on specific items of the consolidated financial statements.

### Recognition of construction contracts

#### Risk identified

A significant part of the Group's revenue and current operating income results from construction contracts accounted for using the percentage-of-completion method. These contracts are often spread over several years.

Thales determines the revenue and the expenses for construction contracts under the conditions described in Note 13-c "Revenue" to the consolidated financial statements.

The recognition of income and expenses relating to construction contracts during an accounting closing primarily depends on:

- estimates of the revenue and margin at completion, and notably the level of provisions for technical and commercial risks;
- technical milestones reached in the performance of the contracts.

For each contract, estimates of costs at completion, as well as the achievement of technical milestones, are based on the Group's internal systems and procedures, notably involving project managers. These estimates are reviewed regularly by the managements of the Global Business Units and the executive management, particularly at each closing date.

We considered the recognition of construction contracts to be a key audit matter, in view of the impact of these contracts on the consolidated financial statements of the Group and the level of estimation required by the management to determine results upon completion.

#### Our response

Our work notably consisted in:

- evaluating the Group's systems and procedures for estimating revenue and costs at completion and measuring technical milestones;
- reconciling the construction contract management data with the accounting data;
- selecting contracts that are significant due to their financial impact and risk profile and interviewing the account managers, the managements of the Global Business Units and the executive management on the progress made on these contracts and their assessment of the risks in order to:
  - assess the reflection in the accounts of the contractual clauses;
  - corroborate the main revenue's and costs at completion's assumptions with the costs incurred to date, the contractual data, and correspondence with the client or their representatives. These procedures take into account the experience gained in previous years on these contracts or on similar contracts;
  - assess the consistency of the revenue recognized on the contract and other items in the income statement and balance sheet in relation to the milestones reached and to the contractual conditions.

### Litigation

#### Risk identified

The Group carries out its activities in France and abroad in legal and regulatory environments that are complex and constantly evolving. Therefore, it is exposed to legal, technical and commercial risks.

The Group's legal department centralizes and handles, with assistance from the subsidiaries concerned, all civil, commercial and criminal litigation and claims.

The assessment of these risks and litigation by the management has resulted in the Group recording liabilities and provisions for impairment. Note 11 "Litigation" to the consolidated financial statements describes potential uncertainties relating to significant litigation and their progress.

We considered the listing and evaluation of litigation and the associated risks to be a key audit matter in view of the significance of the estimates made by the management and the potential materiality of their impact on the Group's income and shareholders' equity, should these estimates change.

#### Our response

With regard to technical and commercial litigation, our work notably consisted in:

- Evaluated the procedures in force within the Group relating to the listing, assessment and reflection in the accounts of civil, commercial and criminal litigation and claims and assessing their correct application via sampling;
- interviewing the Finance department, the Legal Department a Group Secretary and General Council, as well as the managements of the main consolidated entities, on the status of all significant litigation;
- questioning the Group's main lawyers to confirm the listing of litigation and assess the nature of the related risks and liabilities;
- reading the meetings' minutes of the Audit and Accounts Committee and the Board of Directors in order to assess the completeness of the list of significant litigation.

Lastly, we considered whether the risks and significant litigation identified during the implementation of these procedures are described appropriately in Note 11 "Litigation" to the consolidated financial statements.

## Implementation of IFRS 15 relating to revenue recognition

### Risk identified

IFRS 15, which will be mandatorily applicable for the year beginning on January 1, 2018, introduces new criteria for the recognition of revenue.

As from the end of 2016, the Group set up a work group to identify divergences with its current accounting methods. The Group measured the accounting impacts by relying on analyses of the contractual or general conditions applicable to its construction contracts and on a simulation tool developed internally by the Group.

These differences and the expected impact relating to the Group's key figures from January 1 to December 31, 2017 are presented in Note 1.2 to the consolidated financial statements.

We considered the adoption of IFRS 15 relating to the recognition of revenue to be a key audit matter, in view of the differences with the existing principles and methods, notably including the transition from the technical percentage of completion method to the percentage of completion method expense based in order to recognize the revenue from contracts which provide for criteria proving the transfer of control over time.

### Our response

Our work consisted in:

- assessing the compliance of the new revenue recognition principles and methods described in Note 1.2 to the consolidated financial statements with IFRS 15;
- verifying of the quantified impacts presented in the notes to the consolidated financial statements concerning the adoption of IFRS 15 on shareholders' equity and the order book as at January 1, 2017, as well as on revenue and 2017 profit. For this purpose, we:
  - selected contracts on the basis of their financial impact and risk profile;
  - assessed the Group's analyses of these contracts, which allowed it to decide on the transfer of control over time or point in time and, where applicable, the identification of the various performance obligations. We evaluated the contractual conditions for termination for convenience, legal memos and margin simulations performed by the Group;
  - Evaluated the functioning of the simulation tool developed internally and reconciled the data used in the tool and in the analyses done by the main subsidiaries with the accounting data.

Lastly, we assessed the appropriateness of the qualitative and quantitative information given in Note 1.2 to the consolidated financial statements.

## Verification of the Information Pertaining to the Group presented in the management report

As required by law and in accordance with professional standards applicable in France we have also verified the information pertaining to the Group presented in the Board of Directors's management report.

We have no matters to report as to its fair presentation and its consistency with the consolidated financial statements.

## Report on other legal and regulatory requirements

### • Appointment of the statutory auditors

We were appointed as statutory auditors of Thales by the ordinary and extraordinary Annual General Meeting held on June 25, 1983 for MAZARS and on May 15, 2003 for ERNST & YOUNG Audit.

As at December 31, 2017, MAZARS was in the 35th year and ERNST & YOUNG Audit in the 15th year of total uninterrupted engagement.

## Responsibilities of Management and those charged with Governance for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless it is expected to liquidate the Company or to cease operations.

The Audit and Accounts Committee is responsible for monitoring the financial reporting process and the effectiveness of internal control and risks management systems and where applicable, its internal audit, regarding the accounting and financial reporting procedures.

The consolidated financial statements were approved by the Board of Directors.

## Statutory Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

### • Objectives and audit approach

Our role is to issue a report on the consolidated financial statements. Our objective is to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with professional standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As specified in Article L. 823-10-1 of the French Commercial Code (*Code de commerce*), our statutory audit does not include assurance on the viability of the Company or the quality of management of the affairs of the Company.

As part of an audit conducted in accordance with professional standards applicable in France, the statutory auditors exercise professional judgment throughout the audit and furthermore:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence considered to be sufficient and appropriate to provide a basis for his opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management in the consolidated financial statements.
- Assess the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence

obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. This assessment is based on the audit evidence obtained up to the date of his audit report. However, future events or conditions may cause the Company to cease to continue as a going concern. If the statutory auditor concludes that a material uncertainty exists, there is a requirement to draw attention in the audit report to the related disclosures in the consolidated financial statements or, if such disclosures are not provided or inadequate, to modify the opinion expressed therein.

- Evaluate the overall presentation of the consolidated financial statements and assesses whether these statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. The statutory auditor is responsible for the direction, supervision and performance of the audit of the consolidated financial statements and for the opinion expressed on these consolidated financial statements.

#### • Report to the Audit and Accounts Committee

We submit a report to the Audit and Accounts Committee which includes in particular a description of the scope of the audit and the audit program implemented, as well as the results of our audit. We also report significant deficiencies, if any, in internal control regarding the accounting and financial reporting procedures that we have identified.

Our report to the Audit and Accounts Committee includes the risks of material misstatement that, in our professional judgment, were of most significance in the audit of the consolidated financial statements of the current period and which are therefore the key audit matters that we are required to describe in this report.

We also provide the Audit and Accounts Committee with the declaration provided for in Article 6 of Regulation (EU) No. 537/2014, confirming our independence within the meaning of the rules applicable in France as set out in particular in Articles L. 822-10 to L. 822-14 of the French Commercial Code (*Code de commerce*) and in the French Code of Ethics (*Code de déontologie*) for statutory auditors. Where appropriate, we discuss with the Audit and Accounts Committee the risks that may reasonably be thought to bear on our independence, and the related safeguards.

Courbevoie and Paris-La Défense, March 5, 2018

The Statutory Auditors  
(French original signed by)

#### **Mazars**

Anne-Laure Rousselou  
Jean-Marc Deslandes

#### **Ernst & Young Audit**

Philippe Diu  
Serge Pottiez

## 1.3 PARENT COMPANY MANAGEMENT REPORT AND FINANCIAL STATEMENTS

### 1.3.1 Management report on the parent company financial statements

#### 1.3.1.1 Activities and results

**Operating income** amounted to €741 million, compared with €636 million in 2016. Sales totalled €259 million, compared with €233 million in 2016.

Activities are described by sector in the accompanying notes.

Revenues mainly consist of rents re-billed to operating subsidiaries and sales of research, chiefly conducted by the Central Research and Technology department of Thales Group. The increase in revenues was mainly due to the billing of costs for rehabilitation of the site in Jouy en Josas and additional works on the sites in Elancourt and Toulouse Labège.

Other operating income amounted to €443 million, compared with €379 million in 2016. It includes royalties paid by direct operating subsidiaries, as well as expenses re-billed to those subsidiaries, including for general and specific centralised services provided by the parent company, and capitalised production. The main increase corresponds to re-billings in connection with the employee shareholding plan and the delivery of the 2013 free share plan.

**Net loss from operations amounted to -€90 million**, compared with a loss of -€93 million in 2016.

**Net financial income was €516 million**, compared with €464 million in 2016.

Provisions for equity investments and subsidiary risks totalled -€42 million in 2017 compared with -€58 million in 2016. Reversals of provisions for equity investments and subsidiary risks represented €10 million in 2017 compared with €53 million in 2016.

Income from investments amounted to €545 million in 2017, versus €496 million in 2016.

**Non-recurring expense** amounted to -€53 million, compared with -€17 million in 2016. The increase is mainly explained by the liquidation of Thales Belgium SA in 2017.

The Company recorded an income tax benefit of €10 million compared with €78 million in 2016, due largely to Research Tax Credits.

In 2017, non-deductible expenses pursuant to Articles 223 *quater* and 39.4 of the French Tax Code amounted to €0.2 million.

**Net profit for financial year 2017 came to €384 million**, compared with €431 million in 2016.

#### 1.3.1.2 Balance sheet at 31 December 2017

**The balance sheet total at year-end 2017 was €14,636 million**, up €334 million from €14,302 million at year-end 2016.

The total non-current assets of €9,241 million (€9,002 million in 2016) are mainly composed of financial investments. The €211 million increase in equity investments is mainly due to the acquisition of shares in Thales Air Systems SAS for €218 million.

Other financial investments rose by €36 million, largely as a result of the acquisition of treasury shares.

Current assets rose €95 million to €5,396 million at end-December 2017. Cash and cash equivalents increased by €267 million reflecting the improved operating cash flow of subsidiaries. The €406 million decrease in "Other receivables" was mainly due to foreign exchange adjustments (-€344 million) and a decrease in tax receivables from the French government (-€91 million).

The €50 million change in "Treasury shares allocated to plans" resulted mainly from the delivery of shares under the 2013 free share plan for -€49 million.

Other investments of €325 million correspond to deposits with first-tier banks with maturities of 3 to 12 months.

The balance of Group companies' current accounts represented net debt of €4,450 million at year-end 2017, compared with €4,350 million at year-end 2016.

"Borrowings" amounted to €1,571 million at year-end 2017, *versus* €1,459 million at year-end 2016. They mainly include bond issues for a total amount €1,400 million, as well as foreign-currency and euro denominated borrowings from Group subsidiaries and associates.

At year-end 2017, share capital stood at €638.0 million and total equity came to €6,882 million, compared with €6,829 million at year-end 2016.

#### Customer and Supplier payment schedules

Thales pays its suppliers 60 days after invoice date, in line with the maximum period allowed under the French law on the modernisation of the economy (*Loi de modernisation de l'économie* – LME).

The table below presents the ageing of receivables and payables by invoice date:

➤ **INVOICES RECEIVED AND ISSUED AT CLOSING DATE OF FINANCIAL YEAR JUST ELAPSED**  
(TABLE PROVIDED FOR IN SECTION I, ARTICLE D.441-4)

	Article D.441 I.-1e: Invoices received and not settled as at closing date of financial year just elapsed						Article D.441 I.-2e: Invoices issued and not settled as at closing date of financial year just elapsed					
	Day 0 (illustrative)	1 to 30 days	31 to 60 days	61 to 90 days	91 or more days	Total (or more days)	Day 0 (illustrative)	1 to 30 days	31 to 60 days	61 to 90 days	91 or more days	Total (1 or more days)
<b>A. Payment period tranches</b>												
Number of invoices involved	245					313	400					424
Total value of invoices involved (including taxes)	45.3	2.9	0.6	0.1	0.5	4.0	44.6	18.8	6.0	1.1	3.4	29.3
Percentage of total purchases during the year (including taxes)	7.55 %	0.48 %	0.09 %	0.01 %	0.09 %	0.66 %						
Percentage of total sales during the year (including taxes)							5.61 %	2.36 %	0.75 %	0.14 %	0.43 %	3.69 %
<b>B. Invoices excluded from (A) corresponding to debts and receivables in dispute or not posted</b>												
Number of invoices						9						56
Total invoices excluded, define: excluding or including taxes)						0.3						1.6
<b>C. Reference payment periods used (contractual or legal periods – Articles L.441-6 or L.443-1 of Commercial Code)</b>												
Payment periods used for calculating payment terms												
						Contractual periods: 45 days end of month Legal periods: (define)						Contractual periods: 45 days end of month Legal periods: (define)

### 1.3.1.3 Events after the reporting period

A tax audit was carried out on Thales SA's accounting records for the 2011 to 2015 reporting periods. This audit did not result in any significant adjustments for the Company.

### 1.3.1.4 Outlook for the current financial year

The Company results for 2018 are expected to reflect the dividends paid by certain subsidiaries for financial year 2017 and changes in provisions for impairment of equity investments and subsidiary risks as a consequence of trends in their business and performance in 2018.

### 1.3.1.5 Proposed allocations of earnings and dividend policy

The Annual General Meeting, deliberating under the *quorum* and majority conditions required for annual general meetings, noted<sup>(1)</sup> that distributable earnings include:

The net profit for financial year 2017	€383,832,504.79
Less allocations to legal reserve	(€139,187.70)
Plus retained earnings at 31 December 2017	€1,605,673,272.86
Plus interim dividend in the amount of €0.45 per share paid on 8 December 2017 and deducted from retained earnings	€95,195,572.65
<b>For a total amount of</b>	<b>€2,084,562,162.60</b>

The Annual General Meeting decided<sup>(1)</sup> to allocate this amount as follows:

Distribution of a dividend of €1.75 per share on 212,658,725 shares bearing rights as from 1 January 2017 (including the interim dividend of €0.45 per share paid on 8 December 2017 charged to the 2017 dividend, for a total amount of €95,195,572.65)	€372,152,768.75
Retained earnings after dividend	€1,712,409,393.85
<b>Total equivalent to distributable earnings</b>	<b>€2,084,562,162.60</b>

The Annual General Meeting notes that, taking into account the interim dividend of €0.45 per share paid on 8 December 2017 and deducted from retained earnings, the remaining dividend to be paid out is €1.30 per share.

The ex-dividend date is 30 May 2018 and payment date for the balance of the dividend will be 1 June 2018.

The sums corresponding to the dividends which, in accordance with the provisions of the fourth paragraph of Article L. 225-210 of the French Commercial Code, have not been paid on treasury shares held by the Company, will be reallocated as retained earnings.

In accordance with Article 243 *bis* of the French Tax Code, the entire declared dividend (interim and remaining dividend amount) qualifies for the 40% tax relief for individual taxpayers whose tax residence is in France, as provided for in Article 158-3 2° of the French Tax Code. As it relates to the remaining dividend amount, the tax relief is only applicable where an express, irrevocable and general election has been made for assessment according to the progressive scale for income tax. Where such election has not been made, the remaining dividend amount due to such individual taxpayers whose tax residence is in France will be subject to the flat rate tax (*prélèvement forfaitaire unique* or PFU) introduced by the 2018 Budget Law without application of the 40% tax relief.

In accordance with the law, the amounts of dividends paid out for the past three financial years are provided below:

Financial year	Dividend per share	Total amount paid out
2014	€1.12 <sup>(a)</sup>	€230,660,829.08
2015	€1.36 <sup>(a)</sup>	€285,659,762.04
<b>2016</b>	<b>€1.60<sup>(a)</sup></b>	<b>€338,279,587.20</b>

(a) The dividend corresponds to all income distributed for the financial year. The full dividend amount was eligible for the tax relief provided for in Article 158-3 2° of the French Tax Code.

(1) Subject to the approval of the Annual General Meeting of 23 May 2018.

### 1.3.1.6 Parent company management report cross-reference table

In accordance with Articles L. 225-100, L. 232-1, L. 247.1 and R. 225-102 of the French Commercial Code, the parent company management report includes the following information contained in the 2017 Registration Document:

Management report French Commercial Code	Sections/Notes	Pages
<b>1. Thales (parent company) financial statements at 31 December 2017</b>	<b>Section 1.3.2.5</b>	
Table of subsidiaries and equity affiliates	Note 23	112
Table of investments made and shareholding disclosures in French companies	Note 23	112
Table of the results of the Company for the past five financial years	Section 1.3.2.6	115
Table of outstanding stock purchase and subscription options at 31 December	Note 15	103
Change in number and in value of the treasury shares of the Company	Note 14	102
Write-back of general expenses following tax adjustment	Note 6	96
Events after the reporting period	Note 22	111
Information on existing branches (Article L. 232-1, II of the French Commercial Code)	Note 24	115
<b>2. Control and risk management system</b>	<b>Section 1.1.3</b>	<b>28</b>
<b>3. Management report and consolidated financial statements of the Group at 31 December 2017</b>	<b>Chapter 1 et 2</b>	<b>6 to 137</b>
Presentation of the activities of the Company, its subsidiaries and controlled companies	Section 2.4	135
Description of the main risks and uncertainties facing the Group	Section 1.1.2	17
Information on the use of financial instruments (as a complement of the notes to the financial statements)	Section 1.1.2	17
Information on the research and development activities	Section 2.2	130
<b>4. Corporate Governance</b>	<b>Chapter 3</b>	
Compensation of other Group executives	Section 3.4.1	169
Share-based payments	Section 3.4.2	169
<b>5. Company and share capital</b>	<b>Chapter 4</b>	
Breakdown of shareholders and changes performed during the financial year	Section 4.2.1	177
Employee shareholdings	Section 4.2.3.6	186
Description of the share repurchase program adopted by the Annual General Meeting of 18 May 2016	Section 4.2.3.4	182
Transactions involving treasury shares during the financial year	Section 4.2.3.8	188
Summary statement of transactions carried out during the financial year by directors, non-voting directors and related persons	Section 4.2.3.7	187
Regulated agreements (continued existing agreements, with the exception of the assistance agreement between Thales and TSA which is now subject to the rules applicable to agreements relating to current operations (L. 225-39 of the French Commercial Code))	Section 4.3	189
Thales share price trend over the past two financial years	Section 4.4.1.3	193
<b>6. Corporate responsibility</b>	<b>Chapter 5</b>	
Social information	Section 5.1	200
Environmental information	Section 5.2	217
Societal information	Section 5.3	231
Information on the allocation of free shares during the financial year	Section 5.1.4.4	210
Responsibility of the Independent Third-Party	Section 5.4	240

## 1.3.2 Thales parent company financial statements for the year ended 31 December 2017

### 1.3.2.1 Income statement

(in € millions)	Notes	2017	2016
Re-billing of rents		244.4	220.0
Research		14.1	13.3
<b>Sales</b>		<b>258.5</b>	<b>233.3</b>
Royalties		231.1	215.2
Re-billing of expenses		212.3	163.4
<b>Other operating income</b>		<b>443.4</b>	<b>378.6</b>
Reversals of provisions		21.3	16.0
Transfer of expenses		18.0	7.8
<b>TOTAL OPERATING INCOME</b>		<b>741.2</b>	<b>635.7</b>
Purchases and changes in inventories and work-in-progress		(40.2)	(27.3)
Other external charges		(533.2)	(451.2)
Taxes other than on income		(11.8)	(11.9)
Personnel expenses		(207.7)	(191.5)
Depreciation and amortisation		(20.8)	(20.9)
Increase in provisions		(17.1)	(26.1)
<b>Total operating expenses</b>		<b>(830.8)</b>	<b>(728.9)</b>
<b>INCOME (LOSS) FROM OPERATIONS</b>	Note 3	<b>(89.6)</b>	<b>(93.2)</b>
Net interest and finance costs		(1.0)	(1.1)
Income from investments		544.7	496.1
Other financial income		37.6	60.6
Other financial expenses		(65.2)	(92.1)
Financial income (expense)	Note 4	516.1	463.5
<b>PROFIT (LOSS) FROM ORDINARY ACTIVITIES BEFORE INCOME TAX</b>		<b>426.5</b>	<b>370.3</b>
<b>Non-recurring income (expense)</b>	Note 5	<b>(52.5)</b>	<b>(17.2)</b>
<b>PROFIT (LOSS) BEFORE INCOME TAX</b>		<b>374.0</b>	<b>353.1</b>
<b>Income tax benefit (expense)</b>	Note 6	<b>9.8</b>	<b>78.0</b>
<b>PROFIT FOR THE YEAR</b>		<b>383.8</b>	<b>431.1</b>

The Notes to the financial statements are an integral part of the parent company financial statements.

### 1.3.2.2 Balance sheet

#### Assets

(in € millions)	Notes	31/12/2017	31/12/2016
Intangible assets and property, plant and equipment, net	Note 7	112.3	120.4
Equity investments	Note 8	8,999.0	8,787.6
Treasury shares not assigned to plans	Note 14	50.3	11.6
Other financial investments	Note 9	79.1	82.1
<b>Total non-current assets</b>		<b>9,240.7</b>	<b>9,001.7</b>
Inventories and work in progress		11.8	12.0
Advances to suppliers	Note 16	0.4	0.1
Trade receivables	Note 16	197.1	188.8
Other receivables	Note 16	327.6	733.1
Group company current-account receivables	Note 10	1,079.3	875.8
Treasury shares assigned to plans	Note 14	—	50.0
Accrued interests		3.8	7.3
Other investments	Note 11	325.0	250.0
Cash and cash equivalents	Note 11	3,450.5	3,183.1
<b>Total current assets</b>		<b>5,395.5</b>	<b>5,300.2</b>
<b>TOTAL ASSETS</b>		<b>14,636.2</b>	<b>14,301.9</b>

#### Shareholders' equity and liabilities

(in € millions)	Notes	31/12/2017	31/12/2016
Share capital		638.0	636.6
Additional paid-in capital		4,053.2	4,036.9
Reserves and retained earnings		1,806.8	1,724.6
Profit for the year		383.8	431.1
<b>Total shareholders' equity</b>	Note 13	<b>6,881.8</b>	<b>6,829.2</b>
<b>Provisions for contingencies and losses</b>	Note 17	<b>199.0</b>	<b>197.8</b>
Borrowings	Note 12	1,570.7	1,459.2
Group company current-account payables	Note 10	5,528.9	5,225.8
Advances received on contracts in progress	Note 16	17.8	18.8
Trade payables	Note 16	86.8	99.5
Other liabilities	Note 16	351.2	471.6
<b>Total liabilities</b>		<b>7,555.4</b>	<b>7,472.7</b>
<b>TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES</b>		<b>14,636.2</b>	<b>14,301.9</b>

The Notes to the financial statements are an integral part of the parent company financial statements.

### 1.3.2.3 Statement of cash flows

(in € millions)	Notes	2017	2016
<b>Profit for the year</b>		<b>383.8</b>	<b>431.1</b>
<b>Add (deduct):</b>			
Net depreciation, amortisation and impairment charges on intangible assets and property, plant and equipment	Note 7	20.8	20.9
Provisions for post-employment and other employee benefits	Note 17	5.2	5.8
Net provisions for impairment of investments and subsidiary risks	Note 4	32.3	5.3
Loss (gain) on disposals of assets	Note 5	40.4	13.0
Other items		(6.1)	0.6
<b>Operating cash flow</b>		<b>476.4</b>	<b>476.7</b>
Change in working capital and provisions for operating contingencies and losses		261.1	53.5
<b>CASH FLOW FROM OPERATING ACTIVITIES</b>	<b>- I -</b>	<b>737.5</b>	<b>530.2</b>
Payments for acquisitions of intangible assets and property, plant and equipment		(13.1)	(10.2)
Proceeds from disposal of intangible assets and property, plant and equipment		–	0.9
<b>Net operating investment</b>	Note 7	<b>(13.1)</b>	<b>(9.3)</b>
Investments in subsidiaries and associates	Note 8	(281.2)	(147.4)
Disposals of subsidiaries and associates	Note 8	9.8	21.7
Decrease (increase) in other investments	Note 11	(74.8)	(250.0)
Decrease (increase) in other financial investments and treasury shares		(12.4)	(60.3)
Decrease (increase) in current-account receivables		(223.3)	95.6
<b>Net financial investment</b>		<b>(581.9)</b>	<b>(340.4)</b>
<b>CASH FLOW USED IN INVESTING ACTIVITIES</b>	<b>- II -</b>	<b>(595.0)</b>	<b>(349.7)</b>
Dividend distributions	Note 13	(348.9)	(296.8)
Increase in share capital (exercise of subscription options)		18.0	45.7
Increase in borrowings		207.7	600.0
Decrease in borrowings		(128.9)	(641.8)
Increase (decrease) in current-account payables		377.0	345.7
<b>CASH FLOW FROM FINANCING ACTIVITIES</b>	<b>- III -</b>	<b>124.9</b>	<b>52.8</b>
<b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>I + II + III</b>	<b>267.4</b>	<b>233.3</b>
Cash and cash equivalents at the beginning of the period		3,183.1	2,949.8
<b>Cash and cash equivalents at the end of the period</b>		<b>3,450.5</b>	<b>3,183.1</b>

The Notes to the financial statements are an integral part of the parent company financial statements.

### 1.3.2.4 Statement of changes in equity

(in € millions)	Number of shares outstanding (in thousands)	Share capital	Issue premiums	Retained earnings	Profit for the year	Total shareholders' equity
<b>At 1 January 2016</b>	<b>210,961</b>	<b>632.9</b>	<b>3,995.4</b>	<b>1,149.5</b>	<b>871.9</b>	<b>6,649.7</b>
Allocation of 2014 profit	—	—	—	871.9	(871.9)	0.0
Dividend distribution (see Note 13.2)	—	—	—	(296.8)	—	(296.8)
Capital increase	1,234	3.7	41.5	—	—	45.2
2016 profit	—	—	—	—	431.1	431.1
<b>At 31 December 2016</b>	<b>212,195</b>	<b>636.6</b>	<b>4,036.9</b>	<b>1,724.6</b>	<b>431.1</b>	<b>6,829.2</b>
Allocation of 2016 profit	—	—	—	431.1	(431.1)	0.0
Dividend distribution (see Note 13.2)	—	—	—	(348.9)	—	(348.9)
Capital increase	464	1.4	16.3	—	—	17.7
2017 profit	—	—	—	—	383.8	383.8
<b>At 31 December 2017</b>	<b>212,659</b>	<b>638.0</b>	<b>4,053.2</b>	<b>1,806.8</b>	<b>383.8</b>	<b>6,881.8</b>

The Notes to the financial statements are an integral part of the parent company financial statements.

### 1.3.2.5 Notes to the parent company financial statements

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All the amounts in these notes are expressed in millions of euros (€m), with the exception of information related to numbers of employees and shares.

## NOTE 1. ACCOUNTING PRINCIPLES

Thales is a French public limited company (*société anonyme*) and the parent company of Thales Group.

The Thales parent company financial statements are prepared in accordance with the accounting principles applicable in France pursuant to the provisions of the French General Chart of Accounts (*Plan Comptable Général*) as defined in ANC Regulation 2017-03.

As from 1 January 2017, the accounting principles relating to forward financial instruments and hedging transactions are changing in accordance with ANC Regulation 2015-05 of 2 July 2015. This new regulation has no impact on shareholders' equity as at 1 January 2017. The impact on the presentation of the financial statements is described in Notes 16 and 20.

These principles are detailed in each note hereafter.

## NOTE 2. CHANGE IN THALES'S DIRECTLY OWNED INVESTMENTS

As part of the simplification of the legal structures in France, the following operations were carried out in 2017:

### 1- Mergers in DMS France SAS:

In September 2017 Thales sold Thales Microelectronics SAS shares to Thales Systèmes Aéroportés SAS (€4.6 million).

In December 2017, Thales Underwater Systems SAS and Thales Microelectronics SAS merged into Thales Systèmes Aéroportés SAS, with legal effect as of 31 December 2017. Thales now owns 100% of the company, renamed Thales DMS France SAS on 1 January 2018.

The value of Thales DMS France SAS shares as at 31/12/2017 was €802.6 million corresponding to the sum of the book values of the companies' shares before the merger.

### 2- Mergers in LAS France SAS:

In September 2017 Thales purchased the shares of Thales Air Systems SAS held by Thales Systèmes Aéroportés SAS (€218.4 million).

In September 2017 Thales sold Thales Cryogénie SAS shares to Thales Air Systems SAS (€0.7 million) after recapitalising it (€1.0 million).

In October 2017, Thales Systems Ireland Ltd merged into Thales Air Systems SAS.

In December 2017, TDA Armements SAS, Thales Angénieux SAS, Thales Optronique SAS, Thales Air Operations SAS and Thales Cryogénie SAS merged into Thales Air Systems SAS, with legal effect as at 31 December 2017. Thales now owns 100% of the company, renamed Thales DMS France SAS at 1 January 2018.

The value of Thales LAS France SAS shares at 31 December 2017 was €754.9 million, corresponding to the sum of the book values of the companies' shares before the merger.

### 3- Mergers in AVS France SAS:

In September 2017, Thales recapitalised Thales Electron Devices SAS (€40.0 million).

In December 2017, Thales Avionics LCD SAS, Thales Electron Devices SAS and Thales Training & Simulation SAS merged into Thales Avionics SAS, with legal effect as at 31 December 2017. Thales now holds 93.04% of the company, renamed Thales AVS France SAS on 1 January 2018.

The value of Thales AVS France SAS shares at 31/12/2017 was €1,016 million, the sum of the book values of the companies' shares before the merger.

Thales recapitalised Thales SESO SAS (€21.8 million).

On 3 May 2017 Thales Belgium SA was dissolved and liquidated. Thales recognised a capital loss of €26.8 million (Note 5.2) and received a dividend of €25.9 million (Note 4.2). At the same time Forges de Zeebrugge was renamed Thales Belgium SA.

In 2016, Thales purchased the shares in Thales Canada Inc held by Thales Avionics SAS, Thales Overseas Ltd and Thales Nederland BV for €22.1 million, €8.6 million and €1.6 million, respectively. Thales Canada Inc is now wholly-owned by Thales.

Thales had purchased Forges de Zeebrugge from Thales Defense Armements SAS for €26.2 million and then increased the share capital by €8 million with the intention of acquiring the business of Thales Belgium SA.

## NOTE 3. OPERATING PROFIT (LOSS)

In addition to its functions as a holding company (holding equity investments, managing central support functions and cash pooling), the parent company manages the real estate of its French operating subsidiaries and carries out its own research activity in France.

### 3.1 Operating income

Consequently, operating income includes:

- rents re-billed to operating subsidiaries and sales of research, which represent the sales of the parent company (€258.5 million in 2017 compared to €233.3 million in 2016), mainly realised in France;
- royalties paid by subsidiaries for shared services, and re-billed expenses for general and specific services provided to the subsidiaries by the parent company.

### 3.2 Operating expenses

Operating expenses mainly include personnel expenses (employees of Thales parent company and directors), real estate rents and related services, and other external services (notably provided by Thales Global Services, which incorporates the Group's shared services).

## NOTE 4. FINANCIAL INCOME (EXPENSE)

### 4.1 Accounting principles

Financial income (expense) mainly includes:

- interest expenses and finance costs on net debt;
- income and expenses related to Thales' directly owned investments (dividends and depreciation, see Note 8);
- the financial component of the increase in provisions for post-employment and other employee benefits (see Note 17);
- foreign exchange gains and losses (see Note 20).

### 4.2 Analysis of financial income (expense)

	Notes	2017	2016
<b>NET INTEREST AND FINANCE COSTS</b>		<b>(1.0)</b>	<b>(1.1)</b>
<b>Interest and financial income:</b>		<b>27.9</b>	<b>32.8</b>
Interest on Group company current account receivables and loans to subsidiaries and associates		4.9	4.5
Interest on cash and cash equivalents		23.0	28.3
<b>Interest and financial expenses:</b>		<b>(38.6)</b>	<b>(48.4)</b>
Interest on Group company current account payables and borrowings from subsidiaries and associates		(6.6)	(10.2)
Interest on bonds and other borrowings		(32.0)	(38.2)
<b>Interest on interest rate swaps hedging borrowings</b>		<b>9.7</b>	<b>14.5</b>
<b>INCOME FROM INVESTMENTS <sup>(a)</sup></b>	Note 23	<b>544.7</b>	<b>496.1</b>
<b>OTHER FINANCIAL INCOME</b>		<b>37.6</b>	<b>60.6</b>
Reversal of provisions related to associates <sup>(b)</sup>		9.9	53.1
Reversal of provisions for termination payments and other benefits	Note 17	–	1.2
Foreign exchange gains		23.6	0.3
Reversal of provisions for currency risks		1.8	1.7
Amounts recovered on clawback provisions		1.2	0.7
Other		1.1	3.6
<b>OTHER FINANCIAL EXPENSES</b>		<b>(65.2)</b>	<b>(92.1)</b>
Increase in provisions related to associates <sup>(b)</sup>		(42.2)	(58.4)
Increase in provisions for impairment of treasury shares		(2.1)	–
Increase in provisions for termination payments and other benefits	Note 17	(9.0)	(10.6)
Foreign exchange losses		(0.1)	(18.3)
Increase in provisions for currency risks		(1.9)	–
Waiver of loan		(7.5)	–
Other		(2.4)	(4.8)
<b>FINANCIAL INCOME (EXPENSE)</b>		<b>516.1</b>	<b>463.5</b>

(a) Including Thales Belgium SA (€25.9 million).

(b) Provisions related to subsidiaries and associates	2017		2016	
	Reversal	Increase	Reversal	Increase
<b>Provisions for impairment of equity investments</b>	–	(27.3)	52.3	(48.5)
Avimo Group Ltd	–	(10.4)	4.3	–
Thales SESO SAS	–	(10.3)	–	(11.2)
THALES GLOBAL SERVICES SAS	–	(6.2)	–	–
Thales Holdings UK Plc	–	–	35.1	–
Thales Belgium SA	–	–	9.6	–
Thales Microelectronics SAS	–	–	1.2	–
Thales Avionics Electrical Systems SAS	–	–	–	(33.0)
Other	–	(0.4)	2.1	(4.3)
<b>Provisions for subsidiary risks (see Note 17.2)</b>	<b>9.9</b>	<b>(14.9)</b>	<b>0.8</b>	<b>(9.9)</b>
Thales Digital Factory SAS	–	(7.9)	–	–
Thales Global Services SAS	–	(5.3)	–	–
Thales SESO SAS	9.9	–	–	(9.9)
Other	–	(1.7)	0.8	–
<b>TOTAL</b>	<b>9.9</b>	<b>(42.2)</b>	<b>53.1</b>	<b>(58.4)</b>

## NOTE 5. NON-RECURRING INCOME (EXPENSE)

### 5.1 Accounting principles

Non-recurring income (expense) includes:

- restructuring costs: these primarily relate to severance payments, redundancy payments, costs for notice periods not worked and other costs linked to the closure of facilities such as site rehabilitation or asset write-offs. These costs and the costs directly linked to restructuring measures (removal costs, training costs for transferred employees, etc.) are recognised as restructuring costs in the income statement;
- capital gains or losses on disposals, particularly of businesses or equity investments. As an exception to the guidelines of the French General Chart of Accounts and in order to give a more accurate presentation of these transactions, reversals of provisions for impairment of equity investments and reversals of provisions for subsidiary risks are included in income from disposals;
- other income and expenses arising on events that are unusual as regards their frequency, nature or amount.

### 5.2 Analysis of non-recurring income (expense)

	2017	2016
<b>Restructuring costs</b>	<b>(11.3)</b>	<b>(7.7)</b>
<b>Capital gains or losses on disposals</b>	<b>(40.4)</b>	<b>(13.0)</b>
Liquidation of Thales Belgium SA	(26.8)	–
Disposal of Thales Microelectronics SAS	(5.3)	–
Sale of treasury shares	(1.6)	2.4
Disposal of Cryogénie SAS	(0.7)	–
Reimbursement of Thales Suisse capital	–	(13.7)
Disposal of Thales Université SAS	–	(3.4)
Disposal of Thales Geodis Freight & Logistics SA	–	3.6
Other	(6.0)	(1.9)
<b>Reversal (increase) in provisions for non-recurring risks</b>	<b>(0.8)</b>	<b>3.5</b>
<b>NON-RECURRING INCOME (EXPENSE)</b>	<b>(52.5)</b>	<b>(17.2)</b>

## NOTE 6. INCOME TAX

### 6.1 General framework and accounting principles

Since 1 January 1992, Thales has opted for the Group tax consolidation regime. Thales is the head of a tax consolidation group that includes the majority of its French subsidiaries pursuant to the tax regime provided for by Article 223A of the French Tax Code.

In accordance with the tax consolidation agreement entered into between Thales and its subsidiaries, each subsidiary in the tax group records the amount of tax it would have paid had they been taxed separately. Any tax savings arising on the use of tax losses of subsidiaries are recorded by the parent company and recognised in the income statement. However, the parent company may have to record a corresponding tax expense, if and when these subsidiaries return to profit and are able to deduct the losses as they would have done had they been taxed separately.

The corporate income tax rate for fiscal years 2017 and 2016 was 34.43%, including the social contribution on profits. Tax loss carryforwards are attributable up to the limit of 50% of taxable profit in excess of €1 million.

In addition, the amended 2012 Finance Act had introduced a 3% tax on dividends paid. By a decision published on 6 October 2017, the French Constitutional Council overturned this tax entirely. In December 2017, Thales was reimbursed the full amount paid between 2013 and 2017, representing €41.9 million, including default interest. Against this backdrop, the amended Finance Act introduced an exceptional tax for 2017, taking the corporate tax rate for Thales from 34.43% to 44.43%. The corresponding expense amounts to €45.2 million. These amounts were deducted from/reimbursed to subsidiaries according to the existing tax consolidation agreement.

Thales also benefits from tax credits related to its research and development activities at the Palaiseau site which are recorded against income tax expense.

### 6.2 Current tax

The income tax benefit breaks down as follows:

	2017	2016
Income tax benefit received from tax group subsidiaries	176.3	173.4
Income tax due to the French State	(159.0)	(109.8)
<b>Income tax benefit resulting from tax consolidation</b>	<b>17.3</b>	<b>63.6</b>
Exceptional contribution due to Thales by beneficiary subsidiaries	25.1	–
Exceptional contribution due to the French State by Thales	(45.2)	–
<b>Expense resulting from tax consolidation under the exceptional contribution</b>	<b>(21.1)</b>	<b>–</b>
Reimbursement by Thales to beneficiary subsidiaries of the 3% tax on dividends	(30.4)	12.3
3% tax on dividends paid to the French State	(7.6)	(8.9)
Reimbursement by the State of the 3% tax on dividends	41.9	–
<b>Benefit resulting from tax consolidation under the 3% tax on dividends</b>	<b>3.9</b>	<b>3.4</b>
Research tax credit	8.6	7.7
Prior period adjustments and other taxes	1.1	3.3
<b>INCOME TAX BENEFIT</b>	<b>9.8</b>	<b>78.0</b>

In 2017 as in 2016, no non-deductible general expenses were reintegrated as a result of a tax audit. Expenditure excluded from deductible expenses in accordance with Articles 223 *quater* and 39.4

of the French Tax Code amounted to €0.2 million in both 2017 and 2016, reflecting excess amortisation of vehicles.

### 6.3 Deferred tax

The Company has available future tax savings due to temporary differences arising on the different tax and accounting treatments of income and expenses (€143.3 million at 31 December 2017 compared with €128.0 million at 31 December 2016). These mainly reflect provisions for contingencies and losses, in particular provisions

for post-employment benefits, which are not deductible for tax purposes. There were no remaining tax loss carryforwards at 31 December 2017.

The corresponding deferred tax is not recognised.

## NOTE 7. PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

### 7.1 Accounting principles

Intangible assets (mainly software) and property, plant and equipment are recognised at their acquisition cost in the balance sheet. They are amortised or depreciated on a straight-line or declining-balance basis, over the period of their estimated useful lives (20 years for buildings and 3 to 10 years for other assets).

Fixed assets held under finance leases or hire purchase agreements are not recognised and are reported in off-balance sheet commitments.

### 7.2 Breakdown by type

	31/12/2017			31/12/2016		
	Gross value	Cumulated amort. and depr.	Net	Gross value	Cumulated amort. and depr.	Net
<b>Intangible assets</b>	<b>18.9</b>	<b>(18.8)</b>	<b>0.1</b>	<b>18.8</b>	<b>(18.7)</b>	<b>0.1</b>
Buildings	209.7	(122.7)	87.0	201.5	(109.5)	92.0
Industrial plant, equipment and machinery	39.5	(36.3)	3.2	44.0	(41.0)	3.0
Other property, plant and equipment	34.9	(12.9)	22.0	36.0	(10.7)	25.3
<b>Property, plant and equipment</b>	<b>284.1</b>	<b>(171.9)</b>	<b>112.2</b>	<b>281.5</b>	<b>(161.2)</b>	<b>120.3</b>
<b>TOTAL</b>	<b>303.0</b>	<b>(190.7)</b>	<b>112.3</b>	<b>300.3</b>	<b>(179.9)</b>	<b>120.4</b>

### 7.3 Change in net assets

	Intangible assets	Property, plant and equipment	Total
<b>Net value at 01/01/2016</b>	<b>–</b>	<b>132.2</b>	<b>132.2</b>
Acquisitions	0.2	10.0	10.2
Disposals	–	(0.9)	(0.9)
Depreciation and amortisation	(0.2)	(20.7)	(20.9)
Other	0.1	(0.3)	(0.2)
<b>Net value at 31/12/2016</b>	<b>0.1</b>	<b>120.3</b>	<b>120.4</b>
Acquisitions	0.1	13.1	13.2
Disposals	–	–	–
Depreciation and amortisation	(0.1)	(20.7)	(20.8)
Other	–	(0.5)	(0.5)
<b>NET VALUE AT 31/12/2017</b>	<b>0.1</b>	<b>112.2</b>	<b>112.3</b>

## NOTE 8. EQUITY INVESTMENTS

### 8.1 Accounting principles

Equity investments are recorded at cost price and related acquisition costs are recognised in the income statement. In the event that the inventory value exceeds the book value, a provision for impairment is recorded for the difference.

The inventory value is determined based on profitability forecasts, the underlying assets, recent transactions or the market price of any listed securities.

The profitability forecasts are determined on the basis of expected future cash flows set out in the three-year strategic plans and a terminal value.

The assumptions used are prudent with forecast growth in sales and terminal values limited to 2%.

The discount rate used is calculated on the basis of the Group's weighted average cost of capital (8.5% in 2017 as in 2016), adjusted if necessary for the specific risks attributable to each equity investment. This rate is mainly based on the market risk-free rate, risk factors inherent in the Group's businesses, the Group's marginal borrowing rate and specific risks for which cash flows have not been adjusted.

Impairment tests are carried out annually at year-end in line with the Group's internal schedule for the preparation of Group entity strategic plans.

### 8.2 Change in equity investments

A breakdown of equity investments is presented in Note 23. Changes are presented below:

	Notes	Gross value	Provisions	Net
<b>VALUE AT 01/01/2016</b>		<b>10,005.5</b>	<b>(1,332.2)</b>	<b>8,673.3</b>
<b>Acquisitions/capital subscriptions and transactions</b>		<b>147.4</b>		<b>147.4</b>
Increase in capital of Thales Avionics Electrical Systems SAS		76.0	–	76.0
Purchase and increase in capital of Forges de Zeebrugge		34.2	–	34.2
Increase in capital of Thales Université SAS		5.0	–	5.0
Acquisition of shares in Thales Canada Inc		32.2	–	32.2
<b>Disposals</b>		<b>(21.7)</b>	<b>–</b>	<b>(21.7)</b>
Sale of Thales Geodis Freight & Logistics SA		(5.7)	–	(5.7)
Reimbursement of capital of Thales Suisse		(16.0)	–	(16.0)
<b>Increase in provisions for impairment</b>	Note 4	<b>–</b>	<b>(48.5)</b>	<b>(48.5)</b>
<b>Reversal of provisions for impairment</b>	Note 4	<b>–</b>	<b>52.3</b>	<b>52.3</b>
<b>OTHER</b>		<b>(41.1)</b>	<b>25.9</b>	<b>(15.2)</b>
<b>VALUE AT 31/12/2016</b>		<b>10,090.1</b>	<b>(1,302.5)</b>	<b>8,787.6</b>
<b>Acquisitions/capital subscriptions and transactions</b>		<b>281.2</b>	<b>–</b>	<b>281.2</b>
Increase in capital of Thales SESO SAS		21.8	–	21.8
Purchase of Thales Air Systems SAS shares		218.4	–	218.4
Increase in capital of Thales Electron Devices SAS		40.0	–	40.0
Increase in capital of Thales Cryogénie SAS		1.0	–	1.0
<b>Disposals</b>		<b>(9.8)</b>	<b>–</b>	<b>(9.8)</b>
Sale of Thales Microelectronics SAS		(4.6)	–	(4.6)
Sale of Thales Cryogénie SAS		(0.7)	–	(0.7)
Liquidation of Thales Belgium SA		(4.5)	–	(4.5)
<b>Increase in provisions for impairment</b>	Note 4	<b>–</b>	<b>(27.3)</b>	<b>(27.3)</b>
<b>Other</b>		<b>(123.3)</b>	<b>90.4</b>	<b>(32.9)</b>
<b>VALUE AT 31/12/2017</b>		<b>10,238.2</b>	<b>(1,239.4)</b>	<b>8,999.0</b>

## NOTE 9. OTHER FINANCIAL INVESTMENTS

### 9.1 Accounting principles

Other financial investments mainly include loan agreements signed by Thales with its direct or indirect subsidiaries and associates. These loans are presented separately from the current account agreements, which are used in the daily management of cash requirements or surpluses (see Note 10).

Other financial investments also include deposits paid as part of real estate commitments and other financial receivables.

An impairment loss is recognised depending on the risk of non recovery.

### 9.2 Breakdown by type

	31/12/2017			31/12/2016		
	Gross value	Impairment	Net value	Gross value	Impairment	Net value
Loans to direct subsidiaries and associates (see Note 23)	26.1	(25.5)	0.6	27.1	(25.5)	1.6
Loans to other Group subsidiaries	46.7	–	46.7	64.8	–	64.8
Loans to other Group associates	3.9	–	3.9	6.3	–	6.3
Other financial investments	29.5	(1.6)	27.9	11.0	(1.6)	9.4
<b>TOTAL</b>	<b>106.2</b>	<b>(27.1)</b>	<b>79.1</b>	<b>109.2</b>	<b>(27.1)</b>	<b>82.1</b>

### 9.3 Breakdown by maturity and by currency

Breakdown by maturity	31/12/2017	31/12/2016
Less than 1 year	59.9	60.9
From 1 to 5 years	14.0	12.7
More than 5 years	5.2	8.5
<b>TOTAL</b>	<b>79.1</b>	<b>82.1</b>

Breakdown by currency	31/12/2017	31/12/2016
Euro	50.5	48.8
South African rand	12.4	22.3
Chinese yuan	10.3	8.3
Other currencies	5.9	2.7
<b>TOTAL</b>	<b>79.1</b>	<b>82.1</b>

## NOTE 10. GROUP COMPANY CURRENT ACCOUNT PAYABLES

### 10.1 General framework and accounting principles

The Group company current account amounts presented in the parent company balance sheet represent the receivables and payables between the parent company and its subsidiaries as part of the Group's cash pooling organisation.

Under this centralised system, the cash surpluses of subsidiaries are generally transferred to the parent company. In return, the parent company meets the cash flow requirements of the subsidiaries. Except in special cases, this system applies to all subsidiaries in which Thales has majority control.

Group company current account receivables and payables are always recognised as due within one year.

### 10.2 Current account receivables

	31/12/2017	31/12/2016
Amounts due from direct subsidiaries and associates (see Note 23)	911.2	758.0
Amounts due from other subsidiaries	168.1	117.8
<b>TOTAL</b>	<b>1,079.3</b>	<b>875.8</b>

## 10.3 Current account payables

	31/12/2017	31/12/2016
Amounts deposited by direct subsidiaries and associates (see Note 23)	4,880.2	4,097.5
Amounts deposited by Thales Alenia Space (France and Italy)	160.2	185.7
Amounts deposited by Thales Australia Ltd	74.1	319.1
Amounts deposited by other Group subsidiaries	414.2	623.5
<b>TOTAL</b>	<b>5,528.9</b>	<b>5,225.8</b>

## NOTE 11. CASH AND OTHER INVESTMENTS

### 11.1 Accounting principles

Cash and cash equivalents include cash at bank and in hand as well as short-term, liquid investments that are easily converted into a known amount of cash and exposed to negligible risk of a change in value.

### 11.3 Other investments

Other investments correspond to term deposits with banks with maturities of 3 to 12 months.

### 11.2 Cash and cash equivalents

Cash and cash equivalents amounted to €3,450.5 million at 31 December 2017 compared with €3,183.1 million at 31 December 2016. This amount includes €2,199.4 million (€2,886.2 million at year-end 2016) of term deposits, euro-denominated money-market funds ("SICAV"), negotiable debt securities, and other investments with maturities of less than three months.

## NOTE 12. BORROWINGS

### 12.1 Accounting principles

Bonds are recognised at their redemption value. Any issue or redemption premiums are recognised under the corresponding balance sheet line item and taken to financial income (expense) on a straight-line

basis. Bond issue expenses are recognised on a straight-line basis over the term of the bond.

### 12.2 Breakdown of borrowings

	Nominal rate	Variable rate swaps	31/12/2017	31/12/2016
Bonds maturing in June 2023	Fixed rate 0.75%	€400 million	600.0	600.0
Bonds maturing in March 2021	Fixed rate 2.25%	€300 million	300.0	300.0
Bonds maturing in March 2018	Fixed rate 1.63%	€300 million	500.0	500.0
Other borrowings			156.4	45.0
Accrued interest			14.3	14.2
<b>GROSS BORROWINGS</b>			<b>1,570.7</b>	<b>1,459.2</b>

At 31 December 2017, no material Group financing was subject to covenants requiring accelerated or early repayment based on the Group's credit rating or financial ratios.

At 31 December 2017, confirmed and undrawn credit facilities agreed with a pool of banks amounted to €1,500 million, expiring in 2021. These credit facilities are used as a backup to the commercial paper

programme and as a financial reserve. The related agreement states that in the event that the French State no longer holds its golden share and the consolidated net debt/EBITDA ratio<sup>(1)</sup> also exceeds 3, early repayment clauses will apply.

At December 31, 2017, the Group also benefited from an unused bridge loan to finance its acquisition offer for Gemalto.

## 12.3 Breakdown of borrowings by maturity and by currency

Breakdown by maturity	31/12/2017	31/12/2016	Breakdown by currency	31/12/2017	31/12/2016
Less than 1 year	670.7	59.2	euro	1,425.4	1,425.3
From 1 to 5 years	300.0	800.0	Singapore dollar	32.6	33.9
More than 5 years	600.0	600.0	Pound sterling	112.7	—
<b>TOTAL</b>	<b>1,570.7</b>	<b>1,459.2</b>	<b>TOTAL</b>	<b>1,570.7</b>	<b>1,459.2</b>

## NOTE 13. SHAREHOLDERS' EQUITY

### 13.1 Share capital

Thales' share capital of €637,976,175 at 31 December 2017, is composed of 212,658,725 shares, compared with 212,194,766 shares at 31 December 2016, with a par value of €3 each. This represents an increase of 463,959 shares resulting from the exercise of share subscription options. The breakdown of share capital is presented below:

	31/12/2017			31/12/2016		
	Shares	% of capital	% voting rights	Shares	% of capital	% voting rights
TSA	54,786,654	25.76%	35.75%	54,786,654	25.82%	35.86%
French State (including 1 golden share)	2,060	—	—	2,060	—	—
Public Sector <sup>(a)</sup>	54,788,714	25.76%	35.75%	54,788,714	25.82%	35.86%
Dassault Aviation <sup>(b)</sup>	52,531,431	24.70%	28.44%	52,531,431	24.76%	28.53%
Thales <sup>(c)</sup>	568,739	0.27%	—	749,559	0.35%	—
Employees	6,181,444	2.91%	3.50%	5,743,081	2.71%	3.31%
Other shareholders	98,588,397	46.36%	32.31%	98,381,981	46.36%	32.30%
<b>TOTAL<sup>(d)</sup></b>	<b>212,658,725</b>	<b>100.00%</b>	<b>100.00%</b>	<b>212,194,766</b>	<b>100.00%</b>	<b>100.00%</b>

(a) Under the terms of the shareholders' agreement with Dassault Aviation (the "Industrial Partner"), the "Public Sector" (the French State) is represented by the company TSA, excluding the State directly. All Thales shares held directly and indirectly by the French State have been in directly registered form for more than two years and thus have a double voting right on 31 December 2017.

(b) As at 31 December 2017, Dassault Aviation held 42,154,349 shares in directly registered form, of which 34,654,349 shares have been held for more than two years, thus granting it double voting rights, and held 10,377,082 shares in bearer form.

(c) Treasury shares represented 126,000 bearer shares held under a liquidity contract and 442,739 directly registered shares.

(d) During 2017, 463,959 new shares bearing rights from 1 January 2017 were created as a result of the exercise of share subscription options.

At 31 December 2017, there are no securities giving access to the Company's capital, with the exception of the share subscription options described in the Note below.

(1) EBITDA is the sum of operating income, depreciation of non-current assets and impairment of intangible assets, net of goodwill amortisation. This indicator is calculated in accordance with French accounting principles.

## 13.2 Reserves and retained earnings

	31/12/2016	Allocation of 2016 profit	Balance of 2016 dividend	2017 interim dividend	31/12/2017
Legal reserve	63.3	0.4	—	—	63.7
Blocked reserve	8.3	—	—	—	8.3
Ordinary reserve	128.9	—	—	—	128.9
Other reserves	0.3	—	—	—	0.3
Retained earnings	1,523.8	430.7	(253.7)	(95.2)	1,605.6
<b>TOTAL</b>	<b>1,724.6</b>	<b>431.1</b>	<b>(253.7)</b>	<b>(95.2)</b>	<b>1,806.8</b>

Thales allocated €338.3 million of the profit for the 2016 financial year to dividends (€1.6 per share), paying a €84.6 million interim dividend in December 2016, and the balance of €253.7 million in June 2017. Thales paid a €95.2 million interim dividend in December 2017 in respect of the 2017 financial year.

## NOTE 14. TREASURY SHARES

### 14.1 Accounting principles

Thales carries out transactions in its own shares in accordance with the authorisations granted to the Board of Directors by the Annual General Meeting.

At year-end, treasury shares are recognised and measured on the basis of their assigned function:

- treasury shares that have not been assigned are recorded under other financial investments at their acquisition cost. At the reporting date, an impairment loss is recognised if their carrying value exceeds the average stock market price for December;
- treasury shares assigned to a free share plan are recorded under marketable securities, either at their acquisition cost if the shares were assigned from the beginning of the plan, or at their net carrying value at the reclassification date if they were assigned after their acquisition.

These treasury shares are not measured at market value because they are set aside to be granted to employees. Accordingly:

- shares allocated to parent company (Thales) employees are amortised on a straight-line basis over the term of the plan (48 months) through an increase in provisions for contingencies and losses recorded in liabilities;
- shares allocated to other Group employees are maintained at historical cost, as they will be re-billed to the relevant subsidiaries for the same amount.

### 14.2 Change in treasury shares

#### Change in the number of treasury shares

At 31 December 2017, Thales held 568,739 treasury shares, including 126,000 shares (0.06% of share capital) that were freely transferable.

	2017			2016		
	Freely transferable treasury shares	Treasury shares assigned to plans	Total treasury shares	Freely transferable treasury shares	Treasury shares assigned to plans	Total treasury shares
<b>At 1 January</b>	<b>126,044</b>	<b>623,515</b>	<b>749,559</b>	<b>215,830</b>	<b>623,424</b>	<b>839,254</b>
Purchases under the liquidity contract	819,512	—	819,512	513,001	—	513,001
Disposals under the liquidity contract	(743,512)	—	(743,512)	(472,001)	—	(472,001)
Transfer to employees under the employee share purchase plan	(462,217)	—	(462,217)	(41,714)	—	(41,714)
Stock market purchases	852,000	—	852,000	76,044	498,956	575,000
Delivery of free shares	—	(606,603)	(606,603)	—	(607,381)	(607,381)
Exercise of stock options	(40,000)	—	(40,000)	(56,600)	—	(56,600)
Reclassified shares	16,912	(16,912)	—	(108,516)	108,516	—
<b>Net change</b>	<b>442,695</b>	<b>(623,515)</b>	<b>(180,820)</b>	<b>(89,786)</b>	<b>91</b>	<b>(89,695)</b>
<b>At 31 December</b>	<b>568,739</b>	<b>—</b>	<b>568,739</b>	<b>126,044</b>	<b>623,515</b>	<b>749,559</b>

## Change in the value of treasury shares

Freely transferable treasury shares	2017	2016
<b>At 1 January</b>	<b>11.6</b>	<b>8.2</b>
Purchases under the liquidity contract	75.4	39.4
Disposals under the liquidity contract	(69.0)	(35.4)
Transfer to employees under the employee share purchase plan	(43.6)	(1.6)
Stock market purchases	78.3	7.0
Exercise of stock options	(3.7)	(1.9)
Reclassified shares	1.3	(4.1)
<b>At 31 December</b>	<b>50.3</b>	<b>11.6</b>
Of which, acquisition cost	52.4	11.6
Of which, impairment	(2.1)	–
Average share price for December	€88.43	€91.16

Treasury shares assigned to plans	2017	2016
<b>At 1 January</b>	<b>50.0</b>	<b>17.0</b>
Delivery of free shares	(48.6)	(16.6)
Stock market purchases	–	45.5
Reclassified free shares	(1.4)	4.1
<b>At 31 December</b>	<b>–</b>	<b>50.0</b>
Provisions for contingencies and losses	(18.4)	(18.1)

## NOTE 15. FREE SHARE PLANS AND STOCK OPTIONS GRANTED TO EMPLOYEES

At 31 December 2017, the following options, shares and units were outstanding:

- 850 share purchase options at a weighted average exercise price of €38.50;
- 783,204 share subscription options at a weighted average exercise price of €34.13, of which 155,427 are subject to performance conditions;
- 477,860 free shares, of which 360,300 are subject to performance conditions;
- 1,235,940 units, of which 480,150 are subject to performance conditions;
- 142,180 phantom shares, granting the right to a cash payment after a four-year vesting period, of which 103,390 are subject to performance conditions.

### 15.1 Outstanding share purchase option plans

Date of Board decision	Exercise period	Exercise price	Number of options outstanding at 31/12/2016	Options exercised in 2017	Number of options outstanding at 31/12/2017
25/11/08	from 25/11/12 to 24/11/18	€38.50	850	–	850
04/07/07	from 04/07/11 to 03/07/17	€44.77	40,000	(40,000)	–

### 15.2 Outstanding share subscription option plans

Date of Board decision	Exercise period	Exercise price	Number of options outstanding at 31/12/2016	Options exercised in 2017	Options cancelled in 2017	Number of options outstanding at 31/12/2017
15/09/11 <sup>(a)</sup>	from 15/09/15 to 14/09/21	€26.34	126,322	(40,945)	–	85,377
23/09/10 <sup>(a)</sup>	from 23/09/14 to 22/09/20	€26.34	110,150	(40,100)	–	70,050
25/06/09	from 25/06/13 to 24/06/19	€32.88	362,584	(84,342)	(5,490)	272,752
01/07/08	from 01/07/12 to 30/06/18	€38.50	463,237	(96,732)	(11,480)	355,025
04/07/07	from 04/07/11 to 03/07/17	€44.77	258,400	(201,840)	(56,560)	–

(a) Subject to the achievement of internal performance conditions over the three financial years following the grant date.

## Options granted and exercised in 2017

	Number of options granted/ shares subscribed or purchased	Exercise price	Date of plan
<b>1. Directors</b>			
Options granted in 2017	None		
<b>2. The ten biggest option awards granted to employees</b>			
Options granted in 2017	None		
<b>3. The ten biggest exercises of options by employees <sup>(a)</sup></b>			
Options exercised in 2017	8,000	€32.88	25/06/09
	7,291	€26.34	15/09/11
	7,000	€26.34	15/09/11
	5,945	€26.34	15/09/11
	5,500	€38.50	01/07/08
	5,000	€44.77	04/07/07
	4,800	€38.50	01/07/08
	4,600	€44.77	04/07/07
	4,600	€38.50	01/07/08
	4,500	€44.77	04/07/07

(a) All Group companies combined.

## 15.3 Allotment of free shares

Date of Board decision	Vesting period	Share price at grant date	Number of free shares at 31/12/2016	Shares granted in 2017	Shares cancelled in 2017	Shares delivered in 2017	Balance of free shares at 31/12/2017
28/09/17	from 28/09/17 to 28/09/21	€94.66	—	212,540 <sup>(a)</sup>	—	—	212,540
27/10/16	from 27/10/16 to 27/10/20	€83.10	87,860 148,070 <sup>(a)</sup>	— —	(300) (310)	— —	87,560 147,760
17/09/13	from 17/09/13 to 17/09/17	€39.16	397,180 226,335 <sup>(a)</sup>	— —	(9,274) (7,638)	(387,906) (218,697)	— —
20/12/12	from 20/12/12 to 20/12/16	€27.47	50 <sup>(b)</sup>	—	—	(50)	—

(a) Subject to the achievement of internal performance conditions over the three financial years following the grant date.

(b) Adjustment in 2016.

## 15.4 Allotment of share units indexed to the value of Thales shares

Date of allocation decision	Vesting Period	Share price at grant date	Number of units at 31/12/2016	Post-closing adjustments	Units cancelled in 2017	Units delivered in 2017	Balance of units at 31/12/2017
17/09/15	from 17/09/15 to 17/09/19	€61.75	367,730 229,200 <sup>(a)</sup>	(620) <sup>(b)</sup> —	(9,050) (7,750)	(270) —	359,030 221,450
16/09/14	from 16/09/14 to 16/09/18	€42.42	405,210 268,000 <sup>(a)</sup>	— —	(8,210) (9,300)	(240) —	396,760 258,700

(a) Subject to the achievement of internal performance conditions over the three financial years following the grant date.

(b) People in mobility programmes whose units were cancelled in error as their reason for leaving was incorrectly stated.

## 15.5 Allotment of phantom shares indexed to the value of Thales shares

Date of allocation decision	Vesting Period	Share price at grant date	Number of phantom shares at 31/12/2016	Phantom shares cancelled in 2017	Number of phantom shares at 31/12/2017
28/09/17	from 28/09/17 to 29/09/21	—	67,140 <sup>(a)</sup>	(140)	67,000
27/10/16	from 27/10/16 to 27/10/20	— —	39,430 37,910 <sup>(a)</sup>	(640) (1,420)	38,790 36,390

(a) Subject to the achievement of internal performance conditions over the three financial years following the grant date.

## NOTE 16. RECEIVABLES AND PAYABLES

### 16.1 Accounting principles

Payables and receivables denominated in foreign currencies are revalued at the closing price.

Thales (parent company) hedges currency risks related to contracts or normal commercial transactions on behalf of its subsidiaries.

Until the end of 2016, the derivatives subscribed by Thales (parent company) with banks and the foreign exchange guarantees granted to subsidiaries were recorded at their market value in the balance sheet under "Translation difference and exchange rate adjustments".

Following application of the new ANC Regulation 2015-05, unrealised results on derivatives and foreign exchange guarantees are maintained as off-balance sheet commitments.

Temporary cash offsets between the amounts received/paid to subsidiaries and Thales's cash receipts/payments to banks with regard to managing foreign exchange derivatives are recorded in the balance sheet under "Translation difference and exchange rate adjustments", using the symmetry principle applicable to hedging transactions.

### 16.2 Breakdown of receivables and payables

			31/12/2017	31/12/2016
	Gross	Provisions	Net	Net
<b>Advances to suppliers</b>	<b>0.4</b>	<b>—</b>	<b>0.4</b>	<b>0.1</b>
<b>Trade receivables</b>	<b>198.8</b>	<b>(1.7)</b>	<b>197.1</b>	<b>188.8</b>
<b>Other receivables</b>	<b>330.5</b>	<b>(2.9)</b>	<b>327.6</b>	<b>733.1</b>
Income tax receivables from the French State (mainly research tax credits)	229.7	—	229.7	320.7
Translation difference and exchange rate adjustments	12.5	—	12.5	356.5
Tax and social security receivables	30.9	—	30.9	27.2
Other	57.4	(2.9)	54.5	28.7
<b>TOTAL</b>	<b>529.7</b>	<b>(4.6)</b>	<b>525.1</b>	<b>922.0</b>
<b>Advances received on contracts in progress</b>	<b>17.8</b>	<b>—</b>	<b>17.8</b>	<b>18.8</b>
<b>Trade payables</b>	<b>86.8</b>	<b>—</b>	<b>86.8</b>	<b>99.5</b>
<b>Other liabilities</b>	<b>351.2</b>	<b>—</b>	<b>351.2</b>	<b>471.6</b>
Tax liabilities towards consolidated subsidiaries	196.8	—	196.8	152.1
Translation difference and exchange rate adjustments	14.5	—	14.5	187.5
Tax payables, excluding income tax and social security	98.1	—	98.1	82.0
Other	41.8	—	41.8	50.0
<b>TOTAL</b>	<b>455.8</b>	<b>—</b>	<b>455.8</b>	<b>589.9</b>

## 16.3 Breakdown of receivables and payables by maturity at 31 December 2017

	Net	Maturity		
		< 1 year	1 to 5 years	> 5 years
Advances to suppliers	0.4	0.4	–	–
Trade receivables	197.1	197.1	–	–
Other receivables	327.6	218.9	108.7	–
<b>TOTAL RECEIVABLES</b>	<b>525.1</b>	<b>416.4</b>	<b>108.7</b>	<b>–</b>
Advances received on contracts in progress	17.8	17.8	–	–
Trade payables	86.8	86.8	–	–
Other liabilities	351.2	273.4	60.4	13.8
<b>TOTAL PAYABLES</b>	<b>455.8</b>	<b>378.0</b>	<b>60.4</b>	<b>13.8</b>

## NOTE 17. PROVISIONS FOR CONTINGENCIES AND LOSSES

### 17.1 Accounting principles

The Group records a provision when it recognises a legal or constructive obligation resulting from a past event for which an outflow of resources will be required and a reliable estimate can be made of the amount. Provisions are generally recorded for the following:

#### Provisions for post-employment and other employee benefits

The financing of post-employment benefits mainly involves statutory retirement schemes (social security, supplementary schemes such as ARRCO and AGIRC, etc.) for which the recognised expense is equal to the contributions paid. These are recorded in the year in which they are incurred.

The Company grants its employees termination payments and other long-term benefits (long-service awards and an additional week of annual leave during the employee's 35th year of service within the Group). Some senior executives also benefit from a supplementary pension plan.

In accordance with ANC Regulation 2013-02, a provision is recognised for obligations that qualify as defined benefit plans. It is calculated on the basis of an actuarial valuation, determined using the projected unit credit method and taking into account future salary levels. This method consists in assessing, for each employee, the present value of the benefits that he or she can expect at the due date, by applying assumptions concerning discount rates, inflation, mortality and staff turnover.

These plans are recognised in the Company's financial statements as follows:

- the service cost, which corresponds to the increase in the obligation during the reporting period, is recognised in income (loss) from operations;
- the costs of unwinding the net obligation as well as actuarial gains and losses due to changes in assumptions and experience adjustments (difference between projected and actual) are recognised in financial income (expense);
- the impact of plan amendments following renegotiations of employee benefits is recognised in non-recurring income (expense).

#### Provisions for subsidiary risks

Equity investments held by Thales are measured at the end of each reporting period and an impairment loss is recorded if necessary. In the event that the investment is fully written down and Thales's share in the shareholders' equity of the subsidiary or associate becomes negative, a provision for subsidiary risks may be recognised when considered necessary.

#### Provisions for restructuring

Provisions for restructuring costs are recorded when a restructuring programme has been agreed with a third party, approved by Company management and announced before the reporting date, resulting in an obligation to the third parties in question, and for which the Company does not expect any consideration for the costs.

### 17.2 Breakdown of provisions

	31/12/2016	Increase	Reversal	31/12/2017
Post-employment and other employee benefits (see Note 17.3)	105.1	18.3	(13.1)	110.3
Subsidiary risks	10.8	14.9	(9.9)	15.8
Restructuring	8.3	0.1	(8.1)	0.3
Free shares	18.1	7.8	(7.5)	18.4
Other	55.5	0.3	(1.6)	54.2
<b>TOTAL</b>	<b>197.8</b>	<b>41.4</b>	<b>(40.2)</b>	<b>199.0</b>

## 17.3 Post-employment and other employee benefits

The provisions in the balance sheet can be analysed as follows:

	2017		
	Post-employment benefits	Other employee benefits	Total
<b>Provisions at 31 December 2016</b>	<b>(101.6)</b>	<b>(3.5)</b>	<b>(105.1)</b>
<b>Net increase in provisions of which:</b>	<b>(5.0)</b>	<b>(0.2)</b>	<b>(5.2)</b>
Current service cost	(5.2)	(0.2)	(5.4)
Financial expense:	(10.4)	(0.1)	(10.5)
• Net interest cost	(1.5)	(0.1)	(1.6)
• Actuarial gains (losses)	(8.9)	–	(8.9)
Benefits and contributions paid	10.1	0.2	10.3
Other	0.5	(0.1)	0.4
<b>Provisions at 31 December 2017</b>	<b>(106.6)</b>	<b>(3.7)</b>	<b>(110.3)</b>
<b>Of which:</b>			
• Commitments	(156.4)	(3.6)	(160.0)
• Investments	49.7	–	49.7

The actuarial assumptions used to estimate the commitments are the following:

	31/12/2017	31/12/2016
Discount rate	1.20%	1.50%
Inflation rate	1.35%	1.40%
Average salary increase rate	2.20%	2.38%
Expected average remaining working life	8 years	7 years

## NOTE 18. LEGAL AND ENVIRONMENTAL RISKS

### 18.1 Legal risks

Due to the nature of its business, Thales is exposed to the risk of technical and commercial disputes.

To prevent disputes or limit their impact, Thales's policy is to systematically seek alternative dispute resolution mechanisms. This policy is reviewed on a regular basis to take into account changes in the Group's core areas of business and is backed by employee training programmes.

In addition, Thales implemented a procedure several years ago to centralise all civil, commercial and criminal litigation and claims. These are handled by the Corporate Legal Affairs department, with the support of the Group companies concerned.

In October 2017, Thales was notified of an arbitration award relating to a commercial dispute between the Republic of China and a group of three French manufacturers, including Thales Systèmes Aéroportés, a subsidiary of Thales.

This arbitration award, which falls under a contract concluded in 1992, gives rise to a financial conviction of the entities. The total amount of the award, including interest, is €227 million. The share of Thales Systèmes Aéroportés amounts to €64 million. The corresponding charge was recorded in the accounts of the subsidiary as at 31 December 2017.

There are no other government, judicial or arbitration claims, of which the Group is aware, which are pending or threatened, which could have, or which had, in the course of the last 12 months, any significant effect on the financial position or the profitability of the Company and/or the Group.

### 18.2 Environment

Due to the nature of its business, Thales is exposed to environmental risks related to potential adverse environmental and health effects resulting from its activities, the impact of the environment on its operations and non-compliance with new regulations applicable to its activities and products.

For many years, Thales has regularly analysed and updated its environmental risks on the basis of its business activities, scientific and technical developments and emerging environmental challenges.

This analysis, represented by a risk mapping, is intended to:

- ensure that employees and local residents are not exposed to health and environmental risks;
- ensure the compliance of activities and products;
- analyse the impact of new regulations, including on product design;
- identify an appropriate organisational structure and associated action plans, either at Group level or locally, according to the risk mapping results.

In support of this analysis, an environmental management system has been deployed at all sites in order to ensure the control and limitation of the environmental impacts of the Group's products and activities. This management system is deployed throughout the different business lines as part of the Group's framework. Consequently, environmental skills and know-how have been rolled out to services such as engineering, research, procurement and contracts.

At 31 December 2017, provisions for environmental risks amounted to €0.5 million.

## NOTE 19. OFF-BALANCE SHEET COMMITMENTS

### 19.1 Deposits and guarantees

Commitments given:	31/12/2017	31/12/2016
Guarantees given by Thales under commercial contracts signed by operating entities	8,769.6	9,828.7
Guarantees given to banks for facilities granted to subsidiaries	2,314.0	2,216.9
Counter-guarantee given to trustees to hedge pension obligations in the United Kingdom	930.8	974.0
Other guarantees given to Group subsidiaries	704.7	801.8
Other guarantees given to third parties	746.0	677.5
<b>Total<sup>(a)</sup></b>	<b>13,465.1</b>	<b>14,498.9</b>
Of which, related to direct subsidiaries (see Note 23)	3,655.3	4,576.4
Of which, related to other Group subsidiaries	9,487.9	9,632.8
Of which, related to direct and indirect associates	321.9	289.8

Commitments received	31/12/2017	31/12/2016
Debt write-offs granted to related companies with clawback provisions	6.9	120.1

(a) The decrease in guarantees given from 2016 to 2017 is explained in part by changes in exchange rates (€704.7 million).

### 19.2 Property leasing commitments

	31/12/2017	31/12/2016
Operating leases	544.0	608.4
Less than 1 year	113.9	120.9
From 1 to 5 years	293.6	326.7
More than 5 years	136.5	160.8

## NOTE 20. MARKET RISKS

### 20.1 Accounting principles

The Thales parent company Treasury and Financing department is active in the financial markets in order to reduce the interest rate and foreign exchange risks of the Group.

#### Interest rate derivatives

Thales uses interest rate derivatives to manage and reduce its exposure to interest rate fluctuations. When the derivatives are designated as hedging instruments, the gains and losses on the hedge are recognised in the same period as the hedged item.

#### Currency derivatives

Thales hedges currency risks arising on commercial offers entered into by its subsidiaries, which are denominated in currencies other than the main operating currency.

When the hedged item has a sufficient probability of occurrence, the foreign exchange derivatives subscribed by Thales with banking counterparties qualify for hedge accounting. Gains and losses on bank derivatives are then recognised in income at the same rate as the gains and losses realised on the guarantees offered to subsidiaries, in accordance with the principle of symmetry applicable to hedging

transactions. Foreign exchange premiums are amortised in the income statement on a straight-line basis over the term of the hedge.

When hedged items do not have a sufficient probability of occurrence, the foreign exchange derivatives are deemed isolated open positions. In this case, the market value of the derivative is recognised in the balance sheet as an offsetting entry in a suspense account, also in the balance sheet. A provision is recorded in the event of negative valuation. This valuation takes into account Thales's guarantee commitments to subsidiaries under these offers.

Thales hedges currency risks related to firm contracts and normal commercial transactions on behalf of its subsidiaries. As such, it guarantees its operating subsidiaries a specific exchange rate for each transaction and backs up its position by arranging currency derivatives with banking counterparties. Gains and losses on bank derivatives are then recognised in income at the same rate as the gains and losses realised on the guarantees offered to subsidiaries, in accordance with the principle of symmetry applicable to hedging transactions.

Thales hedges the currency risks related to its cash pooling system. The gains and losses on currency derivatives are offset by the gains and losses resulting from the revaluation of the hedged Group company current accounts and loans. However, gains or losses related to the derivatives' swap points are spread over the term of the hedge.

### 20.2 Interest rate risk management

At 31 December 2017 and 2016, Thales held the following derivative instruments, which all qualify as hedges.

	31/12/2017		31/12/2016	
	Nominal	Market value	Nominal	Market value
<b>Fixed-for-floating interest rate swaps:</b>				
• swaps backing bonds maturing in 2023	400.0	(2.5)	400.0	0.1
• swaps backing bonds maturing in 2021	300.0	16.9	300.0	21.6
• swaps backing bonds maturing in 2018	300.0	3.1	300.0	6.2
<b>TOTAL</b>	<b>1,000.0</b>	<b>17.5</b>	<b>1,000.0</b>	<b>27.9</b>
<b>Floating-for-fixed interest rate swaps:</b>				
• swap backing a loan maturing in 2019	5.1	(0.2)	6.3	(0.2)
• cross currency swap backing a loan	14.3	1.5	15.2	1.3
<b>TOTAL</b>	<b>19.4</b>	<b>1.3</b>	<b>21.5</b>	<b>1.1</b>

### 20.3 Currency risk management

At 31 December 2017 and 2016, the derivatives subscribed by Thales with bank counterparties were as follows:

	31/12/2017					31/12/2016	
	USD	GBP	Other	Total	Market value	Total	Market value
<b>Hedges of commercial offers and transactions:</b>							
Forward currency sales	3,650.1	878.4	2,382.7	6,911.2	144.3	7,702.3	(179.3)
Forward currency purchases	1,448.4	992.8	1,928.8	4,370.0		4,163.2	
Currency sales (call and put options)	90.9	—	22.3	113.2	—	94.1	0.6
Currency purchases (call and put options)	111.0	—	1.8	112.8		26.0	
<b>Hedges related to cash pooling:</b>							
Currency sales: foreign exchange swaps	702.0	—	270.3	972.3	(70.3)	1,030.2	(136.1)
Currency purchases: foreign exchange swaps	1.3	569.6	71.9	642.8		1,474.3	

In addition, Thales has granted its operating subsidiaries “mirror” foreign exchange guarantees in relation to firm contracts or normal commercial operations.

Thales has also granted its operating subsidiaries foreign exchange guarantees on commercial offers, subject to the subsidiary winning the contract.

## NOTE 21. RELATED PARTIES

### 21.1 Definition

The Group has identified the following related parties: shareholders of Thales (the parent company), especially the French State and Dassault Aviation, companies controlled by these same shareholders, companies under joint control, companies under significant influence, directors and senior executives.

### 21.2 Agreements with Thales’s shareholders

Section 4.3.3.3 of the 2017 Registration Document describes the main provisions of the shareholders’ agreement governing relations between the French State (the “Public Sector”) and Dassault Aviation (the “Industrial Partner”) within Thales, in relation to the convention on the protection of strategic national interests as well as the specific convention binding the French State and Thales.

### 21.3 Agreements concluded with Naval Group (formerly DCNS)

As of December 2011, Thales holds 35% of the share capital of Naval Group, a subsidiary jointly controlled with the French State.

Thales and Naval Group also signed an industrial and trade cooperation agreement, with the objective of optimising the organisation of the naval business activities of both groups (market access, research and development and purchasing).

### 21.4 Compensation of directors and senior corporate officers <sup>(a)</sup>

The compensation, benefits and social security contributions awarded to Directors and Executive Committee members break down as follows:

	2017	2016
<b>Short-term benefits:</b>		
• Fixed compensation	4.7	4.3
• Variable compensation	4.2	3.7
• Post-employment benefits	0.5	–
• Social security contributions	3.1	2.7
• Attendance fees	0.6	0.5
<b>Other benefits:</b>		
• Post-employment benefits	2.4	1.7
• Share-based compensation <sup>(b)</sup> (Note 15)	2.4	2.5

(a) The components of compensation presented correspond to costs recognised in the Thales parent company financial statements.

(b) Measured in accordance with IFRS 2 – share-based payments.

## NOTE 22. EVENTS AFTER THE REPORTING PERIOD

At the publication date of this document, no event liable to have an impact on Thales’s financial position has occurred since year-end.

## NOTE 23. SUBSIDIARIES AND ASSOCIATES

(in millions)

			Information related to the entity (local currency)			
			Prior year sales excluding VAT	Profit (loss) for last year ended	Share capital	Shareholders' equity other than share capital

### A. Detailed information on subsidiaries and associates whose gross value exceeds 1% of the Company's share capital

<b>1. Subsidiaries</b>	THALES HOLDING UK PLC	GBP	0.0	3.4	726.8	400.1
	THALES AVS FRANCE SAS	EUR	1 733.1	63.4	213.1	315.8
	THALES ALENIA SPACE SAS	EUR	0.0	94.5	918.0	298.1
	THALES DMS FRANCE SAS	EUR	1 797.7	277.3	122.2	138.3
	THALES COMMUNICATIONS & SECURITY SAS	EUR	2 036.6	100.0	164.0	112.3
	THALES DEUTSCHLAND GMBH	EUR	0.0	-5.9	27.1	278.2
	THALES USA INC	USD	1.9	28.4	118.1	327.3
	THALES INTERNATIONAL SAS	EUR	0.0	47.7	313.0	22.3
	THALES IAS FRANCE SAS	EUR	1 881.6	421.8	199.8	210.3
	AVIMO GROUP LTD	SGD	0.0	0.5	22.1	35.1
	THALES NETHERLANDS BV	EUR	424.8	29.7	29.5	167.0
	THALES UNDERWATER SYST NV PAYS BAS	EUR	0.0	0.0	4.5	4.1
	THALES SERVICES SAS	EUR	445.9	203.3	1.5	13.3
	SIFELEC SAS	EUR	0.0	0.0	38.3	0.6
	THALES AVIONICS ELECTRICAL SYSTEMS SAS	EUR	138.8	-4.7	6.9	45.4
	THALES HOLDING NORWAY AS	NOK	0.0	0.0	419.8	-186.8
	THALES CORPORATE VENTURES SAS	EUR	0.0	0.2	15.0	14.6
	THALES CANADA INC	CAD	660.8	-5.4	6.8	-45.0
	THALES EUROPE SAS	EUR	0.0	4.7	43.2	-45.5
	TH. BELGIUM SA (Ex FZ)	EUR	39.2	0.0	14.2	-21.4
	THALES SUISSE SA	CHF	33.1	15.8	40.0	-3.3
	CMT MEDICAL TECHNOLOGIES LTD	USD	20.1	1.2	1.0	27.1
	SNC THALES MERIGNAC	EUR	50.9	2.0	20.0	-0.4
	THALES SESO SAS	EUR	21.4	-0.3	0.4	11.3
	THALES GLOBAL SERVICES SAS	EUR	541.9	-4.7	0.5	-3.6
	THALES COMMUNICATIONS LTDA	BRL	0.0	-0.1	19.8	-0.8
	SAS CHATELLERAULT BRELANDIERE	EUR	2.8	-0.1	2.0	1.5
<b>Total subsidiaries</b>						
<b>2. Associates</b>	UNITED MONOLITHIC SEMICONDUCTORS HOLDING	EUR	0.0	3.9	33.9	12.2
	ELETTRONICA SpA	EUR	0.0	18.1	0.0	74.0
	SOFRADIR	EUR	142.2	24.6	6.0	82.9
	TELESPAZIO SpA	EUR	563.7	33.3	50.0	187.8
	NAVAL GROUP	EUR	3 698.2	136.9	563.0	-177.0
<b>Total associates</b>						

### TOTAL (A)

### B. Detailed information concerning other subsidiaries and associates

#### 1. Subsidiaries not listed in section A

French subsidiaries

Foreign subsidiaries

**Total**

#### 2. Associates not listed in section A

French companies

Foreign companies

**Total**

### TOTAL (B)

### TOTAL (A + B)

### Information concerning related companies

Thales' direct subsidiaries (A)

Thales' direct subsidiaries (B)

Other Group subsidiaries

Contribution of subsidiaries and associates to Thales' financial statements (EUR)							
Carrying amount of investments (gross)	Carrying amount (net)	% share capital held	Loans and advances made by Thales not yet paid	Receivables	Liabilities	Deposits and guarantees given by Thales	Dividends received by Thales during the year
2 571.7	1 870.1	100%	0.0	1.7	111.9	0.0	0.0
1 016.0	1 016.0	93%	0.0	47.4	400.5	128.2	60.9
683.1	683.1	67%	0.0	0.0	17.3	0.0	114.4
802.6	802.6	100%	0.0	0.0	2 302.5	687.2	34.7
590.8	590.8	100%	0.0	10.1	375.5	625.2	45.3
545.0	545.0	100%	0.0	85.0	0.0	0.0	0.0
476.6	476.6	100%	0.0	37.0	0.7	729.7	0.0
398.5	398.5	100%	0.0	107.5	33.7	6.0	129.8
754.9	754.9	100%	0.0	5.1	1 353.3	314.8	100.6
250.7	66.4	100%	0.0	0.0	0.0	0.0	0.0
235.2	235.2	99%	0.0	1.1	208.8	382.3	0.0
129.2	8.5	100%	0.0	0.0	0.0	0.0	0.0
126.4	126.4	100%	0.0	17.4	0.0	0.8	2.4
111.8	38.7	100%	0.0	0.0	30.1	0.0	0.0
94.6	61.6	100%	0.0	49.3	1.0	0.0	0.0
77.2	77.2	100%	0.0	0.0	0.0	0.0	0.0
73.3	18.7	100%	0.0	0.0	13.3	0.0	0.0
51.9	51.9	100%	0.0	96.5	10.7	741.1	0.0
43.2	43.2	100%	0.0	165.5	0.0	0.0	0.0
34.2	34.2	100%	0.0	28.1	1.0	38.6	0.0
26.4	26.4	100%	0.0	0.0	0.0	0.0	7.8
21.8	21.8	100%	0.0	0.0	0.0	0.0	0.0
20.0	19.7	100%	0.0	103.5	0.0	0.0	0.0
36.4	11.5	100%	0.0	0.5	4.6	0.0	0.0
12.4	0.0	100%	0.0	47.7	0.0	1.4	0.0
11.0	0.0	100%	0.0	0.0	0.0	0.0	0.0
10.0	2.5	100%	0.0	0.4	0.0	0.0	0.0
<b>9 204.7</b>	<b>7 981.2</b>		<b>0.0</b>	<b>803.8</b>	<b>4 864.9</b>	<b>3 655.3</b>	<b>495.9</b>
24.3	22.8	50%	0.0	0.0	0.0	0.0	2.0
26.7	26.7	33%	0.0	0.0	0.0	0.0	4.6
26.4	26.4	50%	0.0	0.0	0.0	0.0	5.0
81.6	81.6	33%	0.0	0.0	0.0	0.0	7.2
833.7	833.7	35%	0.0	0.0	0.0	0.0	0.0
<b>992.8</b>	<b>991.3</b>		<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>18.7</b>
<b>10 197.4</b>	<b>8 972.4</b>		<b>0.0</b>	<b>803.8</b>	<b>4 864.9</b>	<b>3 655.3</b>	<b>514.6</b>
23.0	16.8		0.0	36.7	15.3	0.0	2.5
0.7	0.1		0.0	0.0	0.0	0.0	0.0
<b>23.8</b>	<b>16.9</b>		<b>0.0</b>	<b>36.7</b>	<b>15.3</b>	<b>0.0</b>	<b>2.5</b>
9.5		0.0	0.0	0.0	0.0	1.5	
0.1		25.5	70.6	0.0	507.0	0.1	
<b>17.0</b>	<b>9.6</b>		<b>25.5</b>	<b>70.6</b>	<b>0.0</b>	<b>507.0</b>	<b>1.6</b>
<b>40.8</b>	<b>26.5</b>		<b>25.5</b>	<b>107.4</b>	<b>15.3</b>	<b>507.0</b>	<b>4.1</b>
<b>10 238.2</b>	<b>8 999.0</b>		<b>25.5</b>	<b>911.2</b>	<b>4 880.2</b>	<b>4 162.3</b>	<b>518.8</b>
			0.0	803.8	4 864.9	3 655.3	
			25.5	107.4	15.3	0.0	
				0.0		507.0	

## Investments made and thresholds crossed in French companies in 2017

Percentage owned	At 31/12/2016					At 31/12/2017				
	> 5%	> 20%	> 33%	> 50%	> 66%	> 5%	> 20%	> 33%	> 50%	> 66%
<b>1. Increases</b>										
189 Centelec SAS	—	—	—	—	100%	—	—	—	—	—
190 Centelec SAS	—	—	—	—	100%	—	—	—	—	—
191 Centelec SAS	—	—	—	—	100%	—	—	—	—	—
Thales LAS France SAS	—	—	—	—	—	—	—	—	—	100%
<b>2. Decreases</b>										
Thales Underwater Systems SAS	—	—	—	—	—	—	—	—	—	100%
TDA Armements SAS	—	—	—	—	—	—	—	—	—	100%
Thales Angénieux SAS	—	—	—	—	—	—	—	—	—	100%
Thales Belgium SA	—	—	—	—	—	—	—	—	—	100%
Thales Cryogénie SAS	—	—	—	—	—	—	—	—	—	100%
Thales Electron Devices SAS	—	—	—	—	—	—	—	—	—	100%
Thales Optronique SAS	—	—	—	—	—	—	—	—	—	77%
Thales Microelectronics SAS	—	—	—	—	—	—	—	—	—	100%
Thales Systems Ireland Ltd	—	—	—	—	—	—	23%	—	—	—
Revenue Collection Systems France SAS	—	—	—	—	—	—	—	—	—	100%
191 Centelec SAS	—	—	—	—	—	—	—	—	—	100%

## NOTE 24. INFORMATION ON EXISTING BRANCHES (ARTICLE L. 232-1, II OF THE FRENCH COMMERCIAL CODE)

At 31 December 2017, Thales had a secondary facility registered in France with the commercial registry and indicated on its Kbis (company registration certificate).

### 1.3.2.6 Five-year financial summary of the Company

	2013	2014	2015	2016	2017
<b>1. Share capital at year-end</b>					
Share capital	617.2	623.5	632.9	636.6	638.0
Number of ordinary shares outstanding	205,744,500	207,841,111	210,961,404	212,194,766	212,658,725
Maximum number of shares to be created in future by exercise of share subscription options	8,186,261	5,841,789	2,615,865	1,320,693	783,154
<b>2. Operations and results for the year</b>					
Revenues excluding tax	205.9	224.4	208.6	233.3	258.5
Earnings before tax, employee profit-sharing, depreciation, amortisation and provisions	379.7	609.3	625.7	367.9	337.4
Income tax benefit	85.8	77.4	93.8	78.0	9.8
Earnings after tax, employee profit-sharing, depreciation, amortisation and provisions	400.6	662.9	871.9	431.1	383.8
Distributed net profit	227.6	230.7	285.6	338.3	95.2 <sup>(a)</sup>
<b>3. Earnings per share</b>					
Earnings after tax and employee profit-sharing but before amortisation, depreciation and provisions	2.26	3.30	3.41	2.10	1.63
Earnings after tax, employee profit-sharing, depreciation, amortisation and provisions	1.95	3.19	4.13	2.03	1.80
Net dividend per share	1.12	1.12	1.36	1.60	1.75 <sup>(b)</sup>
<b>4. Employees</b>					
Average headcount during the year, of which:	833	852	831	818	812
• Engineers and managers	726	749	735	727	723
• Technicians and supervisors	107	103	96	91	89
Personnel expenses, of which:	177.1	183.2	187.1	191.5	207.7
• Total salary costs for the year	123.9	130.2	131.5	137.8	151.2
• Social security and other social welfare benefits paid during the year	53.2	53.0	55.6	53.7	56.5

2013: Share capital up from €607,019,022.0 to €617,233,500.0 following a capital increase.

2014: Share capital up from €617,233,500.0 to €623,523,333.0 following a capital increase.

2015: Share capital up from €623,523,333.0 to €632,884,212.0 following a capital increase.

2016: Share capital up from €632,884,212.0 to €636,584,298.0 following a capital increase.

2017: Share capital up from €636,584,298.0 to €637,976,175.0 following a capital increase.

(a) Interim dividend.

(b) Subject to approval by the Annual General Meeting of 23 May 2018.

### 1.3.3 Statutory auditors' report on the financial statements

*This is a translation into English of the statutory auditors' report on the financial statements of the Company issued in French and it is provided solely for the convenience of English-speaking users. This statutory auditors' report includes information required by European regulation and French law, such as information about the appointment of the statutory auditors or verification of the management report and other documents provided to the shareholders. This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.*

To the Annual General Meeting of Thales,

#### Opinion

In compliance with the engagement entrusted to us by your annual general meetings, we have audited the accompanying financial statements of Thales for the year ended December 31, 2017.

In our opinion, the financial statements give a true and fair view of the assets and liabilities and of the financial position of the Company as at December 31, 2017 and of the results of its operations for the year then ended in accordance with French accounting principles.

The audit opinion expressed above is consistent with our report to the Audit and Accounts Committee.

#### Basis for opinion

##### • Audit framework

We conducted our audit in accordance with professional standards applicable in France. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the Statutory Auditors' Responsibilities for the Audit of the Financial Statements section of our report.

##### • Independence

We conducted our audit engagement in compliance with independence rules applicable to us, for the period from January 1, 2017 to the date of our report and specifically we did not provide any prohibited non-audit services referred to in Article 5 (1) of Regulation (EU) No 537/2014 or in the French Code of Ethics (*Code de déontologie*) for statutory auditors.

#### Emphasis of Matter

We draw attention to the matter described in Note 16 "Receivables and Debts" to the financial statements regarding the first-time application of Regulation 2015-05 of the French Accounting Standards Authority (*Autorité des normes comptables*). Our opinion is not modified in respect of this matter.

#### Justification of assessments – Key audit matters

In accordance with the requirements of Articles L. 823-9 and R. 823-7 of the French Commercial Code (*Code de commerce*) relating to the justification of our assessments, we inform you of the key audit matters relating to risks of material misstatement that, in our professional judgment, were of most significance in our audit of the financial statements of the current period, as well as how we addressed those risks.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on specific items of the financial statements.

#### Equity investments

##### Risk identified

Equity investments, recorded in the balance sheet as at December 31, 2017 for a net amount of M€ 8,999, represent a significant balance sheet item. They are recorded at their lower acquisition cost or at their value in use.

As stated in Note 8 "Equity investments" to the financial statements, the inventory value is determined based on profitability forecasts, the underlying assets, recent transactions or the market price of any listed securities.

The estimate of the inventory value of these equity investments requires the exercise of the management's judgment in the choice of information to consider depending on the investments concerned. Depending on the situation, this information may correspond to historical information (shareholders' equity) or forecast information (value of future discounted cash flows).

We considered that the correct valuation of equity investments constituted a key audit matter.

##### Our response

In order to assess the reasonableness of the equity investment estimates, our work mainly consisted in:

- a) For valuations based on underlying asset information:
  - comparing the shareholders' equity used against the financial statements of entities which were subject to an audit or analytical procedures.
- b) For valuations based on forecasts:
  - assessing the reasonableness of cash flow projections in relation to the economic and financial contexts of each business;
  - assessing the reliability of the process for establishing forecasts by reviewing the causes for variances between previous forecasts and actual figures;
  - comparing the consistency of the cash flow projections with the most recent management estimates presented to the Board of Directors;
  - evaluating the consistency of the growth rate used for the projected flows with market analyses and the consensus observed;
  - evaluating the calculation of the weighted average cost of capital applied to the flow projections.

Lastly, we also assessed the appropriateness of the information provided in Note 8 to the financial statements.

## Verification of the management report and of the other documents provided to the shareholders

We have also performed, in accordance with professional standards applicable in France, the specific verifications required by French law.

### • Information provided in the management report and in the Other Documents provided to the Shareholders with respect to the Company's financial position and the financial statements

We have no matters to report as to the fair presentation and the consistency with the financial statements of the information given in the Board of Directors' management report and in the other documents provided to the Shareholders with respect to the financial position and the financial statements.

### • Report on corporate governance

We confirm that the Board of Directors' Report on Corporate Governance sets out the information required by Articles L. 225-37-3 and L. 225-37-4 of the French Commercial Code (*Code de commerce*).

Concerning the information given in accordance with the requirements of Article L. 225-37-3 of the French Commercial Code (*Code de commerce*) relating to remunerations and benefits received by the directors and any other commitments made in their favor, we have verified its consistency with the financial statements, or with the underlying information used to prepare these financial statements and, where applicable, with the information obtained by your Company from controlling and controlled companies. Based on this work, we attest the accuracy and fair presentation of this information.

With respect to the information relating to items that your Company considered likely to have an impact in the event of a public purchase offer or exchange, provided pursuant to Article L. 225-37-5 of the French Commercial Code (*Code de commerce*), we have verified that it is in accordance with the underlying documentation provided to us. Based on our work, we have no observations to make on this information.

### • Other information

In accordance with French law, we have verified that the required information concerning the purchase of investments and controlling interests and the identity of the shareholders and holders of the voting rights has been properly disclosed in the management report.

## Report on other legal and regulatory requirements

### • Appointment of the statutory auditors

We were appointed as statutory auditors of Thales by the ordinary and extraordinary Annual General Meeting held on June 25, 1983 for MAZARS and on May 15, 2003 for ERNST & YOUNG Audit.

As at December 31, 2017, MAZARS was in the 35th year and ERNST & YOUNG Audit in the 15th year of total uninterrupted engagement.

## Responsibilities of Management and those charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with French accounting principles and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless it is expected to liquidate the Company or to cease operations.

The Audit and Accounts Committee is responsible for monitoring the financial reporting process and the effectiveness of internal control and risks management systems and where applicable, its internal audit, regarding the accounting and financial reporting procedures.

The financial statements were approved by the Board of Directors.

## Statutory auditors' responsibilities for the audit of the Financial Statements

### • Objectives and audit approach

Our role is to issue a report on the financial statements. Our objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with professional standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As specified in Article L. 823-10-1 of the French Commercial Code (*Code de commerce*), our statutory audit does not include assurance on the viability of the Company or the quality of management of the affairs of the Company.

As part of an audit conducted in accordance with professional standards applicable in France, the statutory auditors exercises professional judgment throughout the audit and furthermore:

- Identifies and assesses the risks of material misstatement of the financial statements, whether due to fraud or error, designs and performs audit procedures responsive to those risks, and obtains audit evidence considered to be sufficient and appropriate to provide a basis for his opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtains an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal control.
- Evaluates the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management in the financial statements.
- Assesses the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. This assessment is based on the audit evidence obtained up to the date of his audit report. However, future events or conditions may cause the Company to cease to continue as a going concern. If the statutory auditor concludes that a material uncertainty exists, there is a requirement to draw attention in the audit report to the related disclosures in the financial statements or, if such disclosures are not provided or inadequate, to modify the opinion expressed therein.
- Evaluates the overall presentation of the financial statements and assesses whether these statements represent the underlying transactions and events in a manner that achieves fair presentation.

- **Report to the Audit and Accounts Committee**

We submit a report to the Audit and Accounts Committee which includes in particular a description of the scope of the audit and the audit program implemented, as well as the results of our audit. We also report significant deficiencies, if any, in internal control regarding the accounting and financial reporting procedures that we have identified.

Our report to the Audit and Accounts Committee includes the risks of material misstatement that, in our professional judgment, were of most significance in the audit of the financial statements of the current period and which are therefore the key audit matters that we are required to describe in this report.

We also provide the Audit and Accounts Committee with the declaration provided for in Article 6 of Regulation (EU) No 537/2014, confirming our independence within the meaning of the rules applicable in France as set out in particular in Articles L. 822-10 to L. 822-14 of the French Commercial Code (*Code de commerce*) and in the French Code of Ethics (*Code de déontologie*) for statutory auditors. Where appropriate, we discuss with the Audit and Accounts Committee the risks that may reasonably be thought to bear on our independence, and the related safeguards.

Courbevoie and Paris-La Défense, March 5, 2018

The Statutory Auditors  
(French original signed by)

**Mazars**

Anne-Laure Rousselou

Jean-Marc Deslandes

**Ernst & Young Audit**

Philippe Diu

Serge Pottiez

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# BUSINESS REVIEW

## > 2





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## 2.1 OPERATING SEGMENTS

The Group has a matrix organisation based on:

- six Global Business Units, grouped into three operating segments: Aerospace (Avionics, Space), Transport (Ground Transportation Systems) and Defence & Security (Secure Communications and Information Systems, Land and Air Systems, and Defence Mission Systems);
- an international organisation split into the major industrial countries in which the Group is present (Germany, France, the Netherlands, the United Kingdom, Canada, the United States and Australia), other European countries and emerging markets.

### 2.1.1 Aerospace segment

The Aerospace segment includes the Avionics and Space Global Business Units.

The **Avionics** Global Business Unit offers a large array of equipment and functions for piloting, navigation and aircraft control systems, electrical generation and conversion, and in-flight entertainment and connectivity systems. This activity also includes simulation and training solutions for military aircraft and civilian and military helicopters as well as microwave and imaging subsystems. As a partner of the major aircraft manufacturers and airlines, Thales is a player across the entire value chain for the aviation sector, in addition to its air traffic management business.

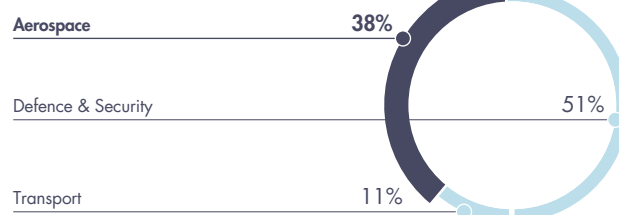
The **Space** Global Business Unit offers space systems and solutions, particularly in the fields of telecommunications, radar and optical observation of the Earth, satellite navigation and exploration of the Universe. The strategic partnership in the space sector between Thales and Leonardo – the Space Alliance – responds to the significant environmental, scientific and security challenges faced by the sector as well as the changes brought about by the expansion of the information society. It is based on the solutions offered by both Thales Alenia Space (67% owned by Thales, 33% owned by Leonardo) in satellite manufacturing and by Telespazio (33% owned by Thales, 67% owned by Leonardo) in related services.

#### 2.1.1.1 Key data

(in € millions)	2017	2016
Order book at 31 December	8,850	9,914
Order intake	5,200	5,872
Sales	5,985	5,812
EBIT <sup>(a)</sup>	601	571
Employees under Group management	18,772	18,741

(a) Non-GAAP indicator. See definition in the section entitled "Presentation of Financial Information" on pages 8 and 9.

#### Sales by segment



#### 2.1.1.2 Avionics

##### 2.1.1.2.1 General overview

Thales supports aircraft manufacturers, the armed forces, airlines, operators, pilots, crews and passengers to improve flight efficiency, safety and comfort. The secure, natively connected systems designed by Thales allow aircraft to fly in all circumstances and to interface all elements of the aeronautic ecosystem, on the ground or in flight.

The range of avionic equipment, systems and applications covers four main areas:

- **Piloting and control of the aircraft:** information display solutions in cockpits are equipped with simplified "human-system" interfaces for optimised flight management and conduct and a permanent connection with airlines and air traffic control.
- **Support and services:** the digital solutions Thales offers simplify the tasks to be performed by the pilot and enable fleets to be tracked in real time in order to optimise operating costs and increase aircraft availability.

- **Passenger experience:** Airlines call upon Thales to personalise the services they offer to their passengers through the latest generation of onboard multimedia systems supported by high-speed connectivity. Thales also makes use of the latest technology in data analytics to enable companies to access new sources of revenue generated by specific applications offered to passengers depending on their profile. In addition, the Group offers cabin lighting and aircraft interior systems, provided through Diehl Aerospace.

- **Simulation and training:** simulator training for pilots of military aircraft and civilian and military helicopters prepare them more effectively for their missions while reducing training costs. Thales provides the flight simulators for many European and Australian defence programmes, as well as training and instruction services.

Thales also provides electric power generation and conversion solutions, and electric motors, in addition to power amplification and X-ray imaging solutions for the space and defence industries and the medical sector.

### 2.1.1.2.2 Competitive position

As one of the leading players in the avionics market alongside Honeywell and Rockwell Collins, Thales supplies the commercial and military aircraft manufacturers Airbus, ATR, Bell, Boeing, Bombardier, Cessna, Dassault Aviation, Embraer, Gulfstream, Leonardo, NHIndustries, Sikorsky and Sukhoi.

In the in-flight entertainment segment, Thales is one of the top two players, with Panasonic Avionics.

The Group has numerous competitors in the simulation solutions market, particularly American defence companies such as Lockheed Martin, Raytheon and L3Com.

Thales continues to be a global market leader in microwave and imaging subsystems, and its main competitors in these markets are Varian Medical Systems, CPI and L3.

### 2.1.1.2.3 Significant events in 2017

In **commercial avionics**, Thales won contracts with Airbus for the supply of flight control computers and probes. The latest standard in avionics, known as standard 3, co-developed by ATR and Thales for ATR-600 regional aircraft was certified by the EASA in July 2017 before its commissioning at the end of 2017. The Thales Pad connected portable electronic solution was selected by more than 20 airlines to optimise their operations on Boeing, Airbus and Sukhoi aircraft.

AirAsia selected Thales for the supply of avionic equipment and the maintenance of its 304 A320neo. The Brazilian company Azul also chose an avionic equipment package for its fleet of 58 A320neo.

For the eleventh year running, Thales has consolidated its position in offering support to airlines, ranked third best supplier in the annual Airbus rankings and number one in Airbus' supplier evaluation.

In **military avionics**, Thales won a major software development contract for Rafale India. 2017 also saw the launch of the in-flight testing campaign for the first French A330MRTT, for which Thales is a major partner of Airbus Defence and Space.

As regards **in-flight entertainment**, 2017 saw the commissioning of the AVANT® system on Japan Airlines' Boeing 787-9 Dreamliners. Meanwhile, SES and Hughes announced the signature of strategic agreements aimed at optimising the availability of the in-flight connectivity service FlytLIVE™, the most efficient to date to cover the Americas.

In **training and simulation**, Thales secured an order for two additional flight simulator models for Airbus A400M, bringing the total number of orders to eight.

Haite Group, a Chinese leader in the supply of aeronautical services, opened its new training centre in Tianjin with the Reality-H EC135 helicopter simulator designed by Thales, who was selected for the first time in China. Airbus Helicopters chose Thales to equip the crews of Caracal helicopters in the Kuwaiti forces with a Reality-H mission simulator in addition to two coaching positions in tactical flying and training procedures.

With regard to **electrical systems**, Safran Landing Systems and Thales decided to combine their expertise to develop an electrical taxi system for aircraft.

In **imaging and microwave subsystems**, Thales was selected to supply the first Ku-band tubes for use in a telecommunications satellite. In the radiology field, Siemens stepped up the promotion of the product ARTPIX EZ2GO developed by Thales which enables hospitals to optimise the cost of ownership of their medical imaging systems while simplifying the work of their employees. Finally, the most powerful free-electron laser in the world was inaugurated in Hamburg. Thanks to the energy supplied by the klystrons and couplers manufactured by Thales, this new system will revolutionise the study of the nanoworld.

## 2.1.1.3 Space

### 2.1.1.3.1 General overview

Thales Alenia Space, a joint venture between Thales (67%) and Leonardo (33%), forms the Space Alliance with Telespazio to offer a full range of solutions including services. For over forty years, Thales Alenia Space has designed, integrated, tested, operated and delivered innovative space systems to meet its customers' needs in terms of telecommunications, navigation, Earth observation and management of the environment, exploration, science and orbital infrastructures. On the strength of unique expertise in dual missions, constellations, high-speed flexible payloads, altimetry, meteorology, optical observation, high-resolution radar and space exploration, Thales Alenia Space has been able to capitalise on its heritage while placing innovation at the heart of its strategy, in a digital, connected world in a state of flux.

Thales Alenia Space offers a full range of solutions which meet demands for planetary constellations, the supply of very high-speed geostationary satellites for connectivity purposes in particular, and the integration of a space component into 5G.

#### A key participant in environmental programmes

Thales Alenia Space's renowned expertise in high-resolution (sub-metric) optical and radar payloads for military, civilian or dual missions covers a wide range of uses, including information gathering, target designation, meteorology, altimetry, oceanography, climatology, cartography and crisis management. Thales Alenia Space satellites help provide a better understanding of planet Earth and how to protect it. In this market segment, alternative solutions are beginning to emerge comprising low-orbit high-revisit constellations or products complementary to satellites such as HAPS (High Altitude Platforms) for instance. In conjunction with its involvement in the continuity of the European Copernicus programme and its Sentinels, and in the 3rd generation of *Meteosat*, Thales Alenia Space and Telespazio (through the Space Alliance) invest in high revisit solutions.

#### At the forefront of the origins of the Universe and deep space exploration

The International Space Station has generated new needs in terms of refuelling for the astronauts on board and future projects beyond Earth are under consideration. Thales Alenia Space manages key technologies for the ISS: 50% of its pressurised module, ATV refuelling cargo spacecrafts. In parallel, Cygnus validated atmospheric re-entry technologies with the success of the IXV mission while vehicles of the future such as Space Rider and soon the spacecraft Orion, rally teams for new challenges. Thales Alenia Space also plays a central role in the adventure of future scientific missions through the programmes ExoMars 2020, Solar Orbiter, Bepi Colombo, Juice, Euclid and NEXT-Step-2.

#### At the forefront of geolocation and navigation systems

Thales Alenia Space remains the European centre of excellence in the field of Satellite navigation systems (EGNOS, Galileo) and at the cutting edge of geolocalisation solutions including Argos NEO and its station MEOLUT Next dedicated to "Search and Rescue" services.

#### At the cutting-edge of innovation

Thales Alenia Space is developing the *Stratobus*, an autonomous stratospheric airship that is complementary to satellite solutions and is designed for regional telecommunications, surveillance and environmental applications.

#### Services for European launchers

Thales Alenia Space contributes to the European policy on access to space by supplying the on-board electronics for the Ariane rocket, the safeguard subsystem of the Soyuz launchers in French Guiana and soon that of the Ariane 6 for which the Company will also supply the telemetry transmitter.

### 2.1.1.3.2 Competitive position

We are witnessing a real transformation of the space sector triggered not only by the ruptures caused by the world of launchers (SpaceX) but also by the new requirements in terms of satellite applications and in particular by the appearance of new requirements in terms of mega-constellations. New initiatives are coming to light, innovation is becoming increasing daring and the turnaround times for development and marketing new concepts are reducing significantly. The major operators are reflecting on the most optimised solutions to address the new requirements of end users. The complementarity of satellite services from different orbits is becoming an increasingly considered option.

In the commercial satellite segment, Thales Alenia Space's main competitors are Space Systems/Loral, Airbus Group, Orbital ATK, Boeing and Lockheed Martin. It is important to also count on the gradual arrival in the commercial market of new international players (from Russia, China, India, Israel, Japan, etc.) in the fields of telecommunications and observation.

The leading competitors in the commercial and military institutional market in Europe, which is to a large extent dependent on the budgetary situation of governments, are Airbus Group and OHB – which are also sometimes partners on some programmes – as well as Boeing and Lockheed Martin for export contracts.

### 2.1.1.3.3 Significant events in 2017

In telecommunications, Thales Alenia Space signed a contract with Inmarsat for the construction of Inmarsat GX, a very-high-throughput satellite (VHTS) offering capacity in the Middle East, Europe and the Indian Sub-continent. The payload will be integrated in a transparent way into Inmarsat Global Xpress' (GX) existing high throughput network. Another highlight of 2017 has been the deployment of the Iridium NEXT constellation with 40 satellites already launched and the placing on the market of fully digital payloads.

In Earth observation, Thales Alenia Space won an equipment contract for the Biomass mission dedicated to the study of carbon, and a contract for the integration in the United Kingdom of the MicroCarb satellite dedicated to the measurement of CO<sub>2</sub>, the main greenhouse gas responsible for climate change.

In science, Thales Alenia Space in the United Kingdom was entrusted with a study for the design of the payload module for the SMILE (Solar Wind Magnetospheric Ionospheric Link Explorer) mission, while Thales

Alenia Space in Spain was entrusted with the communication transponders for the Indian TEAMINDUS and the Korean KPLO (Korea Pathfinder Lunar Orbiter) lunar missions.

In exploration, Thales Alenia Space signed the preliminary development contract with the European Space Agency for Space Rider, a new generation European reusable transport system from low orbit and is taking part in NASA's NEXTStep-2 adventure, to support manned space flights in proximity to the moon.

In observation and geolocalisation, Thales Alenia Space won the contract for the Argos NEO instrument for the nano-satellite demonstrator Angels for geolocalisation data collection. In addition, the MEOLUT Next solution, integrated into Cospas-Sarsat's Search & Rescue system was awarded by the SSPI (Space & Satellite Professionals International) in the "Humanitarian" category for its contribution to saving lives.

In the field of launchers, Thales Alenia Space in Belgium supplied the nozzle activation system for the Ariane 6 launcher while Thales Alenia Space in Spain will deliver the telemetry transmitter.

In 2017, Thales Alenia Space participated in the following thirteen launches: Five telecommunication satellites (Telkom 3S, SGDC, Koreasat 5A and 7, HellaSat 3/Inmarsat-S EAN), two Cygnus cargo spacecraft, one observation satellite (Mohamed VI satellite), one telecommunication payload (REDSAT) and one scientific instrument (Hexapod), 40 satellites for the Iridium NEXT constellation in batches of ten.

In 2017, Thales Alenia Space announced the creation of a new automated production site dedicated to the assembly of photovoltaic cells for solar panels on satellites in Belgium and the opening of a shared Optical Systems and On-board Instrumentation (Systèmes Optiques et Instrumentation Embarquée or SOIE) laboratory with the marseille Astrophysics Laboratory (LAM in French). The company also formalised a minority interest in Airstar Aerospace to secure the development of the *Stratobus* programme. Through its involvement in the Space Alliance, Thales Alenia Space and Telespazio joined forces through a memorandum of understanding with the US company Spaceflight to respond to the very-high revisit and low orbit Earth observation constellations market.

Thales Alenia Space launched its digital transformation and entered the industry 4.0 (smart factory) era, particularly with the introduction of robots and cobots in industrial processes, a record number in parts made using 3D manufacture (more than 1000) in orbit, the use of virtual and augmented reality, automated production chains and the creation of digital twins for future satellites.

## 2.1.2 Transport segment

### 2.1.2.1 Key data

(in € millions)	2017	2016
Order book at 31 December	4,391	4,567
Order intake	1,780	1,504
Sales	1,761	1,603
EBIT <sup>(a)</sup>	72	11
Employees under Group management	7,005	6,812

(a) Non-GAAP indicator. See definition in the section entitled "Presentation of Financial Information" on pages 8 and 9.

### 2.1.2.2 Ground Transportation Systems

#### 2.1.2.2.1 General overview

The Group is one of the foremost global players in railway signalling and control/monitoring systems. It also offers ticketing solutions.

In its three domains, Thales provides systems for urban transport networks (metros and trams) and mainline networks (conventional, high-speed and freight). Thales capitalises on its expertise in the field of critical information systems and cybersecurity to offer transport network operators integrated and protected solutions to effectively supervise and control their operations. The systems provided by Thales also contribute to increasing the security of its customers' passengers, staff and infrastructure.

#### 2.1.2.2.2 Competitive position

Specialised in intelligent critical systems and services, Thales sets itself apart from its "generalist" competitors, who offer product ranges dominated by rolling stock. The rapid digitisation of railway transport products, solutions and operations has made Thales a recognised leading player with strong positions in these markets.

In signalling, Thales is a key player, and its main competitors are Siemens, Alstom, Ansaldo STS, Bombardier Transport and China Railway Signal & Communication (CRSC).

#### 2.1.2.2.3 Significant events in 2017

For **urban** integrated signalling, communications, security and monitoring **activities**:

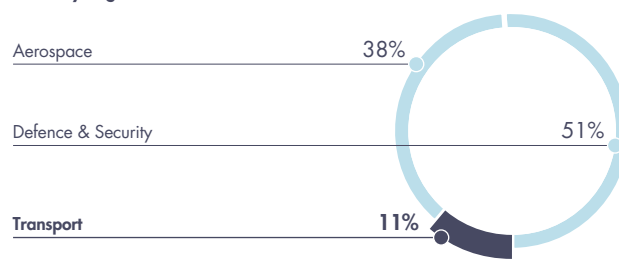
Thales is continuing its expansion in Asia and had two new successes in Taiwan: Thales will supply the signalling and communication systems and equipment for the operational control centres for the extension of the Kaoshiung tramway and for the future Ankeng tramway programme.

Thales also won its first contract in Vietnam for the provision of a complete telecommunications, security and monitoring system for line 3 of the Hanoi metro.

In China, through its Thales SAIC Transportation System (TST) joint venture, Thales won a contract for the signalling of the first automatic driverless metro line (line 14) in the megalopolis of Shanghai. In 2017, TST also commissioned the signalling systems for eight metro lines.

In Dubai, Thales was once again selected for the extension and modernisation of the red metro line, one of the longest driverless metro lines in the world. It will transport the 25 million expected visitors to the 2020 World Expo.

#### Sales by segment



In Cairo, where Thales has provided monitoring, communications and security solutions for over 30 years, a new contract was won for phase 4B of line 3.

In London, Thales continued to roll out the new signalling system for 4 metro lines; the Circle, District, Hammersmith & City and Metropolitan lines which represent 40% of the London network. The first tests involving the release into circulation of several test trains were completed successfully.

In the rest of the world, Thales continued to successfully Commission CBTC (Communications-based train control) lines: in India, in Hyderabad, in Chile with line 6 in Santiago, and in the United States with the Disney line.

For **mainline** integrated signalling, communications, security and monitoring **activities**:

In Egypt, Thales will modernise the signalling and telecommunications of the mainline networks in the 180 km stretch which connects the cities of Assiut and Nagh Hammadi. The three-year project is part of the Egyptian rail infrastructure transformation programme, financed by the World Bank; this new success comes on the back of the project to modernise the Cairo/Alexandria line, currently under deployment by Thales.

Thales also signed the contract for the maintenance of the signalling and telecommunications systems of the "North South Railway Project" in Saudi Arabia, the longest railway line in the world to be equipped with cutting-edge technology signalling systems, through an initiative in line with the Vision 2030 plan. In Eastern Europe, Thales continued to deploy the ETCS signalling system for the modernisation of the rail network in Poland, Romania and Hungary.

On the African continent, Thales won a contract in Senegal for the signalling, telecommunication systems, security and monitoring of the TER "Train Express Régional" connecting Dakar city centre with the new international airport (55 km).

In France, in a record time of 27 months Thales designed and constructed the new Ardoines signal box on behalf of the SNCF. Commissioned in June, this technical centre is a strategic link in the Île-de-France rail network.

In **ticketing** and road tolls, Thales was selected to install new tolling equipment on 38 lanes of the motorway from Mexico to Puebla.

Thales pursued its development in Egypt, winning two new ticketing contracts to equip 19 new metro stations in Cairo and in Thailand, in addition to the Blue metro line in Bangkok.

## 2.1.3 Defence & Security segment

### 2.1.3.1 Key data

(in € millions)	2017	2016
Order book at 31 December	18,605	18,973
Order intake	7,883	9,063
Sales	7,983	7,390
EBIT <sup>(a)</sup>	869	787
Employees under Group management	34,011	33,282

(a) Non-GAAP indicator. See definition in the section entitled "Presentation of Financial Information" on pages 8 and 9.

### 2.1.3.2 Secure communications and information systems

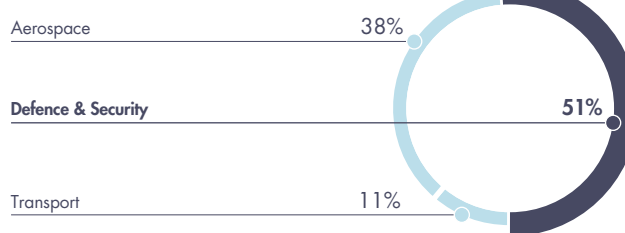
#### 2.1.3.2.1 General overview

The armed forces, security forces and essential operators rely on Thales for their interoperable and secure information and telecommunications systems. Central to the defence-security continuum, these activities, which include radiocommunications, networks, protection systems, critical information systems and cybersecurity, respond to the needs of markets in which the use of new digital technologies such as 4G networks, cryptography, cloud computing, artificial intelligence and big data are of the utmost importance. Thales is present throughout the value chain, from equipment through to systems and systems of systems, as well as logistical support and related services.

These activities are developed around four segments:

- **radiocommunications products:** Thales designs radios and embedded and tactical communications systems for all three sectors (land, air and sea), identification friend or foe (IFF) systems, radio navigation systems and solutions for electronic communications warfare. The armed forces of more than 50 countries around the world are equipped with Thales solutions. The Group is a major player in the development of interoperable, secure Software-Defined Radio (SDR) solutions and is the prime contractor for the French army's CONTACT programme;
- **network and infrastructure systems:** Thales designs, supplies, deploys, supports and operates fixed or mobile communications networks for the defence and security forces, and critical infrastructure operators. Its resilient, secure systems rely on the full range of military and commercial technology. In France, Thales provides the renovation of Defence communication systems through the Descartes programme, the renovation of networks linked to nuclear dissuasion and support to the information system of the Ministry of the Armed Forces. In addition, the Group also operates communication systems in theatres of operation in Afghanistan, Mali and the Central African Republic. Thales also offers satellite communication ground systems, in France with the Syracuse programme and also for export;
- **protection systems:** as a European leader in the digitised battlefield, Thales develops information, command and intelligence systems for the armed forces (military functions known as C4ISR – Computerized, Command, Control, Communications, Intelligence, Surveillance and Reconnaissance). Based on this technology developed for its military

#### Sales by segment



customers (France, NATO, Export), the Group also responds to growing security needs for critical infrastructures such as airports and other particularly sensitive sites. All of these systems are intended to enable the fastest and most relevant decision-making, whether it is automatic or by operators. Based on intelligence of the situation, thanks to a multitude of sensors, they offer users real-time, precise information on their environment and the effects of actions taken;

- **critical information systems and cybersecurity:** States, essential operators and companies in general are enlisting in a digital transformation process to boost their efficiency, reactivity and profitability. As a European leader in cybersecurity and a global leader in data protection, Thales contributes to ensuring a secure digital transformation for its customers thanks to its management of the design and operation of critical information systems. Thales supports its customers in the secure design of their IS or their Cloud hybridation projects and proposes solutions to protect their applications, their communication networks and their sensitive or classified data against cyber threats. In addition, Thales offers solutions for organisations to train and instruct their teams in cyber risks, to anticipate threats, detect the most advanced IT attacks and identify solutions.

#### 2.1.3.2.2 Competitive position

Thales has a variety of competitors depending on the business and market concerned.

In defence applications – radiocommunications, networks, and command and control – the main competitors are predominantly American: Harris, General Dynamics, Raytheon and Rockwell Collins. Israel-based Elbit Systems is also a competitor in the area of integrated command and communication solutions. In Europe, the Group's main competitors are Airbus Group and – particularly in the radiocommunications sector – Rhode & Schwarz, Leonardo and Aselsan.

In security, Thales's competitors are primarily coming from the aeronautic and defence sector (Boeing, Northrop Grumman, Honeywell, Airbus Group, etc.), the equipment sector (such as Siemens and Johnson-Tyco), or from services (INEO, etc.) and information systems (including IBM, Atos and Capgemini). The latter are also competitors of Thales in critical information systems.

Finally, in cybersecurity, Thales is in competition with companies such as RSA and Gemalto in the commercial segment and BAE Systems, Ultra Electronics, Airbus Group and Secunet in defence, and also Atos, Sopra Steria and Cap Gemini in the field of Digital Services Companies.

### 2.1.3.2.3 Significant events in 2017

In the field of **radiocommunication products**, the French software-defined radio programme CONTACT designed for the land, air and sea armed forces continues, particularly with the launch of developments of the airborne component designed primarily for the combat aircraft RAFALE. In parallel, Thales completed the first part of the development of SYNAPS, the CONTACT export version, and has unveiled operational advances for collaborative and high throughput combat to its main European and global customers.

The Group was chosen by the US army to equip new brigades with the hand-held two-channel radio IMBITR. Thales also received orders from several countries for SOTAS vehicular communication systems.

In aeronautics, a high level of activity was maintained with the order for the production of the CNi (communications, navigation, identification) suite for the Rafale combat aircraft for India, and the order of a very-high-throughput connection solution for a country in the Middle East.

In naval communications, Thales received an order for the development of mid-size frigate (FTI or Frégates de taille intermédiaire in French) communications. The Group will also supply the communications electronic warfare system, and a new generation of identification equipment (IFF). In the United Kingdom, Thales secured a major contract to support the communication systems for several Royal Navy vessels. In Germany, Thales was selected for the communications of frigate K130.

In **networks and infrastructure systems**, Thales launched on the market its service as an operator of resilient, secure mobile networks, Elji, and has already secured SNCF as one of its first customers.

In France, the Ministry of Defence granted Thales a 10-year service contract for the implementation of optimised logistics for the resupply of aeronautical consumables (LORCA programme). Following the contract won by the business combination comprising Thales and RUAG Defence France for the implementation of the CERBERE (Training centres representative of battlefields and reproducing engagements), the Group is also involved in the establishment of high-speed LTE 4G communications infrastructure for training ground forces.

In exports, Thales was chosen by a country of the Middle East to supply a tactical communications network, in partnership with the company Ultra. For another customer in the Middle East, Thales provided the first complete satellite-based ground military telecommunication system composed of mobile stations and anchorage integrating SYSTEM 21.

Finally, Thales finalised the deployment of the professional mobile radio infrastructure (TETRA network) for the Mexico City metro.

Thales's **protection systems** address both the defence and security markets. In defence, Thales was notified of the second round of the EMBR (multi-role armoured vehicle) programme of the French land forces, a key component of the SCORPION programme. For this programme, Thales was also selected alongside Nexter and Safran by the French Defence Procurement Agency for the architect-integrator contract. In exports, for Qatar, the C4I system for the Léopard 8x8 combat vehicle was formally accepted and the first vehicles were commissioned.

In security, Thales was selected as one of three protection providers for all the French military sites and for the protection of the United Nations camps in Gao and Kidal (Mali). In addition, John F. Kennedy airport in New York selected Thales's offer for the definition of protection systems for terminal 4, its busiest terminal. In the Middle East, various inaugurations reflected the progress of Thales's two major contracts in the region: security of the Port of Doha and the Dubai Smart City. In France, Thales will also provide security systems under the "PassDef" framework agreement for protection of the national military sites.

The Identification activity was sold to the Imprimerie Nationale (French printing agency) to form a French champion in secure ID documents.

### In the field of critical information systems and cybersecurity

In France, in the public sector, Thales was chosen to support the secure digital transformation of major public players, such as the Ministry of Internal Affairs, the Ministries of Solidarity and Health, Employment, Education and Sports, as well as the ACOSS (Central agency for social security bodies) and IGN (National geographic institute). These missions relate in particular to the development of new digital services and the integration of applications into the ministerial Cloud. The La Poste Group and Thales also announced a 12-month trial aimed at testing the implementation of new legal provisions in cybersecurity including the deployment of the confidence probe for the detection of cyber attacks.

On the global stage, Thales performed the security assessment for the contactless payment application Samsung Pay on the smartphones Galaxy S8 and S8+, which resulted in certification of the application on the two devices.

In addition, Thales opened two centres of excellence in cybersecurity in Cambridge and Toulouse and also opened a new cybersecurity monitoring centre in Hong Kong, and a cyber training facility in Belgium.

## 2.1.3.3 Land and air systems

### 2.1.3.3.1 General overview

Thales systems and equipment help to make the airspace safer and more secure. In commercial air traffic control, Thales's portfolio ranges from conventional navigational aids to radar and **air traffic control** centres, surveillance systems, satellite navigation and airport management solutions.

Thales plays a key role as an architect and integrator in the future air traffic management system, particularly through the OACI's<sup>(1)</sup> "Global Air Navigation Plan – Aviation System Block Upgrades" initiative. Thales is the main industrial partner of the SESAR<sup>(2)</sup> project in Europe and a key player in the NextGen programme in the United States.

Across all continents, Thales offers one of the broadest lines of commercial and military **ground-based and naval radars**, on the market, for surveillance, air traffic management and fire control. 1,300 Thales radars are in service across the world and the Group equips over 70 countries with commercial radars and more than 45 countries with military radars.

In the military segment, Thales is specialised in air operations command and control systems and air defence radar systems, ensuring the protection and security of forces and resources deployed in over 45 countries. As a mission systems integrator, Thales is proud to contribute actively to major military programmes in the world such as ACCS for NATO, SCCOA for France and FLORAKO for Switzerland. Thales excels in the fields of system integration, complex programme management, real time and non-real time software, human-machine interfaces and service oriented architecture.

Thales owns 50% of Thales Raytheon Systems AMDC2, a company that specializes in Integrated Air and Ballistic Missile Defence (IAMD) Command and Control (C2) Systems. Thales Raytheon Systems AMDC2 provides NATO and the NATO Nations with Integrated Air and Missile Defence (IAMD) capability as part of the Air Command and Control System (ACCS).

Thales also offers a wide range of **weapon systems** for medium-range (SAMP/T), short-range (Crotale and RAPIDDefender) and very short-range markets (RAPIDFire cannon and RAPIDRanger missile system). The Group also supplies the lightweight multi-role missile (LMM) family.

In the field of **optronics**, the combination of optical and electronic systems, Thales designs and manufactures components and systems for day and night surveillance, reconnaissance, protection, threat detection and target acquisition on all types of land, sea (surface and subsurface) or air

(1) International Civil Aviation Organization.

(2) Single European Sky ATM Research.

platforms for defence and security customers worldwide. Thales's expertise in optics is also applicable to the commercial segment of high end zoom lenses for cinema and for ultra-high power scientific and industrial lasers.

Thales designs, manufactures and supports **armoured military vehicles** including the Hawkei and the Bushmaster. Thales provides integrated capability solutions at all levels of the value chain, from subsystem supplier to system integrator; mission systems design authority and prime contractor. The open architecture systems of vehicles provides highly standardised "plug and play" capability for on-board sub-systems and products, increasing vehicle capability and performance whilst reducing size, weight and operator workload and whole life system costs.

### 2.1.3.3.2 Competitive position

Thales's expertise in all aspects of air traffic control (automation, navigation and surveillance) is widely recognised by the world's civil aviation authorities. With over 40% of the world's airspace controlled by TopSky ATC, Thales is at the forefront of air traffic control systems and civilian radars.

Other major players in the commercial sector are the US companies Lockheed Martin and Raytheon, European companies Indra and Leonardo (Selex), and in some niche areas, Saab, Frequentis and Harris.

In the military sector, Thales's main competitors for surface radars are the US companies Lockheed Martin, Northrop Grumman, and Raytheon, and Leonardo, Airbus Group, BAE Systems, Indra and Saab in Europe.

Thales is one of Europe's leading suppliers of medium-range, short-range and very short-range missiles and weapon systems. Other principal players in this field in Europe (MBDA) and the United States (Raytheon and Lockheed Martin) are also major customers of Thales's missile electronics and key partners in weapon systems.

Thales is Europe's leading defence optronics supplier facing competition in this segment from US suppliers (Raytheon, Lockheed Martin and Flir Systems) and from Israeli suppliers (primarily Elbit). The protected vehicles systems market segment is dominated, on an international level, by BAE Systems, General Dynamics, Rheinmetall, Krauss-Maffei Wegmann and Nexter. Thales operates in Europe as an independent integrator both for its own and other suppliers' equipment within complex mission systems.

### 2.1.3.3.3 Significant events in 2017

In 2017, the Air Traffic Management (ATM) business line secured a variety of contracts across its full portfolio of technologies. A turnkey contract was secured for Tanzania, for the modernisation of air control infrastructures in response to the increase in traffic in the country and in East Africa. This contract includes TopSky ATC, primary and secondary radar system – Star NG RSM970S, 4 civil radars, civil engineering and training of controllers and engineers.

Thales was selected by Norway for the deployment of 14 ground-based navigational aid systems (TACAN), as part of a campaign to modernise the existing equipment and to renew the ILS navigation systems in Germany and the Netherlands.

In the area of surface radars, Thales launched some new products in 2017:

- the Ground Fire family: a range of new generation multifunction ground radars. These fully digital radars will simultaneously provide for surveillance and air defence missions;

- the new TRAC NG in-flight monitoring radar with exceptional dual capacities (commercial and military). Derived from the STAR NG radar, the most advanced approach radar in the world, the TRAC NG radar responds to requirements to increase the primary in-flight surveillance capacity of increasingly saturated air spaces and ensure heightened surveillance in secure military air space;
- in November 2017, Thales acquired Aveillant, a UK company specialised in the drone detection holographic radar technology.

In terms of commercial success, Thales, alongside the Naval Group, was notified by the Ministry of Defence of the contract for the development and production of five medium-sized frigates (FTI in French) for the French Navy, as part of a programme piloted by the French Defense Procurement Agency (DGA). The first of the five frigates will be delivered in 2023 for entry into active service in 2025. Thales-developed systems at the cutting edge of technology will equip the new frigate BELH@RRA, such as the fully digital multifunction radar SEA FIRE, equipped with four fixed panel antenna which meet the requirements of different missions, including self-defence of the vessel and extended air defence and can take control of ASTER missiles. The Sea Fire is designed to perform in the complex conditions of the littoral or in heavily jammed environments to counter conventional, asymmetric or emerging air and surface threats.

In terms of convincing past performance, during a ballistic missile exercise in the Atlantic Ocean, Thales's SMART-L radar on board the HNLMS De Ruyter successfully detected and followed a ballistic missile launched at an altitude of 300 km and a speed of more than 3 km/second. The system made the data accessible in real time to an Aegis class US Navy vessel which used this data to launch an SM-3 missile. This technology is used by the SMART-L Multi Mission radar currently under development by Thales for the four defence and air command frigates of the Netherlands Royal Navy and for two land versions for the Netherlands Royal Air Force. In parallel with the American exercise, the SMART-L Multi Mission radar installed on the test tower on Thales's site in Hengelo (Netherlands) also detected and tracked the ballistic missile.

A preliminary air defence agreement was signed between Eurosam, a European consortium between Thales and MBDA, and the Turkish manufacturers Aselsan and Roketsan in July 2017. This agreement formalises the willingness of Thales, MBDA, Aselsan and Roketsan to work together to respond to demands from the Turkish authorities to define the architecture for the future air defence and anti-ballistic missile system to enable them to fulfil their mission to protect their population and territory.

The integrated air defence solution ForceSHIELD was commissioned in Indonesia. In addition to the STARStreak air defence missiles, this solution includes the CONTROLMaster 200 surveillance and coordination system, RAPIDRanger mobile integrated weapon systems and Lightweight Multiple Launchers (LML), as well as communication, training and support equipment.

2017 was a year of successful qualification firing tests for the Lightweight Multi-role Missile (LWM). The LWM is on track for official qualification in 2018, following numerous successful firings.

In May 2017, Thales conducted a demonstration in real-life conditions of all of its operational capacities in the surveillance, identification and neutralisation of drones. This trial was carried out in cooperation with companies from the Cluster Paris Drone and Cœur Essonne, on the Brétigny-sur-Orge site near Paris.

Finally, ThalesRaytheonSystems and Lockheed Martin signed a memorandum of understanding to develop anti-ballistic missile territorial capacities for NATO's Air Command and Control System (ACCS).

2017 was a major year for the Hawkei protected tactical vehicle with the launch of the initial production phase of 1,100 armoured vehicles for the Australian army. This step follows a long programme of tests conducted to ensure the customer's demands are fully met. This new vehicle is now ready for export and is presented regularly at the different Defence trade fairs across the world, such as the recent IDEX and MSPO.

In optronics, a contract for airborne reconnaissance pods was signed in the Middle East. The land optronics activity enjoyed exports of armoured platforms from several partners, particularly in South-East Asia and the Middle East.

## 2.1.3.4 Defence mission systems

### 2.1.3.4.1 General overview

Thales manufactures electronic combat, intelligence, surveillance and reconnaissance systems, as well as naval surface and underwater combat systems.

For **airborne combat missions**, Thales produces, in cooperation with Dassault Aviation, radar systems and equipment for the Rafale and the Mirage 2000 fighter aircraft and for future combat unmanned aerial vehicles (UAVs), as well as electronic warfare radar systems, designed to detect threats and protect platforms.

For **intelligence, surveillance and reconnaissance missions**, Thales designs naval, ground and air patrol and surveillance solutions, including a range of electromagnetic-based information-gathering sensors. These systems – which are installed on aircraft or naval platforms – incorporate surveillance radars, acoustic sub-systems and measurement and data linking equipment. Thales also designs complete UAV systems with intelligence, surveillance, reconnaissance and target acquisition capabilities.

In **surface naval warfare**, Thales offers comprehensive combat systems that integrate on-board sensors (radar, sonar, electronic warfare, infrared sensors, etc.), weapon systems and communications and command equipment. Thales also has naval platform engineering and support capabilities.

In **underwater warfare**, Thales offers a broad range of products including submarine sonar suites, hull-mounted and towed array sonar for surface ships, anti-mine systems, including the use of unmanned underwater vehicles, as well as acoustic sensors for submarine guidance.

### 2.1.3.4.2 Competitive position

In electronic combat systems, Thales is one of the leading European players, competing with BAE Systems, Leonardo, and the US companies Raytheon, Lockheed Martin and Northrop Grumman. In intelligence, surveillance and reconnaissance systems, its main competitors are Airbus, Elbit and General Atomics.

In surface naval systems, Thales is one of the principal European players, alongside Leonardo, BAE and Saab, and competes with Lockheed Martin in the United States. In underwater warfare, Thales is one of Europe's main players along with Atlas Elektronik and Ultra Electronics, and is in competition with Lockheed Martin, Raytheon and L3 in the United States.

### 2.1.3.4.3 Significant events in 2017

#### Electronic combat systems

To meet orders for Rafale intended for France and export to Egypt, Qatar and India, the rate of production increased to two pieces of Radar and Electronic Warfare equipment per month starting in March. In addition, Thales and the Indian company Reliance Defence Ltd announced their intention to create a JV to produce a local part of the Thales contract for 36 Rafales in India and to perform part of its offset obligations.

#### Airborne surveillance and intelligence systems

In January, Thales and Lockheed Martin announced the awarding of a contract for the supply of a new air surveillance and control system for the Royal Navy as part of the Crowsnest programme. In March, SIMMAD (Integrated System to Maintain Aeronautical Materials in operational condition of the French Ministry of Defence) entrusted Thales, for a period of 113 months, with management of all the aeronautical material consumables used in Defence. April saw the delivery of the eighth and final Ocean Master radar for Beech 350 King Air aircraft used by the French Customs. These planes are designed for maritime surveillance missions on the Atlantic coast, Mediterranean and overseas. In June, the Chinese government ordered a DORIS (Satellite-based Integrated Orbit Determination and Radio Positioning equipment) to equip an ocean observation satellite. In July, France's Ministry of the Armed Forces announced the order for the development and production of equipment for the electronic warfare suite as part of the launch of the Mid-Size Frigates (FTI) programme.

#### Surface naval systems

In April, a US customer placed the first order for a Tacitcom combat management system to equip the first platform of a new family of vessels. In July, Bangladesh entrusted Thales with the mid-life restoration of the combat system installed on a first heavy corvette. In August, the Canadian government announced a support contract for the re-equipment, distribution, maintenance and associated training for coastal and Arctic patrol vessels. This contract includes an initial service period of eight years as part of a maximum term of 35 years. It is the largest ever signed in the history of the Canadian Royal Navy.

#### Underwater warfare systems

In January, the Navy of the United Arab Emirates ordered two variable depth Captas sonars to equip two of its anti-submarine warfare capacities surface buildings. In March, a contract was signed with the Australian Royal Navy for the supply of an anti-sea mine system (SEA 1778 programme) including five surface naval drones and seven underwater naval drones. In May, as part of the restoration project of three La Fayette frigates (FLF in French), Naval Group announced a contract for three Kinglip hull-mounted sonars. In July, Naval Group also announced an order for the production of the sonar suite to equip future mid-size frigates (FTI). As part of the optimisation project for the support of sensors embedded on surface and underwater platforms of the British Royal Navy (SSOP, Sensors Support Optimisation Project), a contract for the support in service of several suites of sonars was awarded at the end of December.

## 2.2 RESEARCH AND INNOVATION

Thales needs to be able to offer increasingly sophisticated technologies, particularly in the detection, analysis and decision-making fields, in order to design and develop critical information systems. These innovative solutions serve customers in the aeronautics, space, ground transportation, defence and security markets.

Thales bases its vision of innovation on openness and partnership across multiple dimensions:

- a technological dimension, by collaborating with academic laboratories;
- an entrepreneurial dimension by forging closer ties with SMEs and start-ups;
- a “market” dimension, by jointly innovating with customers and their ecosystems to create new usages.

### 2.2.1 Research and development, the key to competitiveness and growth

Some 25,000 Thales employees, over 70% of them engineers, are involved in the Group's technical operations, ranging from research to engineering. In 2017, Thales spent €797 million (5% of sales) purely on self-funded R&D, an essential lever to remain competitive.

A significant portion of this budget is devoted to upstream research in order to develop:

- new technologies;
- new system and product concepts;
- new engineering tools and methods for critical information systems.

### 2.2.2 Four key technical domains

Governance of research and development for key technologies is split into four domains:

- **hardware technologies:** electronics, electromagnetism, optronics, acoustics, radiofrequency techniques and management of thermal constraints;
- **software technology:** processing computers, real-time on-board systems, distributed systems, service-oriented architectures, model-driven engineering, and cybersecurity;
- **information and cognitive sciences:** Artificial Intelligence, big data processing, autonomous systems, synthetic environments, and human factors;
- **systems:** focused on systems design architecture, this area provides support for methodology, processes and expertise.

#### FOCUS 1

##### A world first in 2017, the artificial nano-neuron from the Thales/CNRS joint physics laboratory

In 2017, a team from the CNRS/Thales joint physics unit, in collaboration with American and Japanese researchers unveiled, in the prestigious science journal *Nature*, the first artificial nano-neuron with the ability to recognise numbers spoken by different individuals. This electronic nano-neuron is a breakthrough in artificial intelligence and its applications.

To achieve this result, an exceptionally stable magnetic oscillator was used. Each gyration of this nano-compass generates an electrical output, which imitates the electrical impulses produced by biological neurons.

Interconnected by artificial synapses, these nano-neurons will process and classify, almost instantaneously, the masses of data that will be produced in future years by the billions of connected objects which are gradually invading all sectors of economic life.

## 2.2.3 Thales at the heart of innovation ecosystems

Wherever it is located, Thales seeks to build partnerships within innovation ecosystems, with academic partners, design centres, innovative businesses and industrial groups for joint innovation on applications, business models and technologies.

To develop the technologies it needs, the Group relies heavily on cooperation between its research teams and the academic world. Thales Research & Technology (TRT), an international network of corporate laboratories, is responsible for building relationships with academic partners.

TRT has facilities in France, the United Kingdom, the Netherlands, Singapore and Canada. In France, the Palaiseau laboratory, located on the École Polytechnique campus, is involved in the world-class science and technology complex in Saclay,

While the Singapore centre has partnered with Nanyang Technological University and with France's national research institute CNRS, in one of the few joint international research units with an industrial partner.

In France, Thales has numerous strategic partnerships, for example, with the CNRS, the CEA, École Polytechnique, Telecom Paris Tech, and Université Pierre et Marie Curie (UPMC-Paris VI).

This heavy involvement of the Group in research in close partnership with the public research sector was recently highlighted by the journal *Nature*, which publishes the list of the "Top 100 Corporate research institutions: the leading corporate institutions for high-quality science". In this list, Thales ranks second in France and 27th in the world, streaks ahead of all the other companies in its sector.

The most advanced form of partnership is the joint laboratory, such as those operated by Thales with the CNRS for physics, with CEA-LETI as part of the III-V Lab (an EIG whose members are NOKIA, Thales and CEA-LETI), with CEA-LIST for artificial vision and formal approaches to the development of critical software, and with UPMC in artificial intelligence, etc.

Thales is a major player in various international competitiveness centres and a founding member of the *Institut de Recherche Technologique Saint-Exupéry* technological research institute.

In the United Kingdom, TRT has direct links with several major Universities through its R&T centre, including Bristol. Thales is an active member of many collaborative partnerships in the United Kingdom: the Centre for Secure Information Technologies (CSIT), based at Queen's University Belfast; the Centre for Smart Infrastructure and Construction (CSIC) and the Institute for Manufacturing (IfM), based at Cambridge University; the UK Defence Growth Partnership (DGP); the mobile Virtual Centre of Excellence (mVCE), with numerous Universities; the Defence Academic Pathways (DAP) and the UK Catapults, particularly the Digital Catapult where Thales has contributed to the emergent IoT defining the security implications of pervasive digital Sensors and their associated data.

In Canada, the Group regularly works with research networks and institutions such as CRIAQ (*Consortium de Recherche et Innovation en Aérospatiale au Québec*), the University of Toronto, McGill University, the *École Polytechnique de Montréal* and Laval University, with which Thales has entered into an agreement for a joint research unit in urban sciences.

### FOCUS 2

#### The smart sensor: from physics to artificial intelligence

Sensor technologies form part of the Group's DNA. Combining physics, electronics, signal processing and imaging, in the future these devices will be embedded with an increasing amount of intelligence as close as possible to raw data.

Thales has developed an artificial intelligence solution capable of detecting elements of interest in real time in optronic images taken during air missions. Built into the sensor, this Artificial Intelligence will offer assistance to pilots during a mission. This technology will achieve the "short loop", so long awaited by operational experts from detection through to engagement in a considerably reduced time.

Also in radars, artificial intelligence will come into play immediately after signal digitisation. A new concept of antenna already implements this paradigm, by combining direct digitisation of the signal and intelligence, for the detection, location and identification of hostile signals.

In 2017, Thales created CortAIX, an artificial intelligence laboratory with around fifty people, to develop the use of AI in Thales's systems. The laboratory is situated in Montreal, in the heart of one of the world's leading artificial intelligence ecosystems. Thales researchers from CortAIX are forming collaborations with MILA (the Quebec Institute of Artificial Intelligence), IVADO (Data Optimisation Institute), the Quebec Artificial Intelligence Institute and the Vector Institute in Toronto.

In emerging countries, the Group is developing its R&D activities by establishing innovation platforms locally, using the tried and tested principles of joint innovation with local players and, in so doing, building long-term, trust-based relationships.

In 2017, Thales continued to step up its work with start-ups.

Already a founding member of Starburst, a specialised incubator in the aeronautics and space field, Thales was selected by the world's largest incubator Station F to run its cybersecurity programme. Thales selected nine start-ups adding value to the Group's cyber security offer. Thales and the start-ups selected will offer their customers solutions covering the entire cybersecurity chain (see Focus 3).

Training also forms part of the overall strategy of linking the Group with the academic world. The Group supports around 200 doctoral students worldwide. They work on subjects directly connected with the technical issues facing Thales, which therefore reinforces its appeal to young scientists. Thales also supports six teaching chairs in subjects that are in line with its technical priorities.

### FOCUS 3

#### At the heart of the cybersecurity ecosystem

Harnessing innovation where it is most dynamic, is one aspect of Thales's innovation strategy. By becoming a leading partner of Station F for cybersecurity in 2017, Thales tests the solutions proposed by the start-ups who join the programme.

One such start-up, Keeex, a French start-up founded in 2014, has developed a unique universal embedded digital signature technique which relies on distributed blockchain architecture. This innovation guarantees the integrity and authenticity of the data/documents exchanged, which is a major breakthrough in the digital transformation.

## 2.2.4 A dynamic approach to intellectual property management

Thales supports its R&D activities with a dynamic approach to intellectual property management.

The Group filed more than 300 new patent applications in 2017. The continued large number of patent applications in recent years reflects Thales's commitment to innovation and its ability to translate research results into competitive advantages.

The Thales portfolio, which includes more than 15,000 patents and patent applications, is regularly adapted to operational requirements, particularly to protect Thales's market share.

In 2017, Thales was once again included in the Top 100 Global Innovators ranking compiled by Clarivate Analytics, with the Group standing out for the volume, success and influence of its patents. This achievement underlines Thales's commitment to innovating, protecting its ideas and bringing its inventions to market. Thales has been included in this prestigious ranking five times since 2011, which testifies to the importance the Group places on implementing an active and ambitious intellectual property management strategy.

### FOCUS 4

#### The digital factory: the driving force behind the Group's digitisation

Created in 2017, the Digital Factory will unite 150 world-class experts in digital technologies, recruited internally and externally, to serve Thales's customers in all its businesses, through the extensive introduction of mass data processing and intelligence technologies to the Group's solutions, while also providing data security – a fundamental requirement of the digital economy.

It will host a digital platform ("Digital Platform Foundry") which will maximise economies of scale and synergies, based on which new "As a Service" offers will be developed for customers of the Group.

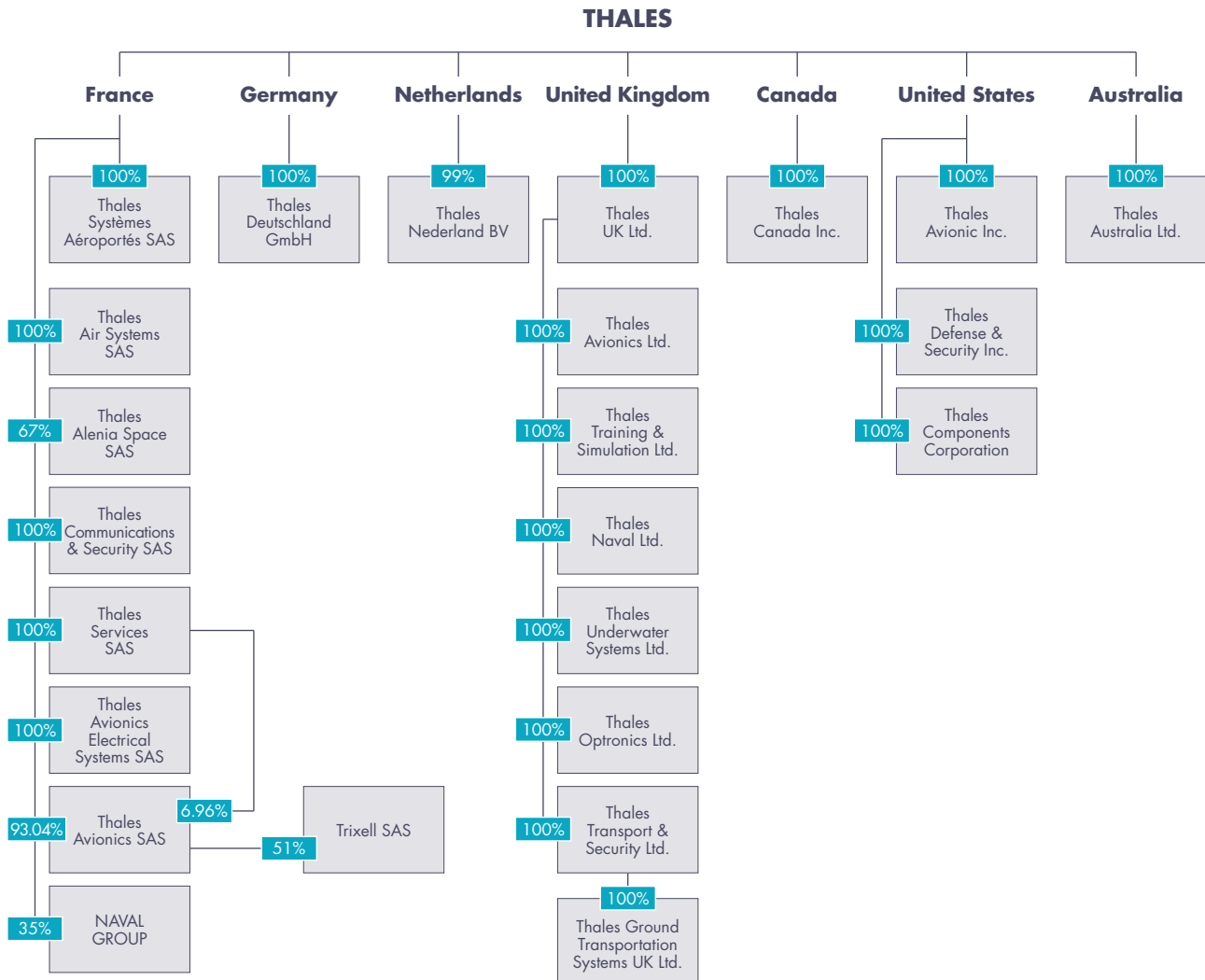
It will also host an incubator for internal and external start-ups and a digital academy designed to disseminate the digital culture within the Group.

## 2.3 RELATIONS BETWEEN THALES AND ITS SUBSIDIARIES

### 2.3.1 Simplified organisational chart at 31 December 2017

This simplified organisational chart includes fully consolidated companies that account for more than 0.5% of consolidated sales, in the main countries in which the Group operates.

The companies consolidated under the equity method are not included in this chart (with the exception of NAVAL GROUP).



## 2.3.2 Role of Thales (parent company) within the Group

Thales (parent company) acts as a holding company for the Group:

- it holds shares in the Group's major subsidiaries;
- it manages central functions such as Group strategy, trading policy, legal and financial policy, operational monitoring, human resources policy and communications;

- it provides subsidiaries with specialist assistance, including legal, tax and financial expertise, for which the subsidiaries pay a fee;
- it provides financing, cash pooling and, where necessary, guarantees.

In addition to these functions, Thales (parent company) conducts its own research, described beginning on pages 130 *et seq.*

A list of the main consolidated companies can be found below.

## 2.3.3 Financial flows between Thales (parent company) and its subsidiaries

Thales (parent company) receives dividends from its subsidiaries, as approved by their respective Annual General Meetings, and in accordance with the applicable legislation and regulations in their countries of operation.

In addition to these dividends and the payment of fees for shared services, the main financial flows between Thales (parent company) and its subsidiaries relate to cash pooling.

As a rule, the cash surpluses of subsidiaries are transferred to the parent company under a centralisation system known as cash pooling. In return, Thales (parent company) meets the cash flow requirements of the subsidiaries. The parent company conducts operations in financial markets to arrange the necessary investments and loans, in the context of cash pooling, to meet its own requirements and those of its subsidiaries. Except in special cases, this system applies to all subsidiaries in which Thales has majority control.

## 2.4 INFORMATION ABOUT MAJOR OPERATIONAL SUBSIDIARIES AND MANUFACTURING SITES

### 2.4.1 List of main consolidated companies

As part of the simplification of legal structures in France, several mergers came into effect on 31 December 2017:

- Thales Air Systems SAS (which became Thales IAS France SAS on 1 January 2018), absorbed the companies TDA Armements SAS, Thales Optronique SAS, Thales Angénieux SAS, Thales Air Operations SAS and Thales Cryogénie SAS;
- Thales Avionics SAS (which became Thales AVS France SAS on 1 January 2018) absorbed the companies Thales Electron Devices SAS, Thales Training & Simulation SAS and Thales Avionics LCD SAS;
- Thales Systèmes Aéroportés SAS (which became Thales DMS France SAS on 1 January 2018), absorbed the companies Thales Underwater Systems SAS and Thales Microelectronics SAS.

The materiality criteria used to prepare these tables have also been applied to the list of the main consolidated companies in Note 17 to the consolidated financial statements.

Company name	Country	% of capital held by Thales	% of voting rights held
<b>1. Controlled companies (fully consolidated)</b>			
Thales Alenia Space SAS	France	67%	67%
Thales Alenia Space Italia SpA	Italy	67%	67%
Thales Air Systems SAS	France	100%	100%
Thales Australia Ltd	Australia	100%	100%
Thales Austria GmbH	Austria	100%	100%
Thales Avionics SAS	France	100%	100%
Thales Avionics Inc	United States	100%	100%
Thales Avionics Electrical Systems SAS	France	100%	100%
Thales Canada Inc	Canada	100%	100%
Thales Communications & Security SAS	France	100%	100%
Thales Defence & Security Inc	United States	100%	100%
Thales Deutschland GmbH	Germany	100%	100%
Thales e-Security, Inc	United States	100%	100%
Thales Espana Grp SAU	Spain	100%	100%
Thales Italia SpA	Italy	100%	100%
Thales Nederland BV	Netherlands	99%	99%
Thales Norway AS	Norway	100%	100%
Thales Polska Sp. z o.o.	Poland	100%	100%
Thales Ground Transportation Systems UK Ltd	United Kingdom	100%	100%
Thales Rail Signalling Solutions AG	Switzerland	100%	100%
Thales Security Solutions & Services Company	Saudi Arabia	100%	100%
Thales Services SAS	France	100%	100%
Thales Solutions Asia Pte Ltd	Singapore	100%	100%
Thales Systèmes Aéroportés SAS	France	100%	100%
Thales Transport & Security (Hong Kong) Ltd	Hong Kong	100%	100%
Thales Transport & Security Ltd	United Kingdom	100%	100%
Trixell SAS	France	51%	51%
Thales UK Ltd	United Kingdom	100%	100%

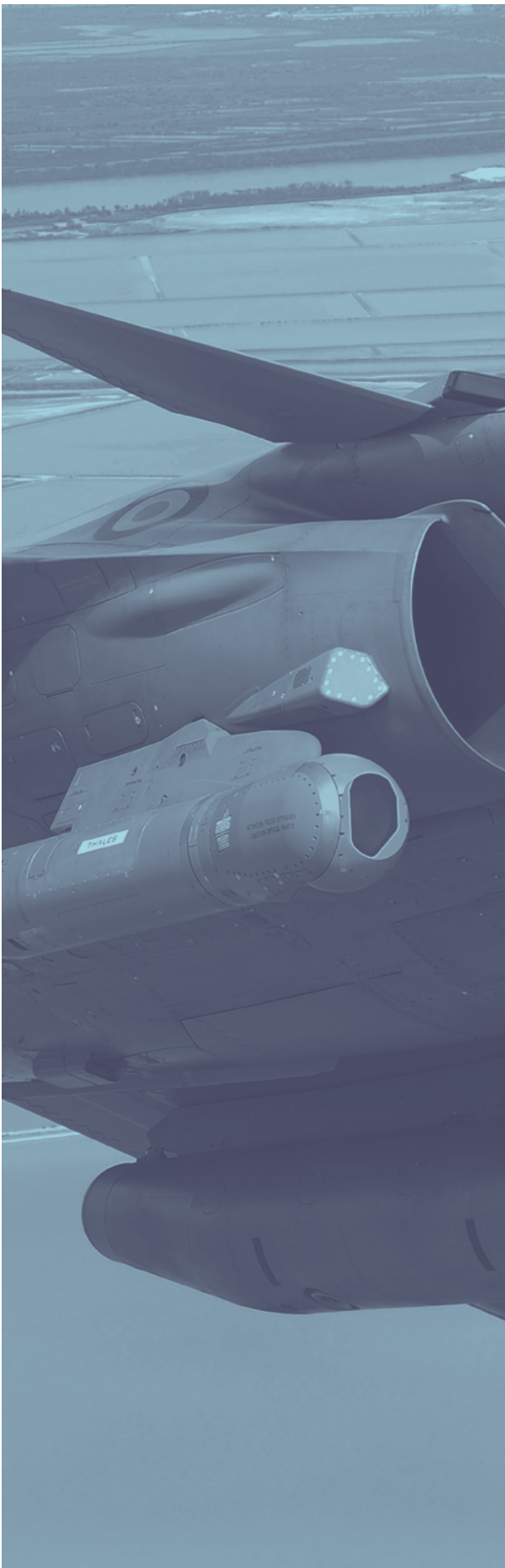
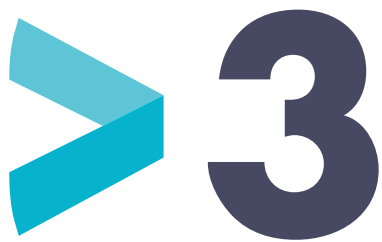
Company name	Country	% of capital held by Thales	% of voting rights held
<b>2. Joint ventures (under equity method)</b>			
Thales-Raytheon Systems Air and Missile Defense Command and Control SAS	France	50%	50%
Citylink Telecommunications Holding Ltd	United Kingdom	33%	33%
NAVAL GROUP	France	35%	35%
Diehl Aerospace GmbH	Germany	49%	49%
Sofradir SAS	France	50%	50%
<b>3. Associated companies (under equity method)</b>			
Aviation Communications & Surveillance Systems	United States	30%	30%
Air Tanker Holdings Ltd	United Kingdom	13%	13%
Elettronica SpA	Italy	33%	33%
Telespazio SpA	Italy	33%	33%

## 2.4.2 Major manufacturing sites

At end-2017, there were 15 sites employing more than 1,000 staff.

At 31 December 2017	Headcount	Owned	Size (m²)
<b>France</b>			
Bordeaux (South-west)	2,850	Leased (Le Haillan), and Owned (Pessac)	62,000
Brest (Brittany)	1,421	Leased	56,000
Cannes (Provence)	2,064	Owned-leased	84,000
Cholet (Pays de la Loire)	1,463	Leased	53,000
Gennevilliers (Île-de-France)	3,593	Leased	90,000
Élancourt (Île-de-France)	3,499	Leased	104,000
Massy (Île-de-France)	1,120	Leased	26,000
Rungis (Île-de-France)	1,215	Leased	23,000
Toulouse (South-west)	4,017	Owned-leased	142,000
Vélizy (Île-de-France)	3,554	Leased	125,000
<b>United Kingdom</b>			
Crawley	1,784	Leased	26,130
<b>Netherlands</b>			
Hengelo	1,195	Property	87,000
<b>Australia</b>			
Sydney	1,249	Leased	84,327
<b>Germany</b>			
Stuttgart	1,595	Leased	59,000
<b>United States</b>			
Irvine	1,016	Leased	30,440

# CORPORATE GOVERNANCE





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## 3.1 COMPOSITION OF THE BOARD OF DIRECTORS AT 31 DECEMBER 2017

### 3.1.1 Directors

#### 3.1.1.1 Appointed at the General Meeting <sup>(1)</sup>

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##### PATRICE CAINE

(47)

**Chairman & Chief Executive Officer**

**Chairman of the Strategic & CSR Committee**

**First appointed**

23 December 2014

**Current term expires:**

AGM 2018

**Number of shares held**

- 6,929 Thales shares (6,773 in registered form, 156 under the Group savings plan);
- 3,438 subscription options for Thales shares.

Patrice Caine was born on 7 January 1970 and is a French citizen. Patrice Caine is a graduate of the École Polytechnique and the École des Mines de Paris and holds the rank of Chief Engineer (*Ingénieur en chef*) of the Corps des Mines. He began his career in 1992 at Fournier, a pharmaceutical company, before working as a consultant in M&A and Corporate Strategy at Charterhouse Bank Limited in London.

From 1995 to 1998, he was special advisor to the Prefect of the Franche-Comté region of France and head of the Industrial Development and Energy Division at DRIRE, the French agency responsible for industry, research and the environment.

From 1998 to 2000, he was part of the Conseil Général des Mines, in charge of human resources for the Corps des Mines. During this time, he oversaw the training of graduate engineers for the civil service at the École des Mines de Paris. From 2000 to 2002, he worked as a technical advisor on energy on the staff of the Minister of the Economy, Finance and Industry.

In 2002, Patrice Caine joined the Thales group's Strategy department before being appointed to manage the following operating units: Aviation & Naval, Communications, Navigation & Identification, Air Systems, Radio Communication Products, Network & Infrastructure Systems and Protection Systems.

He was awarded the bronze National Defence Medal (*Médaille de la Défense Nationale*). In 2014, he was made a Knight of the French National Order of Merit (*Chevalier de l'Ordre National du Mérite*).

In February 2013, Patrice Caine joined Thales' Executive Committee as Senior Executive Vice President, Chief Operating Officer and Chief Performance Officer.

On 23 December 2014, he was appointed **Chairman and CEO of Thales** by the Board of Directors.

**Appointments and other positions held in companies in France and abroad**

**Appointments held in other companies**

In France: Director of Naval Group.

Abroad: none.

**Other positions held by Mr Caine in the last five years**

In France: Director of École des Mines de Paris.

Abroad: none.

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<sup>(1)</sup> Of the directors referred to in this section, Ms Renaud-Basso, director representing the French state, was appointed by order of the Minister of the Economy and Finance pursuant to Article 4 of Order No. 2014-948.

**LAURENCE BROSETA****(49)**

**Director proposed  
by the Public Sector**  
(Article 6 of Order No. 2014-948)

**First appointed**  
14 May 2014

**Current term expires**  
AGM 2021

**Number of shares held**  
500 Thales shares

**In addition, her husband,  
Xavier Broseta, holds:**

- 450 Thales shares;
- 52 Thales shares under the Group savings scheme.

Born on 22 September 1968, Laurence Broseta is a French citizen and a graduate of the École Polytechnique and Télécom ParisTech.

She began her career at RATP where she oversaw operations at its bus, tram and underground departments. She also took part in new rail infrastructure projects in the UK and South Africa, where she started up and managed a locally-based operating company.

In 2008, she became head of RATP Dev's international business unit, with responsibility for operating Transport services (Bus, rail, underground and tram) in nine countries and leading business development.

In March 2013, she became Senior Executive Vice President France of Transdev, an international group that provides mobility and passenger transport services.

Since July 2016, Laurence Broseta has been **Chief Executive Officer of Transdev's International Zone** in charge of Southern Europe and Northern Europe, Asia, the Pacific, South America, the Middle East and Africa, which reported €1.7 billion in revenue and has some 20,000 employees.

**Appointments and other positions held in companies in France and abroad**

**Appointments held in other companies**

**In France:** member of the Supervisory Board of Vallourec and Director of RATP Dev Transdev Asia.

**Abroad:** Director of Transdev group subsidiaries (in Spain, Portugal, South Korea, India, Germany, Chile, Colombia, Australia, New Zealand).

**Other positions held by Ms Broseta in the last five years**

**In France:** Director of Transdev group subsidiaries, Director of Thello, Director and Vice Chairman of the Union des Transports Publics, and Director of the RATP Foundation.

**Abroad:** Director of RATP Dev group subsidiaries.

**CHARLES EDELSTENNE****(79)**

**Director recommended  
by the Industrial Partner**

**Member of the  
Strategic & CSR Committee**

**First appointed**  
19 May 2009

**Current term expires**  
AGM 2018

**Number of shares held**  
509 Thales shares

Born on 9 January 1938 and a French citizen, Charles Edelstenne is a qualified chartered accountant.

He spent his career at Dassault Aviation, where he started in 1960 as Head of the Financial Studies Department. He became Company Secretary in 1975, then Vice President for Economic and Financial Affairs in 1986.

From 2000 to 2012, he was the Chairman & Chief Executive Officer of Dassault Aviation.

In January 2013, Charles Edelstenne became **Chief Executive Officer of Groupe Industriel Marcel Dassault**.

He was the founder, Managing Director then Chairman & Chief Executive Officer, and is now Chairman of the Board of Directors of Dassault Systèmes.

**Appointments and other positions held in companies in France and abroad**

**Appointments held in other companies**

**In France:** Chairman of the Board of Directors of Dassault Systèmes SE<sup>(1)</sup>, Chief Executive Officer and Member of the Supervisory Board of Groupe Industriel Marcel Dassault SAS, Honorary Chairman of Dassault Aviation SA<sup>(1)</sup>, Director of Dassault Aviation SA<sup>(1)</sup>, Dassault Medias SA, Groupe Figaro Benchmark SASU, Carrefour SA<sup>(1)</sup> and Sogitec Industries SA, Honorary Chairman of Gifas, Manager of the non-trading Companies Arie, Arie 2, Nili and Nili 2, and Director of the mutual fund ("SICAV") Monceau DUMAS.

**Abroad:** Director of SABCA<sup>(1)</sup> (Belgium), Director of Dassault Falcon Jet Corp. (United States) and of the bank Lepercq de Neufelize & Co (United States).

**Other positions held by Mr Edelstenne in other companies in the last five years**

**In France:** Chairman and CEO of Dassault Aviation SA<sup>(1)</sup>.

**Abroad:** Chairman of Dassault Falcon Jet Corp. (United States), President de Dassault International Inc. (United States).

<sup>(1)</sup> Listed company.

## YANNICK D'ESCATHA

(69)

**Independent director**

**Chairman of the Governance and Remuneration Committee**

**First appointed**

19 May 2009

**Current term expires**

AGM 2020

**Number of shares held**

500 Thales shares

Born on 18 March 1948 and a French citizen, Yannick d'Escatha is an engineer who graduated from the École Polytechnique and the École des Mines de Paris.

In 1972, he lectured at the École Polytechnique, the École des Mines de Paris and ENSTA, the French engineering and research institute.

In 1973, as a technical expert with the French Ministry of Industry, he took part in the drafting and subsequent implementation of the French technical regulations relating to nuclear-fired water boilers.

In 1978, he was appointed head of the control office for nuclear construction where he was responsible for government technical control of the application of this regulation to the French electro-nuclear programme.

In 1982, he was seconded to Technicatome, a subsidiary of the CEA (French Atomic Energy Commission), whose main activity is industrial general contracting in the field of nuclear propulsion for French naval vessels. Having been director of the Cadarache and Aix-en-Provence sites, Yannick d'Escatha was appointed Deputy Chief Executive Officer of Technicatome on 1 January 1987.

On 1 March 1990, he was asked by the Executive Director of the CEA to accept the post of director of the newly created Advanced Technologies division, and became Deputy Executive Director of the CEA on 14 September 1992.

He was appointed Managing Director of the CEA on 1 July 1995 and Chairman of the holding company CEA-Industrie on 28 June 1999.

On 1 January 2000, he was appointed Executive Vice President Industry at EDF. As the head of EDF's Industry Cluster, he was responsible for the company's production and engineering activities and industrial policy.

In January 2002, he became Chief Operating Officer at EDF.

In February 2003, the French Council of Ministers appointed Yannick d'Escatha as Chairman of the National Space Research Centre (CNES) and renewed his appointment in February 2010, until he reached the age limit of 65 in 2013.

Since May 2013, he has worked as a consultant: Advisor to the Chairman of Sofinel (*Société Française d'Ingénierie Électronucléaire et d'assistance pour l'exportation*) and, since January 2017, to the Chairman of EDF.

### Appointments and other positions held in companies in France and abroad

#### Appointments held in other companies

**In France:** Member of the *Académie des technologies* (the National Academy of Technologies of France).

**Abroad:** none.

#### Other positions held by Mr d'Escatha in the last five years

**In France:** Chairman of the National Space Research Centre (CNES), Chairman of the Board of Directors of the University of Technology of Troyes, member of the Board of Directors of EDF<sup>(1)</sup>, Permanent Representative of the CNES on the Board of Directors of Arianespace SA and Permanent Representative of the CNES on the Board of Directors of Arianespace Participation.

**Abroad:** none.

## PHILIPPE LÉPINAY

(64)

**Director representing employee shareholders**

**Member of the Strategic & CSR Committee**

**First appointed**

8 March 2007,  
effective 1 April 2007

**Current term expires**

AGM 2021

**Number of shares held:**

- 1,105 Thales shares;
- 2,313 Thales shares under the Group savings scheme.

Born on 3 December 1953, Philippe Lépinay is a French citizen and a graduate engineer of the Institut de Marketing International, Université Paris VII.

Between 1977 and 1986, he held a variety of sales and marketing roles with the Appalette & Tourtellier Systèmes, Radiall and Sopema groups.

In 1986, he joined Thales Electron Devices as an export sales engineer, and in 2000 he became head of development at Thales Engineering & Consulting.

He joined Thales International in 2003. Since 2010, he has been **Vice President, International Relations at Thales**.

### Appointments and other positions held in companies in France and abroad

#### Appointments held in other companies

**In France:** International Relations Delegate of the French Federation of Employee Shareholders' Associations (FAS), Vice Chairman of the Federation of Employee Shareholders' Associations of Thales (FAST), member of the Supervisory Committee of the Thales Employee Shareholding FCPE (investment fund) and member of the Development Council of the ENSOA (French School for Active Non-Commissioned Officers).

**Abroad:** none.

#### Other positions held by Mr Lépinay in the last five years

Chairman of the FAS, member of the Steering Committee for Profit-sharing, Incentives, Savings and Employee Shareholding (COPIESAS).

**In France:** none.

<sup>(1)</sup> Listed company.

**ARMELLE DE MADRE****(47)****Independent director****First appointed**  
28 June 2017**Current term expires**  
AGM 2019**Number of shares held**  
500 Thales shares

Born on 2 May 1970, Armelle de Madre, a French and Dutch citizen, graduated from the University of Colombia, New York and HEC, Paris.

Armelle de Madre started her career in 1993 as a Marketing Analyst at Renault. In 2001, she became Training Manager for the Head Office, then HR Manager for Renault's logistics business. In 2006, she was appointed Human Resources Director firstly in charge of the Flins factory, then for Renault's vehicle and mechanical engineers, a remit which included the group's Technocentre, one of the largest R&D centres in France with more than 16,000 employees.

She joined Schneider Electric in 2010 as Strategy and Social Innovation Director, and then the Arkadin Group in 2011, which provides Unified Communications solutions and is a subsidiary of NTT, one of the main telecoms operators in the world, as Vice Chairman of Human Resources in charge of Europe, the Middle East and Africa (EMEA). In 2016, she became Vice Chairman of Marketing, EMEA. Since April 2017, Armelle de Madre has been **Human Resources Director of Arkadin** and, in this capacity, joined the Group's Executive Committee. She is also a member of the International Women's Forum France.

**Appointments and other positions held in companies in France and abroad****Appointments held in other companies**

In France: none.

Abroad: none.

**Other positions held by Ms de Madre in other companies in the last five years**

In France: none.

Abroad: none.

**ODILE RENAUD-BASSO****(52)****Director proposed by the Public Sector, appointed representative of the French state by order of 19 July 2017**  
(Article 4 of Order No. 2014-948)**Member of the Strategic & CSR Committee****Member of the Governance and Remuneration Committee****First appointed**  
19 July 2017**Current term expires**  
AGM 2021**Number of shares held**  
not obliged to hold Thales shares  
(Art. 5 of Order No. 2014-948).

Born on 2 June 1965, Odile Renaud-Basso, a French citizen, is a graduate of the Institut d'Études Politiques de Paris and a former student of the ENA (1990, Jean Monnet year).

After starting her career as an auditor in the *Cour des Comptes* (1990-1994), Odile Renaud-Basso joined the French Treasury Department where she held various positions between 1994 and 2005 related to international, industrial and financial issues. In 2005, she was appointed Director of the Directorate-General for Economic and Financial Affairs (DG Ecfm) of the European Commission and continued her career in the European bodies, becoming Deputy Head of Cabinet of the President of the European Council in 2010.

In May 2012, she became Deputy Director of the Office of the French Prime Minister. Then in 2013, she took up the position of Deputy Chief Executive Officer Caisse des Dépôts and Director of Savings Funds.

Since 30 June 2016, Odile Renaud-Basso has been **Director General of the French Treasury**.

**Appointments and other positions held in companies in France and abroad****Appointments held in other companies**

In France: none.

Abroad: none.

**Other positions held by Ms Renaud-Basso in the last five years**

In France and abroad: 2013-2016: Director of CNP Assurances and of the La Poste Group.

## LOÏK SEGALEN

(57)

**Director recommended  
by the Industrial Partner**

**Member of the Audit  
and Accounts Committee**

**First appointed**  
19 May 2009

**Current term expires**  
AGM 2018

**Number of shares held**  
509 Thales shares

Born on 27 March 1960, Loïk Segalen is a French citizen and a graduate of the École Centrale de Lyon and ESSEC.

He started his career in 1986 in the Finance Department of Dassault International.

He served as financial advisor to Dassault Aviation's Vice President for Economic and Financial Affairs in 1990 and subsequently became Deputy Director (1998-1999), and ultimately Director.

In January 2009, Loïk Segalen was appointed Vice President for Economic and Financial Affairs at Dassault Aviation.

He became Vice President for Economic and Social Affairs at Dassault Aviation in September 2011.

In January 2013, he became **Chief Operating Officer of Dassault Aviation**.

He is a member of the Dassault Aviation Management Committee.

He is a Knight of the French Legion of Honour and a Knight of the French National Order of Merit.

### Appointments and other positions held in companies in France and abroad

#### Appointments held in other companies

**In France:** Director of Sogitec Industries, member of the Board of Directors of Gifas.

**Abroad:** Director of Dassault Falcon Jet Corporation (USA), Dassault International Inc. (USA), Midway Aircraft Instrument Corporation (USA), Sabca<sup>(1)</sup> (Belgium), Sabca Limburg (Belgium) and Dassault Belgique Aviation (Belgium).

#### Other positions held by Mr Segalen in the last five years

**In France:** none.

**Abroad:** Director of Dassault Procurement Services (USA).

## ANNE-CLAIRE TAITTINGER

(68)

**Independent director**

**Chairman of the Audit  
and Accounts Committee**

**First appointed**  
15 May 2012

**Current term expires**  
AGM 2018

**Number of shares held**  
612 Thales shares

Born on 3 November 1949, Anne-Claire Taittinger, a French citizen, is a graduate of the Institut d'Études Politiques de Paris, and holds a Master's degree in Urban Sociology, a post-graduate diploma (DESS) in Urbanism and a degree from the Centre de perfectionnement aux affaires (CPA business school). She began her career in 1976 in the Caisse des Dépôts et Consignations group as manager for urban operations in the Société centrale d'équipement du territoire.

She joined the Groupe du Louvre in 1979 as Company Secretary, then became Chairman & Chief Executive Officer of the Compagnie Financière Deville. She was subsequently Chairman & Chief Executive Officer of the Compagnie Financière Leblanc, Elm-Leblanc, Vice Chairman & Chief Executive Officer of the industrial division of Deville, and Chairman & Chief Executive Officer of Annick Goutal perfumes France USA and later Baccarat.

She became Chief Executive Officer, followed by Chairman of the Management Board of the Société du Louvre in 1997, and, in 2002, Chairman of the Management Board of Groupe Taittinger and Chief Executive Officer of its subsidiary Groupe du Louvre when the positions of Chairman of the Board and Chief Executive Officer were separated. She stepped down from these positions in July 2006, after overseeing the sale of Groupe Taittinger to an investment fund in 2005.

In September 2006, she formed part of a pool of investors that bought Champagne Taittinger.

In 2004, Anne-Claire Taittinger became involved in the Women's Forum for the Economy and Society, both as a co-founder and investor.

### Appointments and other positions held in companies in France and abroad

#### Appointments held in other companies

**In France:** Chairman of SAS Le Riffay, Director and Member of the Appointments and Compensation Committees of Carrefour<sup>(1)</sup>.

**Abroad:** none.

#### Other positions held by Ms Taittinger in the last five years

**In France:** Until 2015: Director and Chairman of the Appointments, Compensation and Corporate Governance Committee of Club Méditerranée<sup>(1)</sup>. Until 2013: Director of FinanCités, of the IFA (*Institut Français des Administrateurs*) and of the Fondation Planet Finance, member of the Supervisory Board of Planet Finance.

**Abroad:** none.

<sup>(1)</sup> Listed companies.

**ANN TAYLOR****(70)****Independent director****First appointed**  
15 May 2012**Current term expires**  
AGM 2018**Number of shares held**  
500 Thales shares

Born on 2 July 1947, Ann Taylor is a UK citizen and studied at the University of Bradford, where she obtained a Bachelor's degree in Political Science and History, and the University of Sheffield, where she obtained a Master's degree in Economic History.

In 1974, she was elected MP (Labour) for Bolton West, holding this seat until 1983.

She subsequently became head of the Housing Corporation and a lecturer at the Hansard Society (a member of Birkbeck College) from 1983 to 1987.

In 1987, Ann Taylor was elected MP (Labour) for Dewsbury. She then held various ministerial roles, notably from 1990 to 1997 as Under Secretary of State for Education and Under Secretary of State for the Environment. In 1998, she reported directly to the Prime Minister and sat on most government committees.

In May 1997, she became member of the Privy Council when she was appointed as Chairman.

In 2001, she chaired the Intelligence and Security Committee under the direct authority of the Prime Minister.

In 2005, she entered the House of Lords (with a life peerage) where she is a representative at the Parliamentary Assembly of the Council of Europe (Political Committee) and the Assembly of the Western European Union (Defence Committee). She is a member of the NATO Parliamentary Assembly.

In 2007, as a British State Minister in the House of Lords, Ann Taylor became responsible for matters of defence, notably as Minister for Defence Equipment and Support in 2007 and 2009, and then as Minister for International Defence and Security from 2008 to 2010.

Ann Taylor is currently a **member of the House of Lords** and chairs its Constitution Committee. She is also a Trustee of the National Coal Mining Museum for England.

**Appointments and other positions held in companies in France and abroad****Appointments held in other companies**

**In France:** none.

**Abroad:** member of the Advisory Board of Thales UK PLC<sup>(1)</sup> and Chair of Council and Pro-Chancellor at the University of Bradford.

**Other positions held by Ms Taylor in the last five years**

**In France and abroad:** none.

**ÉRIC TRAPPIER****(57)****Director recommended  
by the Industrial Partner****Member of the Governance  
and Remuneration Committee****First appointed**  
19 May 2009**Current term expires**  
AGM 2018**Number of shares held**  
500 Thales shares

Born on 1 June 1960, Éric Trappier is a French citizen and a graduate of the École Sud Telecom (formerly Institut National Telecom).

He started his career in 1984 in the Technical Department of Dassault Aviation as head of systems development for the ATL2 and Mirage 2000.

In 1991, he became Director of Sales in Asia (India), and in 1996, in the United Arab Emirates.

After serving as Head of Middle East & Africa in 2000 and head of military exports in 2001, he became Executive Vice President, International in 2002.

In 2006, Éric Trappier became Executive Vice President, International of Dassault Aviation.

He was appointed **Chairman & Chief Executive Officer of Dassault Aviation** in January 2013.

He is an Officer of the French Legion of Honour and a Knight of the French National Order of Merit.

**Appointments and other positions held in companies in France and abroad****Appointments held in other companies**

**In France:** Chairman and Chief Executive Officer of Dassault Aviation<sup>(2)</sup>, Chairman of Gifas, Chairman of Cidef, Director of Sogitec Industries.

**Abroad:** Chairman of Dassault Falcon Jet Corporation (USA), Director and Chairman of Dassault International Inc. (USA), Chairman of the ASD (Belgique), Co-Chairman and Director of Dassault Reliance Aerospace Limited (DRAL) (India) and Director of Dasbat Aviation LLC (United Arab Emirates).

**Other positions held by Mr Trappier in the last five years**

**In France:** Managing Director of Rafale International EIG and Dassault International, Permanent Representative of Dassault Aviation on the Boards of Sofresa, Odas, Sofema and Eurotradia.

**Abroad:** none.

(1) A Thales group company.

(2) Listed company.

## MARIE-FRANÇOISE WALBAUM

(67)

**Director recommended  
by the Industrial Partner**

**First appointed**  
17 September 2013

**Current term expires**  
AGM 2018

**Number of shares held**  
500 Thales shares

Born on 18 March 1950, Marie-Françoise Walbaum, a French citizen, is a graduate in economics and sociology from Paris X University.

She began her career at BNP Paribas in 1973 and held various posts in retail banking and credit analysis until 1981. From 1981 to 1994, she served as senior auditor of BNP's Inspectorate General, Chief Executive Officer for mutual funds and Chief Executive Officer of the brokerage firm Patrick Dubouzet S.A. In 1994, Marie-Françoise Walbaum became Head of Listed and Unlisted Equity Investments and Private Equity Portfolio Manager at BNP Paribas, a firm she left in the summer of 2012 after a career spanning 39 years.

### Appointments and other positions held in companies in France and abroad

#### Appointments held in other companies

**In France:** independent director of Esso (and Chairman of the Audit Committee), FFP (and member of the Finance and Audit Committee and the Governance, Appointments and Remunerations Committee), Imerys (and member of the Audit Committee, the Appointments Committee and the Compensation Committee), and member of the Supervisory Board of Isatis Capital.

**Abroad:** none.

#### Other positions held by Ms Walbaum in the last five years

**In France:** director of Vigeo.

**Abroad:** none.

## 3.1.1.2 Employee representatives

## ANNE-MARIE HUNOT-SCHMIT

(53)

**Director representing  
employees**

**Member of the  
Strategic & CSR Committee**

**First appointed**  
9 December 2016

**Current term expires**  
8 December 2020

**Number of shares held**

- 200 Thales shares;
- 48 Thales shares under the Group savings scheme.

Not required to hold Thales shares (Article L. 225-25, paragraph 3 of the French Commercial Code).

Born on 4 October 1964, Anne-Marie Hunot-Schmit is a French citizen and a graduate of the IAE de Paris business school. After receiving a postgraduate degree in Applied Mathematics, she joined Dassault Electronique in 1987 as a software developer, where she filed the first patent for a ground collision avoidance system (GPWS/GCAS). In 1998, Ms Hunot-Schmit joined the first contract management team for the Mirage 2000-9 programmes.

In 2007, she began working at Thales' registered office, where she was responsible for international business ethics standards and subsequently became head of the Price Control Department.

Since autumn 2016, she has been in charge of Financial Controlling for bids and projects within the Ground Transportation Business Unit.

No appointments or positions held in other companies.

**FRÉDÉRIQUE SAINT**

(59)

**Director representing employees****Member of the Audit and Accounts Committee****Member of the Governance and Remuneration Committee****First appointed**

9 December 2016

**Current term expires**

8 December 2020

**Number of shares held**

- 10 Thales shares;
- 20 Thales shares under the Group savings scheme.

Not required to hold Thales shares (Article L. 225-25, paragraph 3 of the French Commercial Code).

Born on 19 December 1958, Frédérique Saint is a French citizen and holds a degree in Engineering from the École Centrale de Paris. In 1984, she began working for Aérospatiale Cannes, which became Alcatel in 1998, and in 2007, she joined Thales Alenia Space.

Frédérique Saint has worked in various areas in the satellite business, including attitude control and mission analysis for telecommunications customers in Europe and abroad.

Since 2006, she has been a technical expert for the “In-orbit operations” (*Opérations en orbite*) division.

No appointments or positions held in other companies.

**To the knowledge of Thales:**

- there are no family ties between members of the Board of Directors;
- no Board member has been convicted of fraud in the last five years;
- no Board member has been involved in the last five years as a senior executive in a bankruptcy, receivership or liquidation, or has been charged and/or officially disciplined by statutory or regulatory authorities;
- no Board member has been barred in the last five years by a court from acting as a member of a body dedicated to the administration, management or supervision of an issuer, or from being involved in the management or running of such a company's affairs;
- no conflict of interest exists between the Board members' private interests and their duties to Thales.

**3.1.2 Other persons attending board meetings (without voting rights)**

In addition to the secretary of the Board of Directors and members of corporate management who may be invited by the chairman to attend Board meetings, depending on the agenda, the following persons are invited to attend all Board meetings in an advisory capacity:

**Representative of the French state's golden share**

**Bertrand Le Meur**, 52, General Armaments Engineer.

Appointed by decree of the Minister of the Economy, Manufacturing Recovery and Digital Technology on 3 July 2014.

Representing the French State on the Thales Board of Directors in accordance with decree No. 97-190 of 4 March 1997 concerning the French State's golden share (see page 182) and pursuant to Article 10 of the Company's Articles of Association.

**Government commissioner**

**Paul Fouilland**, 62, General Army Inspector on special assignment (*Contrôleur Général des Armées en mission extraordinaire*).

Appointed Government commissioner to Thales and its subsidiaries by decision of the Minister of Defence of 15 September 2014, under the

statutory and regulatory provisions concerning defence contractors and companies engaged in the manufacture and sale of defence equipment.

**Representative of the central works council**

**Marielle Marichy**, 54, Union Steward.

Appointed by the central works council as its representative on the Board of Directors of Thales, pursuant to Article L. 2323-65 of the French Labour Code (*Code du travail*).

**The statutory auditors**

Are invited to attend, at a minimum, the Board meetings relating to the audit or approval of the financial statements, as provided for by law. They may also be invited by the Chairman to attend other Board meetings when their presence could be of particular value to the discussion. The following were invited to Board meetings during the 2017 financial year:

- **Ernst & Young Audit**, represented by Philippe Diu, partner;
- **Mazars**, represented by Jean-Marc Deslandes, partner.

## 3.2 REPORT OF THE BOARD OF DIRECTORS TO THE GENERAL MEETING OF 23 MAY 2018 ON CORPORATE GOVERNANCE

Based on the recommendation of the Governance and Remuneration Committee, the Board of Directors approved, at its meeting on 5 March 2018, this report on corporate governance, drawn up in accordance with the provisions of Article L. 225-37 of the French Commercial Code, and asked the Chairman to present it to the Annual General Meeting of 23 May 2018.

In accordance with French law, in 2008 the Company decided to refer voluntarily, when preparing the Chairman's report, to the Corporate Governance Code for Listed Companies published by the AFEP and MEDEF, which was amended most recently in November 2016.

### 3.2.1 Governance

In accordance with French law, in 2008 the Company decided to refer voluntarily, when preparing the Chairman's report, to the Corporate Governance Code for Listed Companies published by the AFEP and MEDEF,

which was amended most recently in November 2016 and can be viewed on the AFEP website at <http://www.afep.com/publications/code-afep-medef> or at the Company's registered office.

#### "Comply or explain" rule

(information covered by Article L. 225-37-4 8° of the French Commercial Code)

The Company complies with the recommendations contained in the AFEP-MEDEF code as amended in November 2016, except for those concerning:

Heading	AFEP-MEDEF	Thales at 5 March 2018	Explanation
<b>A. Independent directors (ratios):</b>			
• Board of Directors	1/3 (controlled companies)	31%	The terms of the shareholders' agreement do not allow compliance with the ratios of the AFEP-MEDEF code.
• Audit and Accounts Committee	2/3	1/3	
• Governance and Remuneration Committee	> 50%	1/3	
<b>B. Succession plan for the Company representative (Chairman and CEO of Thales)</b>	A Board Committee draws up a succession plan for the Chairman and CEO	No	Under the terms of the above-mentioned agreement, the appointment of the Chairman and CEO is decided by both shareholders.

#### 3.2.1.1 Composition and procedures for the organization and operation of the Board of Directors

(information covered by Article L. 225-37-4 5° of the French Commercial Code)

##### Restatement of the rules of the shareholders' agreement and composition of the Board of Directors

The Company is a *société anonyme* (French public limited company) with a Board of Directors. Under the terms of the shareholders' agreement between the Public Sector and the Industrial Partner (Dassault Aviation), as published by the French financial markets authority (*Autorité des marchés financiers* – AMF), the Board of Directors is composed of 16 directors, 14 of whom are appointed by the General Meeting and 2 of whom are appointed by the trade unions, in accordance with the law (Article L. 225-27 *et seq.* of the French Commercial Code) and the Articles of Association (Article 10).

Of the 14 directors appointed by the General Meeting, 4 are "external directors" selected jointly by the Public Sector and Dassault Aviation, 1 is the representative of employee shareholders, and the others are recommended to the General Meeting by the Public Sector (5) and by Dassault Aviation (4).

The shareholders' agreement also requires the Chairman and CEO to be chosen based on the joint proposal of the Public Sector and Dassault Aviation (or the Chairman of the Board and the Chief Executive Officer if the separation of these roles has been jointly agreed by the two shareholders) and at least one director representing each of the parties to sit on each of the Board Committees.

Directors at 31 December 2017	1st appointment	Positions currently held		Committees*			Attendance 2017			
		Starts	Ends	S&C	A&A	G&R	Number of sessions taken into account and attendance percentage <sup>(e)</sup>			
							Committees			
Boarc										
Appointed by the Annual General Meeting (14)										
Recommended by the Public Sector (5)										
Patrice Caine, Chairman and CEO <sup>(a)</sup>	12/23/2014	12/23/2014	2018 OGM	<div></div>	<div></div>	<div></div>	9	100%	3	100%
Laurence Broseta (proposed by the State – Article 6 of Order No. 2014-948)	05/14/2014	5/17/2017	2021 OGM	<div></div>	<div></div>	<div></div>	9	78%	N/A	N/A
Bernard Fontana <sup>(b)</sup>	1/30/2018	1/30/2018	2021 OGM	<div></div>	<div></div>	<div></div>	N/A	N/A	N/A	N/A
Odile Renaud-Basso (representative of the French State appointed by decree – Article 4 of Order No. 2014-948) <sup>(c)</sup>	7/19/2017	7/19/2017	2021 OGM	<div></div>	<div></div>	<div></div>	4	50%	2	100%
Seat vacant <sup>(d)</sup>	11/29/2016	n/a	2021 OGM	<div></div>	<div></div>	<div></div>	N/A	N/A	N/A	N/A
Recommended by the Industrial Partner (Dassault Aviation) (4)										
Charles Edelstenne <sup>(a)</sup>	5/19/2009	5/14/2014	2018 OGM	<div></div>	<div></div>	<div></div>	9	100%	3	100%
Loïc Segalen <sup>(a)</sup>	5/19/2009	5/15/2012	2018 OGM	<div></div>	<div></div>	<div></div>	9	89%	6	100%
Éric Trappier <sup>(a)</sup>	5/19/2009	5/15/2012	2018 OGM	<div></div>	<div></div>	<div></div>	9	89%	6	100%
Marie-Françoise Walbaum <sup>(a)</sup>	9/17/2013	5/14/2014	2018 OGM	<div></div>	<div></div>	<div></div>	9	100%	n/a	n/a
Representative of employee shareholders (1)										
Philippe Lépinay	4/01/2017	5/17/2017	2021 OGM	<div></div>	<div></div>	<div></div>	9	100%	3	100%
External directors (4)										
Yannick d'Escatha	5/19/2009	5/18/2016	2020 OGM	<div></div>	<div></div>	<div></div>	9	100%	6	100%
Armelle de Madre	6/28/2017	6/28/2017	2019 OGM	<div></div>	<div></div>	<div></div>	5	80%	N/A	N/A
Anne-Claire Taittinger <sup>(a)</sup>	5/15/2012	5/15/2012	2018 OGM	<div></div>	<div></div>	<div></div>	9	100%	6	100%
Ann Taylor <sup>(a)</sup>	5/15/2012	5/15/2012	2018 OGM	<div></div>	<div></div>	<div></div>	9	78%	N/A	N/A
Appointed by the trade unions (2)										
Anne-Marie Hunot-Schmit	12/09/2016	12/09/2016	8/12/2020	<div></div>	<div></div>	<div></div>	9	89%	3	100%
Frédérique Saint	12/09/2016	12/09/2016	8/12/2020	<div></div>	<div></div>	<div></div>	9	100%	12	100%

(a) Director whose mandate reaches maturity on the date of the General Meeting of 23 May 2018 and whose renewal will be proposed at this meeting.

(b) Seat vacant on 31 December 2017 and filled on 30 January 2018 by Mr Bernard Fontana, co-opted on the proposal of the State, in application of Article 6 of Order No. 2014-948 of 20 August 2014 relating to governance and transactions on the capital of publicly owned companies.

(c) Ms Odile Renaud-Basso, who resigned as a director on 29 January 2018, was confirmed as representative of the French State, which was co-opted in her place on 30 January 2018, on the proposal made in application of Article 4 of Order No. 2014-948.

(d) Seat vacant on 31 December 2017 and not yet filled on 5 March 2018.

(e) Attendance is calculated compared to the total number of sessions where the director was in office.

\* **Committee:** Strategic and CSR (S&R), Audit and Accounts (A&A) and Governance & Remuneration (G&R).

**Status:** ■ Member, ■ Chair.

The other positions held by the members of the Board of Directors and their biographical information can be found in Section 3.1. As recommended by the AMF, this section identifies any positions held in Group companies and in other listed companies, in France and abroad.

The term of office of directors was reduced from six to four years by the General Meeting of 24 May 2013, effective from the 2014 General Meeting.

At the end of 2017, the average age of the directors was 60.4. At said date, in the absence of a specific provision in the Articles of Association, the age of the directors was governed by common law:

- the number of directors over the age of 70 may not exceed one-third of the directors in office, in accordance with Article L. 225-19 paragraph 2 of the French Commercial Code;
- the age limit for the Chairman is 65, in accordance with Article L. 225-48 of the French Commercial Code.

### Governance procedures: non-separation (information covered by Article L. 225-37-4 4° of the French Commercial Code)

The Company is a *société anonyme* (French public limited company) with a Board of Directors and there is no separation of the positions of Chairman of the Board of Directors and Chief Executive Officer.

On 13 May 2015 during the confirmation of Mr Patrice Caine's appointment as Chairman and CEO, the Board of Directors ruled that the absence of separation does not affect the active and efficient exercise of its monitoring and supervisory functions, considering that the responsibilities of the Board of Directors, the role of each of its Committees, and the limits applying to the powers of the Chairman and CEO are clearly established (see the extract from Section II of the Board's rules of procedure and Section 3.2.1.5 below).

The Chairman and CEO's compensation is reviewed by a Committee and later by the Board of Directors in the absence of the concerned party.

During Board visits to Group sites, and in particular during the Board of Directors' annual review of its strategic plan, directors may organize meetings without any senior executives in attendance, including the Chairman and CEO, Thales's sole Company representative.

### Increasing the number of women on the Board of Directors

The objectives set by French law No. 2011-103 of 27 January 2011 on gender balance on corporate boards of directors and the monitoring of professional equality (both men and women must represent a minimum of 40% of the directors appointed at the General Meeting, excluding employee representative directors) were achieved on 29 November 2016 (6 women out of 14 directors, or 43%).

On 31 December 2017, the percentage of women on the Board of Thales (excluding employee representatives) reached 50% (6 out of 12 directors), and 57% when taking account of employee representative directors.

### Independence of directors

According to the rules of procedure, the Board of Directors, based on the report of the Governance and Remuneration Committee, conducted its annual review on 5 March 2018 of the situation of its members with reference to the definition of and criteria for independent directors, as specified by the amended AFEP-MEDEF code.

The Board of Directors has decided to retain the strict approach adopted in previous years: directors appointed by the General Meeting on the recommendation of either a "Public Sector" or "Industrial Partner" shareholder, or a category of shareholders (employees), or directors appointed by the trade unions, cannot be considered independent within the meaning of the amended AFEP-MEDEF code. As part of this approach, only directors who qualify as "external directors" under the terms of the shareholders' agreement may be qualified as independent directors (i.e. no more than 4 out of 16).

The Governance and Remuneration Committee carefully examined the responses it received to a detailed questionnaire (covering all the independence criteria defined by the amended AFEP-MEDEF code) that it updated and sent out to each "external director" in early January 2018.

Among these, only Ms Armelle de Madre, as Director of Human Resources of Arkadin, performs a professional activity in a group that has business relationships with Thales (see page 143 of biography). Arkadin and the NTT Group companies to which she belongs provide the Thales group with miscellaneous telephony, event organization and network integration services.

The Committee noted that the total sum of revenues made by Arkadin and NTT Group companies with Thales was very significantly below the threshold of 1% of the revenues of Thales, on the one hand, and of Arkadin and of relevant NTT Group companies on the other hand; the threshold of 1% was set by the Board as a threshold of materiality in assessing whether the business relationship was significant or not.

Given the responses to the other sections of the questionnaire, the Committee concluded that, on this basis, nothing indicated that Ms Armelle de Madre's judgment would be compromised while carrying out her duties as a director of Thales and that nothing may keep her from being qualified as an independent director by the Board.

The three other "external directors" stated that they have no business relationship with either the Company or the Group. In the Committee's opinion, the questionnaires did not contain any responses that call into question these individuals' qualification as independent directors.

In conclusion, on the recommendation of the Governance and Remuneration Committee, the Board of Directors decided to qualify Ms Armelle de Madre, Ms Anne-Claire Taittinger, Ms Ann Taylor and Mr Yannick d'Escaatha as independent directors.

As of 5 March 2018, the closing date of the 2017 financial statements, the Board of Directors had four independent directors, or 31% of its members based on a full Board with no vacancies (excluding directors representing employees and employee shareholders, as stipulated by the amended AFEP-MEDEF code). The proportion is, however, slightly less than the one-third recommended for controlled companies.

### Rules of procedure for the Board of Directors and its Committees

The Board's rules of procedure, adopted in July 2004 and amended most recently by the Board on 27 February 2017, do not supersede the provisions of the law or of the Company's Articles of Association applicable to the Board and its Committees, or the provisions of the Code of Ethics or the Code on Insider Trading, certain provisions of which apply to directors, since together these rules represent a code of professional conduct for directors (see "Prevention of insider trading" below).

In addition to the specific provisions of the shareholders' agreement, the Board's rules of procedure include best practices in respect of corporate governance, particularly those contained in the aforementioned AFEP-MEDEF code. The Governance and Remuneration Committee is in charge of periodic updates and of sending the Board the revisions that it deems necessary.

The Board's rules of procedure are divided into five sections:

#### I) Members of the Board of Directors (Board membership, independence, availability, primary duty, transparency, confidentiality and compensation)

The rules of procedure stipulate that:

- the members of the Board of Directors must inform the Chairman of all management or administrative positions that they hold;
- each Company representative must obtain the opinion of the Board before accepting a new corporate office in a listed company;

- directors must inform the Board of any conflicts of interest, even potential, and should, in such cases, refrain from voting on the corresponding matter.

Directors must also inform the Chairman of any proposed agreement involving them directly or indirectly which may, pursuant to the French Commercial Code, need to receive the prior authorisation of the Board of Directors.

In addition, the directors have individually issued a statement regarding the following points:

- no Board member has any family ties with another member of the Board of Directors or any members of corporate management;
- no Board member has been convicted of fraud in the last five years;
- no Board member has been involved in the last five years as a senior executive in a bankruptcy, receivership or liquidation, or has been charged and/or officially disciplined by statutory or regulatory authorities;
- no Board member has been barred in the last five years by a court from acting as a member of a body dedicated to the administration, management or supervision of an issuer, or from being involved in the management or running of such a company's affairs;
- no conflict of interest exists between the private interests of each of the Board members and their duties with regard to Thales.

## **II) Powers of the Board of Directors (representation and corporate interests, specific powers and shareholders' agreement)**

The annual budget, the strategic plan, the appointment and dismissal of the Chairman and CEO (or the appointment of a Chairman and a Chief Executive Officer in the event of separation or potential separation of these positions), acquisitions or disposals of shareholdings or assets with a value exceeding €150 million (as total commitments or as revenues), as well as strategic alliance agreements and agreements on technological and industrial cooperation, are automatically submitted to the Board for approval, it being understood that the shareholders' agreement stipulates that such decisions must also be approved by the majority of directors representing the Industrial Partner (Dassault Aviation).

Any transactions exceeding €50 million are also submitted to the Board for approval if they involve a change in the Group's strategy as previously approved by the Board.

## **III) Board information (communication and training)**

In particular, it is expected that:

- Board documents shall be sent to participants in a timely manner;
- the French State representative responsible for the golden share, the Government Commissioner and the representative of the Central Works Council shall receive all documents sent to directors and are invited to attend Board meetings;
- new directors shall receive, upon their appointment, the appropriate documents for their office and shall attend a briefing on the Company, its organisational structure and its business, given by the Group's senior executives. Thereafter, each director may request additional training.

## **IV) Board Committees (formation and responsibilities, organization, information, Audit and Accounts Committee, Governance and Remuneration Committee, Strategic and Corporate Social Responsibility Committee)**

It is stipulated that, in addition to the responsibilities of each Committee (see relevant sections below), each Committee is entitled to ask corporate management for any additional information that it deems necessary for the performance of its duties, and may, in exceptional cases, ask the Board of Directors to hire external consultants.

## **V) Functioning of the Board of Directors (meetings, attendance and representation, annual assessment and updating the rules of procedure)**

This topic is covered in the minutes of the Board of Directors' activities, as required by law, in Section 3.2.1.2 below.

## **Prevention of insider trading**

In order to take into account any applicable regulations and the recommendations contained in the AMF guide, Thales has implemented a system of "blackout periods" (no-trading periods): in addition to the periods relating to the annual and half-yearly financial statements (at least 30 calendar days, in each case), two periods of at least 15 days each have been introduced for quarterly reporting (first and third quarters). In each case, the period includes the day following the publication of the financial press release.

The financial calendar for the following six months is published on the Company's website after the third quarter financial press release (including the date of the General Meeting). The calendar is updated for the whole year when the previous year's annual results are published.

The directors have been informed by the Company of their obligation to refrain from carrying out any transactions on Thales shares and related financial instruments during the blackout periods relating to the annual and half-yearly financial statements as well as the quarterly financial information, as defined by the Company, and when they have any insider information (within the meaning of the applicable regulations).

The directors have also been informed of any disclosure requirements with regard to the AMF and the Company concerning the transactions mentioned in Article L. 621-18-2 of the French Monetary and Financial Code (*Code monétaire et financier*), and of their obligation to provide the Company with a list of people they are closely connected to and inform said people of their own obligations.

Directors may, if they wish, consult the Company Secretary or the Group General Counsel prior to dealing in any shares. However, this prior consultation is not compulsory.

## **Obligation to hold a minimum number of shares**

In application of Article 10.3 of the Articles of Association, each director must hold at least 500 shares, unless legally exempt. The Chairman and CEO is also subject to an obligation to retain shares that they hold as part of their long-term compensation (see Section 3.2.2.2 B).

## **Summary of the transactions mentioned in Article L. 621-18-2 of the French Monetary and Financial Code carried out in 2017**

The summary statement (provided for in Article 223-26 of the AMF General Regulations) of the transactions mentioned in Article L. 621-18-2 of the French Monetary and Financial Code carried out in 2017 by persons required to file a disclosure can be found in Section 4.2.3.7.

### 3.2.1.2 Minutes of the Board of Directors' activities during 2017

#### Number of meetings and attendance rate

The Board of Directors met nine times in 2017, including four times away from head office. The average attendance rate for directors was 86%. The individual attendance rates are specified above in Section 3.2.1.1.

The statutory auditors are invited to meetings relating to the audit of the annual and half-year financial statements. In addition, they may be invited to other Board meetings when a report on the work carried out by the Audit and Accounts Committee is presented and when their attendance may be of particular value to the discussion.

#### Key topics covered

In addition to recurring items within the remit of the Board of Directors (annual budget and update of forecasts, strategic plan, preparation of annual consolidated and corporate financial statements, review of the consolidated half-year financial statements, calculation of the Chairman and CEO's compensation and indication of the quantitative and qualitative criteria for his variable compensation, dividend and interim dividend proposal, approval of Annual Meeting documents and notice of the General Meeting, announcement of blackout periods for trading in the Company's shares, prior approval if applicable for related-party commitments or agreements, various delegations of powers to the Chairman and CEO and reporting on the use of such powers, annual review of the independence of the directors, etc.), the agendas of these meetings included the following items in 2017, in some cases with reports from the relevant Board Committee:

- the monitoring of strategic decisions and sensitive issues;
- the review of various M&A projects, including the planned takeover bid for Gemalto;
- the revision of the Board's rules of procedure;
- the introduction of an annual long-term incentive (LTI) plan with performance conditions and that includes Group employees;
- the annual assessment of the Board's performance;
- the Human Resources function.

### 3.2.1.3 Preparatory work for board meetings

#### Information for directors

##### Board documents

Each year, a provisional timetable for meetings is drafted halfway through the year for the following year.

The Board's rules of procedure have set the period for the notice of meeting and provision of documents at five working days, unless this is impossible or there is an emergency – in which case three days is considered a desirable minimum.

Each notice includes the agenda and meeting documents (or at least the main points, if the documents cannot be completed at the time of dispatch) and the draft minutes of the previous meeting, usually sent out initially within one month of each meeting. In some cases, additional material is sent to directors after the notice of meeting, or may even be handed out during the meeting, if the matter is urgent.

The directors are also sent a press review and a selection of financial analyses relating to the Company. National press releases are sent to them directly by e-mail.

Since 2015, the prior sending of documents by email, which can be accessed on dedicated secure tablets, has enabled the timeframe for provision to be optimised; the documents are then sent out in paper form to directors based on their request.

#### Additional training

In accordance with the Board's rules of procedure, directors may ask to receive additional training.

#### Organization and operation of Board Committees

The Board of Directors has three Committees: an Audit and Accounts Committee, a Governance and Remuneration Committee and a Strategic and Corporate Social Responsibility Committee.

##### Audit and Accounts Committee

At 31 December 2017, the powers and duties of this Committee, which are reproduced in the Board's rules of procedure (Article 16), reflect, on the whole, the framework set out in the order of 8 December 2008 implementing Directive 2006/43/EC and are also compliant with EU Regulation No. 537/2014 of 16 April 2014:

"The Audit and Accounts Committee acts under the responsibility of the Board of Directors. Without prejudice to the powers of the Board of Directors, it is specifically responsible for the following tasks:

- a) it monitors the process of drawing up the financial information and, where applicable, formulates recommendations to guarantee its integrity;
- b) it monitors the effectiveness of internal control and risk management systems, as well as the internal audit where applicable, with regard to procedures relating to the preparation and processing of the accounting and financial information;
- c) it supervises the selection procedure for the statutory auditors and issues a recommendation to the Board of Directors on the statutory auditors proposed for appointment by the General Meeting, including the renewal of their mandate;
- d) it monitors fulfilment by the statutory auditors of their mission, taking account of the findings and conclusions of the Haut Conseil du Commissariat aux Comptes (Audit Office Control Board) following audits performed;
- e) it ensures compliance by the statutory auditors with the terms and conditions of independence prescribed by current regulations;
- f) it approves, within the framework authorized by the Board of Directors, the provision by the statutory auditors or members of their respective networks, services other than the certification of the financial statements of the Company and the companies that it controls directly and indirectly. It reviews and validates related procedures and ensures their compliance.

It consults the statutory auditors on the following:

- a) their general program of work as well as the various sample tests they have performed;
- b) changes that they believe should be made to the financial statements to be published or to other accounting documents, making any relevant comments on the assessment methods used in their preparation;
- c) any irregularities and inaccuracies they may have discovered;
- d) conclusions resulting from the aforementioned comments and adjustments to the profits for the period compared to those of the previous period;
- e) risks to their independence and the safeguards applied to mitigate these risks;
- f) significant internal control weaknesses they may have identified, as regards procedures relating to the preparation and processing of accounting and financial information.

It receives from them each year:

- a) a statement of independence;
- b) an update of the information provided for their appointment, detailing the services provided by members of the network to which the statutory auditors belong, as well as services other than the certification of the financial statements that they have provided;
- c) the additional report under Article 11 of EU Regulation No. 537/2014.

Each year it examines the budget for professional fees for the statutory auditors. It reviews and analyses the professional fees paid to the statutory auditors for the preceding financial year.

The Committee relies in particular, for performing its duties, on the work of the Finance department and the Internal Audit department. It approves the annual programme of the Internal Audit department and examines the activity reports.

It reports regularly to the Board of Directors on its work and the results of its mission to certify the financial statements, the way in which this mission contributed to the integrity of the financial information and the role that it played in this process. It informs the Board of Directors immediately of any problems encountered."

In addition, since 2010, with reference to the final AMF audit committee report of 22 July 2010, Committee members have been able to have a discussion with the statutory auditors at the end of each meeting without any meeting secretary or Thales representatives being present.

On 31 December 2017, the members of the Committee were:

- Anne-Claire Taittinger, Chairman and independent director;
- Frédérique Saint, director representing employees;
- Loïk Segalen.

Mr Bernard Fontana joined this Committee from 30 January 2018.

The composition of the Audit and Accounts Committee is consistent with the provisions of the French Commercial Code: the Committee members are all directors and one director, the Chair of the Committee, in addition to being qualified as an independent director, has the requisite financial, accounting and statutory audit expertise (see biography of Ms Anne-Claire Taittinger on page 144).

Nevertheless, independent directors make up only one-third of the Committee's membership and not two-thirds, as recommended by the AFEP-MEDEF code (the director representing employees, Ms Frédérique Saint, is not included in this calculation). As previously mentioned, this is due to the terms of the shareholders' agreement, which stipulates that one representative of each of the two shareholders in the agreement must sit on each Committee. With regard to the Audit and Accounts Committee, this comprised Ms Delphine Gény-Stephann until 24 November 2017, who was replaced by Mr Bernard Fontana, appointed on 30 January 2018 on the recommendation of the Public Sector, and Mr Loïk Segalen, appointed on the recommendation of Dassault Aviation.

The Committee met six times in 2017, with an attendance rate of 100%.

The statutory auditors, invited to all Committee meetings, are involved in all discussions, except when there is a conflict of interest (e.g. during a review of the appointment of statutory auditors or renewal of their terms of office). Twice a year, they submit their report on the audit of the accounts (annual and half year), and specify the accounting options used and the highlights of their audit of the financial statements.

The Senior Executive Vice President, Finance and Information Systems, the Company Secretary and the director of Audit, Risks & Internal Control are invited to all meetings, as is the Group director of Financial Control and, periodically and depending on the agenda, other representatives of the Finance department and the Group General Counsel.

In addition to the annual and half-year financial statements, in 2017 the Committee also reviewed:

- the execution of difficult contracts and their accounting implications;
- the follow-up of the main disputes;
- the external audit plan and statutory auditors' fees;
- the organisation of internal control, updates to the risk mapping and assessment of the implementation of the annual audit plan;
- the audit plan for 2018;
- the independence of a statutory auditor in view of the rotation of their account signatory partners;
- the implementation of IFRS 15, a new revenue recognition standard applicable in 2018; and

- the section of the Chairman's report for 2016 covering internal control and risk management.

During meetings more specifically devoted to audit and internal control, the Committee reviewed the reports of the Audit, Risks & Internal Control Department. It laid out its recommendations for the follow-up on assignments.

At the meeting devoted to the financial statements, the Committee acknowledged the memorandum on the Group's risk exposure and major off-balance sheet commitments, in accordance with AFEP-MEDEF recommendations. This memorandum, which was circulated to all directors, is included in the section of the 2016 Registration Document on "Risk factors" (see Section 1.1.2 of the management report).

The Committee was also involved in the preparation of financial press releases relating to the results and to the implementation of the IFRS 15 standard.

Following the meetings – which, in the case of the closing or examination of the financial statements, are held at least two (and wherever possible three) days prior to the Board meeting – a written report is produced and submitted to all directors at the next Board meeting. Pursuant to the AMF recommendation in its audit working group report on audit committees of 22 July 2010, this report is systematically included or attached to the minutes of the next Board meeting after being approved by the Committee. In addition, the Committee proceedings are recorded in the minutes, which may be more detailed.

### **Governance and Remuneration Committee**

In compliance with Section 17 of the Board's rules of procedure, the Governance and Remuneration Committee has the task of examining:

- the compensation policy for the Company's senior executives;
- the compensation of the Chairman and CEO and any related-party commitment concerning him, the compensation of the directors (attendance fees) and, if applicable, that of other Company representatives;
- the proposed long-term incentive (LTI) plans, which are submitted to the Board;
- the proposed employee share ownership schemes;
- candidates for external directors, regarding whom the two major shareholders held consultations in accordance with the provisions of the aforementioned shareholders' agreement;
- at least once a year, the independence of the directors;
- and in general, any issues relating to the application of the AFEP-MEDEF Corporate Governance Code for Listed Companies.

The Committee is also responsible for preparing the Board's assessment of its own performance (see Section 3.2.1.4 below) and reporting on it to the Board in order to facilitate discussion.

On 31 December 2017, the members of the Committee were:

- Yannick d'Escatha, Chairman and independent director;
- Frédérique Saint, director representing employees;
- Éric Trappier;
- Odile Renaud-Basso.

It met six times in 2017, with an attendance rate of 100%.

The ratio of independent directors recommended by the AFEP-MEDEF code (at least half) is not met, because it currently stands at one-third (the director representing employees, Ms Frédérique Saint, is not included in this calculation pursuant to the AFEP-MEDEF code). As previously mentioned, this is due to the terms of the shareholders' agreement, which stipulates that one representative of each of the two shareholders in the agreement must sit on each Committee. Ms Odile Renaud-Basso was appointed to the Governance and Remuneration Committee on the recommendation of the Public Sector and Mr Éric Trappier was appointed on the recommendation of Dassault Aviation.

The Senior Executive Vice President, Human Resources, and the Company Secretary were invited to all Committee meetings, and the Chairman and CEO was invited to some of the meetings, depending on the agenda or in cases where his presence could be of particular value to the discussion.

The items reviewed by the Committee in 2017 included:

- the Group's long-term incentive (LTI) policy and the preparation of a free share plan with performance conditions according to the level of responsibility of the beneficiaries;
- the examination of the compensation package for the Chairman and CEO and in particular the qualitative criteria applicable for his variable compensation;
- the revision of the Board's rules of procedure;
- the independence of the directors;
- the terms for the annual assessment of the performance of the Board of Directors, the choice of external consultant pertaining to it and the related report presented to the Board;
- as well as this section of the Chairman's report on corporate governance.

For all of these items, the Committee presented its recommendations to the Board: each meeting was systematically recorded in minutes issued to all directors at the following Board meeting. In addition, the Committee proceedings are recorded in the minutes, which may be more detailed.

#### The Strategic and Corporate Social Responsibility Committee

In compliance with the Board's rules of procedure, the Strategic and Corporate Social Responsibility Committee's main tasks are to assess the Group's strategy in its key business segments, and in particular:

- to examine the Group's strategic approach in each of its major fields of operation, before these are submitted to the Board of Directors;
- to analyse the framework for submission of the budget and the three-year rolling plan to the Board, and to examine the proposed annual budget in the context of this plan;
- to analyse major acquisitions and asset disposal plans (in excess of €150 million), as well as proposed strategic agreements or partnerships.

The Board of Directors, at its meeting on 27 February 2017, decided to add corporate social responsibility to these duties, pursuant to the AFEP-MEDEF code as amended in November 2016 (see Section 3, "The Board of Directors and Strategy"). As a result of these new duties, the Committee is henceforth known as the "Strategic and Corporate Social Responsibility Committee".

On 31 December 2017, the members of the Committee were:

- Patrice Caine, Chairman;
- Charles Edelstenne;
- Anne-Marie Hunot-Schmit, director representing employees;
- Philippe Lépinay, director representing employee shareholders;
- Odile Renaud-Basso.

For this type of Committee, no conditions are set for the independence of directors, either by law or by the AFEP-MEDEF code.

The Committee met three times in 2017, with a 100% attendance rate, mainly to examine the 2017 budget, to follow up on strategic decisions and to review various proposed M&A transactions.

In 2017, the Senior Executive Vice President of Finance and Information Systems, the Company Secretary, the Senior Executive Vice President of Operations & Performance and the Executive Vice President of Strategy were invited to meetings by the Chair of the Committee. Minutes of each meeting were presented at the following Board meeting by the Chairman and CEO, as Chair of the Committee, either verbally or accompanied by a report.

The meetings of the Strategic and Corporate Social Responsibility Committee are the subject of minutes.

### 3.2.1.4 Assessment of the Board's performance

Since 2011, the Company has conducted a formal self-assessment, based on the personal interviews of directors with the Company Secretary preceded, until 2015, by a detailed questionnaire and, in 2016, without a preliminary questionnaire but using an interview guide prepared by the Company Secretary with the Chair of the Governance and Remuneration Committee.

In 2017, the Board decided to conduct an external assessment, given, on one hand, the length of time since the last external assessment (six years) and, on the other hand, the opportunity to combine this exercise with the end of the three-year term of office of the Chairman and CEO in anticipation of its renewal at the end of the 2018 General Meeting. The results of this assessment were reported to the Governance and Remuneration Committee and then to the Board of Directors on 22 and 30 January 2018 respectively.

The directors were unanimous in acknowledging that the Board and its Committees are working well and a majority of them consider that its operation has improved even further since they have been Board members. The directors particularly commended the quality of the Board documents and presentations, as well as its discussions in plenary sessions and the quality of its annual strategic seminar.

Concerning the composition of the Board, the directors issued a positive assessment: the expertise and experience of its members are varied, complementary and cover the majority of the business sectors in which the Group is present (aviation, defence, space, transport, etc.) as well as finance, industry, human resources and digital; its composition is balanced in terms of gender; the proportion between directors with the greatest length of service on the Board and those appointed more recently is deemed appropriate. The Board wanted the balance of its composition to be analysed at each renewal to encourage diversity of profiles and skills.

In addition, the external assessment revealed that the individual contributions of directors to the work of the Board of Directors and its Committees are satisfactory.

The assessment also helped to identify certain areas in which the Board can make further improvements. In particular, it was suggested that the Board might discuss topics of strategic thinking more frequently, in addition to at the annual strategic seminar and in the work of the Strategic and CSR Committee. Lastly, some areas of improvement were proposed to make the organization and operation of the Board and its Committees smoother, in particular with a better balance between written and oral presentations and the provision at board meetings of more insights into the work of the Committees.

### 3.2.1.5 Restrictions to the Chief Executive Officer's powers (information covered by Article L. 225-37-4 7° of the French Commercial Code)

Since 23 December 2014, Mr Patrice Caine has served as Chairman and CEO, with the confirmation of the principle of non-separation on 13 May 2015, with no limitation of powers other than those stipulated in the applicable legislation, with respect to the specific powers of the Board of Directors or the Annual General Meeting.

As stipulated in Section 3.2.1.1 above, the policy is for automatic submission for Board approval of any acquisitions or disposals exceeding €150 million, as are any non-strategic transactions that exceed €50 million. This practice effectively limits the powers of the Chief Executive Officer.

### 3.2.1.6 Other information

#### Notice of Annual General Meetings and conditions for attendance (information covered by Article L. 225-37-4 9° of the French Commercial Code)

All shareholders, regardless of the number of shares they own, are entitled to take part in Annual General Meetings. They are sent a notice of meeting and business is transacted according to the law. The date and place of the meeting, the agenda and the draft resolutions of the meeting are published in the French Legal Gazette (Bulletin des annonces légales obligatoires, BALO) at least 35 days prior to the date of the meeting, with the final notice of meeting being sent no later than 15 days prior to the meeting. The Board of Directors ensures, in the interests of all shareholders, that the period of notice for meetings is much longer than the minimum requirements.

At least 21 days prior to the meeting, all documentation required by current regulations is provided on the Company's website ([www.thalesgroup.com](http://www.thalesgroup.com)). It is available for shareholders at the registered office within the statutory deadline.

The date of the General Meeting is published on the Company's website approximately six months in advance.

At the General Meeting of 23 May 2018 and subsequently, shareholders are able to vote electronically.

Participation in Annual General Meetings, in any form whatsoever, is conditional upon registration of the shares in accordance with the conditions and within the time limits provided for under the current regulations.

Any shareholder who has already voted by post or by proxy, or requested an admittance card or share ownership certificate, may sell all or some of their shares at any time.

However, in accordance with the regulations in force since 1 January 2015, should the intermediary account-holder notify the Company of a disposal occurring before midnight (Paris time) on the second trading day prior to the Annual General Meeting, the Company will invalidate or modify the vote, proxy, admittance card or share ownership certificate, as the case may be.

No sale or other operation carried out after midnight (Paris time) on the second trading day prior to the meeting, irrespective of the means used, is notified by the approved intermediary or taken into consideration by the Company, notwithstanding any agreement to the contrary.

The right to vote, and consequently the right to attend Annual General Meetings, belongs to the beneficial owner at Ordinary General Meetings, and to the bare legal owner at Extraordinary General Meetings. Owners of pledged shares retain their voting rights. Co-owners of shares are represented at Annual General Meetings by one of the co-owners or by a joint proxy who, in the event of disagreement, is appointed by the court at the request of the co-owner who acts first.

Each person present at the Annual General Meeting has one vote for each share owned or represented, without limitation, subject to the following provisions on the right to a double vote, and to the exceptions provided by law.

Shareholders who can prove that their shares have been registered in their name in the Company's share register (kept by Société Générale, duly authorized for this purpose – see Section 4.3.1 below), for at least two years without interruption, are entitled to double voting rights at Annual General Meetings for each share so held. Registered shares that have been granted to a shareholder as free shares in respect of shares they already hold with double voting rights attached are also entitled to double voting rights as soon as the shares have been granted.

Double voting rights automatically end for any share that is converted to bearer form or is transferred (except in the case of inheritance, either intestate or by will, spousal community property, *inter vivos* gifts to a spouse or relative who may inherit, or in the case of a transfer as a result of a merger or demerger of a shareholding company).

Double voting rights may be cancelled by a decision of an Extraordinary General Meeting, following approval by a special Annual General Meeting of Shareholders entitled to double voting rights.

Under the Articles of Association, there is no limit on voting rights.

In accordance with the law, shares owned by the Company itself do not carry voting rights.

#### Key factors likely to have an impact in the event of a takeover bid (information covered by Article L. 225-37-5 of the French Commercial Code)

The structure of share ownership and the distribution of voting rights mean that Thales is unlikely to be affected by any public offer. Furthermore:

1. the two main shareholders (Dassault Aviation and TSA) have declared that they are acting in concert under a shareholders' agreement, the key terms of which are described on page 148, which stipulates in particular that the Chairman and CEO is chosen based on a joint proposal by the parties;
2. in the absence of termination on expiry of the contract on 31 December 2016, the agreement was tacitly renewed for a period of five years, expiring on 31 December 2021. It may be tacitly renewed for five-year periods;
3. any crossing of the threshold of one-tenth or a multiple of one-tenth of the share capital or voting rights of the Company must first be approved by the Minister for the Economy; in addition, under the conditions set by Decree No. 93-1296 of 13 December 1993, the Minister responsible for the Economy may oppose decisions on the sale or the allocation as collateral for assets referred to in the appendix of Decree No. 97-190 of 4 March 1997 (see Section 4.2.3.3.5).

## General Meeting authorizations valid at 31 December 2017 for increases in capital (information covered by Article L. 225-37-4 3° of the French Commercial Code)

Table prepared pursuant to Article L. 225-37-4 9° of the French Commercial Code summarizing the use of authorizations (valid at 31 December 2017) granted by the Annual General Meeting for increases in capital.

Annual General Meeting of 18/05/2016	Used by the Board of Directors	Observations
<b>Issue of securities giving access to equity capital:</b> <ul style="list-style-type: none"> <li>with pre-emptive subscription rights (fourteenth resolution): 60 million shares and €3 billion in debt securities;</li> <li>without pre-emptive subscription rights (fifteenth resolution): 20 million shares and €2 billion in debt securities;</li> <li>without pre-emptive subscription rights by private placement (sixteenth resolution): 20 million shares and €2 billion in debt securities;</li> <li>possibility of over-allotment ("Green shoe") (seventeenth resolution): maximum of 15% of issues carried out attributable to each resolution/transaction above.</li> </ul> <p>26 months, i.e. until 17 July 2018 See overall ceilings in observations column</p>	No utilisation	Overall ceiling (nineteenth resolution) for transactions coming under resolutions 15, 16 and 17: 20 million shares and €2 billion in debt securities (nineteenth resolution)
<b>Issue of new shares as consideration for contributions of the securities of third-party companies up to a maximum of 21 million securities,</b> i.e., 10% of share capital (eighteenth resolution) <p>26 months, i.e. until 17 July 2018 See overall ceilings in observations column</p>	No utilisation	Overall ceiling of resolutions 14, 15, 16, 17 and 18: 60 million shares and €3 billion in debt securities (nineteenth resolution)
<b>Issue of new shares reserved for employees who are members of a Group savings scheme</b> (twentieth resolution – as a legal consequence of resolutions on capital increase in cash above) <p>Ceiling: 2 million shares Maximum discount: 20% for a five-year employee savings plan and 30% for a ten-year holding period Term: 26 months, i.e. until 17 July 2018</p>	No utilisation	Note: Employee shareholding operations are now conducted using existing shares, which have previously been bought back by the Company under a share repurchase programme.

## Agreements concluded by the subsidiaries with related parties (information covered by Article L. 225-37-4 2° of the French Commercial Code)

During financial year 2017, no agreement was reached, directly or through an intermediary, between, on the one hand, one of the Company representatives or one of the shareholders holding a fraction of the voting rights greater than 10% of the Company's share capital and, on the other hand, another company of which Thales holds directly or indirectly more than half the share capital, with the exception of current agreements concluded under normal conditions.

## 3.2.2 Compensation of Company representatives

### 3.2.2.1 Compensation of the Chairman and CEO and other Company representatives for financial year 2017

The annual fixed and variable compensation for 2017 for Mr Patrice Caine was established in accordance with the compensation policy for the Chairman and CEO of Thales approved by the General Meeting of 17 May 2017 (7th resolution). It comprises:

- fixed compensation of €700,000 (gross amount);
- a target annual variable compensation of €700,000 in the event of achieving objectives that is capped, in the event of exceeding these objectives, at a maximum of €962,500 (137.5% of the target).

The criteria for determining the variable compensation are set at an overall level of 75% financial and 25% non-financial. In order to reward over-performance of the financial criteria, the amount of the payment relative to these criteria may exceed the target up to 150%. This is not the case for the non-financial portion which is capped at 100%. Consequently, annual variable compensation is capped at 137.5% of the target.

#### (i) Financial criteria

For the financial part, the criteria were EBIT (35%), order intake (20%), and free operating cash flow (20%). The table below sets out the achievement level against these three financial criteria.

➤ **FINANCIAL CRITERIA FOR 2017 ANNUAL VARIABLE COMPENSATION**

Criteria	Weighting	Threshold	Payment as % of target
EBIT	35%	If results ≤ 90% of budgeted objective	0%
		If results = 100% of budgeted objective	35.00%
		If results ≥ 120% of budgeted objective	52.50%
		Variations between 0% and target, and between target and maximum calculated on a straight-line basis	
Order intake	20%	If results ≤ 90% of budgeted objective	0%
		If results = 100% of budgeted objective	20.00%
		If results ≥ 120% of budgeted objective	30.00%
		Variations between 0% and target, and between target and maximum, calculated on a straight-line basis	
Free operating cash flow	20%	If results ≤ budgeted objective – 2% of budgeted revenues	0%
		If results = 100% of budgeted objective	20.00%
		If results ≥ budgeted objective + 2% of budgeted revenues	30.00%
		Variations between 0% and target, and between target and maximum, calculated on a straight-line basis	
TOTAL FINANCIAL CRITERIA		75%	

The definition and calculation of these criteria are set out in Section 1.1.1.2 of the 2017 Registration Document.

Meeting on 5 March 2018, the Board of Directors examined the results obtained for the financial criteria.

Regarding the Group's EBIT, the budgeted objective was particularly ambitious since it corresponded to a further year of strong growth of this index and to the achievement of a level of EBIT margin never reached in the Group's history. The Board observed that, in spite of negative currency and scope effects, the Group's EBIT had reached €1,543 million in 2017, €53 million above the middle of the objective range communicated to the market (€1,480 million to €1,500 million).

This performance, above the budgeted objective, triggered payment on this criterion.

The Board also observed that the Group had recorded an order intake of €14,920 million, also above the budgeted objective and the objective of €14 billion communicated to the market.

Lastly, it noted a significant over-performance on the free operating cash flow criterion, the Group achieving a record free cash flow level over the year of €1,365 million, corresponding to a conversion rate of adjusted net income into free operating cash flow of 139%. As this level of achievement exceeded the scale maximum, the compensation for this criterion was capped.

For confidentiality reasons, the achievement of each financial criterion is only represented graphically in the table below.

Criteria	Achieved	Weighting	Level reached		
			Minimum	Target	Maximum
EBIT (in €m)	1,543	35%		■	
Orders (in €m)	14,920	20%		■	
Operational free cash flow (in €m)	1,365	20%			■
<b>Financial portion of variable annual compensation</b> (as % of the target)					<b>120.9%</b>

(ii) **Non-financial criteria**

In accordance with the aforementioned compensation policy of the Chairman and CEO of Thales, he was assessed in 2017 on the achievement of the following four non-financial criteria:

- **Global development strategy:** implementation of initiatives to pursue the Group's global development strategy, focused on selected major countries;
- **Leadership:** deployment of empowerment and accountability initiatives, deployment of processes for selecting leaders, development of training programmes to prepare the next generation of Thales leaders;
- **Gender diversity:** roll-out of gender diversity initiatives with a target for women to represent 40% of new hires over the 2017-2018 period;
- **Digital:** deployment of a digital platform, significant strengthening of talents in four key digital technologies (connectivity, big data, artificial intelligence and cybersecurity) and development through targeted acquisitions, as necessary.

Each of these objectives represents one-fourth of the 25% of the weighting attributed to non-financial criteria.

Meeting on 5 March 2018, the Board of Directors reviewed and discussed the achievements of the Chairman and CEO for each of the four non-financial criteria (Globalization, Leadership, Diversity and inclusion and Digital). It decided to maintain the 2017 achievement level, i.e. 97.5% of the target. Through this decision, the Board wanted both to highlight the many initiatives and specific achievements obtained against the four criteria concerned under the leadership of Mr Patrice Caine, as well as the progress recorded by the Group, both qualitative and quantitative.

Following this review and the recommendation by the Governance and Remuneration Committee, the Board of Directors decided that the variable compensation to be paid in 2018 to Mr Patrice Caine for financial year 2017 should be increased to €805,522, which represents 115% of the target annual variable compensation. It is noted that the payment of this variable compensation is subject to the approval of the General Meeting of 23 May 2018 (15th resolution), in application of Article L. 225-100-II of the French Commercial Code.

On 28 September 2017, the Board of Directors also granted Mr Patrice Caine long-term compensation in the form of a maximum of 5,000 performance units indexed to the Thales share price, in accordance with the Company representative compensation policy approved by the General Meeting of 18 May 2017 (7th resolution). Acquisition of this compensation depends in particular on performance conditions calculated over three financial years and on an attendance

condition over four years. This long-term compensation is detailed in Table 6 below.

The components of the compensation of the Chairman and CEO, subject to the vote of the General Meeting of 23 May 2018 in application of Article L. 225-100-II of the French Commercial Code (15th resolution), are detailed in the summary table below.

#### ➤ SUMMARY TABLE OF THE COMPONENTS OF COMPENSATION OF MR PATRICE CAINE, CHAIRMAN AND CEO, FOR 2017

Components of compensation	Policy approved by the General Meeting of 17 May 2017	Paid for financial year 2017	Allocated for financial year 2017 (as amount or accounting valuation)
Annual fixed compensation	The policy provides for a fixed annual compensation of €700,000.	€700,000	
Annual variable compensation	<p>The policy provides for a target annual variable compensation of €700,000.</p> <p>The criteria set are as follows:</p> <ul style="list-style-type: none"> <li>financial criteria at 75% (see description above). The targets are set by the Board of Directors during the budgetary process but are not made public for reasons of confidentiality;</li> <li>non-financial criteria make up the remaining 25% of variable compensation (see description above).</li> </ul> <p>In the event of over-performance of the financial objectives, the variable compensation may reach a maximum of €962,000, i.e. 137.5% of fixed annual compensation.</p>		€805,522 <sup>(a)</sup>
Total annual compensation		€1,505,522	
Multiyear variable compensation	None	—	—
Long-term compensation	<p>The number of units ultimately vested will depend on the level of achievement, calculated over three years, of the following performance conditions:</p> <ul style="list-style-type: none"> <li>40% based on a growth objective measured in terms of average order intake over the 2017-2019 period;</li> <li>40% based on a competitiveness objective measured in terms of cumulative free operating cash flow over the 2017-2019 period; and</li> <li>20% based on Thales's stock market performance and measured by Total Shareholder Return (TSR) (dividend reinvested).</li> </ul> <p>The objectives, thresholds and payment percentages according to the target appear in Table 6 on page 162.</p> <p>Acquisition is also subject to an attendance condition over four years (i.e. until 27 February 2021), except in the event of death or disability. Half of the payment is made in kind with Thales shares and half is made in cash.</p> <p>The detailed conditions of this long-term compensation appear in Section 3.5.1.2 B c) of the 2016 Registration Document.</p>	—	€449,400 <sup>(b)</sup>
Exceptional compensation	None	—	—
Non-competition clause	None	—	—
Compensation linked to taking up appointment	None	—	—

(a) The payment of variable annual compensation for 2017 to Mr Caine is conditional upon the approval of the Annual General Meeting of 23 May 2018 (resolution 15).

(b) Total determined by multiplying the maximum number of units granted (5,000) by the Thales share price at 31 December 2017.

Components of compensation	Policy approved by the General Meeting of 17 May 2017	Paid for financial year 2017	Allocated for financial year 2017 (as amount or accounting valuation)
Deferred incremental and conditional compensation <sup>(a)</sup>	<p>The Thales Company representative is entitled to deferred incremental and conditional compensation, the amount of which is determined on the basis of an identical allocation method to the Group supplementary pension scheme in operation within Thales at the date of the Board meeting for Group executives whose compensation exceeds the contributions ceiling set by Agirc, the French executive pension fund. Entitlement to the rights acquired by the Company representative, calculated in points as for the Agirc mechanism, is not subject to the employment condition in the Company at the time of payment of the retirement benefits. This deferred compensation is only deemed to have been acquired on condition that the Company representative has carried out a full term in office. Their entitlement is subject to performance conditions over the last three years.</p> <p>It is increased (doubling the annuity) if the Company representative accumulates a minimum of 10 years' service on the Executive Committee of Thales.</p> <p>This related-party commitment was approved by the General Meeting of 13 May 2015 (resolution 16). For more details, see paragraph "Deferred incremental and conditional compensation", page 163.</p>	—	€14,554 of potential annual deferred compensation acquired for 2017, i.e. 2.08% of the fixed salary.
Severance pay <sup>(a)</sup>	<p>Subject to fulfilment of the same performance conditions as for deferred incremental and conditional compensation, compensation could be paid to Mr Patrice Caine if his term of office as Company representative were terminated, except in the case of resignation, serious misconduct or gross negligence.</p> <p>The amount of compensation is fixed at 12 months of his reference salary (fixed and variable compensation paid over the last 12 months of activity, excluding long-term compensation).</p> <p>This related-party commitment was approved by the General Meeting of 13 May 2015 (resolution 14). For more information, please see the paragraph "Benefits and rights upon the termination of office of the Company representative", page 163.</p>	—	—
Private unemployment insurance <sup>(c)</sup>	<p>Mr Patrice Caine is entitled to private unemployment insurance subject to fulfilment of the same performance conditions as those envisaged for severance pay.</p> <p>This related-party commitment was approved by the General Meeting of 13 May 2015 (resolution 15). For more information, please see the paragraph "Benefits and rights upon the termination of office of the Company representative", page 163.</p>	—	2017 employer's contribution: €12,356
Attendance fees	By decision of the Board of Directors on 27/02/2017, Mr Patrice Caine does not receive attendance fees, which are retained by the Company.	—	—
Benefits of any kind	<p>Mr Patrice Caine is entitled to:</p> <ul style="list-style-type: none"> <li>the services of a chauffeur-driven car for his business travel;</li> <li>external legal and tax assistance.</li> </ul> <p>In addition, he is entitled to the private healthcare scheme for French employees, an annual check-up like other Thales senior executives and directors' liability insurance, including criminal liability<sup>(b)</sup>.</p>	€3,987 €34,545	

(a) Related-party commitment (Articles L. 225-42-1 and R. 225-34-1 of the French Commercial Code).

(b) The cost of healthcare and annual check-up benefits to the Company for financial year 2017 amounted to €3,868. Liability insurance is a collective insurance, the cost of which cannot be individualized.

## Components of 2017 compensation for other company representatives

### Attendance fees

The total amount of attendance fees to be divided among directors and non-voting members for services to the Board, including compensation payable to directors who are Committee members in respect of their participation in these Committees is set at €600,000 per year, an amount that has remained unchanged since 2008. The Board decided that directors would receive:

- for services to the Board, fixed compensation of €14,000 per year (prorated in the event of appointment or resignation during the year), subject to the maximum ceiling on variable compensation, and variable compensation based on attendance at meetings amounting to €2,500 per meeting;
- for services to the Committees, compensation (entirely variable), based on attendance fees of €1,250 per meeting, with the chairman of each Committee receiving an additional €2,000 per year (prorated based on the number of meetings chaired, if applicable).

If, on account of the high number of meetings (variable compensation being paid first), the total amount of €600,000 per financial year (gross amount before any deductions) is likely to be exceeded, the fixed

component of directors' compensation will be duly reduced in order to remain within the annual budget approved by the shareholders. For 2017, the fixed component was thus reduced from €14,000 to €13,490 for the full year.

Non-voting members receive €2,500 per Board meeting, i.e., the same variable compensation as directors, but excluding any fixed compensation. There have been no non-voting members on Thales's Board of Directors since 18 May 2009.

For 2017, attendance fees totalled €599,885 (gross amount before any deduction at source and levy) (€595,732 for 2016). This includes attendance fees not received by the Chairman and CEO and retained by the Company. The payment of these attendance fees was made in full in February 2018. Out of the total of €558,145 actually paid, the variable part formed the majority, as recommended by the French AFEP-MEDEF code, amounting to €364,000 (approximately 65% of the total received).

For information purposes, the gross amount (before any deduction at source or levy) paid during financial year 2017 (after any retention by the Company) and representing the balance of attendance fees due for financial year 2016, amounted to €305,132.

The tables from the appendices of the AFEP-MEDEF code relating to executive compensation (Table 2 – Company representative and Table 3 – Directors) give details of names (see page 161).

## ► COMPLIANCE WITH THE RECOMMENDATIONS OF THE AFEP-MEDEF CODE

Recommendations of the AFEP-MEDEF code	Thales provisions for Mr Patrice Caine, Company representative since 23 December 2014
<b>Severance pay</b>	
Only in the event of forced departure	Yes
Performance conditions over two years	Performance conditions over the last three financial years
Maximum amount: two years' compensation (fixed and variable)	12 months of his reference salary (fixed and variable compensation paid over the last 12 months of activity, excluding long-term compensation).
<b>Supplementary pension</b>	
Not applicable <sup>(a)</sup>	

(a) The deferred incremental and conditional compensation of Thales' Company representative is an arrangement that is modelled on pension schemes, but which is not governed by Article L. 137.11 of the French Social Security code or Article 24.2.6 of the AFEP-MEDEF Corporate Governance Code. This benefit is not subject to the condition of the recipient serving out the rest of his/her career with the Company. Under this arrangement Thales awards, under conditions relating to seniority in office and performance, deferred compensation paid as an annuity when the beneficiary claims their mandatory pension. The calculation procedures for this deferred compensation, and the corresponding amounts, comply with the principles relating to the compensation of directors as defined by Article 24-1 of the AFEP-MEDEF Corporate Governance Code.

## ► TABLE 1: COMPENSATION, OPTIONS AND SHARES GRANTED TO THE COMPANY REPRESENTATIVE

(in € thousand)	2017	2016
<b>Patrice Caine, Chairman and CEO since 23 December 2014</b>		
Compensation due for the year (detailed in Table 2)	1,505.5	1,090.2
Value of stock options granted during the financial year	–	–
Value of performance shares granted during the financial year	–	–
Value of performance units granted during the financial year	449	–
<b>TOTAL</b>	<b>1,954.5</b>	<b>1,090.2</b>

➤ **TABLE 2: COMPENSATION OF THE COMPANY REPRESENTATIVE**

(in € thousand)	2017		2016	
	Due for the financial year	Paid during the financial year	Due for the financial year	Paid during the financial year
<b>Patrice Caine, Chairman and CEO</b>				
Fixed compensation	700.0	700.0	450.0	449.2
Variable compensation <sup>(a)</sup>	805.5	599.9	599.9	518.3
Exceptional compensation	—	—	—	—
Attendance fees <sup>(b)</sup>	—	—	—	2.7
Benefits in kind <sup>(c)</sup>	38.5	38.5	40.3	40.3
<b>Total Patrice Caine</b>	<b>1,543.5</b>	<b>1,338.4</b>	<b>1,090.2</b>	<b>1,007.8</b>

(a) See Section 3.2.2.1 on the review of variable compensation for 2017.

(b) Does not receive any fees that would be granted due to his participation in meetings of the Board of Directors and the Strategic & CSR Committee. These are retained by the Company (decision of the Board of Directors on 27 February 2017). The amount of fees calculated and not paid to Mr Patrice Caine in 2017 following this decision is €24,350.

(c) The Company representative is entitled to the services of a chauffeur-driven car, and independent tax and legal advice.

➤ **TABLE 3: ATTENDANCE FEES AND OTHER COMPENSATION RECEIVED BY NON-EXECUTIVE DIRECTORS IN 2017 AND 2016 (GROSS AMOUNTS BEFORE ANY DEDUCTION AT SOURCE OR OTHER LEVY)**

Beneficiary (gross amount in euros)	Paid in 2017 <sup>(a)</sup>	Paid in 2016	Notes
Th. Aulagnon (up to 23 August 2016 incl.)	10,101	32,242	(b)
L. Brosseta	17,350	30,750	
Y. d'Escatha	25,600	42,750	
G. Dyevre	17,350	24,362	
Ch. Edelstenne	22,350	42,000	
D. Gény-Stephann (from 29 November 2016 incl.)	888		(b)
Ph. Lépinay	22,350	42,000	
H. Proglia (up to 12 May 2015 incl.)		3,888	
L. Segalen	22,350	42,000	
A.-C. Taittinger	24,350	44,000	
A. Taylor	19,850	33,250	
E. Trappier	23,600	38,250	
M.-F. Walbaum	17,350	33,250	
Inter CFDT (D. Floch up to 8 December 2016 incl. + M. Saunier up to 12 October 2016 incl.)	39,455	85,250	(b)
Inter CFE-CGC (A.-M. Hunot-Schmit from 09 December 2016 incl.)	619		(b)
FGMM-CFDT (F. Sainct from 9 December 2016 incl.)	619		(b)
Treasury Accountant – Art. 139 NRE (L. Collet-Billon + M. Vial)	40,950	88,051	
<b>TOTAL GROSS AMOUNT OF ATTENDANCE FEES PAID</b>	<b>305,132</b>	<b>582,043</b>	(c)
Company representative	—	—	(d)

(a) From a decision of the Board of Directors on 27 February 2017, attendance fees are paid annually. The payments made in 2017 correspond to the sum of the fixed portion of attendance fees due for financial year 2016 and the variable portion of attendance fees due for the second half of 2016 only.

(b) These amounts are determined proportionate to time spent for the appropriate period.

(c) Above are gross amounts paid in 2016 and 2017. The gross amount of attendance fees due for these two years (including attendance fees not received by the Company representative and retained by the Company) are €599,885 and €595,732 respectively, less than the annual budget of €600,000 authorized by the General Meeting.

(d) By decision of the Board, Mr Patrice Caine has not received attendance fees since February 2015. These fees are retained by the Company. The amount of fees calculated and not paid to Mr Patrice Caine as a result of this decision was €44,000 for financial year 2016 and €24,350 for financial year 2017. This is noted in Table 2 (summary of compensation paid to the Company representative).

➤ **TABLE 4: SUBSCRIPTION OR PURCHASE OPTIONS AWARDED DURING THE FINANCIAL YEAR TO THE COMPANY REPRESENTATIVE BY THE ISSUER OR BY ANY OTHER GROUP COMPANY**

None. The Company has not awarded subscription or purchase options since 2012.

➤ **TABLE 5: SUBSCRIPTION OR PURCHASE OPTIONS EXERCISED DURING THE FINANCIAL YEAR BY THE COMPANY REPRESENTATIVE**

None.

➤ **TABLE 6: PERFORMANCE SHARES AWARDED DURING THE FINANCIAL YEAR TO THE COMPANY REPRESENTATIVE**

During financial year 2017, no performance shares were awarded to Mr Patrice Caine. In the context of the 2017 compensation policy approved by the General Meeting of 18 May 2017 in its seventh resolution, he was awarded a long-term incentive plan in the form of performance units, the main conditions of which are shown below.

Director's name	Date of plan	Maximum number of performance units	Vesting conditions
Patrice Caine	27/02/2017 and 28/09/2017	5,000	Shares vested after a four-year vesting period from 27 February 2017 and subject to performance conditions

➤ **LONG-TERM INCENTIVE PLAN CRITERIA AND WEIGHTINGS (2017 LTIP)**

2017 LTIP criteria	Weighting	Objectives	Threshold	Payment as % of target
Cumulative free operating cash flow 2017-2019	40% (2,000 units)	Floor: €2.4 billion	If results < floor	0%
			If results = floor (=33% of maximum)	13.20%
		Ceiling: €3.35 billion	If results ≥ ceiling for the period	40.00%
			Variations between floor and ceiling calculated on a straight-line basis	
Average order intake for 2017-2019	40% (2,000 units)	Floor: €15 billion	If results < floor	0%
			If results = floor (=50% of maximum)	20.00%
		Ceiling: €17 billion	If results ≥ ceiling for the period	40.00%
			Variations between floor and ceiling calculated on a straight-line basis	
Total Shareholder Return compared to a panel of European companies <sup>(a)</sup> Measure based on performance at 31/12/2019 compared to 31/12/2016	10 % (500 units)	Floor: median of the panel	If TSR < median of the panel	0%
			If TSR = median of the panel (=50% of maximum)	5.00%
		Ceiling: highest quintile of the panel	If TSR is in the highest quintile of the panel	10.00%
			Variations between median and entry point of highest quintile calculated on a straight-line basis	
Total Shareholder Return compared to the Euro Stoxx index. Measure based on performance at 31/12/2019 compared to 31/12/2016	10% (500 units)	Floor: median of the Euro Stoxx index	If TSR < median of the index	0%
			If TSR = median of the index (=50% of maximum)	5.00%
		Ceiling: highest quintile of the index	If TSR is in the highest quintile of the index	10.00%
			Variations between median and entry point of highest quintile calculated on a straight-line basis	

(a) The panel includes: Airbus, BAE Systems, Dassault Aviation, Leonardo, Gemalto, Rolls-Royce, Safran et Zodiac Aerospace.

➤ **TABLE 7: PERFORMANCE SHARES THAT HAVE BECOME AVAILABLE DURING THE FINANCIAL YEAR FOR THE COMPANY REPRESENTATIVE**

As indicated in Tables 1 and 6, Mr Caine's compensation as Company representative does not include performance shares. All performance shares that have become available during the financial year were awarded to him under his previous salaried positions and prior to his appointment as Company representative.

Director's name	Date of plan	Number of shares that have become available during the year	Vesting conditions
Patrice Caine	15/09/2013	4,891	Shares vested after a four-year vesting period and subject to a performance condition

➤ **TABLE 8: PAST AWARDS OF SUBSCRIPTION OR PURCHASE OPTIONS TO THE COMPANY REPRESENTATIVE**

None. Mr Caine has not received any subscription or purchase options during his term in office. He has retained those that had been awarded to him with respect to his previous salaried positions.

➤ **TABLE 9: SUBSCRIPTION OR PURCHASE OPTIONS GRANTED TO THE TOP TEN EMPLOYEES WHO ARE NOT COMPANY REPRESENTATIVES, AND OPTIONS EXERCISED BY THE TEN EMPLOYEES WITH THE HIGHEST NUMBER OF OPTIONS PURCHASED OR SUBSCRIBED DURING 2017**

	Total number of options	Weighted average price
Options granted during the year by the issuer and any company within the scope of the grant of options, to the ten employees of the issuer and any company within that scope, having the highest number of options thus granted	Nil	Nil
Options held on the issuer and the companies referred to above and exercised during the financial year by the ten employees of the issuer and of these companies, having the highest number of options thus purchased or subscribed	57,236	€34.96

The Company has not awarded subscription or purchase options since 2012.

➤ **TABLE 10: MULTI-ANNUAL VARIABLE COMPENSATION PAID TO THE COMPANY REPRESENTATIVE**

None.

➤ **TABLE 11**

Company representative	Employment contract		Supplementary pension scheme		Indemnifications or benefits due or likely to become due as a result of termination or change of position		Indemnifications relating to a non-competition clause	
	Yes	No	Yes	No	Yes	No	Yes	No
Patrice Caine		x		x <sup>(a)</sup>	x <sup>(b)</sup>			x

(a) See Note (a) to the table "Compliance with the recommendations of the AFEP-MEDEF code", page 160.

(b) Decisions taken in 2015.

**Deferred incremental and conditional compensation of Mr Patrice Caine, company representative**

Following the decision of the Board of Directors on 25 February 2015, the Thales Company representative is entitled to deferred incremental compensation, the amount of which is determined using the same points method as for the Group supplementary pension scheme in operation at the date of the Board meeting for Group executives whose compensation exceeds the contributions ceiling set by Agirc, the French executive pension fund.

This arrangement is based on defined benefit plans but is not governed by Article L. 137.11 of the French Social Security Code as its benefit is not subject to the recipient serving out the rest of their career with the Company:

- the acquisition of rights is progressive and is based on capped compensation received during each year. The system draws upon the Agirc retirement plan and its points calculation. Acquisition relates to the tranche of salary not affected by compulsory schemes, namely salaries higher than 8 annual Social Security caps (*Plafonds Annuels de Sécurité Sociale – PASS*) (> €317,856 in 2018);
- the calculation is made each year on the compensation declared to URSSAF and using the annual values of Social Security caps and the official Agirc reference salary. The acquisition base is equal to 20% of the portion of salary paid between 8 PASS and 32 PASS maximum (i.e. between €317,856 and €1,271,424 in 2018), which has the effect of limiting annual acquisition to a maximum of approximately €14,500;
- this base is then divided by the Agirc reference salary for the year (acquisition price of one point) to obtain a number of notional points acquired for the year. The potential compensation to be paid is equal to the total number of points acquired multiplied by the value of the Agirc point on the date of setting up the annuity.

Entitlement to the rights acquired by the Company representative is not subject to the employment condition in the Company at the time of payment of the retirement benefits. On the other hand, this deferred

compensation is only deemed to have been acquired on condition that the Company representative has carried out a full term in office and has drawn their retirement benefits. Their entitlement is also subject to achieving a performance criterion over the last three full financial years: the average rate of achievement of annual EBIT objectives set by the Board for the Company representative must be higher than or equal to 80%.

This mechanism (annuities and social costs of the employer) is provisioned and financed by the Company.

This deferred compensation is increased (doubling the annuity) if the Company representative accumulates a minimum of 10 years' service on the Executive Committee of Thales.

In 2017, Mr Patrice Caine potentially acquired annual deferred compensation of €14,554.

At 31/12/2017, the theoretical annual annuity, accumulated since the beginning of the term of office, stood at €30,240 (i.e. 4.32% of the annual fixed salary).

**Benefits and rights upon the termination of office of Patrice Caine, company representative**

**Severance pay**

Following the decision by the Board and in accordance with the conditions laid down by the AFEP-MEDEF code, with which the Company has declared that it complies, compensation may be paid to Mr Patrice Caine if his term of office as Company representative should be terminated, except in the case of resignation, serious misconduct or gross negligence.

The amount of this severance pay is fixed at 12 months of his reference salary (fixed and variable compensation paid over the last 12 months of activity, excluding the long-term incentive plan). The Chairman and CEO resigned when he took up office and no longer has an employment contract with the Company.

The payment of this compensation is subject to achieving a performance criterion over the last three full financial years: the average

rate of achievement of annual EBIT objectives set by the Board for the Company representative must be higher than or equal to 80%.

### Private unemployment insurance

A decision was also made to take out private unemployment insurance based on the same performance criteria as for severance pay. This provides for one year's compensation for an amount limited to the sum of the amounts corresponding to 70% of the A and B (Social Security) tranches of net taxable income and 50% of the C tranche of this same income. At 31 December 2017, this private unemployment insurance would have represented private annual compensation equal to approximately €199,000, i.e. 28% of the Chairman and CEO's fixed compensation.

In accordance with current law, the related-party commitments (deferred incremental and conditional compensation, severance pay and private unemployment insurance) on behalf of Mr Patrice Caine were published on the Company's website five days after the Board of Directors' meeting on 25 February 2015 at which these decisions were made. They were put to the vote at the General Meeting on 13 May 2015 following a special report by the statutory auditors.

## 3.2.2.2 Compensation of the Chairman and CEO for 2018

### A. Compensation policy for the Chairman and CEO: general framework

The General Meeting of 18 May 2017 approved a compensation structure for the Chairman and CEO with the following components:

- annual fixed compensation;
- annual variable compensation whose target level is equal to the fixed compensation, based on a combination of financial and non-financial criteria, with financial criteria being of overriding importance;
- long-term incentives (Long-term Incentive Plan – LTIP) linked to the value of the Thales share, in the form of performance shares or units;
- severance pay<sup>(1)</sup>;
- private unemployment insurance<sup>(1)</sup>;
- deferred incremental and conditional compensation<sup>(1)</sup>;
- legal and tax advice;
- private healthcare benefits identical to those offered to senior executives;
- directors and officers liability insurance;
- reimbursement of business expenses in accordance with Thales' rules and guidelines;
- an annual medical check-up like other Thales senior executives;
- the services of a chauffeur-driven car.

The Company complies with the AFEP-MEDEF Corporate Governance Code (Section 24.1), whereby:

- the Company representative's compensation should be competitive, tailored to the corporate strategy and environment and must be intended to boost the Company's long-term performance and competitiveness. It must be designed to retain and motivate an effective Company representative;
- when determining the compensation, the following principles must be considered: comprehensiveness, balance between different components of compensation, consistency with the compensation of other company executives and employees, understandability of the rules (simple, stable and transparent) and balance in terms of the corporate interest, market practices, the performance of the Company representative and the views of other stakeholders.

The compensation of Executive Committee members and most of the Group's senior executives is made up of a fixed component, an annual

variable component and a long-term incentive plan (LTIP). The respective proportion of each component is determined based on the level of responsibility of each position and on benchmark compensation studies conducted in various national markets where Thales has employees.

For the Company representative, these components are weighed up and determined in the following manner:

- the fixed component is determined based on the level of responsibility and on benchmark compensation studies of comparable profiles;
- annual target variable compensation is equal to the fixed compensation; in the event that maximum objectives are achieved, it is capped at 137.5% of fixed compensation;
- the value of the target long-term incentive plan at the grant date may not exceed 100% of the fixed compensation.

Long-term incentive is based on the achievement of demanding performance criteria measured at the end of a three-year period. It vests in a single instalment at the end of a four-year period. Most of the long-term incentive is subject to internal performance criteria linked to strategic objectives laid down by the Board that take into account the objectives communicated to financial markets (if these exist).

The Company representative must hold the Thales shares delivered to them at each LTIP maturity date, at 50% of the net after-tax gain from these LTIPs until they have accumulated the equivalent of one year's fixed compensation in shares. They must keep these shares for their entire term of office as Company representative.

The Company representative is also entitled to a deferred incremental and conditional compensation mechanism detailed in Section 3.2.2.1.

Lastly, the severance payment shall only be paid to the Company representative in the event of forced departure, contingent upon the achievement of performance targets over three financial years. They are capped at 12 months of reference salary (fixed and variable compensation paid over the last 12 months of activity, excluding LTIP), which is less than the amount recommended under the AFEP-MEDEF code.

Pursuant to the AFEP-MEDEF code (Section 24.1.2), the rules for determining the Company representative's compensation should be stable and the performance criteria used should be, to the greatest extent possible, long lasting. As regards fixed compensation, in principle this should only be reviewed at relatively long intervals (Section 24.3.1 of the AFEP-MEDEF code).

For 2018, the Board wishes, in compliance with the principles of the French AFEP-MEDEF code, to renew the compensation policy for the Chairman and CEO approved by the General Meeting on 18 May 2017.

If the planned takeover bid for Gemalto is successful, the Board will examine the opportunity of reviewing the compensation policy of the Chairman and CEO, especially taking into account the change in the Group's size.

### B. Implementation of compensation policy for the Chairman and CEO in 2018

In accordance with the provisions of Article L. 225-37-2 of the French Commercial Code, the Board of Directors must submit the principles and criteria for determining, breaking down and allocating the fixed, variable and exceptional items that make up the total compensation and benefits in kind granted to the chairman, the Chief Executive Officers and Deputy Chief Executive officers, for the approval of the Annual General Meeting at least once a year.

This section sets out the draft resolution for 2018 (No 19) concerning the compensation payable to the Chairman and CEO, the Company's only Company representative.

<sup>(1)</sup> Related-party agreements, subject to performance conditions. the renewal of these commitments will be subject to the approval of the general meeting of 23 May 2018.

If this resolution is adopted by the Annual General Meeting of 23 May 2018:

- the principles and criteria set out in this section will be applicable beginning in 2018, subject to any possible amendment at a subsequent Annual General Meeting deliberating on the same subject, in accordance with the aforementioned provisions of Article L. 225-37-2;
- the components of total compensation and benefits in kind paid or granted to the Chairman and CEO for 2018 in accordance with these principles and criteria will be put to the vote at the Annual General Meeting called to approve the financial statements for 2019, in accordance with Articles L. 225-37-2 and L. 225-100-II of the French Commercial Code which stipulate *inter alia* that payment of variable and exceptional items are subject to the approval of the Annual General Meeting.

At its meeting on 5 March 2018, the Board of Directors, on the recommendation of the Governance & Remuneration Committee, decided to keep the structure and level of compensation payable to the Chairman and CEO for 2018 unchanged.

#### a) Structure of overall compensation for 2018

The Board of Directors has decided to:

- keep the annual fixed compensation at €700,000;
- keep the annual target variable compensation at 100% of annual fixed compensation, capped at 137.5% of the target, i.e. €962,500 if targets are exceeded;
- keep the amount of the Long-Term Incentive Plan (LTIP), which will comprise a maximum of 5,000 performance units, each tied to the value of the Thales share at the closing price on 4 March 2022. The exact amount of this compensation will depend on the achievement of performance and attendance conditions, as well as

on the value of the Thales share on the vesting date of the performance units. Based on the value of the Thales share at end-2017, this compensation would correspond to a maximum of approximately €449,400, or 64% of fixed compensation for 2018, if the maximum objectives are reached.

In accordance with Articles L. 225-37-2 and R. 225-29-1 of the French Commercial Code, the Chairman and CEO's annual variable compensation in respect of 2018 will only be paid further to approval by the Annual General Meeting to be held in 2019.

#### b) Criteria for setting variable compensation for 2018

As in previous years, the criteria for determining the variable compensation are set at an overall level of 75% financial and 25% non-financial. In order to reward over-performance of the financial criteria, the amount of the payment relative to these criteria may exceed the target up to 150%. This is not the case for the non-financial portion which is capped at 100%. Consequently, annual variable compensation is capped at 137.5% of the target.

##### (i) Financial criteria for 2018

The Board of Directors has decided to keep financial criteria and weightings identical to those prevailing in the calculation of the 2017 variable compensation, namely:

- 35% based on EBIT;
- 20% based on order intake;
- 20% based on free operating cash flow.

For each criterion, annual variable compensation will only be paid if a demanding threshold is reached. For the first two criteria (EBIT and order intake), no amount is due when the actual figure reported is less than or equal to 90% of the target. For free operating cash flow, no amount is due when the actual figure reported is below the budgeted objective by more than 2% of targeted budgeted revenue.

Triggering ranges for each of the financial criteria are detailed below:

Financial criteria for annual variable compensation	Weighting	Threshold	Payment as % of target
EBIT	35%	If results ≤ 90% of budgeted objective	0%
		If results = 100% of budgeted objective	35.00%
		If results ≥ 110% of budgeted objective	52.50%
Order intake	20%	If results ≤ 90% of budgeted objective	0%
		If results = 100% of budgeted objective	20.00%
		If results ≥ 110% of budgeted objective	30.00%
Free operating cash flow	20%	If results ≤ budgeted objective – 2% of budgeted revenues	0%
		If results = 100% of budgeted objective	20.00%
		If results ≥ budgeted objective + 2% of budgeted revenues	30.00%
<b>TOTAL FINANCIAL CRITERIA</b>	<b>75%</b>		

The definition and calculation of these criteria are set out in Section 1.1.1.2.

The Board may adjust the objectives in the event that the takeover bid for Gemalto is successful and Gemalto is consolidated before the end of the year. The Board will report on this at the 2019 Annual General Meeting.

For reasons of confidentiality, the exact objectives underlying these financial criteria, determined by the Board and tied to the approved annual budget, cannot be disclosed. The level of achievement for each financial criterion will be detailed *a posteriori* in the 2018 Registration Document.

##### (ii) Non-financial criteria for 2018

For 2018, the Board has decided to retain four non-financial objectives, each representing a quarter of the 25% allocated to the non-financial portion:

- Five-years strategic priorities:** definition of profitable growth objectives for the coming years and organization of the next "Capital Markets Day";
- Globalization:** Implementation of new initiatives to pursue the Group's global development strategy, focused on selected major countries;
- Corporate Social Responsibility:** Continued deployment of actions relating to diversity and inclusion within Thales at all levels of companies – Definition of new three-year environmental objectives – Re-launch of a global training program for the executives and staff most exposed to the risks of corruption and influence peddling;
- Digital strategy/Gemalto:** demonstrate the initial impacts of the Digital Factory to "digitalize" Group activities. Execution of the planned takeover of Gemalto.

**c) 2018 Long-Term Incentive Plan (LTIP)**

The LTIP is designed to reward the Chairman and CEO for the Group's long-term performance.

Its structure and size for 2018 are unchanged compared with the programme implemented in 2017.

It therefore consists of performance units tied to the value of the Thales share. The units will be paid at 50% in Thales shares and at 50% in cash. The grant approved by the Board consists of a maximum of 5,000 performance units, comprising the number of units that may ultimately vest in the event that related maximum objectives are reached *vis-à-vis* the criteria listed below.

These performance units are subject to a vesting period of four years from 5 March 2018. The performance units that actually vest in 2022 will depend on the achievement of performance conditions measured over a three-year period (2018-2020).

Pursuant to Articles L. 225-37-2 and R. 225-29-1 of the French Commercial Code, the related payments will be submitted to the vote of the Shareholders' Meeting in accordance with legal conditions.

**(i) 2018 LTIP performance criteria**

The Board of Directors has decided to apply demanding performance criteria tied to the Group's key levers of long-term value creation and their implementation as part of the "Ambition 10" strategic vision focused on growth and competitiveness. Therefore, performance is measured as follows over this three-year period:

- 40% based on a growth objective measured in terms of average order intake over the 2018-2020 period;
- 40% based on a competitiveness objective measured in terms of cumulative free operating cash flow over the 2018-2020 period; and
- 20% based on Thales' stock market performance and measured by Total Shareholder Return or TSR (which includes reinvested dividends). Half of this stock market performance weighting (10%) is based on a comparison with a panel of European companies in comparable sectors of activity (which includes the following eight equally weighted companies: Airbus, Atos, BAE Systems, Capgemini, Dassault Aviation, Leonardo, Rolls-Royce, Safran) and the other half (10%) with the Euro Stoxx index. The calculation is based on a comparison of performance at 31 December 2020 with performance at 31 December 2017.

The following thresholds are applied:

**➤ WEIGHTING OF THE 5,000 2018 LTIP PERFORMANCE UNITS**

2018 LTIP criteria	Weighting	Objectives	Threshold	Payment as % of target
Cumulative free operating cash flow 2018-2020	40% (2,000 units)	Floor:	If results < floor	0%
		€2.6 billion	If results = floor (=33% of maximum)	13.20%
		Ceiling:	If results ≥ ceiling for the period	40.00%
		€3.6 billion	Variations between floor and ceiling calculated on a straight-line basis	
Average order intake for 2018-2020	40% (2,000 units)	Floor:	If results < floor	0%
		€15.5 billion	If results = floor (=50% of maximum)	20.00%
		Ceiling:	If results ≥ ceiling for the period	40.00%
		€17.5 billion	Variations between floor and ceiling calculated on a straight-line basis	
Total Shareholder Return compared to a panel of European companies <sup>(a)</sup> Measure based on performance at 31/12/2020 compared to 31/12/2017	10% (500 units)	Floor: median of the panel	If TSR < median of the panel	0%
			If TSR = median of the panel (=50% of maximum)	5.00%
		Ceiling: highest quintile of the panel	If TSR is in the highest quintile of the panel	10.00%
			Variations between median and entry point of highest quintile calculated on a straight-line basis	
Total Shareholder Return compared to the Euro Stoxx index Measure based on performance at 31/12/2020 compared to 31/12/2017	10% (500 units)	Floor: median of the Euro Stoxx index	If TSR < median of the index	0%
			If TSR = median of the index (=50% of maximum)	5.00%
		Ceiling: highest quintile of the index	If TSR is in the highest quintile of the index	10.00%
			Variations between median and entry point of highest quintile calculated on a straight-line basis	

(a) The panel includes: Airbus, Atos, BAE Systems, Capgemini, Dassault Aviation, Leonardo, Rolls-Royce and Safran.

The Board may adjust the objectives in the event of the planned takeover bid for Gemalto being successful. The Board will report on this at the 2019 Annual General Meeting.

After the end of the 2020 financial year, the Board of Directors will disclose the number of performance units that actually vest following a review of the achievement of the performance conditions.

#### **(ii) Additional 2018 LTIP vesting criteria**

Payment of the performance units is subject to the Chairman and CEO still being with the Company at the end of the four-year vesting period. If he should leave the Group during the vesting period, all performance unit entitlements shall be forfeited. Entitlement shall only be maintained in the event of death, disability or retirement. The value of each vested performance unit will correspond to the value of the Thales share at the close of trading on 4 March 2022, the last published price before the performance units are vested to the grantee.

The Chairman and CEO must hold the Thales shares delivered to him at 50% of the net after-tax gain from the LTIP, until he has accumulated a portfolio of shares equivalent to one year's fixed salary, and hold onto these shares for his entire term of office as Company representative.

In accordance with Section 24.3.3 of the AFEP-MEDEF Corporate Governance Code and the Internal Code on Insider Trading, the Chairman and CEO has undertaken not to use any hedging instruments in relation to his risk exposure on any shares or performance units he holds.

#### **d) Other items of the Chairman and CEO's compensation**

The Chairman and CEO is entitled to three other items of compensation subject to related-party commitments:

- severance pay;
- private unemployment insurance;
- deferred incremental and conditional compensation.

These three items of compensation, described in Section 3.2.2.1, were put in place in February 2015 for the benefit of the Company representative after his employment contract with the Group was ended.

They were again authorized by the Board of Directors on 5 March 2018 and then published on Company's website. They are subject to the vote of the General Meeting of 23 May 2018, as related-party commitments, in view of the renewal of the Chairman and CEO's term of office.

The Chairman and CEO is also entitled to other items of compensation as follows:

- legal and tax advice;
- private healthcare benefits identical to those offered to senior executives;
- directors and officers liability insurance;
- reimbursement of business expenses in accordance with Thales's rules and guidelines;
- an annual medical check-up like other Thales senior executives;
- the services of a chauffeur-driven car.

The Board of Directors has also confirmed that the Chairman and CEO does not receive attendance fees in his capacity as director.

For more information, please refer to Section 3.2.2.1.

### 3.3 CORPORATE MANAGEMENT AND EXECUTIVE COMMITTEE

#### Executive Committee at 31 December 2017



**Marc Darmon**  
Executive Vice  
President, Secure  
Communications and  
Information Systems



**Alex Cresswell**  
Executive Vice  
President,  
Land & Air Systems



**Philippe Duhamel**  
Executive Vice  
President, Defence  
Mission Systems



**Gil Michielin**  
Executive Vice  
President, Avionics



**Jean-Lôic Galle**  
Executive Vice  
President, Space



**Millar Crawford**  
Executive Vice  
President, Ground  
Transportation  
Systems



**Patrice Caine**  
Chairman and CEO



**Pierre-Éric  
Pommellet**  
Senior Executive Vice  
President, Operations  
& Performance



**Pascale Sourisse**  
Senior Executive  
Vice President,  
International  
Development



**David Tournadre**  
Senior Executive  
Vice President,  
Human Resources



**Pascal Bouchiat**  
Senior Executive  
Vice President,  
Finance and  
Information Systems



**Isabelle Simon**  
Company Secretary



**Philippe Keryer**  
Executive  
Vice President,  
Strategy, Research  
and Technology

## 3.4 COMPENSATION OF OTHER EXECUTIVES

### 3.4.1 Compensation of other Group executives

Total compensation paid in 2017 to Executive Committee members (proportionate to the time spent on the Committee) excluding the Chairman and CEO, was €8,551k, including 41% in variable

compensation for 2016. As is the case for the Chairman and CEO, the variable component is based on financial and non-financial performance criteria.

#### ➤ DETAILS OF COMPENSATION PAID TO THE EXECUTIVE COMMITTEE (EXCLUDING THE CHAIRMAN AND CEO) IN 2016 AND 2017

(in € thousand)	2017	2016
	Paid during the financial year	Paid during the financial year
<b>Executive Committee (excl. Chairman and CEO)</b>		
Fixed compensation	4,489	4,298
Variable compensation	3,528	3,182
Payments due upon retirement	502	–
Benefits in kind	32	29
<b>Total before social contributions</b>	<b>8,551</b>	<b>7,509</b>
Employer social contributions	2,690	2,433
<b>TOTAL EXPENSE</b>	<b>11,241</b>	<b>9,942</b>

In addition, at the end of December 2017, the members of the Executive Committee, other than the chairman, together had a total of 7,252 stock options, 65,070 performance shares, 91,500 performance units and 11,200 phantom shares. The breakdown by grant date and

the characteristics, as well as any options exercised, are shown in the tables on pages 183 and 184 with the summary of transactions carried out by directors, non-voting directors and related persons (Section 4.2.3.7).

### 3.4.2 Share-based compensation

#### Description of the different plans granted by the Group

The Group regularly grants its employees and executives share subscription options, share purchase options (until 2011) and/or free shares (since 2007), as part of its standard performance management policy for Group employees. These different plans are described below:

#### Outstanding options at 31 December 2017

At 31 December 2017, the following options, shares and units were outstanding:

- 850 share purchase options at a weighted average exercise price of €38.50;
- 783,204 stock subscription options at a weighted average exercise price of €34.13, of which 155,427 are subject to performance conditions.

➤ **OUTSTANDING SHARE PURCHASE OPTIONS**

Date of Board decision	25/11/2008	04/07/2007
Discount at grant	Nil	Nil
Performance conditions	No	No
Exercise period	from 25/11/2012 to 24/11/2018	from 04/07/2011 to 03/07/2017
Exercise price	€38.50	€44.77
<b>NUMBER OF OPTIONS OUTSTANDING AT 31/12/2017, NET OF OPTIONS CANCELLED <sup>(a)</sup> AND EXERCISED</b>	<b>850</b>	<b>–</b>
Of which exercisable options at 31/12/2017	850	–
Of which outstanding options at 31/12/2017 held by:		
• the Chairman and CEO, Patrice Caine	–	–
• the other members of the Executive Committee	–	–
<b>NUMBER OF BENEFICIARIES OF OUTSTANDING OPTIONS</b>	<b>1</b>	<b>–</b>
Of which members of the Executive Committee (excluding the Chairman) at 31/12/2017	–	–
Total grant to top ten beneficiaries (at plan date)	73,200	–

(a) Notably due to termination of the employment contract between the beneficiary and the Group since the grant date.

➤ **SHARE SUBSCRIPTION OPTIONS**

Date of Board decision	15/09/2011	23/09/2010	25/06/2009	01/07/2008
Discount at grant	Nil	Nil	Nil	Nil
Performance conditions	Yes	Yes	No	No
Exercise period <sup>(a)</sup>	from 15/09/2015 to 14/09/2021	from 23/09/2014 to 22/09/2020	from 25/06/2013 to 24/06/2019	from 01/07/2012 to 30/06/2018
Exercise price	€26.34	€26.34	€32.88	€38.50
<b>NUMBER OF OPTIONS OUTSTANDING AT 31/12/2017, NET OF OPTIONS CANCELLED <sup>(b)</sup> AND EXERCISED</b>	<b>85,377</b>	<b>70,050</b>	<b>272,752</b>	<b>355,025</b>
Of which exercisable options at 31/12/2017	85,377	70,050	272,752	355,025
Of which outstanding options at 31/12/2017 held by:				
• the Chairman and CEO, Patrice Caine <sup>(c)</sup>	1,538	1,900	–	–
• the other members of the Executive Committee	2,752	4,500	–	–
<b>NUMBER OF BENEFICIARIES OF OUTSTANDING OPTIONS</b>	<b>37</b>	<b>28</b>	<b>293</b>	<b>255</b>
Of which members of the Executive Committee (excluding the Chairman) at 31/12/2017	2	2	–	–
Total grant to top ten beneficiaries (at plan date)	124,000	161,500	222,000	230,000

(a) Applicable to France for plans awarded prior to 2009 and to all countries since 2010.

(b) Primarily because of the termination of the employment contract between the beneficiary and the Group since the grant date or because of cancellation related to partial or complete failure to achieve the performance conditions.

(c) Grant prior to his appointment as Chief Executive Officer.

<b>Date of Board decision</b>	<b>04/07/2007</b>
Discount at grant	Nil
Performance conditions	No
Exercise period <sup>(a)</sup>	from 04/07/2011 to 03/07/2017
Exercise price	€44.77
<b>NUMBER OF OPTIONS OUTSTANDING AT 31/12/2017, NET OF OPTIONS CANCELLED<sup>(b)</sup> AND EXERCISED</b>	<b>—</b>
Of which exercisable options at 31/12/2017	—
Of which outstanding options at 31/12/2017 held by:	
• the Chairman and CEO, Patrice Caine <sup>(c)</sup>	—
• the other members of the Executive Committee	—
<b>NUMBER OF BENEFICIARIES OF OUTSTANDING OPTIONS</b>	<b>—</b>
Of which members of the Executive Committee (excluding the Chairman) at 31/12/2017	—
Total grant to top ten beneficiaries (at plan date)	240,000

(a) Applicable to France for plans awarded prior to 2009 and to all countries since 2010.

(b) Primarily because of the termination of the employment contract between the beneficiary and the Group since the grant date or because of cancellation related to partial or complete failure to achieve the performance conditions.

(c) Grant prior to his appointment as Chief Executive Officer.

### Conditions of exercise

All Thales share purchase and subscription options are granted for a 10-year period, at no discount to the market price.

Share purchase and subscription options granted between 1 July 2008 and 15 September 2011 can now be exercised in full.

The options granted on 15 September 2011 were contingent upon the achievement of internal performance conditions over the three financial years following their grant date. The three criteria used were EBIT, operating cash flow and order intake, with these criteria having a weighting of 60%, 25% and 15% respectively.

The rights were validated in one-third tranches at the Board of Directors' meetings to close the accounts for the three financial years concerned, resulting in the validation of 80.90% of the options granted.

### ➤ VALIDATION OF PERFORMANCE CONDITIONS FOR FINANCIAL YEAR 2017

Option, share, unit and phantom share plans subject to performance conditions	Validation of the 1st third of the allotment		Validation of the 2nd third of the allotment		Validation of the 3rd third of the allotment	
	Reference year	% achievement of performance conditions	Reference year	% achievement of performance conditions	Reference year	% achievement of performance conditions
16 September 2014	2015	100%	2016	100%	2017	100%
17 September 2015	2016	100%	2017	100%	2018	—
27 October 2016	2017	100%	2018	—	2019	—
28 September 2017	2018	—	2019	—	2020	—

➤ **OPTIONS GRANTED AND EXERCISED IN 2017**

	Number of options granted/shares subscribed or purchased	Exercise price	Maturity date	Date of plan
<b>1 - Directors</b>				
Options granted in 2017	Nil			
Patrice Caine	Nil			
<b>2 - The ten biggest option awards granted to employees</b>				
Options granted in 2017	Nil			
<b>3 - The ten biggest exercises of options by employees <sup>(a)</sup></b>				
Options exercised in 2017	8,000	€32.88	–	25/06/2009
	7,291	€26.34	–	15/09/2011
	7,000	€26.34	–	15/09/2011
	5,945	€26.34	–	15/09/2011
	5,500	€38.50	–	01/07/2008
	5,000	€44.77	–	04/07/2007
	4,800	€38.50	–	01/07/2008
	4,600	€44.77	–	04/07/2007
	4,600	€38.50	–	01/07/2008
	4,500	€44.77	–	04/07/2007

(a) For all Group companies combined.

## 3.5 INCENTIVES AND PROFIT-SHARING

### 3.5.1 Profit-sharing

The Group agreement on pooled profit-sharing for the employees of Thales group companies, signed on 23 December 2004 by all trade unions represented at Group level, resulted in payment in France in 2017 for the 2016 financial year of profit-sharing rights totalling €50.8 million. This agreement illustrates solidarity among Group companies, since all employees benefit from the same agreement and from a single profit-sharing fund distributed on the basis of common criteria.

### 3.5.2 Incentive scheme

Each company in France may also negotiate an incentive agreement (accord d'intéressement) on the basis of indicators which represent its key objectives. Under the terms of the Group profit-sharing agreement in France, it is mandatory to comply with the rule which sets an upper limit on the amount of the premium (total incentives + profit share) in relation to payroll.

22 French Group companies paid incentives in 2017 for financial year 2016 totalling €38.5 million.

➤ **GROSS AMOUNTS PAID OUT IN INCENTIVES AND PROFIT-SHARING IN RECENT YEARS**

(in € millions)	2017	2016	2015	2014	2013	2012
<b>In the Group in France</b>						
Profit share paid	50.8	34.87	18.70	15.34	22.56	24.29
Incentives paid	38.5	45.22	57.03	43.45	42.38	45.15
<b>By Thales (parent company)</b>						
Incentives paid	3.96	4.12	4.30	4.12	3.83	4.80

## 3.6 STATUTORY AUDITORS

For the period covered by the historical financial data, the Thales group statutory auditors were as follows:

### 3.6.1 Principal statutory auditors

#### Mazars

61, rue Henri Regnault  
92400 Courbevoie – France  
Represented by Mr Jean-Marc Deslandes and Ms Anne-Laure Rousselou.  
Current term approved by the General Meeting of 24 May 2013 and expiring with the audit of the 2018 financial statements.

#### Ernst & Young Audit

1/2, place des Saisons  
92400 Courbevoie – Paris-La Défense 1 – France  
Represented by Mr Serge Pottiez and Mr Philippe Diu.  
Current term approved by the General Meeting of 13 May 2015 and expiring with the audit of the 2020 financial statements.

### 3.6.2 Additional statutory auditors

#### Hervé Hélias

61, rue Henri Regnault  
92400 Courbevoie – France  
Current term approved by the General Meeting of 24 May 2013 and expiring with the audit of the 2018 financial statements.

#### Auditex

1/2, place des Saisons  
92400 Courbevoie – Paris-La Défense 1 – France  
Current term approved by the General Meeting of 13 May 2015 and expiring with the audit of the 2020 financial statements.

### 3.6.3 Statutory auditors' fees

The fees paid to auditors in 2016 and 2017 are presented in the table below<sup>(a)</sup>:

(in € thousand)	Mazars		Ernst & Young Audit		Total	
	2017	2016	2017	2016	2017	2016
<b>Audit of the financial statements</b>	<b>6,221</b>	<b>5,427</b>	<b>5,052</b>	<b>4,627</b>	<b>11,273</b>	<b>10,054</b>
• Issuer	927	779	920	856	1,847	1,635
• Subsidiaries	5,294	4,648	4,132	3,771	9,426	8,419
<b>Other services</b>	<b>690</b>	<b>526</b>	<b>1,030</b>	<b>791</b>	<b>1,720</b>	<b>1,317</b>
• Issuer	197	190	193	31	390	221
• Subsidiaries	493	336	837	760	1,330	1,096
<b>TOTAL</b>	<b>6,911</b>	<b>5,953</b>	<b>6,082</b>	<b>5,418</b>	<b>12,993</b>	<b>11,371</b>

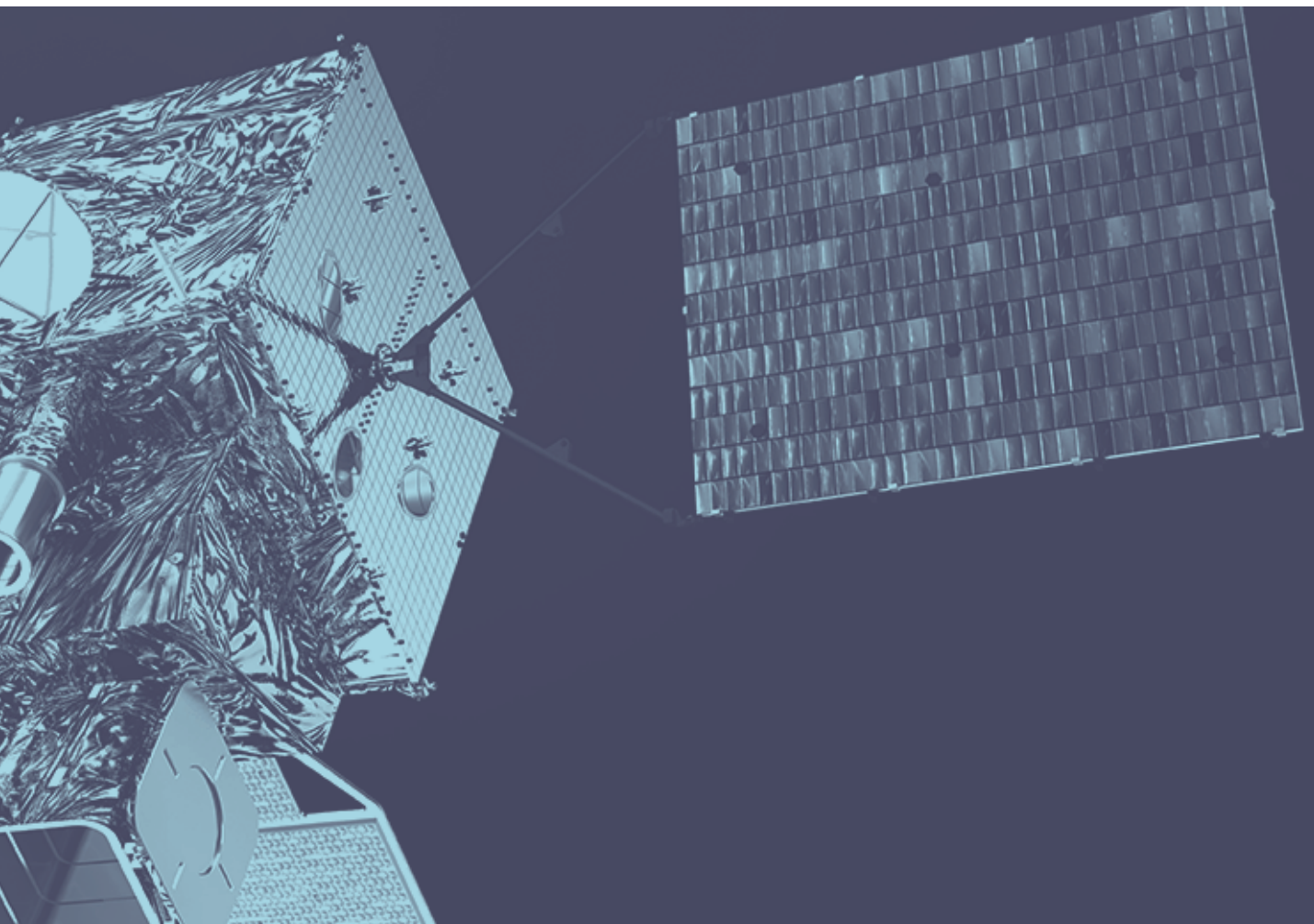
(a) With regard to the period under consideration, these are services performed in respect of a financial year charged to the Income Statement.

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## COMPANY AND SHARE CAPITAL

> 4






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## 4.1 GENERAL INFORMATION ABOUT THE COMPANY

### Company name

Thales

### Legal structure

Thales is a public limited company with a Board of Directors. It is governed by French law, particularly the French Commercial Code and certain provisions of the amended law on privatisation of 6 August 1986, since the French State owns more than 20% of the share capital.

### Registered office

Tour Carpe Diem – Place des Corolles – Esplanade Nord – 92400 Courbevoie – France. Telephone: +33 (0)1 57 77 80 00.

### Registration

No. 552 059 024 in the Nanterre Register of Trade and Companies; APE business identifier code: 7010 Z.

### Term

Initially incorporated on 11 February 1918 for 99 years, the Company's term was extended by the Annual General Meeting of 24 May 2013. The expiry date is now set at 23 May 2112.

### Corporate purpose

The corporate purpose is, directly or indirectly, in all countries:

1. the design, construction, installation, maintenance, operation, manufacture, purchase, sale, exchange, supply or hire of all equipment, tools, stations, appliances, finished or semi-finished products, materials, substances, components, systems, devices, processes and, in general, all products relating to electronic applications in any field.

For this purpose, the registration, purchase, sale, exchange, supply, concession or use of all business and manufacturing patents, licences and trademarks;

2. the research, obtaining, acquisition, disposal, exchange, supply, hire or use of all concessions or undertakings, whether private or public, training of staff, and the provision of all services pertaining thereto;
3. the formation of any company or association, or investment in any form whatsoever in any company or undertaking, having a similar or related purpose to that of the Company;
4. and in general, all commercial, industrial, financial and movable or immovable property transactions that relate directly or indirectly to the aforementioned activities.

### Financial year

The Company's financial year covers a period of 12 calendar months from 1 January to 31 December.

Corporate documents and information about the Company can be consulted at the Group Secretary and General Counsel's office at the Company's registered office.

### Distribution of profits as per the articles of association

Profits are distributed in compliance with current legislation. Under the Articles of Association, the Annual General Meeting called to approve the financial statements for the previous financial year is empowered to grant each shareholder the option to receive payment of all or part of the dividend distributed either in cash or in shares.

### Notifications concerning the crossing of statutory thresholds

Any natural person or legal entity owning a number of shares equal to or exceeding 1% of the share capital (but not voting rights), or any multiple thereof, is required to inform the Company of the total number of shares held within five trading days of the date on which this threshold is exceeded.

This obligation to inform the Company applies, under the same conditions, when the number of shares held falls below one of the thresholds mentioned in the previous paragraph.

In the event of failure to comply with this obligation, the shareholder shall be deprived of the voting rights attached to any shares exceeding the first undeclared threshold, subject to the conditions and limitations defined by law.

As part of its regulated information, every month, the Company publishes on its website the number of shares comprising the capital and the total number of voting rights attached – based on all threshold excesses (statutory and legal).

### Annual General Meeting: notice of meetings and conditions for attendance, double voting rights and exercise of voting rights

The information regarding these sections can be found in the Corporate Governance report, Section 3.2.1.6.

## 4.2 SHARE CAPITAL AND SHAREHOLDERS

### 4.2.1 Information on the distribution of capital issued

At 31 December 2017, the share capital stood at €636,976,175, divided into 212,658,725 shares with a par value of €3 each.

Pursuant to the applicable regulations, each month the Company publishes on its website ([www.thalesgroup.com](http://www.thalesgroup.com)), under "Investor/Publications/Regulated Information", the information pertaining to the total number of voting rights (theoretical and exercisable) and the number of shares making up the share capital, and forwards this information to the news distribution service.

Changes in share capital and shareholders' rights are governed by the applicable laws.

Shares in the Company may be held in either registered or bearer form, at the shareholder's discretion. The share register is kept on behalf of the Company by Société Générale (Securities Services – 32, rue du Champ-de-Tir – BP 81236 – 44312 Nantes CEDEX – France).

The share capital is fully paid up. It includes a golden share resulting from the conversion of an ordinary share belonging to the French State, as decided by decree No. 97-190 of 4 March 1997, implementing the law on privatisation of 6 August 1986 (see page 182).

#### 4.2.1.1 Changes in the share capital over the last five financial years

Date	Type of transaction	Acquisition, issue and merger premiums	Number of shares created	Nominal amount of the changes in capital	Amount of share capital	Aggregate number of shares making up the capital
<b>31 December 2012</b>		<b>3,731,620,794</b>			<b>607,019,022</b>	<b>202,339,674</b>
Financial year 2013	Exercise of stock subscription options	94,942,634	3,404,826	10,214,478		
<b>31 December 2013</b>		<b>3,826,563,428</b>			<b>617,233,500</b>	<b>205,744,500</b>
Financial year 2014	Exercise of stock subscription options	63,313,408	2,096,611	6,289,833		
<b>31 December 2014</b>		<b>3,889,876,836</b>			<b>623,523,333</b>	<b>207,841,111</b>
Financial year 2015	Exercise of stock subscription options	105,567,702	3,120,293	9,360,879		
<b>31 December 2015</b>		<b>3,995,444,538</b>			<b>632,884,212</b>	<b>210,961,404</b>
Financial year 2016	Exercise of stock subscription options	41,484,459	1,233,362	3,700,086		
<b>31 December 2016</b>		<b>4,036,928,997</b>			<b>636,584,298</b>	<b>212,194,766</b>
Financial year 2017	Exercise of stock subscription options	16,276,572	463,959	1,391,877		
<b>31 DECEMBER 2017</b>		<b>4,053,205,569</b>			<b>637,976,175</b>	<b>212,658,725</b>

### 4.2.1.2 Changes in the distribution of capital and voting rights over the last three financial years

At 31 December 2017, the total number of exercisable voting rights was 306,516,976. This includes double voting rights attached to shares that have been registered for at least two years under the conditions set out in the Articles of Association (see Section 3.2.1.6.

As previously mentioned, the number of shares and voting rights (theoretical and exercisable) is published monthly on the Company's website ([www.thalesgroup.com](http://www.thalesgroup.com), under "Investor/Publications/Regulated information").

	31 December 2017			31 December 2016			31 December 2015		
	Number of shares	% of share capital	% of voting rights	Number of shares	% of share capital	% of voting rights	Number of shares	% of share capital	% of voting rights
TSA <sup>(a)</sup>	54,786,654	25.76%	35.75%	54,786,654	25.82%	35.86%	54,786,654	25.97%	36.04%
French State (including 1 golden share)	2,060	—	—	2,060	—	—	2,060	—	—
Public Sector <sup>(a)</sup>	54,788,714	25.76%	35.75%	54,788,714	25.82%	35.86%	54,788,714	25.97%	36.04%
Dassault Aviation <sup>(b)</sup>	52,531,431	24.70%	28.44%	52,531,431	24.76%	28.53%	52,531,431	24.90%	28.67%
Thales	568,739	0.27%	—	749,559	0.35%	—	839,254	0.40%	—
Employees	6,181,444	2.91%	3.50%	5,743,081	2.71%	3.31%	5,684,120	2.69%	3.24%
Other shareholders	98,588,397	46.36%	32.31%	98,381,981	46.36%	32.30%	97,117,885	46.04%	32.05%
<b>TOTAL</b>	<b>212,658,725</b>	<b>100%</b>	<b>100%</b>	<b>212,194,766</b>	<b>100%</b>	<b>100%</b>	<b>210,961,404</b>	<b>100%</b>	<b>100%</b>

(a) Under the terms of the shareholders' agreement with Dassault Aviation (the "Industrial Partner", see AMF 27-11-2008), the "Public Sector" is represented by TSA, excluding the State directly. All Thales shares held directly and indirectly by the French State have been in directly registered form for more than two years and thus have a double voting right on 31 December 2017.

(b) As at 31 December 2017, Dassault Aviation held 42,154,349 shares in directly registered form, including 34,654,349 for more than two years, thus granting it double voting rights, and also held 10,377,082 shares in bearer form.

### 4.2.1.3 Major changes in share ownership over the last five years

The Company's treasury shares held totalled 1.38% of the capital at 31 December 2012.

**During 2013**, the number of treasury shares was reduced due to the following transactions:

- 524,861 shares were purchased on the market;
- 1,582,469 shares were purchased under a liquidity contract;
- 1,624,034 shares were sold under a liquidity contract;
- 306,130 shares were assigned as free shares;
- 8,900 shares were assigned under an allocation of stock options;
- 473,653 shares were sold to employees as part of the 2013 employee shareholding scheme.

Treasury shares thus amounted to 1.21% of the capital, i.e., 2,490,177 shares, at 31 December 2013.

**During 2014**, the number of treasury shares was reduced due to the following transactions:

- 2,146,816 shares were purchased under a liquidity contract;
- 2,216,116 shares were sold under a liquidity contract;
- 544,145 shares were assigned as free shares.

Treasury shares thus amounted to 0.9% of the capital, i.e., 1,876,732 shares, at 31 December 2014.

**During 2015**, the number of treasury shares was reduced due to the following transactions:

- 807,144 shares were purchased under a liquidity contract;
- 822,144 shares were sold under a liquidity contract;
- 535,532 shares were assigned as free shares;
- 29,350 shares were assigned under an allocation of stock options;
- 457,596 shares were sold to employees as part of the 2015 employee shareholding scheme.

Treasury shares thus amounted to 0.4% of the capital, i.e., 839,254 shares, at 31 December 2015.

**During 2016**, the number of treasury shares was reduced due to the following transactions:

- 575,000 shares were purchased on the market;
- 513,001 shares were purchased under a liquidity contract;
- 472,001 shares were sold under a liquidity contract;
- 607,381 shares were assigned as free shares;
- 56,600 shares were assigned under an allocation of stock options;
- 41,714 shares were sold to employees as part of the 2015 employee shareholding scheme.

Treasury shares thus amounted to 0.35% of the capital, i.e., 749,559 shares, at 31 December 2016.

**During 2017**, the number of treasury shares was reduced due to the following transactions:

- 852,000 shares were purchased on the market;
- 819,512 shares were purchased under a liquidity contract;
- 743,512 shares were sold under a liquidity contract;
- 606,653 shares were assigned as free shares;
- 40,000 shares were assigned under an allocation of stock options.

## 4.2.2 Potential capital

### 4.2.2.1 Maximum potential capital at 31 December 2017

	In number of shares with par value of €3
Share capital at 31 December 2017	212,658,725
Current stock option plans	783,204
1 July 2008 plan: 355,025 options at €38.50	
25 June 2009 plan: 272,752 options at €32.88	
23 September 2010 plan: 70,050 options at €26.34	
15 September 2011 plan: 85,377 options at €26.34	
Maximum potential capital (+0.37%)	213,441,929

### 4.2.2.2 Outstanding securities giving access to share capital (bonds, warrants and options)

At 31 December 2017, excluding the exercise of stock options, if any, there were no other outstanding securities giving immediate or future access to the share capital.

For convenience, even though they have no impact on the potential capital since they involve existing shares, share purchase options have been presented with stock subscription options in the paragraph on the financial statements of the parent company.

#### Share purchase and stock subscription options

At 31 December 2017, the following were outstanding:

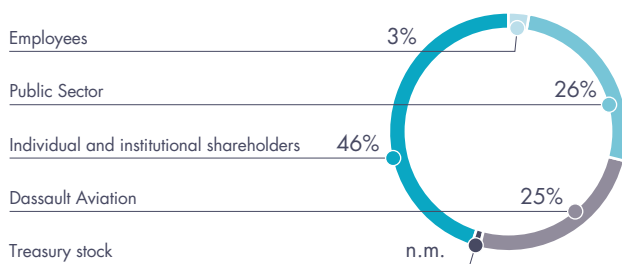
- 850 share purchase options at a weighted average exercise price of €38.50;
- 783,204 stock subscription options at a weighted average exercise price of €34.13, of which 155,427 are subject to performance conditions.

Thales decided to stop granting options in 2012.

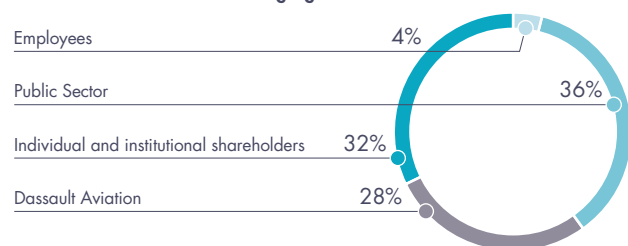
## 4.2.3 Shareholders

### 4.2.3.1 Breakdown at 31 December 2017

#### Breakdown of shareholders



#### Breakdown of exercisable voting rights



### 4.2.3.2 Shareholders acting in concert

#### 4.2.3.2.1 “Public sector” (TSA)

TSA is a holding company wholly owned by the French State at 31 December 2017. It directly holds 54,786,654 Thales shares.

The French State directly holds 2,060 shares, including a golden share, which gives it the principal rights<sup>(1)</sup> described in Section 4.2.3.3.5.

#### 4.2.3.2.2 “Industrial Partner” (Dassault Aviation)

Dassault Aviation, whose shares are listed on the Euronext Paris market, is a public limited company that owns 24.70% of Thales’ share capital, i.e. 52,531,431 Thales shares at 31 December 2017.

Dassault Aviation is controlled by the company Groupe Industriel Marcel Dassault (GIMD) which at 31 December 2017 held 62.17% of the share capital and 76.79% of the exercisable voting rights of Dassault Aviation.

### 4.2.3.3 Shareholders’ agreement, agreement on the protection of strategic national interests, specific agreement and golden share

By signing in 2009 an “endorsement agreement” with the French State and Alcatel-Lucent, Dassault Aviation assumed the rights and obligations of Alcatel-Lucent, subject to certain amendments, by endorsing the agreements signed on 28 December 2006 – namely the shareholders’ agreement and the agreement on the protection of strategic national interests in Thales<sup>(2)</sup>.

#### 4.2.3.3.1 Shareholders’ agreement between the “Public Sector” and the “Industrial Partner”

On 28 December 2006, TSA and Alcatel-Lucent signed a shareholders’ agreement that governs relations between the Public Sector and the Industrial Partner within Thales.

This agreement came into effect on the date of transfer of assets from Alcatel-Lucent Participations (5 January 2007). The agreement was signed pursuant to the cooperation agreement entered into on 1 December 2006 between Thales, Alcatel-Lucent and TSA, which replaced the previous cooperation agreement signed on 18 November 1999 by Alcatel, Thales and GIMD<sup>(3)</sup><sup>(4)</sup>.

On 19 May 2009, when Dassault Aviation acquired the Thales shares previously owned by Alcatel-Lucent, an agreement took effect under which Dassault Aviation endorsed the shareholders’ agreement existing between Alcatel-Lucent and the Public Sector, subject to amendments. The agreement under which TSA and Dassault Aviation act in concert

with regard to Thales under Article L. 233-10 of the French Commercial Code, as TSA has a majority within the concert, sets out the following provisions<sup>(5)</sup>:

#### Members of the executive bodies of Thales

Thales’ Board of Directors, which has 16 members, has to adhere to the following breakdown at 31 December 2016:

- 5 members proposed by the Public Sector;
- 4 members proposed by Dassault Aviation;
- 2 employee representatives;
- 1 representative of employee-shareholders;
- 4 external individuals, selected jointly by the Public Sector and Dassault Aviation.

The number of directors appointed upon the proposal of Dassault Aviation may not be higher than the number of directors appointed upon the proposal of the Public Sector. The number of Directors for each will be at least equal to the greater of the following two numbers: (i) the number of directors other than the employee representatives and external individuals, multiplied by the percentage of Thales shares held by Dassault Aviation, compared to the amount of Public Sector and Dassault Aviation holdings and (ii) the number of directors representing the employees.

Should Dassault Aviation’s shareholding exceed that of the Public Sector, the parties to the agreement will increase the total number of Thales directors from 16 to 17, so as to be represented by five directors each.

The Chairman and CEO is chosen on the joint proposal of the parties.

Furthermore, the parties have agreed that, in the event of a change of Chairman and CEO in accordance with the terms of the shareholders’ agreement, they do not intend to propose as a candidate any employee, manager or senior executive belonging to the Dassault group or having recently left this group.

Finally, it is specified that at least one director representing each of the parties must sit on each of the committees of the Thales Board of Directors.

#### Decisions to be submitted to the Thales Board of Directors

The parties undertake to submit for mandatory approval by the majority of the Directors representing Dassault Aviation, decisions of the Thales Board of Directors relating in particular to the appointment and dismissal of the Chairman and CEO, the adoption of the annual budget and the multi-year strategic plan, and significant acquisitions and disposals of shareholdings or assets (in excess of €150 million) as well as strategic alliance agreements on technological and industrial cooperation.

However, Dassault Aviation has expressly undertaken to forego the exercise of the right of veto which it has, by virtue of the agreement, over some of Thales’ strategic operations; this decision concerns a series of potential acquisitions or disposals. In return, the Public Sector has foregone its right to terminate the agreement in the event of persistent disagreement regarding a strategic operation likely to have an adverse impact on its strategic interests<sup>(6)</sup>.

Should Dassault Aviation exercise its right of veto over the appointment of the Chairman and CEO, after a consultation period of three months, either of the parties may terminate the agreement.

(1) Pursuant to Article 3 of decree No. 97-190 of 4 March 1997.

(2) See Decision No. 207CO013 of 2 January 2007, published in the French Legal Gazette (BALO) of 5 January 2007.

(3) Published in the Official Journal of the French Republic on 12 December 2006 [see the Official Journal website: [www.journal-officiel.gouv.fr](http://www.journal-officiel.gouv.fr)] taken in accordance with the provisions of Article 1 – 1° of decree 93-1041 of 3 September 1993 and pursuant to law No. 86-912 of 6 August 1986.

(4) This agreement is set out in the appendix to the Thales Board of Directors’ report to the Extraordinary General Meeting of 5 January 2007, registered by the AMF on 19 December 2006 under number E.06-194 ([www.thalesgroup.com](http://www.thalesgroup.com)).

(5) With regard to a proposal to separate the functions of CEO and Chairman, an amendment to the shareholders’ agreement regarding Thales was concluded between the Public Sector and Dassault Aviation on 7 April 2015, designed to amend the shareholders’ agreement so that the Board of Directors of Thales is composed of 18 members including 6 proposed by the Public Sector, 5 by the Industrial Partner (Dassault Aviation), 2 employee representatives, 1 representative of employee-shareholders and 4 external individuals. As the proposal to separate the functions of CEO and Chairman was rejected, the shareholders’ agreement was reverted to its initial version dated 19 May 2009 through a second amendment signed on 13 May 2015, and the stipulations of the agreement therefore remain unchanged. For more details on these amendments, refer to D&I 215C0404 of 7 April 2015 and D&I 215C0643 of 15 May 2015 published on the AMF’s website.

(6) Acquisitions or disposals identified by the French State as having potentially significant importance with regard to its strategic defence interests and having the objective of strengthening the industrial and technological defence base in France.

### Shareholder interests

Dassault Aviation must hold at least 15% of the share capital and voting rights in Thales and remain the largest private shareholder in Thales. The Public Sector must take whatever measures are required to enable Dassault Aviation to comply with this undertaking.

The Public Sector undertakes to restrict its shareholding to 49.9% of Thales' capital and voting rights.

### Term of the shareholders' agreement

In the absence of termination on expiry of the contract on 31 December 2016, the agreement was tacitly renewed for another period of five years, expiring on 31 December 2021. It may be tacitly renewed for five-year periods.

The agreement will be automatically terminated and the concerted action between TSA and Dassault Aviation will also automatically cease should one of the parties commit, without prior consultation with the other party, an action which creates an obligation to make a public offer for Thales.

### Option of unilateral termination of the agreement and agreement to sell to the Public Sector

The Public Sector has the option of terminating the agreement and asking Dassault Aviation to suspend the exercise of the voting rights that it holds above a threshold of 10%, or to reduce its shareholding to less than 10% of Thales' capital, in the event of:

- a serious breach by Dassault Aviation of its obligations so as to substantially compromise the protection of the strategic interests of the French State, given that said obligations are subject to an "agreement on the protection of strategic national interests in Thales" (see below);
- a change in control of Dassault Aviation.

In this respect, Dassault Aviation gives the Public Sector an irrevocable and definitive undertaking to sell all shares held by Dassault Aviation upon confirmation that Dassault Aviation's shareholding of Thales has remained above 10% of Thales' capital in the six months following the Public Sector's request to reduce its shareholding.

The Public Sector<sup>(1)</sup> was bound by an undertaking to hold a stake in Thales granting it at least 10% of the voting rights. This undertaking expired on 31 December 2014<sup>(2)</sup>.

### 4.2.3.3.2 Agreement on the protection of strategic national interests

Furthermore, on 19 May 2009 Dassault Aviation endorsed the "agreement on the protection of strategic national interests in Thales" signed on 28 December 2006 by Alcatel-Lucent and the French State in the presence of TSA. This endorsement gives rise to the following obligations for Dassault Aviation:

- Dassault Aviation's registered office and operational headquarters must remain in France;
- directors of Thales proposed by Dassault Aviation must be nationals of the European Union;
- access to sensitive information concerning Thales is strictly controlled within Dassault Aviation;
- managers who are responsible for Dassault Aviation's holdings in Thales are French nationals;

- Dassault Aviation must make its best efforts to prevent any action or influence in the governance and businesses of Thales by foreign national interests. In this respect, in the event of (i) a serious and unremedied breach by Dassault Aviation of its obligations under the agreement on the protection of strategic national interests or if it emerges that the application of a foreign law by Dassault Aviation creates constraints for Thales that substantially compromise the protection of the strategic interests of the French State, or (ii) a change in control within Dassault Aviation, contrary to the strategic interests of the Public Sector, the Public Sector may:

- terminate the rights that Dassault Aviation enjoys under the shareholders' agreement; and, if it sees fit,
- ask Dassault Aviation either to suspend the exercise of any voting rights it holds in excess of 10%, or
- ask it to reduce its shareholding to less than 10% of Thales' capital through the divestment of shares on the market (under conditions consistent with its financial interests and market constraints). At the end of a six-month period from the date on which it was asked to reduce its shareholding, if the shareholding of Dassault Aviation is still in excess of 10% of Thales' capital, the French State may proceed with the aforementioned undertaking to sell.

### 4.2.3.3.3 Crossing of thresholds and declaration of intent

Following the substitution of Alcatel-Lucent Participations by Dassault Aviation, within the Concert formed with the Public Sector *vis-à-vis* Thales and the disposal of Thales shares owned by GIMD to Dassault Aviation, on 19 May 2009 the latter exceeded, jointly with the Public Sector, the thresholds of 25% of the voting rights, 1/3 of the capital and voting rights and 50% of the voting rights of Thales and, on 20 May 2009, the threshold of 50% of the capital of Thales.

On 20 May 2009, the Public Sector, together with Dassault Aviation, exceeded the threshold of 50% of the capital of Thales.

These changes were granted dispensation from the obligation to submit a proposal for a public offer. This decision is reproduced in Décisions 208C2115 of 27 November 2008 and published in the French Legal Gazette (Bulletin officiel des annonces légales obligatoires, BALO), of 1 December 2008.

It is available on the BALO website at <https://www.journal-officiel.gouv.fr/balo/index.php>.

Dassault Aviation announced it had individually exceeded the 25% threshold of voting rights on 9 July 2012 and individually held 52,531,431 Thales shares representing 86,531,431 voting rights, equal to 25.96% of the capital and 29.33% of the voting rights at that date.

This threshold was crossed due to the allocation of double voting rights to Dassault Aviation on a portion of its holding.

Dassault Aviation declared that, on 13 January 2016, it had<sup>(3)</sup> "fallen below the threshold of 25% of the capital of the Company and that it individually owns 52,531,431 Thales shares representing 87,185,780 voting rights, or 24.90% of the capital and 28.59% of the Company's voting rights."

Dassault Aviation also revealed that this threshold crossing was due to an increase in the total number of Thales shares and voting rights and that, on this occasion, the concert party formed by TSA (Public Sector) and Dassault Aviation had not exceeded any thresholds.

(1) TSA and Sofivision in accordance with the terms of AMF decision no. 208C2115. Sofivision was taken over by TSA in the second half of 2012.

(2) See AMF decision No. 208C2115 of 27 November 2008 published in the French official bulletin of legal notices (BALO) of 1 December 2008, available for consultation on the AMF's website. "The Public Sector shall agree to hold, following the standard expiration of the shareholders' agreement, a stake in Thales granting it at least 10% of the voting rights, and up until the earliest of the following three dates: (i) 31 December 2014, (ii) three years as from the termination of the shareholders' agreement or (iii) date on which Dassault Aviation ceases to hold at least 15% of Thales' share capital."

(3) See AMF decision No. 216C0199, available for consultation on the AMF's website.

#### 4.2.3.3.4 Specific agreement

On 28 December 2006, the French State (Ministry of Defence and Ministry of the Economy) and Thales signed an agreement to give the French State control not only over the transfer of assets already mentioned in the appendix to decree No. 97-190 of 4 March 1997, but also over shares in Thales Alenia Space SAS (hereinafter referred to as the “Strategic Asset”). This agreement, to which the Industrial Partner is not party, was therefore not amended by the substitution of Alcatel-Lucent by Dassault Aviation in May 2009 and thus continues to be effective.

##### a) Where the Strategic Asset is a company (the “Strategic Company”)

- Any proposed transfer of shares in the Strategic Company to a third party such that the third party exceeds the threshold of 33.3% of the share capital.
- Any proposed transfer of shares in the Company that directly or indirectly controls the Strategic Company to a third party such that the third party exceeds the threshold of 33.3% of the share capital.

##### b) Where the Strategic Asset is an isolated asset, unincorporated division or branch of the business (the “Strategic Division”)

- Any proposed transfer of shares in the Company that owns the Strategic Division to a third party such that the third party exceeds the threshold of 33.3% of the share capital.
- Any proposed transfer of shares in the Company that directly or indirectly controls the company referred to in the previous paragraph to a third party such that the third party exceeds the threshold of 33.3% of the share capital.

##### c) Any proposed transfer of sensitive assets to a third party

##### d) And any proposal intended to confer or having the effect of conferring particular rights on a third party

Shall be disclosed to the French State, which undertakes to issue its acceptance or refusal decision within thirty (30) working days from the receipt of said notification. Failure by the French State to communicate its decision during said time is deemed to signify acceptance of the proposed transaction.

#### 4.2.3.3.5 Golden share held by the French State and other restrictions related to foreign investments in France

The golden share held by the French State<sup>(1)</sup> entitles it to the following rights:

- “Any increase in the direct or indirect holding of securities, irrespective of the nature or legal form, beyond a threshold of one-tenth, or a multiple thereof, of the capital or voting rights of the Company, by any natural person or legal entity, whether acting alone or in concert, must be approved in advance by the Minister for the Economy (...);”
- “Upon the proposal of the Minister of Defence, a representative of the French State, appointed by decree, sits on the Board of Directors of the Company as a non-voting director;”
- “(...) decisions to dispose of or assign by way of guarantee the assets specified in the appendix to this decree may be opposed.”

At 31 December 2017, these assets consisted of the majority of the share capital in the following companies:

Thales DMS France SAS (formerly known as Thales Systèmes Aéroportés SAS), Thales (Wigmore Street) Ltd, Thales Communications & Security SAS,

Thales IAS France SAS (formerly known as Thales Air Systems SAS), Thales Nederland BV, Thales AVS France SAS (formerly known as Thales Avionics SAS), Thales Underwater Systems NV.

In addition, as a result of some of Thales activities, particularly in the defence sector, shareholders and investors may be subject to certain restrictions applicable to foreign investments in France in accordance with Article L. 151-3 of the French Monetary and Financial Code and Article 10 of law No. 86-912 of 6 August 1986 on the terms and conditions of privatisation.

#### 4.2.3.4 Treasury shares

At 31 December 2017, Thales held 568,739 treasury shares (0.27% of capital), i.e. the balance after shares bought and sold in the market or otherwise under the authorisations described below granted to the Board of Directors by the Annual General Meeting.

Treasury shares are not subject to any restrictions and are freely transferable.

##### 4.2.3.4.1 Authority to trade in the Company's shares

At its meeting of 27 October 2016 at which it delegated to the Chairman & CEO the authority to trade in the Company's shares in 2017, the Board of Directors set the maximum purchase price at €100 per share. By decision of the Board of Directors of 4 April 2017, the maximum price was increased to €120 as from the Annual General Meeting on 17 May 2017.

The transactions carried out in 2017 show a net sale of 180,820 treasury shares, the details of which are as follows:

- transactions related to the delivery of securities to employees (net sale of 256,820 shares):
  - exercise of stock options and delivery of free shares to employees (-646,653 shares),
  - shares sold to employees under the 2017 employee shareholding scheme (-462,167 shares),
  - shares purchased directly in the market to meet the commitments to employees of the 2017 delivery of free shares (852,000 shares);
- liquidity contract, net purchase for the period: 76,000 shares.

##### 4.2.3.4.2 Authority to cancel Company shares

The 24-month authorisation granted to the Board of Directors by the Annual General Meeting of 17 May 2017 to cancel – on one or more occasions – shares held by the Company, up to a limit of 10% of share capital, as part of an authorisation to buy back its own shares, has not been used.

##### 4.2.3.4.3 Allotment of free shares

###### Allotment of free shares and/or performance shares

The Board of Directors, with the approval of the Annual General Meeting, implemented a ninth free share allotment plan.

The Chairman and CEO (the only Company representative) is not entitled to benefit from this plan.

The allotment on 28 September 2017 took the following form:

###### Performance shares

- The allotted shares are all subject to the fulfilment of internal performance conditions during the three financial years following the grant date. The performance criteria are current operating income (after restructuring), operating cash flow and order intake, with weightings of 60%, 15% and 25%, respectively;

(1) Pursuant to Article 3 of decree No. 97-190 of 4 March 1997.

- shares may be validated in tranches of one-third once the Board of Directors has approved the Group's consolidated financial statements for the three financial years concerned;
- the number of shares vested will not exceed the number of shares initially allotted;
- all designated beneficiaries of the plan are allotted shares validated at the end of a four-year vesting period subject to compliance with the employment conditions stipulated under the plan's rules.

Date of Board decision	28/09/2017	27/10/2016		17/09/2013		20/12/2012	
	Performance shares	Free shares	Performance shares	Free shares	Performance shares	Free shares	Performance shares
Number of beneficiaries at grant date	764	550	232	4,161	341	5,186	336
Share price at grant date	€94.66	€83.10	€83.10	€39.16	€39.16	€27.47	€27.47
Number of shares allotted	212,540	88,020	148,070	424,830	299,460	487,940	230,350
Number of free shares at 31/12/2016	N/A	87,860	148,070	397,180	226,335	—	—
Cancellation of allotments during the financial year <sup>(a)</sup>	—	300	310	9,274	7,638	—	—
Early allotments during the financial year <sup>(b)</sup>	—	—	—	—	—	—	—
Post-closing adjustments	—	—	—	—	—	50 <sup>(c)</sup>	—
Number of shares delivered on expiry of the plan	N/A	N/A	N/A	387,906	218,697	438,470	168,661
Number of beneficiaries of delivery on expiry	N/A	N/A	N/A	3,793	304	4,649	300
Balance of free shares net of cancellations and early allotments at 31/12/2017	212,540	87,560	147,760	—	—	—	—
Number of beneficiaries remaining at 31/12/2017	764	547	231	—	—	—	—
Vesting period	from 28/09/2017 to 29/09/2021	from 27/10/2016 to 28/10/2020		from 17/09/2013 to 18/09/2017		from 20/12/2012 to 21/12/2016	

(a) Due to the departure of the beneficiary or, for the plans concerned, due to eliminations related to partial or total non-achievement of the performance conditions.

(b) Due to death of the beneficiary during the vesting period.

(c) Due to excessive eliminations in 2016.

#### Allotment of shares in financial year 2017

Ten largest allotments of shares to employees during the year	Number of shares allotted	Share price at allotment date	Date of plan
Performance shares	212,540	€94.66	28/09/2017

During 2017, the allotment of shares subject to performance conditions to employees of the Company or its subsidiaries, excluding Thales executive officers, was between 80 and 4,700 shares.

#### 4.2.3.4.4 Allotment of units or units subject to performance conditions indexed to the Thales share price

No plan for the allotment of units was implemented for employees in 2017 except for that granted for the only Company representative (see page 156).

##### Unit plan subject to performance conditions allotted in 2014 and 2015

- Each unit allotted confers the right, at the end of the four-year vesting period and subject to the employment condition stipulated in the regulations, to the payment of a monetary value;
- this monetary value will be calculated at the end of the vesting period, and will be equal to the average of the daily opening prices for the Thales share during the vesting period. Extreme upwards or downwards variations in the stock market price will be neutralized;
- the amount due at the expiry date to the beneficiaries that meet the employment conditions will be equal to the number of units allotted multiplied by the value of the unit. Half of the payment will be made in shares, while the other half will be paid in cash.

##### Unit plan subject to employment and performance conditions

- The units subject to performance conditions follow the same rules as for units, i.e. vesting period and employment conditions, but the number of units that are actually issued at the expiry date will depend on the fulfilment of internal performance conditions over the three financial years following their allotment date; units may be validated in tranches of one-third once the Board of Directors has approved the Group's consolidated financial statements for the three financial years concerned;
- the number of units validated may not exceed the amount initially allotted;
- the three performance criteria used for the 2014 and 2015 plans are EBIT, free operating cash flow and order intake, with weightings of 60%, 15% and 25%, respectively.

Date of Board decision	17/09/2015		16/09/2014	
	Units	Performance units	Units	Performance units
Number of beneficiaries at grant date	3,885	293	3,684	310
Unit price at grant date	€61.75	€61.75	€42.42	€42.42
Number of units allotted	376,840	232,000	425,920	281,050
Balance of units at 31/12/2016	367,730	229,200	405,210	268,000
Cancellation of allotments during the financial year <sup>(a)</sup>	9,050	7,750	8,210	9,300
Early allotments during the financial year <sup>(b)</sup>	270	–	240	–
Post-closing adjustments <sup>(c)</sup>	620			
Balance of units at 31/12/2017	359,030	221,450	396,760	258,700
Number of beneficiaries remaining at 31/12/2017	3,688	278	3,434	286
Vesting period	from 17/09/2015 to 18/09/2019		from 16/09/2014 to 17/09/2018	

(a) Due to the departure of the beneficiary or, for the plans concerned, due to eliminations related to partial or total non-achievement of the performance conditions.

(b) Due to death of the beneficiary during the vesting period.

(c) Cancellation error concerning people who are still part of the Group.

#### 4.2.3.4.5 Allotment of phantom shares or phantom shares subject to performance conditions indexed to the Thales share price

In September 2017, a phantom share performance plan based on the Thales share price was put in place for all international employees. This

plan is equivalent to the performance-based free share plans offered to employees in France.

Through this plan, 307 people received 67,140 phantom shares under the same performance conditions as the free shares allotted on the same date.

#### 4.2.3.4.6 Validation of performance conditions for financial year 2017

Option, share, unit and phantom share plans subject to performance conditions	Validation of the 1st third of the allotment		Validation of the 2nd third of the allotment		Validation of the 3rd third of the allotment	
	Reference year	% achievement of performance conditions	Reference year	% achievement of performance conditions	Reference year	% achievement of performance conditions
16 September 2014	2015	100%	2016	100%	2017	100%
17 September 2015	2016	100%	2017	100%	2018	–
27 October 2016	2017	100%	2018	–	2019	–
28 September 2017	2018	–	2019	–	2020	–

#### 4.2.3.4.7 Description of the share buy-back programme proposed to the Annual General Meeting of 23 May 2018

- Maximum proportion of capital subject to repurchase: 10%, on the buy-back date.
- Maximum number of shares that may be purchased: 21,265,872.
- Maximum amount of the programme: €2,658,234,000.
- Maximum unit purchase price: €125.

##### Objectives of the programme

- To sell or allot shares to Group employees under the conditions and in the manner stipulated by law, particularly when share purchase options are exercised or existing free shares are allotted, or when shares are sold and/or supplemented under an employee shareholding scheme transaction on existing shares;
- to retain shares for later use in connection with acquisitions, mergers, demergers or contributions;

- to ensure trading in the shares through a liquidity contract prepared in accordance with a code of Conduct approved by the AMF;
- to cancel shares in accordance with an Annual General Meeting resolution in force;
- to carry out in general any transaction in accordance with applicable regulations.
- **Duration of the programme:** eighteen months from the date of approval of the resolution that will be submitted to the Annual General Meeting of 23 May 2018, i.e. no later than 21 November 2019.
- **Liquidity contract:** in November 2004, Thales signed a liquidity contract, in accordance with the AFEI code of Conduct, in order to regulate share trading. The contract was amended to comply with the AFEI code of Conduct appended to the AMF decision of 22 March 2005.

### 4.2.3.5 Shares owned by the public

The Company is entitled at all times, as provided by law, to ascertain the identity of and the number of shares held by holders of bearer shares, which now or in the future, represent a specific fraction of its share capital (the “TPI” Identifiable Bearer Security procedure).

Based on the most recent surveys on identifiable holders of bearer shares carried out by Euroclear France, and the Company’s information on employee shareholders, private ownership of Company shares is estimated as follows:

(in thousands of shares)	31/12/2017	31/12/2016
French institutional investors	26,308	22,491
Non-resident institutional investors	62,434	65,668
Others (e.g. brokerage firms)	3,802	4,212
Company employee savings scheme	6,181	5,743
Individual shareholders and associations <sup>(a)</sup>	5,735	5,285
Not identified	2	726
<b>S/Total Entire public</b>	<b>104,772</b>	<b>104,125</b>
<b>TOTAL NUMBER OF SHARES</b>	<b>212,659</b>	<b>212,195</b>

(a) Mainly French residents.

	As % of the total capital		As % of the free float (excluding treasury shares)	
	31/12/2017	31/12/2016	31/12/2017	31/12/2016
French institutional investors	12.4%	10.6%	25.1%	21.6%
Non-resident institutional investors	29.4%	30.9%	59.5%	63.1%
Others (e.g. brokerage firms)	2.0%	2.0%	4.0%	4.0%
Company employee savings scheme	2.6%	2.7%	5.4%	5.5%
Individual shareholders and associations	2.7%	2.5%	5.5%	5.1%
Not identified	0.3%	0.3%	0.5%	0.7%
<b>ENTIRE PUBLIC</b>	<b>49.3%</b>	<b>49.1%</b>	<b>100.0%</b>	<b>100.0%</b>

#### ➤ GEOGRAPHIC BREAKDOWN OF INSTITUTIONAL INVESTORS

31/12/2017	Number of shares held (in thousands)	As % of the total capital	As % of the free float	Number of investors
France	26,308	12.37%	26.54%	87
Continental Europe (exc. France)	13,136	6.18%	13.25%	143
North America	24,530	11.53%	24.74%	147
United Kingdom & Ireland	21,688	10.20%	21.88%	76
Rest of world	3,079	1.45%	3.11%	50
<b>TOTAL</b>	<b>88,741</b>	<b>41.73%</b>	<b>89.51%</b>	<b>503</b>

### 4.2.3.6 Employee shareholdings at 31 December 2017

At 31 December 2017, Group employees held, within the meaning of Article L. 225-102 of the French Commercial Code, 6,181,444 Thales shares, representing 2.91% of the capital (and 3.50% of voting rights)

through the Group savings scheme (PEG), either directly or via the Company Mutual Fund (FCPE) or its equivalent in the UK, or directly through the allotment of free shares.

At 31 December 2017, approximately 65% of the Thales shares held by employees were freely transferable (compared with 60% at 31 December 2016).

Holding by country	In number of shares	In % of employee shareholders L. 225-10 <sup>(d)</sup>	In % of capital	Related voting rights as % of total voting rights
France and world (three dedicated funds <sup>(a)</sup> )	3,827,921	61.93%	1.80%	2.38%
Netherlands (two dedicated funds <sup>(b)</sup> )	71,469	1.16%	0.03%	0.04%
United Kingdom (SIP – Trust <sup>(c)</sup> )	207,053	3.35%	0.10%	0.07%
Shares directly held in the Group savings scheme (2002, 2008, 2013, 2015 and 2017 schemes)	81,031	1.31%	0.04%	0.04%
Shares directly held resulting from the allotment of free shares (Article L. 225-197-1 of the French Commercial Code)	1,954,949	31.63%	0.92%	0.96%
Total Article L. 225-102 of the French Commercial Code	6,181,444	100.00%	2.91%	3.50%
<b>Total number of shares held by employees</b>	<b>6,181,444</b>	<b>100.00%</b>	<b>2.91%</b>	<b>3.50%</b>
<b>TOTAL SHARE CAPITAL</b>	<b>212,658,725</b>			

(a) "Actions Thales", "World Classic", and "Action Protect 2013" funds.

(b) "Netherlands Classic" and "Netherlands Action Protect 2013" funds.

(c) Share Incentive Plan.

(d) L. 225-10 of the French Commercial Code.

### 4.2.3.7 Summary statement of transactions indicated in Article L. 621-18-2 of the French Monetary and Financial Code carried out in 2017

In accordance with Article 223-26 of the General Regulations of the French financial markets authority (AMF).

To the best of the Company's knowledge, the following disclosures have been made to the AMF, for publication on its website (<http://www.amf-france.org>):

Director's name	Financial instrument	Type of transaction	Transaction amount (in euros)	Unit price (in euros)
<b>Alexander Cresswell</b>	Share	Sale	204,908.00	93.14
<b>Marc Darmon <sup>(a)</sup></b>	Share purchase options	Exercise	263,040.00	32.88
	Share purchase options	Exercise	52,680.00	26.34
	Share purchase options	Exercise	55,314.00	26.34
	Share purchase options	Exercise	65,760.00	32.88
	Share purchase options	Exercise	76,386.00	26.34
	Share	Sale	196,000.00	98.00
	Share	Sale	209,412.00	99.72
	Share	Sale	190,000.00	95.00
<b>Delphine Gény-Stephann</b>	Share	Acquisition	49,995.00	99.99
<b>Michel Mathieu</b>	Share purchase options	Exercise	158,040.00	26.34
	Share	Sale	312,320.00	97.60
<b>Gil Michielin</b>	Share purchase options	Exercise	28,789.62	26.34
	Share	Sale	107,463.76	98.32
<b>Pierre-Éric Pommellet</b>	Share purchase options	Exercise	39,510.00	26.34
	Share purchase options	Exercise	21,072.00	26.34
	Share purchase options	Exercise	192,044.94	26.34
	Share	Sale	132,600.00	88.40
	Share	Sale	78,280.00	97.85
	Share	Sale	686,958.02	94.22
<b>Pascale Sourisse</b>	Share purchase options	Exercise	184,380.00	26.34
	Share purchase options	Exercise	156,591.30	26.34
	Share	Sale	615,300.00	87.90
	Share	Sale	523,160.00	88.00

(a) This refers to individuals required to make a disclosure as indicated in Articles L. 621-18-2 a), b) and c) of the French Monetary and Financial Code. The individuals concerned by Article L. 621-18-2 b) of the French Monetary and Financial Code include the members of the Executive Committee.

Moreover, the final share allotment, following the purchase period provided for in the free share allotment plan regulation of 17 September 2013, resulted in statements sent to the AMF and published on its website (<http://www.amf-france.org>).

These statements related to the following individuals: Messrs. Patrice Caine, Pascal Bouchiat, Millar Crawford, Alexander Cresswell, Marc Darmon, Philippe Duhamel, Jean-Loïc Galle, Michel Mathieu, Gil Michielin and Ms. Pascale Sourisse.

### 4.2.3.8 Trading in company shares during 2017

In 2017, Thales traded in Company shares as part of its share buy-back programme drawn up in accordance with the AMF General Regulations (Article 241-1 *et seq.*).

These transactions were carried out as part of the share buy-back programme authorised at the Annual General Meeting of 18 May 2016 for transactions performed between 1 January 2017 and

17 May 2017, and in accordance with the authorisation given by the Annual General Meeting of 17 May 2016 for transactions performed between 18 May 2017 and 31 December 2017.

At 1 January 2017, Thales held 749,559 treasury shares, representing 0.35% of the capital, compared with 568,739 treasury shares at 31 December 2017.

The net balance of 2017 trading was the disposal of 180,820 shares, broken down by objective as follows:

a) Net disposal or allotment of shares to Group employees and directors in the manner stipulated by law, particularly when share purchase options are exercised or existing free shares are allotted, and employee shareholding plans	(256,820)
b) Regulation of the market price by a liquidity contract drawn up in accordance with the AFEI code of Conduct	76,000

#### Breakdown of treasury shares by objective at 31 December 2017

The total number of shares held at that date was 568,739, representing 0.27% of Thales' share capital. The breakdown by objective was as follows:

a) Disposal or allotment of shares to Group employees and directors as stipulated by law, particularly when share purchase options are exercised or existing free shares are allotted	492,739
b) Regulation of the market price by a liquidity contract drawn up in accordance with the AFEI code of Conduct	76,000

#### Market value of the portfolio at 31 December 2017

€51,118,261.32, at the closing price on 29 December 2017, i.e. €89.88.

	Aggregate gross amounts from 1 January 2017 to 31 December 2017		Positions open on the date of the programme description					
			Open purchase positions			Open sale positions		
	Purchases	Sales	Calls purchased	Puts sold	Forward purchases	Calls purchased	Puts sold	Forward sales
No. of shares	1,671,512	1,852,332	—	—	—	—	—	—
<b>Average maximum maturity</b>								
Average transaction price (in euros) including possible discounts and free shares	93.255	51.784	—	—	—	—	—	—
<b>Average exercise price</b>								
Amounts (in euros)	155,876,190	95,920,532	—	—	—	—	—	—

Thales did not make use of derivatives (futures sales) as part of this redemption programme.

## 4.3 RELATED-PARTY AGREEMENTS

### 4.3.1 Commitments and agreements authorised after year end

On the date this document was filed, three new related-party commitments covered by Article L. 225-42-1 of the French Commercial Code had been authorised by the Board of Directors since year end.

At its meeting on 5 March 2018, the Board of Directors authorised the renewal, under the terms and conditions specified below and in the 2017 Corporate Governance report (Section 3.2.2.1), of three remuneration items which had been authorised by the Board on 25 February 2015 and put in place for the benefit of the Chairman and CEO upon termination of his employment contract. As their duration is linked to that of his current term of office, it was the Board's intention to authorise them again in the event of the renewal of said term of office following the Annual General Meeting of 23 May 2018. These commitments were authorised on the condition of renewal of the term of office as director of Mr Patrice Caine by the Annual General Meeting of 23 May 2018 called to vote on the financial statements for the year ended 31 December 2017 and the renewal of his term of office as Chairman and CEO by the Board of Directors which will take place following this meeting.

These commitments were the subject of a press release dated 9 March 2018, available on the Company's website ([www.thalesgroup.com](http://www.thalesgroup.com)).

- **Compensation payments likely to be payable to Mr Patrice Caine, Chairman and CEO, upon termination of his term of office as Company representative**

Subject to the fulfilment of the performance conditions imposed by the Board of Directors and if so decided by the Board, compensation may be paid to Mr Patrice Caine, if his term of office as Company representative should be terminated, except in the case of resignation, serious misconduct or gross negligence.

The amount of compensation is fixed at 12 months of his reference salary (fixed and variable compensation paid over the last 12 months of activity, excluding long-term compensation).

The payment of this compensation will be subject to the fulfilment, as recorded by the Board, of performance conditions established by the latter subject to compliance with the following condition: the payment will be made if the average rate of achievement of the annual operational profitability objectives is equal to or higher than 80% over the past three years.

If that is not the case, no compensation payment will be due.

- **Renewal for Mr Patrice Caine, Chairman and CEO, of private employment insurance subscribed to by the Company**

Entitlement to this insurance is subject to the same performance condition as the above-mentioned compensation for the termination.

- **Commitment related to the deferred progressive and conditional compensation scheme applicable to Mr Patrice Caine, since his appointment as Chairman and CEO**

The amount of this compensation is calculated based on the point allocation method identical to that used for employees entitled to the additional group retirement scheme applicable within Thales group.

This deferred compensation is only deemed to have been acquired on condition that the Company representative has carried out a full term in office. Entitlement is subject to the same performance condition as the above-mentioned compensation for the termination.

An increase in this deferred compensation will be applied provided that the Chairman and CEO has a minimum of 10 years' service as part of the Thales Executive Committee.

More information on these three related-party commitments is provided in Section 3.2.2.1.

### 4.3.2 Commitments and agreements authorised during 2017

In 2017, one related-party agreement was authorised by the Board of Directors.

#### **Board of Directors' meeting on Tuesday, November 28, 2017**

##### **Amendment to the agreement on assistance to TSA**

At its meeting on 28 November 2017, the Board of Directors authorised certain amendments to the agreement on assistance to TSA, the signing of which was authorised by the Board of Directors on

29 September 2009. These amendments took effect on 1 December 2017, following the conclusion, on 26 January 2018, of an amendment to the agreement. At its meeting on 28 November 2017, the Board of Directors also ruled on the downgrading, with effect from these amendments, of the aforementioned agreement on assistance to a current agreement pursuant to the French Commercial Code.

Under this agreement, Thales provides TSA with assistance from the Group's specialist financial, legal and administrative services, since TSA no longer has the internal resources to operate alone.

### 4.3.3 Agreements authorised during previous financial years

The agreements authorised by the Board of Directors and approved by the Annual General Meeting in previous financial years that continued to be performed in 2017 have been disclosed to the statutory auditors in accordance with the applicable regulations. They are also described in a special report presented to the Annual General Meeting called to approve the financial statements for 2017.

#### Board of Directors' meeting held on 25 February 2015

On 25 February 2015, the Board of Directors authorised three related-party commitments under Article L. 225-42-1 of the French Commercial Code, relating to:

1. Compensation payments likely to be payable to Mr Patrice Caine, Chairman and CEO, upon termination of his term of office as Company representative.

Subject to the fulfilment of the performance conditions imposed by the Board of Directors and if so decided by the Board, compensation may be paid to Mr Patrice Caine, if his term of office as Company representative should be terminated, except in the case of resignation, serious misconduct or gross negligence.

The amount of compensation is fixed at 12 months of his reference salary (fixed and variable compensation paid over the last 12 months of activity).

Payment of this compensation will be subject to the Board's assessment as to whether the performance criteria set by the Board have been met under the following conditions:

- if the departure takes place before the end of the 2017 financial year, compensation will be paid if the average level of achievement of the targets for annual operating profit is at least 80%, depending on the financial criteria available for the period between the start and end of the term of office,
- if the departure occurs after the closure of the 2017 financial year, compensation will be paid if the average level of achievement of the targets for annual operating profit is at least 80% over the last three full financial years.

If that is not the case, no compensation payment will be due.

2. The private unemployment insurance that the Company has decided to subscribe for the benefit of Mr Patrice Caine and for which entitlement is subject to the same performance condition as the above-mentioned compensation for termination.
3. The deferred incremental and conditional compensation scheme for the "Company representative" applicable to Mr Patrice Caine, from 1 January 2015.

The amount of this compensation is calculated based on the point allocation method identical to that used for employees entitled to the additional group retirement scheme applicable within Thales group.

It is only deemed to have been acquired on the condition of carrying out a full term of office, and its benefit is subject to the achievement of the following performance condition: if the average level of achievement of the annual operating margin targets set by the Board of Directors for the Company representative is equal to or greater than 80% for the last three full financial years.

The increase in this deferred compensation is subject to a minimum of ten years' service as part of the Thales Executive Committee.

These commitments, authorised by the meeting of the Board of Directors held on 25 February 2015, were approved at the Annual General Meeting of 13 May 2015 (resolutions 14, 15 and 16, respectively). These commitments will expire, at the same time as the Chairman and CEO's current term of office, at the end of the Annual General Meeting on 23 May 2018. Their early renewal was authorised by the Board of Directors on 5 March 2018 under the terms and conditions specified in Section 4.3.1.

#### Board of Directors' meeting held on 29 September 2009

##### Assistance agreement between Thales and TSA

The services invoiced from 1 January 2017 to 30 November 2017 by Thales to TSA under the assistance agreement, covering the provision of administrative, legal and financial services provided by Thales to TSA, came to €452,833 excluding tax. This agreement was downgraded with effect from 1 December 2017 to a current agreement pursuant to Article L. 225-39 of the French Commercial Code (see Section 4.3.2).

#### Board of Directors' meeting held on 6 March 2008

##### FSTA: commitments to be undertaken by the parent company, authorised by the meeting of the Board of Directors on 6 March 2008

Having noted the characteristics of the "FSTA" public-private partnership, which has a significant importance and high visibility for the Group, and which thus consolidates its presence in the United Kingdom, the Board of Directors:

- has approved the transaction to be concluded by Thales UK Ltd in its capacity as a member and subcontractor of the consortium (Thales UK Ltd has since then assumed the subcontracting commitments of the companies Thales Avionics Ltd, Thales Training & Simulation Ltd and Thales Air Operations Ltd);
- has approved the issue of the three guarantees required (Resources and Materials parent company Guarantee, Opco Primary Subcontracts parent company Guarantee and Deed of Indemnity and Security) as per the terms submitted to it;
- has delegated to the chairman, who may sub-delegate, all powers necessary for the fulfilment of these guarantees, for the signature of any deeds or documents, and in general to do what is necessary for carrying out this operation.

For the period from 28 October 2016 to 27 October 2017, Thales invoiced Air Tanker in the amount of £312,668.00 (or €364,584.89), pursuant to letters of credit in force.

## 4.3.4 Statutory auditors' special report on related-party agreements and commitments

*This is a translation into English of a report issued in French and it is provided solely for the convenience of English-speaking users. This report should be read in conjunction with and construed in accordance with French law and professional standards applicable in France.*

To the General Shareholders' Meeting of Thales S.A.,

In our capacity as your company's statutory auditors, we hereby report to you on regulated party agreements and commitments.

It is our responsibility to report to shareholders, based on the information provided to us, on the main terms and conditions of agreements and commitments that have been indicated to us or that we may have identified as part of our engagement, without commenting on their relevance or substance or identifying any undisclosed agreements or commitments. Under the provisions of Article R. 225-31 of the French Commercial Code, it is the responsibility of the shareholders to determine whether the agreements and commitments are appropriate and should be approved.

Where applicable, it is also our responsibility to provide the shareholders with the information required by Article R. 225-31 of the French Commercial Code in relation to the implementation during the year ended 31 December 2017 of the agreements and commitments previously approved by the Shareholders' Meeting.

We performed the procedures that we deemed necessary in accordance with the guidance issued by the French Institute of statutory auditors (*Compagnie nationale des commissaires aux comptes*) for this type of engagement. These procedures consisted in verifying that the information given to us is consistent with the underlying documents.

### Agreements and commitments submitted for approval to the General Shareholders' Meeting

#### Agreements and commitments authorized and concluded during year ended 31 December 2017

In accordance with Article L. 225-40 of the French Commercial Code, we have been informed of the following agreement concluded and authorized during the year ended 31 December 2017 by the Board of Directors.

- **With TSA (shareholder of 25.76% of Thales)**

#### Amendment to the agreement on assistance to TSA

At its meeting on 28 November 2017, the Board of Directors authorized certain amendments to the agreement on assistance to TSA, the signing of which was authorized by the Board of Directors on 29 September 2009. These amendments took effect on 1 December 2017, following the conclusion, on 26 January 2018, of an amendment to the agreement. At its meeting on 28 November 2017, the Board of Directors also ruled on the downgrading, with effect from these amendments, of the aforementioned agreement on assistance to a current agreement pursuant to the French Commercial Code.

Under this agreement, Thales provides TSA with assistance from the Group's specialist financial, legal and administrative services, since TSA no longer has the internal resources to operate alone.

Royalties invoiced by Thales from 1 January to 30 November 2017 under this agreement amounted to EUR 452,833 excluding taxes.

TSA, which holds more than 10% of the voting rights of your company, is controlled by the French State in accordance with Article L. 233-3.

The persons concerned are the directors of your company proposed by the French State, namely Mrs. Laurence Brosseta.

#### Reasons justifying why the Company benefits from this agreement

Your Board of Directors has motivated this agreement as follows:

At the year ended 31 December 2017, TSA has no remaining Participating Securities and is no longer required to prepare consolidated financial

statements. As a result, the scope of services provided by Thales to TSA has been reduced.

### Agreements and commitments authorized and concluded after closing

We have been informed of the following agreements and commitments authorized and concluded by the Board of Directors, after closing.

- **With Mr. Patrice Caine, Chairman and Chief Executing Officer since 23 December 2014**

At its meeting on 5 March 2018, the Board of Directors authorized, subject to the renewal of the term of office of Mr. Patrice Caine by the General Shareholders' Meeting on 23 May 2018 called to approve the financial statements for the year ended 31 December 2017 and the renewal of the mandate of Chairman and Chief Executive Officer by the Board of Directors which will be held at the end of this General Meeting, the renewal of the following regulated commitments, already authorized by the Board of Directors held on 25 February 2015, and approved by the Shareholders' Meeting of 13 May 2015, the execution of which continued during the year ended 31 December 2017:

#### Commitment related to compensation payments likely to be payable to Mr. Patrice Caine upon termination of this term of office as Company representative

Subject to the fulfilment of the performance conditions imposed by the Board of Directors and if so decided by the Board, compensation may be paid to Mr. Patrice Caine, if his term of office as Company representative should be terminated, except in the case of resignation, serious misconduct or gross negligence.

The amount of compensation is fixed at 12 months of his reference salary (fixed and variable compensation paid over the last 12 months of activity, excluding long-term compensation).

The payment of this compensation will be subject to the fulfilment, as confirmed by the Board, of performance conditions established: namely, if the average rate of achievement of the annual operational profitability objectives is equal to or higher than 80% over the past three years.

If that is not the case, no compensation payment will be due.

#### Commitment related to a private unemployment insurance scheme for Mr. Patrice Caine

The private unemployment insurance that the Company has decided to subscribe to the benefit of Mr. Patrice Caine and for which entitlement to this insurance is subject to the same performance condition as the above-mentioned compensation for the termination.

#### Commitment related to the deferred progressive and conditional compensation scheme applicable to Mr. Patrice Caine

The amount of this compensation is calculated based on the point allocation method identical to that used for employees entitled to the additional group retirement scheme applicable within Thales group.

It is only deemed to have been acquired:

- on the condition of carrying out a full mandate, and
- is subject to the same performance condition as the above-mentioned compensation for the termination.

The annuity increase is subject to a minimum of 10 years' service as part of the Thales Executive Committee.

### Reasons justifying why the Company benefits from this agreement

These three elements were put in place after Mr. Patrice Caine had terminated his employment contract. As their duration is linked to his current mandate, the Board of Directors has decided to authorize them again in view of the renewal of this mandate at the end of the General Meeting of 23 May 2018.

### Agreements and commitments previously approved by the Shareholders' Meeting

#### Agreements and commitments approved in previous years whose implementation continued during the year ended 31 December 31 2017

In accordance with Article R. 225-30 of the French Commercial Code, we have been informed of the following agreements and commitments approved in prior years and which continued during the year ended 31 December 31 2017.

- With Thales UK, a wholly-owned subsidiary of Thales

#### Commitments to be undertaken by the parent company within the public-private partnership "FSTA"

Under the partnership public-private "FSTA", Thales granted guarantees to Thales UK Ltd, as a member of the consortium Air Tanker (Thales UK Ltd had taken over the subcontracting commitments of Thales Avionics Ltd, Thales Training & Simulation Ltd and Thales Air Operations Ltd).

At its meeting held on 6 March 2008, the Board of Directors approved the issuance of the three required guarantees ("Resources and Materials Parent Company Guarantee", "Opco Primary Subcontracts Parent Company Guarantee" and "Shareholder Deed of Indemnity and Security") as per the terms submitted to it.

Pursuant to letters of credit in force to cover the following period from 28 October 2016 to 27 October 2017, Thales invoiced Air Tanker the total amount of GBP 312,668 (EUR 364,584.89).

Courbevoie and Paris-La Défense, March 5, 2018

The statutory auditors

#### Mazars

Anne-Laure Rousselou

Jean-Marc Deslandes

#### Ernst & Young Audit

Philippe Diu

Serge Pottiez

## 4.4 STOCK MARKET INFORMATION AND FINANCIAL COMMUNICATION

### 4.4.1 Thales shares

#### 4.4.1.1 Listing markets

Thales' stock is listed on the Euronext Paris regulated market (Compartment A). It is eligible for the SRD deferred settlement system.

ISIN code<sup>(1)</sup>: FR0000121329

Reuters: TCFP.PA

Bloomberg: HO FP

#### 4.4.1.2 Index listing

At 31 December 2017, Thales stock was included in the following main indices:

- NYSE Euronext Paris indices: CAC Next 20, SBF 120, SBF 250, CAC Large60 and CAC All-Shares. The market capitalisation used to select stocks in the NYSE Euronext Paris indices is calculated on the basis of the free float<sup>(2)</sup> and not on the total number of shares outstanding. For information, based on the 2017 closing price, Thales' total market capitalisation was €19,550 million;
- international indices: DJ Euro Stoxx, FTSEurofirst 300.

#### 4.4.1.3 Share price and trading volumes on Euronext Paris

##### 4.4.1.3.1 Monthly data from January 2016 to December 2017 (share prices in euros)

	No. of trading days	No. of shares traded	Total value traded (€m)	Average daily volume	Weighted average price	Share price High	Share price Low	Closing price
<b>2017</b>								
January	22	5,563,759	494.75	252,898	88.92	92.800	85.990	86.780
February	20	5,947,267	532.04	297,363	89.46	93.920	87.200	93.000
March	23	6,531,262	588.54	283,968	90.11	93.470	87.870	90.660
<b>Q1 2017</b>	<b>65</b>	<b>18,042,288</b>	<b>1,615.33</b>	<b>277,574</b>	<b>89.530</b>	<b>93.920</b>	<b>85.990</b>	<b>90.660</b>
April	18	4,687,059	435.05	260,392	92.82	96.940	89.170	96.520
May	22	5,421,844	531.51	246,447	98.03	99.670	96.060	98.320
June	22	6,135,606	599.51	278,891	97.71	100.450	93.850	94.240
<b>Q2 2017</b>	<b>62</b>	<b>16,244,509</b>	<b>1,566.07</b>	<b>262,008</b>	<b>96.406</b>	<b>100.450</b>	<b>89.170</b>	<b>94.240</b>
July	21	5,384,116	509.83	256,386	94.69	97.470	92.350	93.590
August	23	4,493,019	422.51	195,349	94.04	96.250	91.080	93.065
September	21	5,300,997	497.73	252,428	93.89	96.350	92.210	95.734
<b>Q3 2017</b>	<b>65</b>	<b>15,178,132</b>	<b>1,430.07</b>	<b>233,510</b>	<b>94.219</b>	<b>97.470</b>	<b>91.080</b>	<b>95.734</b>
October	22	7,660,946	713.32	348,225	93.11	97.320	88.000	89.396
November	22	7,741,193	680.93	351,872	87.96	90.560	83.510	84.971
December	19	7,842,087	693.45	412,741	88.43	94.600	83.250	89.880
<b>Q4 2017</b>	<b>63</b>	<b>23,244,226</b>	<b>2,087.70</b>	<b>368,956</b>	<b>89.816</b>	<b>97.320</b>	<b>83.250</b>	<b>89.880</b>
<b>2017</b>	<b>255</b>	<b>72,709,155</b>	<b>6,699.17</b>	<b>285,134</b>	<b>92.137</b>	<b>100.450</b>	<b>83.250</b>	<b>89.880</b>

(1) International Securities Identification Numbers.

(2) As per the definition of the NYSE Euronext Indices Steering Committee (*Conseil Scientifique des Indices*), the free float corresponds to the total capital less treasury shares, shares held directly or indirectly by the founders and/or the French government, controlling interests and shares subject to a shareholders' agreement that do not fall under the above-mentioned categories and shareholdings that are deemed stable.

	No. of trading days	No. of shares traded	Total value traded (€m)	Average daily volume	Weighted average price	Share price High	Share price Low	Closing price
<b>2016</b>								
January	20	8,896,397	618.32	444,820	69.502	73.950	66.500	70.170
February	21	9,904,954	658.55	471,664	66.487	73.410	59.770	73.410
March	21	7,559,496	559.71	359,976	74.041	77.620	70.420	77.000
<b>Q1 2016</b>	<b>62</b>	<b>26,360,847</b>	<b>1,836.58</b>	<b>425,175</b>	<b>69.671</b>	<b>77.620</b>	<b>59.770</b>	<b>77.000</b>
April	21	6,293,902	479.04	299,710	76.112	79.230	74.350	75.500
May	22	6,081,556	465.59	276,434	76.558	78.110	74.620	77.785
June	22	7,432,393	550.29	337,836	74.040	77.910	67.650	75.010
<b>Q2 2016</b>	<b>65</b>	<b>19,807,851</b>	<b>1,494.92</b>	<b>304,736</b>	<b>75.471</b>	<b>79.230</b>	<b>67.650</b>	<b>75.010</b>
July	21	6,574,729	512.70	313,082	77.980	82.570	73.050	81.490
August	23	4,815,365	389.00	209,364	80.783	83.400	77.530	77.630
September	22	6,319,531	507.02	287,251	80.231	82.750	76.950	81.990
<b>Q3 2016</b>	<b>66</b>	<b>17,709,625</b>	<b>1,408.72</b>	<b>268,328</b>	<b>79.545</b>	<b>83.400</b>	<b>73.050</b>	<b>81.990</b>
October	21	6,276,943	524.30	298,902	83.528	86.100	80.360	85.770
November	20	8,527,155	763.72	426,358	89.563	93.160	83.330	92.130
December	21	5,655,754	515.59	269,322	91.162	93.330	89.230	92.130
<b>Q4 2016</b>	<b>62</b>	<b>20,459,852</b>	<b>1,803.61</b>	<b>329,998</b>	<b>88.154</b>	<b>93.330</b>	<b>80.360</b>	<b>92.130</b>
<b>2016</b>	<b>255</b>	<b>84,338,175</b>	<b>6,543.83</b>	<b>330,738</b>	<b>77.590</b>	<b>93.330</b>	<b>59.770</b>	<b>92.130</b>

#### 4.4.1.3.2 Annual data from 2016 and 2017 (share prices in euros)

##### ➤ SHARE PRICE AND PERFORMANCE

	2017	2016
Closing price	89.88	92.13
Session high	100.45	93.33
Session low	83.25	59.77
Weighted average price	92.14	77.59
Net dividend in respect of the previous year	1.60	1.36
Total shareholder return (TSR) <sup>(a)</sup>	-0.71%	35.7%
Change in Thales stock over the period (%)	-2.44%	33.3%
CAC 40 performance over the period (%)	9.3%	7.5%
CAC Next 20 performance over the period (%)	12.8%	3.6%

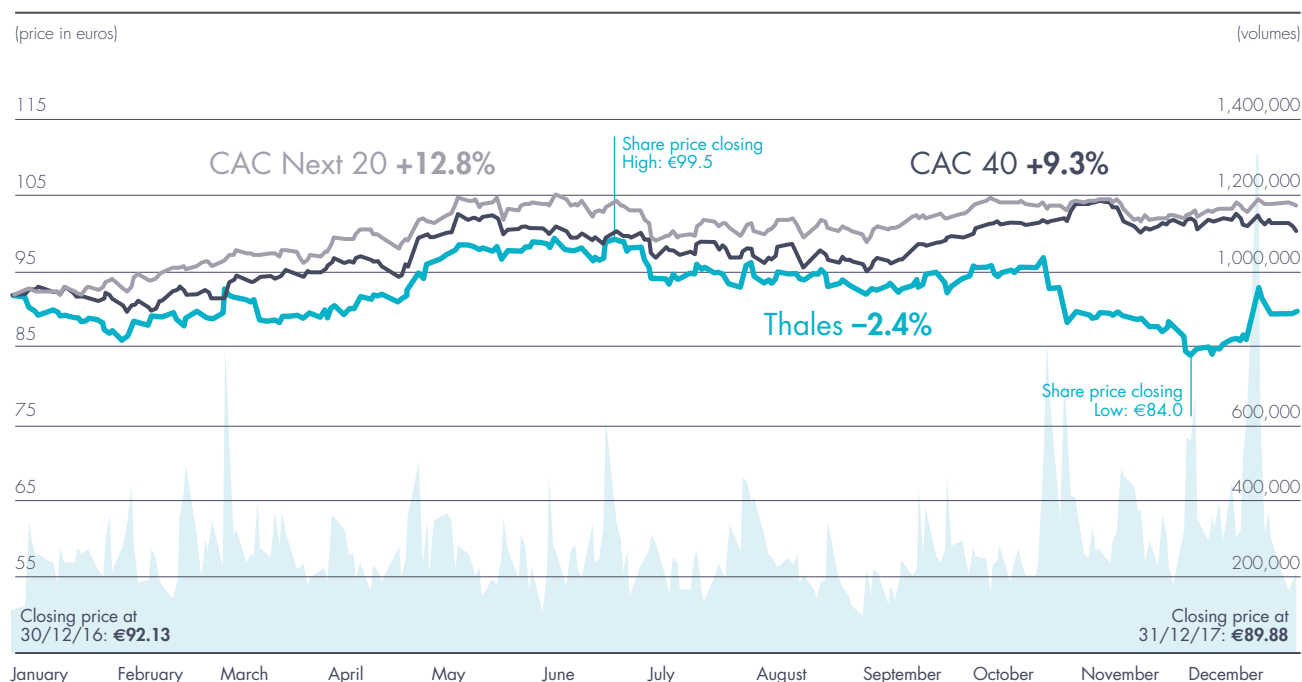
(a) Total shareholder return: differential between annual closing prices, plus dividend after tax credit paid during the year in respect of the previous year, relative to the opening price.

	2017	2016
Average number of shares traded daily (thousands)	285.1	330.7
Total number of shares traded over the period (millions)	72.7	84.3
Total value traded over the period (€ millions)	6,699.2	6,543.8
Average number of shares traded per month (thousands)	6,059	7,028
Average value traded per month (€ millions)	558.3	545.3
Total number of shares in capital (period-end, in millions)	212.7	212.2
Total number of shares in free float (period-end, in millions) <sup>(a)</sup>	104.9	104.1

(a) At the end of the period and in accordance with the definition of free float used by the NYSE Euronext Paris Indices Steering Committee.

### 4.4.1.3.3 Chart and comments on the change in price and volumes traded from 1 January 2017 to 31 December 2017

#### ➤ CHANGE IN SHARE PRICE AND TRADED VOLUMES FROM 1 JANUARY 2017 TO 31 DECEMBER 2017



#### Comments on share price in 2016 and 2017

- During 2017, the Thales share price fluctuated around €92, ending the year slightly down (-2.44%) from the start of the year, underperforming against the CAC 40 and CAC Next 20 indices, which were up +9.3% and +12.8%, respectively.
- In 2016, the Thales share price continued to increase, overperforming against the CAC 40 and CAC Next 20 indices, which were up 7.5% and 3.6%, respectively.

#### Comments on traded volumes in 2016 and 2017

- In 2017, with close to 73 million shares traded, volumes remained high, despite pulling back from 2016 levels (down 15%). Daily traded volumes reached an average of almost 285,134 shares. The volumes traded experienced occasional increases during the year: typically, at the time of announcement of the annual and interim results but also with a peak the day after the announcement of the acquisition offer made on Gemalto (close to 1.3 million shares).
- In 2016, with over 84 million shares traded, volumes remained high, despite pulling back from 2015 levels (down 16%). Daily traded volumes reached an average of almost 331,000 shares. Traded volumes experienced one-off increases throughout the year: typically, when the annual and half-year results were announced.

### 4.4.1.4 Dividend policy

Dividends are paid to the holders of shares in accordance with the law. The Company uses the Euroclear direct payment procedure.

The Board of Directors' meeting held on 5 March 2018 proposed applying a distribution rate equivalent to 37.7% of adjusted net income.

A proposal will therefore be put forward at the Thales Annual General Meeting on 23 May 2018 to pay a dividend of €1.75 per share for 2017, entirely in cash. As an interim dividend of €0.45 per share was paid in December 2017, the amount to be paid after the Annual General Meeting will relate to the balance of the dividend for 2017 of €1.30 per share.

As required by law, the per-share dividend information for the last three financial years is given below. In accordance with the French General Tax Code (Article 158-3, point 2), dividends paid in respect of 2014, 2015 and 2016 qualified for a possible tax credit.

#### ➤ DIVIDENDS PAID FOR THE PAST THREE YEARS

(in euros)	2017 restated <sup>(a)</sup>	2016	2015	2014
Dividend before tax credit	1.75	1.60	1.36	1.12

(a) Subject to the approval of the Annual General Meeting of 23 May 2018, which will vote on the 2017 financial statements. The ex-dividend date will be 30 May 2018 and the payment date will be 1 June 2018.

## 4.4.2 Financial communication policy

### 4.4.2.1 General overview

Thales' policy is to provide its shareholders with regular, clear and transparent information, in compliance with the financial reporting rules and practices applicable to listed companies.

In addition to this Registration Document submitted to the French financial markets authority (AMF), which includes details of all the consolidated financial statements and associated analysis, business activities and results by business segment, the main statutory information about the Company and its corporate responsibility policy, Thales also publishes an interim report and a letter to shareholders as well as regular press releases. Other publications include a corporate activity report with key information about the Group, a corporate social responsibility report and a social report providing a detailed description of its commitments and achievements in these areas.

All Thales information documents, presentations and financial press releases are available on the Thales website at [www.thalesgroup.com](http://www.thalesgroup.com).

Thales also holds briefings for the financial community, by teleconference where appropriate, particularly when announcing results (annual and interim financial statements and quarterly information) or important strategic or financial operations.

Regular meetings between Thales executives and institutional investors are held in Europe and North America, typically as part of roadshows, Capital Markets Days or visits to operational sites. These include a more detailed presentation of the Group's business activities and strategy.

Thales also regularly exchanges information on its corporate social responsibility policy with the Socially Responsible Investor (SRI) community. These reports cover corporate, social, environmental, governance and international trade issues, especially regarding anti-corruption measures and the control over the export of defence equipment and technologies or dual-use goods and technologies.

Finally, Thales also maintains an ongoing dialogue with international financial analysts and institutional investors to provide them with information about the Group's business activities and strategy.

### 4.4.2.2 Provisional financial reporting calendar for 2018

<b>3 May</b>	Q1 2018 financial information
<b>23 May</b>	Annual General Meeting
<b>30 May</b>	2017 ex-dividend date
<b>1 June</b>	Payment of 2017 dividend balance
<b>20 July</b>	2018 interim consolidated results
<b>18 October</b>	Q3 2018 financial information

### 4.4.2.3 Contacts

#### Investor Relations department

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Tel.: +33 1 57 77 89 02  
e-mail: [ir@thalesgroup.com](mailto:ir@thalesgroup.com)

### 4.4.2.4 Annual information document: key information for shareholders

This section lists information published in the 12 months preceding the filing of this Registration Document, pursuant to the provisions of Article 221-1-1 of the AMF General Regulations.

Thales' Articles of Association and financial information about the Group are publicly available from its website ([www.thalesgroup.com](http://www.thalesgroup.com)).

#### 2016 full year results

In the "Investor" section, under the heading "Publications/Releases & publications":

- press release – 28 February 2017: 2016 full-year results;
- presentation – 28 February 2017: 2016 full-year results;
- consolidated financial statements at 31 December 2016.

#### Quarterly information at 31 March 2017

In the "Investor" section, under the heading "Publications/Releases & publications":

- press release – 3 May 2017: orders and sales at 31 March 2017;
- presentation – 3 May 2017: orders and sales at 31 March 2017.

#### 2017 Annual General Meeting of Shareholders

In the "Investor" section, under the heading "Retail Investors/Annual General Meeting":

- meeting notice – Balo (French Legal Gazette) – 10 March 2017;
- total number of shares and voting rights as of the date of the meeting notice – Article R. 225-73-1;
- correction to meeting notice – 20 March 2017 BALO (French Legal Gazette);
- translation in English of draft resolutions (for convenience only) (21 April 2017);
- convening notice – AGM 17 May 2017;
- 2016 Registration Document;
- availability of background documents (Article R. 225-83) – AGM 17 May 2017;
- parent company social audit report & opinion of workers' council (in French only);
- legal certificate related to remunerations (in French only);
- legal certificate and information related to patronage and sponsorship (in French only);
- AGM 17 May 2017 – slideshow;
- AGM 17 May 2017 – *quorum* and vote results;
- AGM 17 May 2017 – press release.

### 2017 first-half results

In the “Investor” section, under the heading “Publications/Releases & publications”:

- press release – 26 July 2017: 2017 first-half results;
- presentation – 26 July 2017: 2017 first-half results;
- consolidated financial statements at 30 June 2017.

### Quarterly information at 30 September 2017

In the “Investor” section, under the heading “Publications/Releases & publications”:

- press release – 19 October 2017: orders and sales at 30 September 2017;
- presentation – 19 October 2017: orders and sales at 30 September 2017.

### Merger agreement between Thales and Gemalto of 17 December 2017 including a cash tender offer on all Gemalto shares

In the “Investor” section, under the heading “Publications/Releases & publications”:

- press Release – 17 December 2017

### 2017 full year results

In the “Investor” section, under the heading “Publications/Releases & publications”:

- press release – 6 March 2018: 2017 full-year results;
- presentation – 6 March 2018: 2017 full-year results;
- consolidated financial statements at 31 December 2017.

## 4.4.3 Other market securities at 31 December 2017

### 4.4.3.1 Bonds maturing in 2018, 2021 and 2023

In March 2013, Thales issued a €800 million bond, structured in the form of a five-year €500 million tranche with a coupon of 1.625% (including €300 million swapped to variable rate) and an eight-year €300 million tranche with a coupon of 2.25% (entirely swapped to

variable rate), in order to refinance the €600 million bond that matured in April 2013.

In May 2016, Thales issued a €600 million bond at a fixed rate of 0.75% (including €400 million swapped to variable rate). This bond is listed on the Paris stock exchange and matures in June 2023. It was issued to refinance the €600 million bond that matured in October 2016.

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# CORPORATE RESPONSIBILITY

> 5





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## 5.1 HUMAN RESSOURCES INFORMATION

Aware that its success depends on innovation, expertise, and collective performance, Thales has chosen to invest in sustainable and responsible relations with its employees.

The Group's long-term strategic vision "Ambition 10", the principles of which were defined in 2013, places employees at the heart of the Group's long-term growth plan.

This strategic vision is based on a talent development policy capable of attracting, developing and retaining the best talent, to support the Group's digital transformation, and to promote and deploy a leadership model as well as a culture of diversity and inclusion which measures up to the challenges that must be met by the Group.

With cohesion and commitment playing a decisive role in the Group's ability to achieve its objectives, in 2017 Thales wanted to formalise three sets of commitments towards its employees based around three unifying ideas: give everyone the opportunity to perform to their full potential, develop together in a changing world and be attentive to everyone. Through a participative initiative, the Group's employees were invited, during the second half of the year, to propose drivers and initiatives aimed at ensuring the effectiveness of these commitments and in doing so to work together to define Thales's future identity.

At the same time, Thales further developed its candidate attraction policy through measures aimed at boosting its visibility to young graduates on social networks, through more targeted content and the use of dedicated applications.

In terms of professional training, the digital transformation forms an integral part of the strategy of the Thales Learning Hub, Thales's new university, which opened on 6 September 2017 and which promotes innovative teaching methods.

Based on the conviction that innovation comes from a cross-disciplinary approach and profile diversity, during the year the Group also developed its policy in favour of diversity and inclusion, in particular through the deployment of mentoring and co-development programmes and awareness-raising actions. In this area, a communication campaign aimed at combating stereotypes and unconscious bias was rolled out across the Group.

This momentum contributes to the Group's Corporate Social Responsibility (CSR) initiative, which, since 2014, has involved executives in the highest levels of responsibility thanks to a specific CSR objective, taken into account when determining their variable compensation.

Thanks to more than 15 years of initiatives as part of its Corporate Responsibility Policy, in 2017 the Group came in on top in the Defence & Aerospace sector in the World version of the Dow Jones Sustainability Index (DJSI), which lists top-performing companies according to economic, environmental and social criteria.

Thales signed the United Nations Global Compact in 2003 and adheres to its ten principles relating to Human Rights and labour rights, which were inspired by the Universal Declaration of Human Rights and the International Labour Organization's Declaration on Fundamental Principles and Rights at Work.

Implemented on the basis of the agreements and best practices that guarantee the Group's responsible business conduct, these commitments enabled Thales to achieve the "Global Compact Advanced" level in the differentiation programme of the United Nations Global Compact beginning in 2012.

### 5.1.1 A responsible employment policy

With recognised technological expertise, a broad international presence, a wealth of talents and skills and a long tradition of innovation in all its areas of operation, the Group has been in a position to rise to the challenges of a fast-changing world. The data for 2017 demonstrate the stability of the Group's social dimension.

In comparison to the previous year, employees under Group management increased in 2017 (65,118 versus 64,071 in 2016). In addition, Thales recruited 4,708<sup>(2)</sup> employees during the year on open-ended employment contracts, demonstrating the Group's hiring momentum and attractiveness.

#### 5.1.1.1 Employment in the Group

The breakdown of the Thales group's 65,118 employees<sup>(1)</sup> by geographic area and level of responsibility demonstrates:

- its international footprint, with 30,296 employees (46.5% of total workforce), working outside France at end-2017;
- its highly qualified workforce, 77.7% of whom hold a position equivalent to engineer, specialist or manager;
- the presence of women, who make up 23% of the global workforce;
- the proportion of long-term jobs, i.e. open-ended contracts (97.8%); and
- the volume of full-time jobs (93.4%).

#### 5.1.1.1.1 Breakdown of employees worldwide

The international footprint of the Group is one of the pillars of Thales's strategy, in line with its long-term development model. While the diversity of its geographical footprint exemplifies the Group's international character, Europe remains its principal employment zone, representing 52,460 active employees, or 80.6% of total workforce. France, Australia, Canada, India and Portugal recorded the highest growth in terms of workforce.

(1) In this chapter, Thales uses the term "employee" to designate all active employees.

(2) This figure does not include the 1,469 work-study contracts in 2017. Nor does it include the conversion of short-term employment agreements or apprenticeship agreements into open-ended employment contracts. In 2016, 4,844 employees were recruited on open-ended employment contracts.

(headcount at 31 December)		2016	2017
Major countries for the Group	Germany	3,142	3,126
	Australia	3,341	3,605
	Canada	1,471	1,581
	United States	3,017	3,010
	Netherlands	1,683	1,691
	United Kingdom	6,483	6,364
Rest of Europe	Austria	315	297
	Belgium	879	873
	Denmark	112	108
	Spain	1,029	1,062
	Greece	31	40
	Italy	2,639	2,649
	Norway	217	215
	Poland	268	289
	Portugal	260	343
	Romania	234	271
	Switzerland	298	288
	Other <sup>(a)</sup>	23	22
Emerging markets	Algeria	31	30
	South Africa	143	120
	Saudi Arabia	596	551
	Brazil	178	191
	Chile	42	50
	China-Hong Kong	523	606
	South Korea	29	28
	Egypt <sup>(b)(c)</sup>		149
	India	263	385
	Israel	87	86
	Indonesia	21	20
	Japan	52	44
	Malaysia	71	49
	Morocco	38	44
	Mexico	328	286
	Middle East (excluding Saudi Arabia) <sup>(c)(d)</sup>	696	738
	Russia	24	21
	Singapore	695	709
	Taiwan	26	32
	Thailand	12	21
	Turkey	105	115
	Other <sup>(a)</sup>	172	187
France	France <sup>(e)</sup>	34,463	34,822
WORLD		64,071	65,118

(a) Other countries with fewer than twenty employees and permanent establishments: Algeria, Argentina, Azerbaijan, Bolivia, Colombia, Dominican Republic, Egypt, India, Israel, Kazakhstan, Kenya, Latvia, Panama, Peru, Turkmenistan, Qatar, Russia, Senegal, Sweden, Uzbekistan, Venezuela, Vietnam.

(b) Thales's workforce in Egypt was included in the Middle-East scope until 2016.

(c) Thales's workforce in these countries also includes the employees of permanent establishments belonging to Thales Communications & Security, one in Qatar and one in Egypt.

(d) The Middle East includes: UAE, Lebanon, Oman, Pakistan, Qatar and Bahrain.

(e) At 31 December 2017, the total workforce registered in France was 38,024.

The Group's scope of consolidation changed slightly in 2017 due to acquisitions and disposals.

	Operations	Workforce included in or removed from the Group's scope of consolidation
<b>Acquisitions</b>	USA: acquisition of Guavus	Inclusion of 250 employees
	UK: acquisition of Aveillant Ltd	Inclusion of 19 employees
<b>Disposals</b>	France: disposal of Thales Communications & Security's ID business	Removal of 80 employees from the Group's scope of consolidation

#### 5.1.1.1.2 Breakdown of active employees by operating segment

The breakdown of employees among Thales's three operating segments remained broadly unchanged in 2017.

	Defence & Security	Aerospace	Transport	Others	Total
<b>2017</b>	<b>34,011</b>	<b>18,772</b>	<b>7,005</b>	<b>5,330</b>	<b>65,118</b>
2016	33,282	18,741	6,812	5,236	64,071

#### 5.1.1.1.3 Breakdown of employees by type of contract

The majority of the Group's employees have open-ended employment contracts and work full-time. This trend is a major characteristic of Thales's workforce and applies to all of the countries where it does business. Fully 97.8% of Group employees have open-ended employment contracts and 93.4% work full-time. Lastly, the use of temporary workers has remained relatively limited; in 2017, the Group used only 2,959 temporary workers worldwide. In France, the Group's companies used 925 temporary workers (786 in 2016).

#### 5.1.1.1.4 Breakdown of employees by level of responsibility

Thales classifies all of its jobs throughout the world according to 12 levels of responsibility (LR), reflecting the skills and experience required, the complexity and importance of the objectives and the difficulties associated with the working environment. Levels 1 to 6 of the classification correspond to positions for operators, administrative staff, supervisors and technicians. Levels 7 to 12 include positions at levels equivalent to engineers, specialists or managers. At 31 December 2017, a total of 77.7% of Thales employees held a position equivalent to engineer, specialist or manager level (LR 7 to 12).

#### 5.1.1.1.5 Breakdown of employees by age bracket

Thales, in common with peer groups in the sector, reports data related to length of service with the Company and average age, which are relatively high but stable. Many employees remain with Thales throughout their career.

Thales favours both the employment of older employees (36.1% of employees are aged 50 and over) and the integration of young people (34.1% of employees are under the age of 40).

In France, 35.9% of employees are aged 50 and over and 33.2% are under 40. The average age of employees was 45 at 31 December 2017 (versus 44 at end-2016), while the average seniority was 16 years.

### 5.1.1.2 Recruitment

Thanks to an employment policy appropriate to its needs, and despite the slowdown in certain employment markets and necessary efforts to adapt in certain countries, the Group recruited 7,233 employees in 2017: 4,708 on open-ended employment contracts, 1,056 on short-term employment contracts and 1,469 on work-study contracts. Recruitment therefore remained stable compared to 2016 (7,206). France, Australia, the United Kingdom, the United States and Canada saw the most hires. A large majority of new hires were offered long-term employment.

Between 1 January and 31 December 2017, the Group signed 1,469 work-study contracts, mainly in France, Canada, the United Kingdom and China. This increase (from 1,407 contracts signed in 2016) illustrates the Group's commitment to integrating young people into the workforce.

In France, of the 3,753 employees recruited in 2017 (3,834 at end-2016), a total of 2,119 were hired on open-ended employment contracts, 1,145 on work study contracts (770 apprenticeship contracts and 375 vocational training contracts) and 489 on short-term employment contracts.

### 5.1.1.3 Departures

During 2017, a total of 5,263 employees left the Group. These departures mainly comprised resignations (2,146), retirements (1,325), dismissals (897 across the board) and the expiry of short-term employment contracts (571). Excluding expired short-term contracts, the number of departures was 4,692 (versus 4,083 in 2016).

The proportion of redundancies for economic reasons (521) remained stable compared to 2016, despite difficulties faced in some countries. Redundancies in 2017 related primarily to a decline in business in some fields and the completion of a number of projects (mainly in the United Kingdom, the United States, and Germany). Countries that had to resort to economic redundancy adopted a series of measures (such as transfers, support and outplacement) to limit the effect on employment. Some temporary external redeployment measures (temporary external mobility) were implemented to limit the number of employees made redundant for economic reasons.

In France, the total number of departures, including expired short-term employment contracts, stood at 2,417, resulting mainly from retirements (1,038), resignations (589) and expired short-term contracts (397).

### 5.1.1.4 Candidate attraction policy

To support its growth worldwide, the Group is continuing and stepping up its search for new talent through global recruitment campaigns, with the aim of hiring employees from a wide range of backgrounds in terms of gender, training, experience and culture. Thales's success and performance effectively depend on its ability to attract top talent from a variety of labour markets (both in France and abroad) and on the commitment of its employees.

#### 5.1.1.4.1 Continuity of the Group's employer brand

Unveiled in 2014, the Group's employer brand plays a key role in attracting new talent around the world and increasing diversity within teams. The Global Resourcing function is responsible for enhancing the Group's attractiveness and recruiting the talent needed to deploy the "Ambition 10" strategy. This function strengthens the Group's ability to diversify its skills and helps to boost growth in its businesses by implementing strategies that improve awareness of Thales on social media and university campuses, and in major events such as the 2017 edition of the Paris Air Show (Salon du Bourget).

The Group has also developed its recruitment site to increase its visibility and make it easier for candidates from all countries to consult available job offers.

The work carried out in 2017 to formalise the Group's commitments towards its employees is also fully in line with Thales's candidate attraction policy, as these commitments should help to meet existing employees' expectations while also attracting new talent.

#### 5.1.1.4.2 Digital and social media attractiveness

With the internet now the number one source of information and job searches, in 2017 Thales continued to step up its presence on social networks (LinkedIn, Twitter, Viadeo, Facebook, Instagram). At end-2017, the Group had more than 278,000 followers on LinkedIn.

Thales also increased its presence on sites specifically for young graduates (Jobteaser, l'Étudiant, Studyrama, Yypeek, Wizbii) and on generic job sites (Monster, RegionJob, Indeed), and advertised opportunities within the Group through new sites such as Work4us and SoNetJob.

Thales renewed partnerships with several recruitment sites in late 2017 and, through the use of the Multiposting and eQuest solutions, now multicasts job vacancies to some 50 recruitment and social media sites. This approach, which is based on channels used the most by candidates, makes it easy for them to access information about the Group, to read its latest news, to search for jobs and to apply online. A high number of applications are now received via social media, online recruitment sites and the Thales website. In France, these channels account for nearly 70% of applications (or more than 135,000).

Thales has also developed innovative interactive interfaces to encourage people to learn about the Group. Available since mid-2015, the new Thales mobile app allows users to find job vacancies and recruitment events within the Group, as well as offering the opportunity to apply via smartphone. Deployed in all countries in which Thales operates, the app helps to reinforce the Group's employer brand and presence on social media.

Thales also provides the first virtual reality recruitment experience. This unique solution which relies on "HTC Vive" technology has been deployed since June 2017 at recruitment forums and events attended by the Group and offers potential candidates the opportunity to experience and discover the Group's business activities in an interactive way.

#### Contests to boost attractiveness

Aware that electronic and cyber security profiles are rare on the employment market, Thales is continuing to take innovative action in order to attract candidates with these areas of expertise. To this end, the Group is involved in different events and challenges such as the "cyber security challenge" (European Cyber Week) and "Project Arduino".

Now in its fifth consecutive year, Project Arduino invites engineering students from around the world to put their skills to the test by developing an innovative project linked to Thales and its areas of business using an Arduino kit (printed circuit board with a programmable microcontroller). The aim of the initiative is to increase awareness of the Thales employer brand and boost the Group's appeal with a view to attracting new talent.

Working in teams, students are given three weeks to complete their project and submit a video presentation. Online voting by the general public will determine which three teams will present their project before a panel of Thales employees, who selects the winning team.

Already deployed in the United States, the United Kingdom, Singapore, France, the Netherlands, China and Hong Kong, several new countries (Portugal, Canada, UAE and Australia) took part in the 2017 edition of Project Arduino.

For the first time, "Girls on the Move", the international version of the "Elles Bougent" network, a French non-profit organisation with the role of encouraging young women to take up careers in science and technology, is acting as partner to the competition.

#### 5.1.1.4.3 Thales and the professional integration of young people

As part of its Human Resources strategy, Thales has implemented a recruitment policy for young people designed not only to respond to its hiring needs but also to help young people enter the workforce. As a training method, work-study contracts are an important component for Thales in integrating young people. In 2017, for example, the Group signed 1,469 work-study contracts worldwide, notably in France (1,145), Canada (112), the United Kingdom (94), and China (including Hong Kong) (37).

In France, at 31 December 2017, the Group's companies included 1,401 apprentices (770 of whom were hired during the year), 476 young people on vocational training contracts (375 of whom were recruited during the year) and 111 individuals with CIFRE fellowships (40 of whom were recruited during the year).

Continuing its programmes to promote young people's integration into the workforce, Thales continued to show its commitment with the signature of a new agreement with the French government on the Development of Growth and Employment, which was entered into in July 2017 for a three-year term. In particular, this agreement provides for the number of work-study students in France to be maintained at 5% of the average annual workforce.

Under this agreement, the Group has committed to approximately 6,500 new hires during the period from 1 January 2016 to 31 December 2019, including 35% candidates aged under 30 on open-ended contracts. Through this agreement, the Group has also undertaken to prioritise the recruitment of young people who have successfully completed a work-study programme within the Group, where possible depending on vacancies.

To support young people at professional baccalaureate or BEP level, currently on work-study programmes and who intend to remain in education to access a higher level of qualification (BTS, DUT), the Group also granted 23 "Prix Thales Education" bursaries in November 2017.

Each year, the Semaine de l'Industrie (Industry Week) is an opportunity for the Group's French sites to host secondary school and university students. These visits, conducted in partnership with the non-profit organisation "Elles bougent", are an opportunity to present the job roles and business activities carried out at Thales to young training students in the Group's target schools, and also to spark the interest of young female students in a career in the industry.

#### 5.1.1.4.4 Educational partnerships and links with schools and students

Students from schools and universities are all potential future Group employees. To help them all throughout their schooling and higher education and facilitate their integration into the workforce, Thales has formed a number of partnerships with schools and universities in France and abroad, notably in Australia, the Netherlands, Germany, the United Kingdom and Romania.

To strengthen Thales's links with universities, in July 2017 the Group brought together a considerable number of universities from ten countries for the "Global Academics Partner" event. This event, which was held over two days in the Paris region on the sites in Palaiseau (Research & Technology centre) and Gennevilliers (Thales Communications and Security), was devoted to the presentation of the Group's innovations in research and development and its commercial markets. It was a platform for numerous discussions in particular regarding the Group's digital strategy, cyber security, the future of big data and artificial intelligence. The event also helped to strengthen collaboration between the Group and the university sector and to further develop partnerships focused on a mutual desire to develop future technology and talent.

##### Promoting careers in science and technology

The Group is also keen to encourage an interest in science and technology careers among secondary school students.

In 2017, Thales's companies in France repeated the "First Internship with a Company" campaign in partnership with "Elles Bougent". As part of the campaign, internships were offered to young female Year-10 students to allow them to discover various aspects of the Group's business.

For the tenth year running, a number of Group sites also opened their doors to contestants of the "Je filme le métier qui me plaît" youth film contest of which Thales is a partner.

##### Our employees, our best ambassadors

In France, the Group carried out around one hundred initiatives in schools in 2017 as well as took part in some 50 forums in schools and universities supported notably by an internal network of more than 100 Campus Managers. Former students from partner schools who are now Group employees, Campus Managers act as Thales ambassadors with students sharing their experiences to help them to make better career decisions and find out more about the Group's various businesses. They represent essential links and ensure a close relationship between educational establishments, students and the Group. Thales also encourages its employees to take part in events organised by their children's schools to introduce the students to the various aspects of the business.

In 2017, Thales was also ranked the third most attractive employer for students at engineering schools in France (Universum rankings) according to the same rankings, students from engineering schools ranked Thales as the company which organised the "Best recruitment events" in 2017, demonstrating the success of its candidate attraction policy.

## 5.1.2 High-quality social dialogue

In all areas of common interest, Thales promotes cooperation with its employees and their representatives, and provides them with high-quality information, in particular by supporting and encouraging employee relations.

### 5.1.2.1 Collective bargaining

#### 5.1.2.1.1 Collective bargaining around the world

At the end of 2017, a total of 86.3% of Thales group employees worldwide were covered by collective agreements, including the European agreements signed by the Group. The companies in question can add locally negotiated agreements to this common framework. More than 60 new collective agreements were signed in France in 2017, showing the importance and dynamism of social dialogue.

By involving employee representatives at a transnational level, Thales has endeavoured to strengthen social dialogue at European level since 2009. In June 2009, Thales thus signed its first European agreement with the European Metalworkers' Federation (EMF, now IndustriAll European Trade Union) on Improving professional Development through Effective Anticipation (IDEA). The IDEA agreement concerns more than 50,000 employees and defines very specific objectives for improving employees' professional development, through some 20 or so programmes.

The momentum created at European level by the IDEA agreement led to the April 2010 signing of a second European agreement with the EMF on the Transparent annual Activity discussion for mutual Listening and developing professional Knowledge (TALK). The TALK agreement sets a clear framework and practical guidelines for conducting the Annual Activity Discussion. It defines basic principles to ensure that discussions are held in the best possible conditions and that the rights and responsibilities of all parties are respected.

#### 5.1.2.1.2 Collective bargaining in France

In France, numerous Group agreements have been signed since 2006, forming a basis that is common to all employees, whichever company they work for. This is the case, in particular, for (i) the Group Anticipation agreement, renewed in 2013, which articulates a shared and transparent approach to workforce and skills planning, (ii) the Group benefits agreement, which harmonises employee benefits, (iii) the Group framework agreement on professional gender equality (framework agreement of 13 January 2004, amended by supplemental agreement on 27 June 2012), and (iv) the Group framework agreement of 24 April 2015 on teleworking.

Thales began a new round of collective bargaining in 2017, motivated by the belief that this process contributes significantly to its economic performance while helping to improve employee working conditions. In 2017, five new structural agreements were signed at Group level in connection with this social dialogue:

- The Group agreement on the Development of Growth and Employment, dated 23 February 2017. This agreement establishes a set of measures on the following topics:
  - Social cohesion and solidarity: One of the key provisions of the agreement is to extend the legal framework allows for the allocation of rest days, the generalisation of subrogation, the payment of a supplement to the daily parental presence benefit for employees obliged to take leave for parental presence.

- Organisation of working time and support for growth:  
The agreement provides a framework for the *ad hoc* use of atypical working time and provides the option to adjust the fixed number of days worked for employees in return for an increase in their basic salary. This measure is applicable on a voluntary basis and according to annual reversibility.
- Adaptation of Employment and Growth:  
The agreement establishes measures related to recruitment, the integration of young people into business, the retention of older employee in employment and the passing on of knowledge and skills.
- The Group agreement on incentives, dated 23 February 2017 which establishes a pooled incentive plan applicable to all employees of the Group in France.
- The Group agreement on the Time Savings Account, dated 23 February 2017 which allows eligible employees, on a voluntary basis and through the investment of untaken leave or rest days and/or cash payments, to build up savings in the form of days which may in particular be used for the future funding of leave which is unpaid in principle, or for a reduction in hours to part time. While one of its main aims is to enable employees to pursue personal projects, the time savings account is also a means of boosting solidarity between the entities of the Group. Accordingly, for any contribution made in time to an individual savings account, the Company will pay the equivalent of 10% of the rights saved within a socially-responsible reserve, which may be used by any company of the Group in the event of a short-term decrease in activity.
- The Group agreement on the organisation of negotiations in connection with the project to simplify the legal structures of the Thales group in France dated 23 November 2017. This agreement establishes the procedures for the organisation of negotiations aimed at standardisation of the collective statutes applicable to employees as part of the project to simplify legal structures and to provide for the continued application, during these negotiations, of the collective statute in force.
- The Group agreement for people with disabilities dated 27 November 2017 formalised for the years 2018-2019-2020 is primarily intended to strengthen the different actions undertaken by the Group for the development of work-study programmes and the retention in employment of people with disabilities.

In addition to carrying out compulsory annual negotiations, the Group's French subsidiaries also signed several agreements in 2017. The main areas of negotiation were: gender equality, implementation of teleworking, and the adaptation of Active Employment Management measures at the relevant companies. In addition, as part of the project to simplify the Group's legal structures, transition agreements were entered into aimed at maintaining the collective agreements in force in absorbed companies for a specific period.

## 5.1.2.2 Appropriate social dialogue bodies

### 5.1.2.2.1 European Works Council

Created by an anticipation agreement, the European Works Council (EWC) comprises representatives from Thales's 11 main European countries.

It operates on the basis of:

- two ordinary Annual Plenary Meetings and further meetings convened in exceptional circumstances;
- a Select committee that meets in order to ensure regular provision of information;
- information and discussion meetings on the strategic outlook at the level of each Group Global Business Unit (GBU).

In 2017, two ordinary plenary meetings, two extraordinary plenary meetings and four meetings of the European Works Council Select committee were held. In addition, twelve information and discussion meetings took place as part of the work of the European Works Council, within the Group's business activities, to discuss the strategic and social perspectives of these activities with staff representatives.

### 5.1.2.2.2 European Anticipation Commission/National anticipation Commissions/European Convention

The European IDEA agreement stipulates that a European Anticipation Commission should be set up to conduct a forward-looking analysis of job families and discuss the annual training priorities of Thales Learning Hub. National anticipation Commissions have also been set up since 2009 in the European countries covered by the IDEA agreement. These bodies play a vital role in anticipating changes in the various job families.

### 5.1.2.2.3 Trade union coordination body at Group level in France

The Group has set up a body to coordinate representative trade unions at Group level in France. In addition to acting as the interface between the Group and the trade unions present in each of its companies, this body is responsible for addressing all negotiations with Group-wide impact and ensuring agreements are rolled out within the relevant companies. All Group agreements implemented in Thales companies in France have been entered into within this framework.

### 5.1.2.2.4 Group Works Council in France

The Thales group Works Council was created in 2000 as the result of an agreement whose provisions were revisited in conjunction with all the trade unions in 2011. The 30-member Group Works Council is a body for information, deliberation and discussion aimed at developing dialogue between corporate management and employee representatives on the position and strategic focuses of the Group's main areas of business. It is also consulted annually on Thales group-level strategic focuses. The Group Works Council met three times in plenary sessions in 2017.

## 5.1.3 Support for professional development

Thales believes that the individual development of each employee is necessary for the Group's success as a whole. In a constantly changing economic and technological environment, the Group's professional development policy relies, in particular, on forward planning, and results

in its ability, firstly, to predict key changes or innovations and to prepare action plans to deal with them, and secondly, to train and support every employee with a view to diversifying their experience, providing them with opportunities and thus designing a better career path.

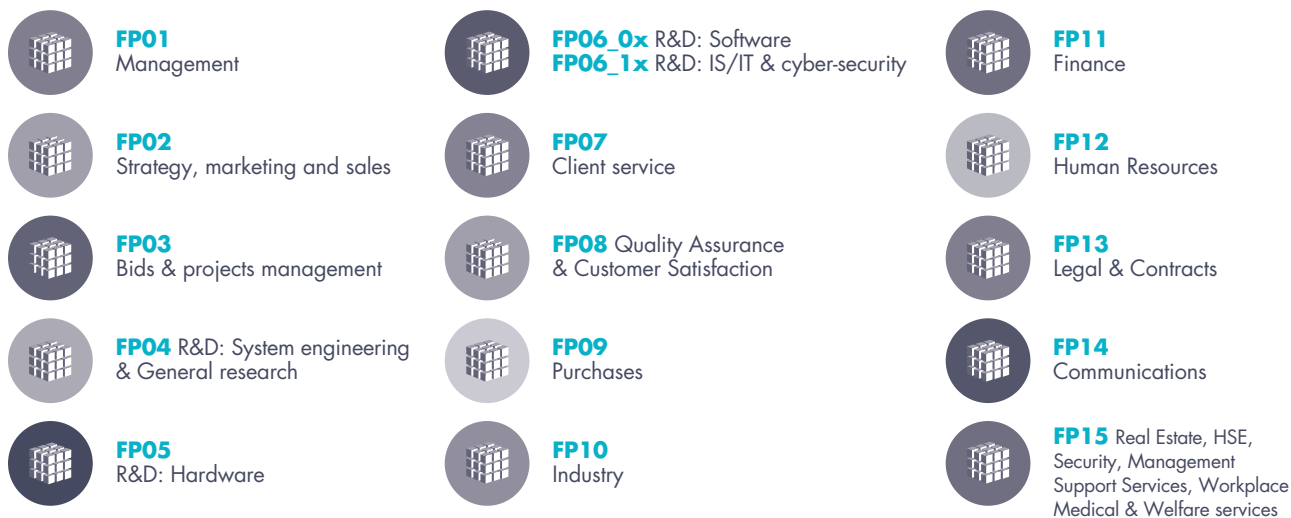
### 5.1.3.1 Management of job families

Thales has identified fifteen generic job families of equal importance for the Group's success. The architecture of these job families worldwide has been fundamentally adjusted to meet ongoing changes in the Group's markets and to better enhance employees' skills. Each job family is managed at the highest level and benefits from the expertise of an operational leader and an operational committee, an HR contact person and a training support team to anticipate changes and future trends, as well as to put forward a collective professional development action plan (covering recruitment, training, job roles to be developed, etc.).

Each job family works on its own transformation in accordance with new demands from the Group's customers and markets, the adaptation to widespread development of digital technology in the content specific to job roles or in the processes related to the activities of the job family (tools, methodologies, information exchange flows, user experience, etc.) to offer employees a shared vision of these changes and service offers to better support these changes (training, innovation, coaching, etc.).

The Group's framework is regularly adapted to take into account changes in certain job families.

#### ➤ THE VARIOUS JOB FAMILIES



#### Management of key and critical skills

In a highly competitive economic environment, employees' technical skills are a major advantage. Skills management provides substantial leverage in terms of professional development. To this end, the Group has developed a "skills management" approach for its key job families (R&D, Industry, Customer Services), centred on the identification and sharing of available technical skills. This approach, which relies on an inventory and assessment of skills, helps to anticipate operational requirements, provides practical responses to issues identified in programmes or helps to form new teams thereby securing bids and projects. It also favours the implementation of tailored development actions to meet operational requirements and gives managers the opportunity to anticipate needs and to ensure their teams' key skills are up to date, through better alignment with the agreed professional development plans (covering skills transfer, coaching, training and recruitment of specific profiles).

At end-2017, nearly 28,000 employees worldwide had already listed their skills using the tool, which is continuously being improved.

#### Management of specialists

Thales's technological innovation relies largely on a community of specialists/experts. The Group recognises their contribution at all levels of responsibility and within each job family. Thus, at a comparable level of responsibility, specialists/experts and managers are treated in an identical way based on a two-tier career development scale implemented at international level. Lateral mobility is encouraged.

### 5.1.3.2 Anticipation to help safeguard career paths

The forward-planning process, supported by negotiations with the Group's French and European social partners, contributes to the success of the job families' management mechanisms. It guides Thales's social policy in Europe, with strong involvement from three players:

- the employer, who chooses to share job-related information and actions in an effort to improve transparency and makes that information available to employees along with support mechanisms and online tools to facilitate the construction of their career plans;
- the employee, who becomes an active participant in his or her development through new and significant involvement, and who may benefit from a detailed, real-time understanding of the development of his or her job family within the Group, as well as from ongoing access to all of the mechanisms and tools in place;
- employee representatives, who, having a greater awareness of future developments in the job families, are well versed in these analysis methods and voice their opinion on the short-, medium- and long-term action plans put forward.

The Group has recognised the fundamental role played by employee representatives in setting up a forward-planning policy for changes within the various job families and job roles. In France, the Group collective agreement of 23 April 2013, which has a term of five years, forms part of the approach instigated by the agreement of 23 November 2006 aimed at developing workforce and skills planning. It also defines the conditions, procedure and measures associated with Active Employment Management in the event of foreseeable economic difficulties linked to new skills requirements, or in the case of technological breakthroughs that could have an impact on employment under certain job families.

Joint efforts by the Company and employees resulted in the implementation of Active Employment Management in the companies Thales Electron Devices and Thales Services in 2017, after their staff representatives had been informed of and consulted on the economic projections, the effects on employment and the timeliness of implementing the initiative.

### 5.1.3.3 The employee as active participant in his or her professional development

Thales believes that all employees should be active participants in their own career development plan. An analysis of the changes in job families and job roles and communication of the corresponding results enables each employee to construct a career plan in step with developments and the associated skills requirements in his or her field.

The Group also ensures that its employees receive a professional development discussion each year. This individual discussion is an important step in the process of professional development and constitutes a special opportunity for employees to take stock with their manager of how best to grow in their current role and to define their career path. This meeting also provides employees and managers with the opportunity to jointly define an action plan that includes training as well as any other initiatives aimed at professional development. During their professional development discussion each year, employees are informed by their line manager of trends in their job family and their job role, and resources that could contribute to their professional development.

In 2017, a total of 88.4% of Thales's employees worldwide had a professional development discussion with their manager (compared to 91.4% in 2016).

Thales also makes computer tools available to its employees in the form of applications that they can use to list and update their experience, skills and requests for professional development (e-HR Together), to look at job offers on the internal job board, to submit their CVs online via the application portal (e-HR Staffing), to see the training sessions that have been validated and to enrol themselves for available sessions (e-HR Training).

Career Corners have also been set up at many sites in France and the rest of Europe in order to provide a forum for information and discussion, where employees can meet with HR professionals and experts and receive individualised advice on career planning.

### 5.1.3.4 Mobility and career paths

Faced with increasingly competitive markets, employee mobility and professional development increase the Group's ability to adapt to future changes and to offer rich and varied career paths to employees. Active career management is thus encouraged.

Mobility also offers the opportunity to increase skills in a matrix organisation within which the "market" vision must fit in with the "product" vision of the Global Business Units.

Professional mobility is integral to each job family and business segment to strengthen and enhance skills. In addition, career gateways (from one job family to another, from one job role to another within the same job family, and/or from one establishment to another) are identified by the job family list applicable to the Group as a whole.

Facilitating the geographical mobility of employees is also a key issue. The Group has taken steps to help employees in this process, in particular by harmonising support measures in each of the European countries. Thales guarantees each employee access to information about job vacancies on a confidential basis in the context of internal mobility. In France, common rules have been defined to facilitate the process, whether for assistance with a change in position or a geographical relocation or both, covering relocation, help with finding housing, a moving bonus, etc. In 2017, a total of 1,054 employees relocated in France as part of a geographical mobility programme.

### International mobility

The Group has implemented several processes to encourage international mobility:

- the International Business Volunteers (V.I.E.) programme in 2017 allowed more than 75 young people aged between 18 and 28 from the European Economic Area to go on assignments of 6 to 24 months in a foreign country;
- the "Career Plus" programme, which has now absorbed the "Career 1st" initiative, matches operational needs with the desire of employees of all kinds aspiring to temporary international mobility. At end-December 2017, 112 employees on "Career Plus" were enrolled in this programme;
- the launch in 2017 of the e-JET (Job Exchange within Thales) initiative contributes to developing the Group's international culture while also attracting and retaining new talent. This programme thus gives new recruits, with more than two years' experience in their job, the opportunity to go on an exchange to a similar job abroad for a period of 6 to 12 months. Thanks to a mobile application developed to identify these exchanges, four employees have already benefited from this experience;
- other international secondments are dependent on the Group's strategy and the needs expressed by the countries of operation.

Thanks to these initiatives, at 31 December 2017, at total of 755 Group employees (coming from 28 countries of origin to 65 destination countries) were on international mobility assignments, in all business sectors.

International mobility postings are spread across every region of the world, with 26% in the Middle East, 24% in the Europe, 19% in Asia-Pacific, 16% in North and South America, and 15% in the rest of the world. Participating employees were primarily from Europe, especially France (66%), with smaller numbers from Asia-Pacific (Singapore, Australia, etc.), North America as well as some emerging economies.

In particular, these programmes should contribute to the achievement of the Group's objectives in terms of diversity.

### 5.1.3.5 Training

Thales's commitment to training stems from the view that building a successful career path means maintaining every employee's expertise at all times, as a guarantee of employability. The Group's training policy has a dual aim:

- meeting the needs of the Group's companies by implementing growth and performance improvement projects and supporting the Group's transformation;
- taking into account employees' individual aspirations in terms of skills development with regard to their job or professional mobility.

#### Key training figures for 2017

The Group's employees completed 18.5 hours on average of training in 2017, with 77.4% completing at least one training course. Overall, a total of 1,177,692 training hours were received Group-wide in 2017.

In France, the number of training hours per employee (20.08 hours) remained the same. The amount of spending on training has increased and stands at 3.98% of payroll versus 3.58% in 2016.

## Thales Learning Hub: “to share knowledge and transform Thales”

Present in ten countries<sup>(1)</sup> (representing approximately 90% of total workforce), Thales Learning Hub (formerly Thales University) contributes to employees' professional development in the various countries where the Group operates, while ensuring a common culture that reinforces cohesion around the Group's key values.

The concept of the Thales Learning Hub, founded in July 2017 to coincide with the move of the Thales University campus in Jouy-en-Josas to the Hélios site (Vélizy), embodies a training approach based on learning, meeting, sharing, facilitation and active participation for all employees. It therefore increases the importance of “Thales enseigne Thales” (Thales teaches Thales) and the idea that every employee, with their abundance of knowledge, contributes to the development of their colleagues and the Group in general.

The purpose of Thales Learning Hub is to enable employees to adapt their individual and collective skills to changing job roles, while supporting the Group's strategic goals. For several years now, the Group training body has therefore been requested to provide support in the roll-out of key transformation programmes: the Group's long-term strategic vision, “Ambition 10” and its operational offshoot, “Ambition Boost”. In 2017, more than 91,000 hours of digital training were delivered worldwide (an increase of 12.3% compared to 2016). The international digital portal was used by more than 27,600 employees in 2017, i.e. an increase of 20% compared to 2016.

In France, 14,645 employees took part in training at Thales Learning Hub in 2017, versus 14,203 in 2016. The number of training hours delivered by Thales Learning Hub in 2017 in France stood at 220,360 hours (compared to 218,198 hours in 2016). Thales Learning Hub therefore provides more than 31% of the training hours in France.

In 2017, efforts to develop the training offer continued with the introduction of new multimodal programmes comprising a range of different teaching methods and provided in the Thales Learning Hub international portal. The training offer was also enhanced through a continued focus on social learning and training in the field (engineering forums, international mentoring programmes and case studies based on real-life situations).

In the digital field, new teaching methods were developed and offered to employees: “Learning Channels” such as those created for the Welcome Convention and TDAYS (periodic meetings for the Group's Top management), digital learning communities and the participation of Thales Learning Hub in the implementation of the first Small Private Online Course (SPOC) in collaboration with the Engineering Department.

In terms of innovation, in 2017 Thales Learning Hub launched the “Quick Apply” service aimed at strengthening the principle of “co-creation” of digital content with the support of the operational departments (rapid video recording made available to employees, development of “digital capsules”).

Through these initiatives, Thales Learning Hub contributes to the emergence of a “learning organization”, where all employees can play a more active role in their training and professional development.

## Training programmes to meet the needs of the Group and its employees

In France, since 2007 training has been organised through a shared training service in order to:

- create a combined organisation to serve the Group's companies, with a joint team providing advice, administrative processes and homogeneous shared tools. This helps to optimise training purchases and financing, and centralise the securing of subsidies;
- position the companies' priorities and key Group issues around major topics such as the definition of training guidelines, key actions and the creation of training plans;
- develop expertise in training advice at the most local level in support of the Group's entities for the implementation of training plans for the benefit of employees and their professional development.

### 5.1.3.6 Development of a leadership model

In 2014, the Group promoted a new leadership model. Developed in collaboration with managers, this new leadership model defines the professional behaviour expected of leaders. It comprises six key skills<sup>(2)</sup> which are described through desirable and undesirable types of behaviour. One of the six key skills “Cooperate to succeed” was used as a guiding principle when setting the objectives of Group managers in strategic roles.

Written and published in several languages (French, English, German and Chinese), the presentation for this model was disseminated in all the Group's major countries. As it stands, the vast majority of managers have been made aware of this model either through attendance-based workshops, through modules integrated into Thales Learning Hub training sessions, or through participation in local initiatives. The training programmes for management delivered through Thales Learning Hub have been adapted based on the six key skills described in this model.

Actions aimed at developing talents based on the leadership model have been taken since 2015 in all the major countries where the Group operates in order to prepare future leaders: 360° questionnaires, development centres, project team charter, etc. At the end of 2017, more than 2,100 Group leaders had received a 360° questionnaire debriefing based on the leadership model. Since the implementation of this new leadership model, more than 1,600 leaders have had the opportunity to complete a development programme. The leadership model is now integrated into the majority of the Group's HR processes (personnel review, professional development discussion, recruitment, induction) and systematically incorporated into all collective development initiatives.

A self-perception questionnaire was also made available to all Group employees in their form for the professional development discussion, helping them to become aware of their strengths and their areas for development.

Since 2016, a platform for sharing best practices was also implemented based on the leadership model. Thanks to this platform, initiatives from around the world were shared, thereby spreading the leadership model further throughout the Group.

A specific initiative, called “Team-Up!” was also rolled out in 2016, with the aim of creating team engagement and enthusiasm for the “Ambition 10” objectives and improving their collective efficiency. Thales's Executive Committee was the first team to test the initiative, working on their collective leadership through a variety of questionnaires. Throughout 2016, most of the Group's top-level teams (Executive Committee, Global Business Units and Management Committee) took part, helping more than 300 people to improve their leadership skills. Since its launch, 80 management teams representing more than 900 people across the world have had the opportunity to benefit from this initiative.

(1) Germany, France, Italy, the Netherlands, the United Kingdom, Canada, the United States, the United Arab Emirates, Australia and Singapore.

(2) Managing complexity, acting with responsibility and ambition, succeeding through cooperation, influencing key players, engaging and developing teams, and displaying emotional intelligence.

## 5.1.4 A group employee profit-sharing policy

An integral component of its employment policy, the Group's salary policy combines collective results and individual performance. Its implementation process is based on transparency, equity and dialogue.

An Annual Activity Discussion is held at the beginning of the year between managers and each member of their teams. An ideal time to define individual objectives for the year and place them in the context of the team's collective objectives, the Annual Activity Discussion is also an opportunity to discuss the appraisal of the results achieved over the past year. Worldwide, 93.7% of employees took part in such a discussion in 2017 (94.6% in 2016).

### 5.1.4.1 Compensation and salary progression

Individual pay rises depend on fulfilment of responsibilities, achievement of annual targets, market positioning and allocated budget. Since

2000, the compensation and benefits policy applied in all Group companies has also included a global variable compensation plan for employees in a position with a level of responsibility of 8 to 12, which defines a target rate of variable pay for each level of responsibility. This variable compensation plan aims to recognise the individual results of the employees concerned (60% of the amount of variable compensation depends on the level of achievement of the annual individual targets and the ongoing goals for the role), to encourage teamwork and to give team members a stake in the business results of the Group and the Company to which they belong, as assessed by indicators.

In 2017, compensation rose by over 2.4% in France. This increase includes both individual pay rises and, for the employees concerned, the collective pay rises negotiated with the trade unions.

Payroll, including profit-sharing and incentives (excluding Naval Group) totalled €6,292 million in 2017, compared with €6,025 million in 2016. The €267 million increase in payroll from 2016 to 2017 includes a negative foreign exchange rate effect of €51 million.

(in € millions)	2016	2017
France	3,414	3,628
Europe excluding France	1,492	1,486
USA, Canada, Australia	831	874
Rest of world	288	304
<b>TOTAL</b>	<b>6,025</b>	<b>6,292</b>

Note: the changes in payroll in France shown in this table differ from the progression in average compensation of the headcount because it takes into account changes in headcount and its structure and changes in the age pyramid, as well as developments in profit-sharing and incentive schemes.

### 5.1.4.2 Incentives and profit-sharing in France

In order to strengthen the loyalty of employees beyond their local entity and solidarity among the Group's French entities, in 2004 entities in the country entered into a pooled profit-sharing agreement. The amount of the global profit-sharing reserve distributed in 2017 for financial year 2016 amounted to €50.8 million (compared with €34.8 in 2016 for 2015).

Independently of their participation in the pooled profit-sharing agreement, in 2017 a total of 22 of the Group's companies in France paid, in accordance with their incentive agreement, incentive rights for financial year 2016, totalling €38.5 million (the amount paid in 2016 for 2015 incentives was €45.2 million). Incentives are intended to involve employees in the company's results and performance.

The parent company paid €3.96 million in incentives in 2017 for 2016 compared with €4.1 million paid in 2016 for 2015.

### 5.1.4.3 Group employee savings schemes

The Group's employee savings schemes are made up of a Group savings scheme (PEG) set up in France in 1998 and, since 2007, a collective retirement savings plan (PERCO).

At 31 December 2017, the total savings under management by Group schemes amounted to €1,082 million (compared with €995 million at end-2016), held by 57,200 former and current Group employees.

#### 5.1.4.3.1 Group savings scheme (PEG) and employee shareholding

At the end of 2017, assets under management in the Group savings scheme (PEG) stood at around €718 million, including €352 million excluding the employee shareholding fund. Under the Group savings scheme, the employee shareholding fund is the main framework within which Group employees hold company shares.

Set up for the employee share offer in 1998, the fund holds shares acquired during the offers in 2000, 2002, 2004, 2008, 2011, 2013, 2015 and 2017.

At 31 December 2017, assets under management amounted to approximately €366 million, consisting of Thales company shares managed within the PEG on behalf of around 31,300 shareholders.

Including shares from free share plans, employee shareholding in Thales amounted to 2.91% of the Company's share capital at 31 December 2017.

#### 5.1.4.3.2 Collective retirement savings plan in France (PERCO)

Set up in 2007, the collective retirement savings plan (PERCO) gives employees the opportunity to set aside savings for their retirement with the Company's help. By supplemental agreement dated 29 March 2011, the parties to the original PERCO agreement changed the plan to significantly increase the amount of corporate assistance in the event of voluntary payments.

At 31 December 2017, assets under management as part of the PERCO plan amounted to €364 million, on behalf of 34,300 beneficiaries (compared with €308 million on behalf of 32,600 beneficiaries in 2016).

#### 5.1.4.4 Allotment of free shares and "phantom shares" subject to performance conditions

On 28 September 2017, Thales's Board of Directors approved a plan to allot free shares, all subject to performance conditions, to 764 French senior executives.

A plan to allot "phantom shares" (monetary equivalent of a Thales share), all subject to performance conditions, was also put in place for 307 non-French senior executives.

A total of 1,071 employees in 27 of the Group's host countries took part in these two plans.

Short- and medium-term incentive schemes lasting between two and three years have also been introduced for technicians, engineers and managers.

### 5.1.5 A safe and healthy work environment: workplace health and safety

One of the Group's key priorities is to provide a safe and healthy work environment for all employees, in compliance with applicable law, by monitoring procedures, preventing health and occupational risks and training employees.

Thales is committed to a deliberate, responsible approach to prevention and protection for the safety of the Group's employees. This commitment, included within its ethical principles, has been a driver for the Group for over 15 years and is reflected in a policy to reduce health and safety impacts and risks in its various activities worldwide, in its products and at the various levels of the organisation.

Independently of ensuring compliance with applicable regulations and anticipating future regulatory changes, this deliberate policy has two key areas of focus in terms of health and safety:

- providing a safe and healthy working environment for its employees, on its own premises and on external sites;
- design, purchase, produce and provide solutions, products and services which meet health, safety and environmental requirements.

#### 5.1.5.1 A dedicated organisation

The Group has established a global organisation designed to prevent risks related to workplace health and safety, whether at Thales sites or external sites, and to manage major health crises that could occur internationally.

Within the Group, the Human Resources and Health, Safety and Environment Departments share the vast domain of health and safety (H&S). In collaboration with the Group's medical coordinator, they define the H&S strategy, policy and processes. They coordinate good practices, and associated frameworks, rolled out in the different countries in accordance with the national legislation and constraints. They also take concrete actions in terms of prevention, health and safety in the workplace by taking into account the situation of each of the entities as regards regulatory compliance, workstation risk analysis, training and awareness plans, equipment maintenance, operational control and technological risks, as well as exercises in relation to emergency scenarios.

With a view to constantly improving its performance in terms of health, safety, and risk prevention, thanks to a network of "Health and Safety site/operations" coordinators in each country and entity, the Group has put in place a global organisation to ensure deployment of prevention measures on sites (exposure and protection of employees, risk analysis

and implementation of avoidance and tailored protection measures, etc.) and in the context of operations carried out (industrial processes, substances, external sites, etc.).

#### 5.1.5.2 A key priority: prevention and employee training

With health and safety one of the Group's key priorities, for many years Thales has conducted regular analyses and updates of environmental risks to keep pace with changes in its business activities, scientific and technical developments and emerging challenges.

This analysis, formalised through risk mapping, is intended to:

- check the conformity of business activities and products used or placed on the market;
- ensure that employees are not exposed to specific risks;
- monitor that business activities are not likely to affect the environment through technological accidents;
- analyse and anticipate the impact of new regulations.

Risk mapping consolidates an overview of areas for improvement, which are addressed via action plans both at Group level and locally. Coordinated by the Risk Assessment Committee, the process to manage these risks likely to affect employees is monitored regularly.

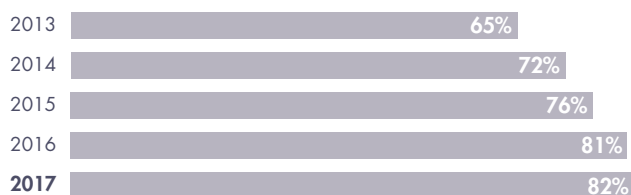
Finally, international Health and Safety Steering Committees ensure coordination of these policies.

To underpin the Group's skills in health and safety matters, dedicated training modules are also advertised in the Thales Learning Hub brochure. As well as health and safety managers, these modules target the different job families: purchasing, design, operational managers, etc.

Thanks to these initiatives, in 2017, Thales pursued its programmes with a view to instilling a real "safety culture" by through the introduction of manager involvement.

Finally, as part of its deployment of certified management systems, at 31 December 2017 the Group recorded 107 OHSAS18001 certificates representing 82% of the worldwide workforce.

### ➤ CHANGE IN NUMBER OF EMPLOYEES WORKING AT OHSAS 18001 SITES



### 5.1.5.3 Tangible measures and procedures

Practical measures in relation to employee health and safety in the workplace are also implemented by the Group's Human Resources Department and Health, Safety and Environment Department, specifically in relation to quality of life at work.

Accordingly, in France, the "quality of life at work" agreement of 4 February 2014 defined a general framework for Thales's health and safety policy and established a system for identifying and preventing occupational risks. The agreement is based on a preventive approach involving all players in occupational health. It is aimed at preventing the appearance of psychosocial risks (PSR) by paying particular attention to primary prevention, through the formalisation of actions to prevent their appearance, thanks to a unique risk assessment document for each establishment.

As the agreement of 4 February 2014 expired in 2017, negotiations were initiated in September 2017 with a view to concluding a new Group agreement on "quality of life at work".

To raise employee awareness of the importance of factoring quality of life at work into their daily activities, most Group companies in France now organise an annual "quality of life at work" Week, during which employees can attend a number of workshops and conferences in areas such as workplace well-being, the prevention of PSR and cardiovascular risks, balanced diets and sleep.

Tangible measures have also been taken to make it easier for employees to reconcile professional and personal obligations, including the creation of inter-company crèches and concierge services.

In 2017, a total of 328 management-level employees received training in psychosocial risks from Thales Learning Hub.

The Group framework agreement of 24 April 2015 on teleworking, which has since been supplemented by company agreements, is fully in line with this commitment to improve quality of life at work.

Lastly, a central "quality of life at work" committee supports all of these initiatives.

To increase employees' health and safety, as part of the annual Health, Safety and Environment campaign, an awareness raising initiative on road safety was rolled out to all Group sites. During the campaign, a series of posters was presented and distributed to employees to highlight the main dangers and train them in good habits to help to reduce risks.

Internal and external audits on working conditions are also conducted on Group sites and external sites abroad. The Corporate Health, Safety and Environment team carries out similar assessments thanks to a team of 23 qualified auditors who conducted various assignments in 2017 in several countries (India, Hong Kong, Middle East, Portugal, Norway, United Kingdom, Spain, Italy, Mexico, France, etc.).

This coincided with the actions taken to develop tools to contribute to safety management on external sites and project management.

Finally, the rollout of the LEAN culture continues within the Group with the integration of workstation cleanliness/safety.

### 5.1.5.4 Information on work-related accidents and absenteeism

Worldwide, the Group's overall absenteeism rate is 2.54%.

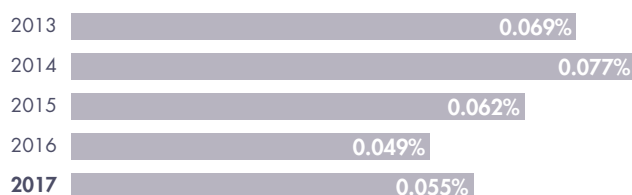
In France, the total rate of absenteeism calculated in accordance with the social report was 3.25% in 2017. This rate has been relatively unchanged for the last few years (3.27% in 2016, 3.18% in 2015). The absenteeism rate, excluding parental leave, also remained unchanged at 2.57%. The proportion of absenteeism relating to accidents at work, commuting accidents and occupational illnesses was similar to the proportion recorded in the previous year and remained consistently low.

For accidents at work, the overall frequency rate worldwide was 2.19 in 2017 and the severity rate was 0.05. The rates differ substantially for each country, depending in particular on the activities taking place there. In France, in 2017, the frequency rate of accidents at work was 2.56 and the severity rate was 0.08.

#### ➤ CHANGE IN FREQUENCY RATE (WORKING DAYS LOST DUE TO ACCIDENTS AT WORK)



#### ➤ CHANGE IN SEVERITY RATE



It should be noted that the inherent difficulty in defining the concept of occupational illness in the countries has not allowed this information to be consolidated across all countries in which the Group is established. The information on occupational illness is consequently shown only for France. In France, 1,637 working days were lost due to occupational illness in 2017.

### 5.1.5.5 Solid welfare cover

Offering employees quality health and death/disability coverage helps to support them throughout their working lives. Some countries have brought in specific measures in this regard. In France, since the conclusion of the Group agreement on welfare provisions on 23 November 2006, employees have had a harmonised collective status across all companies and identical welfare cover, whatever the legal entity concerned.

The agreement of 12 December 2016 adapted this system to reflect regulatory changes.

### 5.1.5.6 Working time

For the Group, the organisation of working time should allow a balance between work and personal life, with each country adapting working time according to the applicable legislation, regulations and agreements.

A total of 93.4% of Group employees are full-time; part-time contracts generally reflect the employee's choice.

A total of 93.4% of Group employees are covered by working time regulations, which in several countries (such as France, Spain, Germany and the Netherlands) result from collective agreements limiting working time. In all, 77.7% of Group employees are of a level equivalent to engineer, specialist or manager, which means that few employees are subject to unconventional working hours (nights, alternating shifts, etc.).

Many Group employees work on the basis of 40 hours per week. For example, Belgium, Spain, Italy, Norway, Austria, South Africa, the Netherlands, Poland, Portugal, Switzerland and China (including Hong Kong) operate a 40-hour week. In certain countries, the working week is shorter than this, pursuant to legal or contractual provisions. In the United Kingdom, most of Thales's activities are organised on the basis of a 37-hour working week. In Germany, branch collective agreements give a working time of 35, 38 or 40 hours per week, depending on the region. In France, most of the Group's companies have signed agreements implementing the 2000 framework agreement on working time which, for non-managerial staff, provides for working time of 35 hours per week on average over the year, with reduced working time days granted; for managerial staff, it provides for a flat-rate system in hours or days over the year based on 210 working days a year (excluding the country's "solidarity day").

The total amount of overtime worked in France was equal to 49,183 hours in 2017, as compared with 45,970 in 2016.

## 5.1.6 Gender equality and diversity

The commitments made by the Group and formalised in its Code of Ethics demonstrate its determination to act responsibly and fight all forms of discrimination.

Accordingly, the Group is particularly committed to promoting an inclusive approach, making everyone feel fulfilled in their roles without discrimination with respect to origins, gender, age, sexual orientation, political opinions, religion, union membership or disability.

One of the objectives of the Group's "Ambition 10" strategic visions is to build a global, diversified company.

In early 2016, the Group's Chairman announced ambitious commitments for the following years in terms of percentage of women hires (40%), access for women to positions of senior responsibility (30%) and the presence of at least three women on each management committee.

To adapt its organisation to reflect this commitment to becoming a more diverse and inclusive company and structure itself to implement the related objective, the Group created a dedicated Governance system in 2016, comprising:

- a Steering Committee made up of the members of the Group's Executive Committee and chaired by the Chairman and CEO. The Steering Committee is responsible for defining the Group's Diversity strategy, approving the allocated resources and promoting and monitoring the fulfilment of any commitments made to this end;
- a Diversity Board comprising members who are representative of the Group's various departments. The Diversity Board is primarily responsible for raising collective awareness of the concepts of inclusion, bias and stereotyping through mentoring and sponsorship initiatives and the deployment of programmes to give tangible form to Group-level commitments.

In addition, the governance system draws on existing networks such as the professional development network, the Recruitment network, the Gender Equality working group and Thales Learning Hub to ensure information on initiatives taken within the organisation is cascaded down extensively throughout the Company.

Since 2016, several actions have been taken at the initiative of the Diversity Board such as the development of a Mentoring programme which gave 28 women in important positions in the Group in Europe the opportunity to receive support and advice from a mentor to contribute to their personal and professional development, as well as various internal and external surveys which were conducted on the state of diversity and inclusion within Thales. In addition, a communication campaign was rolled out in 2017 across all of the Group's sites to combat stereotypes and unconscious biases and to make all employees aware of the challenges linked to diversity and inclusion.

This initiative, specifically targeting women in the Group, is a real springboard into positions of responsibility.

In addition, with the support of the Diversity Board and Thales Learning Hub, an awareness raising module in diversity and inclusion for all employees was developed. Various sessions in this module were held in 2017 in France and further afield, including in Singapore, Australia, the United States, India and several European countries.

This section includes the elements of the Group's policy on professional equality and equal pay as provided in Article L225-37-1 of the French Commercial Code.

### 5.1.6.1 Action to promote equality

The Group has maintained its commitment to ensuring that women are even more involved in its development, based on a committed, concrete policy supported by constructive social dialogue. The positive changes seen in recent years attest to the Group's commitment in this domain. As a result, at 31 December 2017, women made up 23% of the total workforce, 23.1% of the European workforce and 24.4% of employees in France. Within the Group, women are predominantly employed in long-term, highly skilled positions. In all, 96.8% of women employees worked under open-ended employment contracts, and 67.1% (as compared with 60.5% in 2013) held positions at a level equivalent to engineer, specialist or manager (levels of responsibility 7 to 12).

#### 5.1.6.1.1 Commitments

The Group has long been committed to proactively making advances with regard to professional equality. In 2004 in France, Thales took decisive action in this area, in cooperation with the representative trade unions (action plans were negotiated that were prepared on the basis of comparative situation reports). In Europe, the IDEA agreement signed in 2009 brought commitments in all areas of gender equality: recruitment, career development, equal compensation, and work-life balance.

Since 2014, the Group's corporate management has clearly reaffirmed its commitment to promoting gender equality at all levels of responsibility. To this end, specific action plans were devised involving all the Company's stakeholders (Executive Committee, managers, Human Resources, and employees). A dedicated organisation was set up in many countries, and exchanges of best practices were organised at Group level. Lastly, goals in terms of women's career development and/or recruitment were set in some countries, as well as in a number of Group companies.

### 5.1.6.1.2 Concrete action

- **Recruitment:** Steps taken to promote recruitment resulted in Group companies hiring 1,243 women on open-ended contracts in 2017. This brought the percentage of women among all new recruits on open-ended contracts to 26.4%, compared with 25.7% in 2016. In France, women accounted for 26.3% of total new hires on open-ended contracts.

Measures have also been taken to hire women on short-term and work-study contracts to balance out the special emphasis on recruitment through open-ended contracts. In all, 2,214 women were hired at Thales in 2017 representing 30.6% of new recruits worldwide, 31.8% in Europe and 33.3% in France. Data relating to the recruitment of women reflect the firm commitment made by some countries, including Brazil (where women made up 40.4% of new recruits), Mexico (36.7%), Portugal (36.6%) and Poland (36%).

Thales also continued its partnership with Elles Bougent, a French non-profit organisation that encourages young women to take up careers in science and technology. At end-2017, Thales had 218 Elles Bougent sponsors (a figure which continues to rise) within its workforce who offer advice to young women choosing a career path. 2017 was a particularly active year in terms of events, through which Thales took the opportunity make its contribution to young participants. Launched in March to coincide with International Women's Day, the "Girls on the move" initiative, which aims to extend the action of Elles Bougent and its partners beyond France, gave rise to the organisation, within Thales, of awareness raising actions, workshops and site visits for the benefit of young female primary and secondary school pupils and students in Germany, China and the United Kingdom. The event "Elles s'envolent au Bourget", organised on 22 June 2017, was an opportunity for 150 female secondary school pupils and students to make an unprecedented visit to the event, accompanied by six Thales women sponsors, offering them an insight into jobs in the Aerospace sector.

- **Career:** Efforts to promote the career development of women employees were increased in 2017. Stereotype awareness sessions were conducted for more than 123 managers throughout the Group in France, bringing the number of managers attending such sessions since 2013 to more than 1,450. Co-development measures have been taken in Europe to encourage the promotion of women. Since 2014, 339 female employees have taken part in personal development sessions aimed at furthering their career development. By the end of 2017, 22 female employees in Germany had been involved in a mentoring programme since the initiative's launch in 2014.

Thales encourages the creation of networks that promote gender equality in the workplace. In 2017, these networks were developed in France and abroad (Middle East and South Africa) and include more than 1,200 employees of the Group.

- **Remuneration and promotion:** Thales is vigilant in maintaining equality of treatment with respect to compensation. Since 2006, Thales has set aside an annual budget in France equal to 0.1% of payroll specifically dedicated to dealing with any unjustified gender pay gaps and promoting women. In all, 960 women benefited from this measure in 2017. The proportion of women promoted to the highest levels of responsibility (10 to 12) represented 22.9% of all promotions at these levels compared with 19.5% the previous year.
- **Work/life balance:** Thales is committed to supporting working parents and improving employees' work/life balance. In France, Thales has been involved since 2010 in setting up inter-company crèches, which, at the end of 2017, looked after 359 children. Since 2014, Germany has also offered employees from one of its sites the opportunity to reserve places in a crèche located in Ditzingen, with eight places reserved on average per month, and will now offer this service across all sites. In addition to this service for smaller children, Germany recently developed a daily childcare concept for employees with school children during school holidays, based on the organisation of workshops also aimed at raising technological awareness. The Ditzingen site was selected as the pilot for the launch of this initiative, which, if successful, should be rolled out to all German sites.

## 5.1.6.2 Diversity and inclusion

### 5.1.6.2.1 Promoting cultural diversity

As an international group, Thales respects and encourages a range of cultures in the workplace. In the context of an increasingly globalised employment market, cultural diversity has emerged as a source of wealth and contributes to the Group's strength. The Group pays particular attention to the recruitment of employees in the countries where it is present.

In France, following on from the "Intergenerational Agreement", the agreement on the Development of Growth and Employment signed on 23 February 2017 continues to promote equal opportunities, in particular through the development of partnerships with partner organisations and schools and participation in recruitment forums on diversity organised by the public authorities.

Within Thales Alenia Space in France, managers who recruited employees of foreign nationality (16.3% of recruitments in the company in 2017) were offered support through a training session on inter-culturalism.

In the Netherlands, the target of achieving a proportion of 5% recruitments of non-nationals out of all recruitments made in 2017 was exceeded, with the achievement of 6% in 2017.

In the United Kingdom, Thales became involved, in partnership with the youth charity Prince's trust, in several "Get Into" programmes, aimed at helping young people aged between 16 and 25 who are out of the schooling system or the job market to gain skills and experience to enable them to access or return to work. Currently being rolled out, the aim of this initiative is to enable the recruitment within Thales of 30% of the young people supported through the programmes, and the return of 50% of them to an educational course, training or volunteering.

### 5.1.6.2.2 Fostering generational diversity

In France, the Group's desire to give fresh impetus to its efforts by adopting innovative measures to boost employment of over-fifties led to the conclusion in 2009 of an agreement on over-fifties employment in the Thales group. This was followed in 2012 by a Group agreement known as the "Intergenerational Agreement" which expired in December 2016. The provisions from this agreement were however reworked to a large extent in the "agreement on the Development of Growth and Employment" entered into in February 2017. The provisions of this agreement were intended to prevent any risk of age discrimination, to develop the skills of over-fifties, to improve their working conditions and to take into consideration personal situations of unsuitable work or difficult work situations. Quantifiable objectives were also set, aimed at increasing the proportion of new recruits aged 55 and over to 2% of the total and increasing the proportion of employees aged 57 and over to 1.5% of the official workforce by February 2020.

In application of the agreement on the Development of Growth and Employment, the Group is also committed to continuing to develop mentoring programmes which, for a given period, pair experienced employees with new recruits or employees preparing to take on new responsibilities. These programmes form an integral part of the Group's skills transfer policy.

### 5.1.6.2.3 Disabled employment around the world

Regardless of the country in which they operate, the Group's companies make a point of complying with the legal requirements and all local regulations and recommendations designed to promote disabled employment.

While some of these national regulatory frameworks are essentially aimed at banning all forms of discrimination (the United Kingdom, the Netherlands, Australia and Norway), others (Germany, Austria, Spain, Italy and South Africa) contain an employment obligation, and companies that do not fulfil the obligation are generally made to pay a

specific contribution. In a different approach, some legislative systems (Portugal) provide financial incentives to companies that adopt a policy of recruiting people with disabilities.

Many Group companies based in various countries have also adopted a series of measures aimed at going beyond the legal requirements and promoting the employment of people with disabilities.

#### 5.1.6.2.4 Disabled employment in France

Thales has long had a Group taskforce on disabled employment in France, Mission Insertion, the Director of which leads a network of disability contacts for each labour pool. Disability Employment Commissions have also been formed within each company with 250 or more employees.

As a result of the deployment of multi-year Group agreements in France, concluded in 2004, 2007, 2011 and 2014 by unanimous agreement of the trade unions, the overall employment rate for disabled people in the Group has continued to rise to REACH 6.33% in 2016, compared with 5.9% at the end of 2015 and 5.1% in 2011. In 2017, this rate stabilised thanks to efforts to recruit and retain people with disabilities.

These results have been achieved thanks to the proactive policy implemented by Thales for over 20 years. It reinforces the actions taken to promote and facilitate the retention in employment, professional

development and integration of people with disabilities within the Group. This entire approach led to the signature in 2017 of a new agreement notably providing for the recruitment of 140 people with disabilities between 2018 and 2020, as well as 260 interns and 50 young people on work-study contracts.

One of the aims of this agreement is to implement the requirements of the AFNOR X 50-783 "Organismes Handi-accueillants" (disability-friendly organisations) standard on all sites by the end of 2019. At end-2017, 44 sites in France had undertaken initiatives in this area and 27 of them had confirmed their conformity.

Thanks to this new agreement, Thales's actions are clearly in line with its territorial policy for the training and employment of people with disabilities through four areas of focus: young people, supported employment, professional reintegration and SME support.

Similarly, partnerships concluded with education authorities and universities were continued, in order to support young people with disabilities in their studies and professional integration. Since 2016, these partnerships have been included in France's regional disabled employment plans (PRITH), the first of which was signed in the Île-de-France region.

In addition, in 2017, the Group continued to strengthen the partnerships forged in previous years with the GESAT network for sheltered and adapted employment to facilitate and enhance subcontracting to the disability-friendly sector.

## ➤ SCOPE OF VERIFICATION OF QUANTITATIVE DATA

Indicator	2017 data	Scope
<b>GLOBAL WORKFORCE<sup>(a)</sup> AT 31 DECEMBER 2017</b>	<b>65,118</b>	<b>100%</b>
<b>Workforce by country</b>		
Workforce France	34,822	100%
Workforce Europe	52,460	100%
Workforce excluding France	30,296	100%
<b>Workforce by gender</b>		
% of women	23.0%	98.4%
% of men	77.0%	98.4%
% of women in France	24.4%	100%
<b>Workforce by type of contract</b>		
% of permanent contracts	97.8%	98.4%
% of full-time contracts	93.4%	98.4%
<b>Workforce by age group</b>		
<30	11.2%	98.4%
30-39	22.9%	98.4%
40-50	29.8%	98.4%
>50	36.1%	98.4%
<b>Workforce by level of responsibility (LR)</b>		
LR 1-6	14,308	98.4%
LR 7-12	49,737	98.4%
Number of temporary staff	2,959	98.5%
<b>Departures by type</b>		
Number of departures	5,263	98.5%
% of resignations	40.8%	98.5%
% of redundancies	17.0%	98.5%
% of retirements	25.2%	98.5%
% of expiries of short-term contracts	10.8%	98.5%
% of other departures (including death)	6.2%	98.5%
<b>Recruitment</b>		
Total number of new recruits	7,233	98.5%
Of which open-ended contracts	4,708	98.5%
Of which short-term contracts	1,056	98.5%
Of which work-study contracts	1,469	98.5%
% of women	30.6%	98.5%
<b>Training</b>		
% of employees benefiting from an EDP <sup>(b)</sup>	88.4%	98.1%
% of employees trained	77.4%	98.1%
% of women trained	79.8%	98.0%
Average number of hours of training per employee	18.5	97.9%
Total number of hours of training	1,177,692	97.9%
% of employees covered by a collective agreement	86.3%	98.4%
% of employees covered by working time regulations	93.4%	98.4%

(a) Workforce shown corresponds to active workforce.

(b) EDP: professional development discussion (*Entretien de Développement Professionnel* in French).

Indicator	2017 data	Scope
<b>Health and safety</b>		
Overall absenteeism rate – World	2.54%	93.9%
Total absenteeism rate – France (social report) excluding maternity/paternity leave	2.57%	100%
Total absenteeism rate – France (social report)	3.25%	100%
Severity rate of accidents at work – World	0.05%	98.5%
Severity rate of accidents at work – France	0.08%	100%
Frequency rate of accidents at work – World	2.19%	98.5%
Frequency rate of accidents at work – France	2.56%	100%
Number of days lost due to occupational illness in France	1,637	100%
<b>Other</b>		
Payroll – World <sup>(c)</sup>	€6.292 billion	100% financial consolidation
Employment rate of people with disabilities in France	6.3%	
Number of jobs created by GERIS in 2017	210	
% of purchases from EU suppliers	71%	
% of purchases from suppliers in France	41%	
Volume of industrial subcontracting services in France	€1.62 billion	

(c) Excluding Naval Group.

## Note on methodology

### Social reporting method

The social report provides detailed information on social data, social policy and its impacts, practices and action that fall within the Group's social responsibility. It reflects Thales's international dimension. The information it contains sets out the position of the Thales group at 31 December 2017. The social report is available to download from the Group's website [www.thalesgroup.com](http://www.thalesgroup.com), in the "Commitments" section under "Key corporate responsibility documents".

### Organisation and methodology

To ensure that the data collected are accurate and reliable, a dedicated organisational structure and suitable methodology have been implemented. Thus, continuing the process initiated in 2011 with the roll-out of the e-Social Responsibility Reporting computerised reporting tool, the information contained in the social report is approved by the country directors of Human Resources. These directors have to complete a qualitative and quantitative questionnaire covering indicators that, while satisfying current legislative requirements, are also based on the indicators proposed by the Global Reporting Initiative<sup>(1)</sup> or negotiated with social partners, particularly at European level. The data reported by each country are consolidated by the Group HR Department, which checks for consistency before drafting the report.

### Scope

The definition of the companies taken into account for the purposes of preparing the social report and the Registration Document was not modified this year and is in accordance with the IFRS 10 and 11 financial consolidation standards. Workforce under Group management as at 31 December 2017 thus includes only the workforce of companies controlled by Thales within the meaning of Article L233-3 of the French Commercial Code (*Code de commerce*), as well as companies meeting those criteria but below the threshold for financial consolidation.

In addition, the Group's scope of consolidation changed slightly in 2017 due to acquisitions<sup>(2)</sup>.

Moreover, the scope of the social report is specified for each figure: for greater transparency, the percentage of employees covered is stated for all responses. For each item of quantitative data, the table of scope of verification of quantitative data provides the percentage of the workforce covered.

### Details

- Workforce under Group management as included in the Registration Document comprises all employees in each country, regardless of their contract type (open-ended, short-term or full- or part-time). It does not take into account apprenticeships or vocational training

(1) The Global Reporting Initiative (GRI) is a non-profit organisation that is developing a common working framework for drafting sustainability reports. Founded in 1997, the GRI published an initial version of its guidelines in 1999. Companies' adherence to this text is completely voluntary.

(2) In the United States, acquisition of Guavus (250 employees), in the United Kingdom, acquisition of Aveillant Ltd (19 employees) and in France, disposal of the ID business of Thales Communications & Security (removal of 80 employees from the Group's scope of consolidation).

contracts (however, the number of contracts entered into is given in the recruitment section), employees on unpaid leave, employees on sick leave (of over three months), employees on parental leave, or employees on unworked notice periods as at 31 December of the year in question.

- The total number of new recruits includes the work-study contracts concluded in 2017, but does not include the conversion of short-term employment contracts or apprenticeship contracts into open-ended employment contracts during the year. Nor does it include the conclusion of internship contracts, International Business Volunteer (VIE) agreements or CIFRE Research Training Fellowships or the transition from active to inactive employee status or vice versa.
- The total number of departures includes resignations, redundancies for economic reasons, other redundancies (data relating to mutually agreed contract terminations are recorded in this category), retirements, deaths and other types of termination, as well as expiries of short-term employment contracts.
- Data relating to absenteeism and rates of frequency and severity of accidents at work are calculated with reference to a number of days theoretically worked within countries, and based on active headcount and paid inactive employees (employees with a long-term illness do not therefore fall within the scope of calculation of this indicator).

These figures have been obtained by reconciling data entered in the HR and Environment Departments' reporting tools.

- The overall absenteeism rate corresponds to the percentage of days lost for any reason, work-related or otherwise, relative to the number of days theoretically worked in the various countries. Authorised leave such as annual leave, sabbatical leave, parental leave and personal leave is excluded.
- The total rate of absenteeism in France, calculated in accordance with the social report, corresponds to the percentage of days lost for any reason, work-related or otherwise, relative to the number of days theoretically worked. It includes authorised leave, parental leave and leave for family events.
- The frequency rate represents the number of lost-time accidents at work over the course of the year, multiplied by 1,000,000 and divided by the number of hours theoretically worked during the year.
- The severity rate represents the number of days lost due to accidents at work, multiplied by 1,000 and divided by the number of hours theoretically worked during the year.
- The employment rate for workers with disabilities corresponds to the overall number of beneficiary units (disabled workers and use of subcontracting from the disability-friendly sector).

## 5.2 ENVIRONMENTAL INFORMATION

### 5.2.1 General policy on environmental issues

#### 5.2.1.1 Long-standing commitments

Thales is committed to a deliberate, responsible approach to protection of the environment. This commitment, written into the Code of Ethics, has been a driver for the Group for over 15 years and is reflected in a policy to reduce environmental impacts and risks in its various activities worldwide, in its products and at the various levels of the organisation.

In addition to ensuring compliance with applicable regulations and anticipating future regulatory changes, the policy has four key areas of focus:

- preventing impacts on people and the environment from the Group's activities:
  - by reducing and controlling environmental risks and impacts on health,
  - by consuming fewer natural and energy resources,
  - by respecting biodiversity and cultural heritage;
- taking the environment into account in product policies and services:
  - by limiting their environmental footprint whenever possible,
  - by developing solutions that are beneficial for the environment,
  - by using the environment as a driver for innovation;
- significantly reducing our own carbon footprint, as well as that of our clients and civil society:
  - by reducing emissions from our own operations,
  - by promoting low-carbon solutions;

- fostering a spirit of innovation with regard to the environment:
  - by sharing expertise,
  - by communicating transparently,
  - by encouraging the involvement of employees, suppliers and other stakeholders.

To reinforce its commitment, the Group has set performance targets for all of its entities since 2007. Five years ago, these were extended to purchasers, and to staff involved in product policy and engineering, industry and projects.

The current goals have been set for the period 2015-2018 and relate to energy, climate, waste, environmental management of the supply chain and product design, in line with the Group's environmental challenges.

The Group is also organised to manage the anticipated gradual replacement of hazardous substances banned for use which could result in obsolescence of our products.

Finally, following on from previous actions, in particular those taken during the COP 21 events in 2015, in signing the French Business Climate Pledge<sup>(1)</sup> (11 December 2017), Thales confirmed its desire and its commitments to combating climate change (for instance by mapping direct and indirect emissions (scopes 1, 2 and 3), reducing its direct emissions and by developing innovative products and services to help its customers to reduce their emissions, etc.).

(1) French Business Climate Pledge: on the eve of the One Planet Summit on 12 December 2017, 91 French companies of all sizes and from all sectors announced the signature of a shared commitment to climate. Each of these companies put forward its actions as a committed player in the fight against global warming.

## ➤ GOALS FOR 2015-2018

2018 target

**Natural resources**

Energy consumption -3%

**CO<sub>2</sub> emissions**

Energy and substances (scopes 1 and 2) -5%

**Non-hazardous waste**

Quantity per person -5%

Recycling rates &gt;60%

**Responsible purchasing**

Evaluation of Class A and new suppliers 100%

Training for new buyers 100%

**Eco-design**

Environmental impact assessment for all new products 100%

Training for *Design Authority* line managers 50%

Detailed values are given in the table in Section 5.2.7.

## 5.2.1.2 Commitment from employees

### 5.2.1.2.1 World organisation

Aiming to consistently improve its environmental performance and prevent risks, the Group has set up an organisation that reflects its challenges. This Group Health Safety Environment Department is responsible for setting out strategy, policy, processes, methods and associated standards, and for supervising and monitoring their implementation across the Group as a whole, with global facilitation of:

- a network of “site/operations environment managers” at country and entity level, responsible for the environmental aspects of sites (buildings, infrastructure, energy, etc.) and the operations performed (industrial processes, substances, waste, external sites, etc.), bolstered by a real estate management network;
- a dedicated network of “products and services environment” managers in the Group Business Units and Business Lines in charge of integrating environmental aspects upstream of and during offer and product development phases, supported by contacts in the cross-functional services (engineering, industry, purchasing, services, offers, projects, etc.). Its purpose is also to facilitate action to anticipate and research appropriate alternative solutions to substances that are not recommended or prohibited.

At end-2017, the “sites/operations environment” network involved close to 400 people and the “environment in product design” network around 200, either full-time or by sharing time with other assignments.

Given that the environmental risks and issues in the Group’s different business lines require employees with managerial or technical skills in environmental matters, the operational management relies on these networks which are seated within a dedicated job family to enhance their skills, determine the need for recruitment and training, predict future developments and share their expertise as part of a single community.

### 5.2.1.2.2 Employee training and information

E-learning modules are available to educate Group employees on the basic aspects of environmental risk control, general themes such as eco-responsibility or specific issues such as the REACh (Registration, Evaluation and Authorisation of Chemicals) regulation, the labelling system for hazardous chemicals or climate change.

To support the environmental skills within the Group, other dedicated training modules are offered (Thales Learning Hub) which, as well as environmental managers, target the different job families: purchasing, design, sales, etc. In 2017, the training of purchasers continued (on top of the 1,058 already trained) in addition to modules for engineering managers and product developers (35% on top of the 641 already trained prior to 2016) and those responsible for product policies, to ensure the environment is taken into account in their daily work.

The Group Health – Safety – Environment Department also attends various conventions in other business lines to present the HSE strategy, challenges, individual roles in terms of HSE: supplier auditor convention, Welcome Convention to welcome newcomers, product policy convention, engineering/industry hardware seminar, R&D days.

Given that an environmental approach necessarily requires buy-in from all employees, the aim is to keep a constant eye on this theme and take it into account in day-to-day business practices. Thales offers various communication tools and forums for all employees, including a dedicated intranet, notices, competitions and events.

A collaborative IT platform specifically for Group employees across the world provides a forum for exchanging news and information about the Group. Members include personnel working in areas such as design, communications, sites and operations, in addition to those involved directly in environmental management.

### 5.2.1.3 Relations with stakeholders

#### 5.2.1.3.1 Involving suppliers

To extend its eco-responsible approach to all suppliers, Thales requires the companies with which it works to sign the Purchasing and Corporate Responsibility Charter, a contractual document intended to help them align their policies and internal processes with the principles that Thales is committed to respecting. At end-2017, 12,700 supplier sites around the world had committed to this charter.

Moreover, as part of the selection process, potential suppliers are requested to complete a self-assessment enabling them to measure the maturity of their environmental management and commit to a process of continuous improvement. This self-assessment may subsequently be verified during supplier audits conducted by Thales, which may also lead to a request for an improvement plan, or even to Thales deciding to remove a supplier from its list if certain essential criteria are not met.

To reinforce this approach, the Group Purchasing Department has set the target of assessing the environmental maturity of all of its new and class A suppliers at the end of 2018 (representing 80% of purchasing volumes). At end-2017, 7500 supplier sites underwent this assessment; 67% of the panel concerned were class A.

In the call for tenders phase, the environment is now included in the weighted criteria for supplier selection.

Thales has also maintained very close partnerships over many years with certain suppliers to work together on shared actions for progress.

#### 5.2.1.3.2 Relations with other stakeholders

Thales is committed to communicating in a totally transparent way with local authorities, as well as with its local neighbours and civil society.

Where there are particular operational requirements, sites will volunteer information on its business news and challenges, and also when certain activities are going to be exceptionally noisy, when emissions have exceeded the authorised threshold, or when a pollution incident occurs. Procedures are also in place to receive, deal with and communicate reports and requests swiftly.

To meet the requirements of civil society, investors, rating agencies and clients, Thales provides its environmental data on its website and also participates in reporting for the Carbon Disclosure Project and the Dow Jones Sustainability Index. It is also possible to send questions to the Group's Environment Department using a dedicated e-mail address.

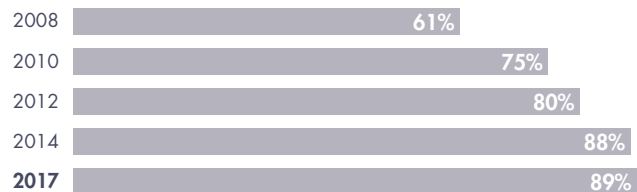
In the course of its partnerships, particularly with schools, Thales promotes preservation of the environment through programs on climate change and natural resources, or by working with universities.

### 5.2.1.4 Management and prevention of environmental risks and pollution

#### 5.2.1.4.1 Continuous improvement and prevention process

Aware of its responsibility towards the environment, Thales has fully integrated the control of environmental impacts and risks in its Group management system, which is available to all employees and in all entities worldwide.

##### ► EMPLOYEES WORKING AT ISO 14001 SITES



The Environmental Management System has been implemented at all sites as part of a dedicated process for ensuring the control and limitation of environmental risks and impacts of operational activities (buildings, industrial base, equipment and sites), the supply chain (purchases, supplier audits) and products delivered (product policy, design, bids, projects and services).

Integrated into the different processes governing the Group's activities, it defines good practices and methodological guides, as well as specifying the rules to be respected at all levels of the organisation.

It also defines the risk management and alert procedures in the event of an accident.

At end-2017, 124 Group entities were ISO 14001-certified, representing 89% of the Group's workforce. Of these sites, 86 were certified to ISO 14001:2015, which covers the management of environmental impacts of products among other things.

The planning of audits takes place on an annual basis. Audits are conducted by the internal audit teams (audit policy, maturity assessment) as well as by external auditors for ISO 14001 certification or prevention visits.

In addition, to provide support to the sites, the risk management software suite eHSE was adapted to changes in standards, particularly in relation to taking into account challenges, stakeholder demands, risks and opportunities within environmental analysis and the effectiveness of actions and associated resources.

#### 5.2.1.4.2 Risk mapping

Environmental risks are one of the risk factors that may have an impact on the Group's financial position (see Section 1.1.2.1.4). For many years, Thales has conducted regular analyses and updates of environmental risks to keep pace with changes in its business activities, scientific and technical developments and emerging challenges.

This analysis, integrated into a risk mapping, is intended to:

- ensure the compliance of activities and products;
- ensure that employees and local residents are not exposed to health and environmental risks;
- check that activities do not present a threat to the environment;
- analyse and anticipate the impact of new regulations, including on product design.

Risk mapping consolidates an overview of areas for improvement, which are addressed via action plans either at Group level or locally.

Since 2007, the Group's Risk Assessment Committee has overseen an annual evaluation of the risk management system by each of the Group's operational entities, leading if necessary to the development of an improvement plan in collaboration with Group experts.

To enhance its risk analysis of Group sites, Thales has an active policy of prevention engineering with an external partner. It aims to improve the risk profile of industrial activities on strategic sites, thus limiting potential damages (fire, natural events, pollution, machinery breakdown,

water damage, etc.) liable to cause major accidents and severely disrupt the supply chain. The prevention visits conducted on 139 sites lead to recommendations aimed at reducing the probability of incidents and preventing their consequences.

Risks related to natural disasters and water stress (risks associated with climate change) are also assessed (see Section 5.2.4.4).

Management of environmental risks also encompasses disposals or acquisitions of assets, in respect of which it is important to limit the type, value and duration of any guarantees provided or risks acquired.

Materiality of impacts	Industrial type activities	Tertiary type activities	Comments
Water consumption	Low <sup>(a)</sup>	Insignificant	(a) With the exception of an Australian industrial site for which this is significant (see paragraph 5.2.3.1.1).
Emissions in water	Low <sup>(a)</sup>	None	Tertiary sites discharge their sanitary waste water into local authority networks like any other municipal resident. Industrial sites collect and process their waste water before discharge.
Atmospheric emissions	Insignificant <sup>(a)</sup>	None	Industrial activities emit very few atmospheric pollutants.
Energy consumption	Low	Insignificant	Few energy-intensive processes. Alternative energy optimisation research work and promoting the development of eco-efficient products.
Greenhouse gas emissions (scopes 1, 2 and 3)	Moderate	Moderate	Contribution mainly to scope 3.
Production of non-hazardous waste	Low	Insignificant	Selective sorting in place.
Production of hazardous waste	Low	Insignificant	Some particularities on industrial sites using hazardous substances or primarily producing WEEE (electronics industry). Collected and disposed of through authorised channels.
Management of chemical products (obsolescence)	Low	None	Anticipation and qualification of industrial processes in accordance with regulatory timetables.
Soil pollution	Moderate	Insignificant	Some sites with a legacy of historically polluted soils under management and controlled.

#### 5.2.1.4.3 Accidents and site pollution

Since 1998, the Group has also been engaged in an extensive pollution risk assessment programme. Few sites have shown significant signs of contamination, and where contamination has been identified, it is usually due to earlier industrial activities.

When available techniques allow, steps are taken to remove pollution even if this is not a regulatory requirement. The impact on the available environmental resources is then reduced to a minimum by preferring *in situ* treatment to transferring pollution to another site. The water table is periodically monitored at industrial sites and sites located in industrial areas.

Only one Group site is a Seveso upper tier establishment. In addition to the preventive measures mentioned above and in Section 5.1.5 "A safe and healthy work environment", a safety management system (including measures such as a major accident prevention policy, an internal emergency plan and risk assessment) is deployed and inspected once a year by the Regional Directorates of the Environment, Land-Use Planning, and Housing (Direction régionale de l'environnement, de l'aménagement et du logement or DREAL) in relation to Seveso classifications.

The insurance and compensation policies for victims of accidents, including technological accidents for which the Group may be liable, cover all sites insured by the Group including the upper tier Seveso site.

Risks arising from accidents (such as fire or pollution) are managed locally, with the support of the concerned Corporate departments if necessary. Accident prevention and management procedures, as well as procedures for handling specific complaints, are in place for such cases. An accident reporting tool makes it possible to analyse accidents that do occur and draw suitable lessons from them. In 2017, 15 accidents occurred; they had no significant impact on health and the environment as corrective measures were immediately taken.

#### 5.2.1.5 Guarantees, provisions and compensation

Thales was not cited in any environmental dispute that gave rise to compensation in 2017, and only granted one generic guarantee in relation to the environment.

At 31 December 2017, the amount of reserves for environmental contingencies at Group level was €5.7 million.

## 5.2.2 Pollution and waste management

### 5.2.2.1 Limiting discharges

#### 5.2.2.1.1 Industrial atmospheric discharges

In general, Thales's activities do not generate atmospheric discharges, except for those linked to site operation (in particular heating). A few sites discharge industrial atmospheric emissions which are channelled and treated where necessary (with filters, scrubbers, etc.) and regularly checked. This primarily relates to solvents.

#### 5.2.2.1.2 Solvent discharges to the atmosphere

With the exception of the Mulwala propellant manufacturing plant in Australia, the use of solvents is mainly linked to isolated individual activities such as paintwork detailing or small-capacity component degreasing baths. The quantities used are therefore limited and it is difficult to measure atmospheric emissions as they are not channelled.

69 (out of 155) entities purchase solvents; three of these entities account for 89% of purchases. The Mulwala site alone accounts for 86% of purchases and 92% of discharges resulting from the manufacture of propellants requiring a large quantity of solvents.

It should be noted that several sites have stopped using solvents or replaced them with detergents.

#### 5.2.2.1.3 Industrial wastewater discharge

Thales's activities generate little in the way of industrial wastewater: 91% of wastewater is discharged from six sites, and 65% from the Mulwala, Australia site alone.

Consolidated wastewater discharges have fallen by 17% compared with 2012, as a result of ongoing plant optimisation and modernisation measures and wastewater recycling.

Some sites that are not connected to public networks discharge their industrial wastewater into surface water, after treatment, in accordance with regulations, and with the approval of local authorities.

### 5.2.2.2 Fighting pollution

#### 5.2.2.2.1 Noise

Noise is also a concern for Thales, despite the fact that its activities generate little in the way of noise pollution. Cooling systems are the most common sources of noise pollution, and precautions are taken to limit noise levels associated with this equipment. Sound levels are checked periodically. The few sites where noise is a particular issue are equipped with acoustic attenuation systems, or only conduct noise-generating activities within specific time periods. The increasing use of computer simulations for pyrotechnic testing, for example, also helps to reduce noise.

#### 5.2.2.2.2 Odours

Thales's activities do not generally generate odour, except for one entity where systems to capture atmospheric emissions have been installed and are regularly checked. The redevelopment under way at this site will modernise the facility concerned and eliminate these odours.

## 5.2.3 Circular economy

### 5.2.3.1 Sustainable use of resources

For several years, Thales has been developing a specific strategy for natural resources and has launched various schemes to help manage and reduce consumption, including in relation to the energy efficiency of buildings and industrial processes, optimisation of water use and the reuse of materials. To support these measures, it is crucial to raise employee awareness of best practices.

#### 5.2.3.1.1 Water consumption

Water is a vital resource to be protected. Accordingly, since 2000, Thales has been engaged in a far-reaching programme to reduce its consumption by, among other things, dealing with leaks, centralising the management of its networks, replacing water-intensive equipment, optimising industrial processes and reusing water in industrial processes.

	2012-2015*	2015*-2017
Water consumption (cubic metres)	-11%	3%

\* At constant scope of consolidation over the period.

The increase in water consumption over the period 2015-2017 is due to one site which installed a geothermal facility pumping ground water at 12°C for process cooling (furnaces, test benches) which is entirely returned to the natural environment.

The Group's overall consumption is down 8% since 2012 confirming the collective efforts made by all sites (including the Mulwala site which alone accounts for 36% of the Group's water consumption). These achievements are due to increased employee awareness and to widespread use of best practices.

#### 5.2.3.1.2 Consumption of raw materials

Thales designs, develops and supplies equipment, systems and services in aeronautics, space, transport, security and defence. The raw materials consumed by Thales are natural resources (see Sections 5.2.3.1 and 5.2.3.3) and various materials used in the manufacture of products by Thales and its subcontractors.

The search for new technologies and the design of new equipment involve restricting the use of materials to cut down on size and mass and to facilitate dismantling (see Section 5.2.6), as well as replacing the most toxic substances for health and the environment. These requirements are conveyed to suppliers of the equipment and components that Thales assembles at its sites.

The manufacturing processes are also optimised to limit loss of materials and amounts of discharge and waste. The process of additive manufacturing (also called 3D printing), for example, is now used by Thales to manufacture parts in the space domain (opening of its new Thales 3D Morocco site in Casablanca in 2017). Boasting a low consumption of raw materials, this new technology also makes it easier to repair parts.

The principle is based on the manufacture of parts, not by removing material, but by adding successive layers of powder (metal, plastic) agglomerated by means of a laser or electron beam, solely in places where material is necessary. Thales thus produces monobloc antenna supports in aluminium.

Thales has also reduced the use of materials such as wood, cardboard and plastic by limiting and reusing packaging either for supplies on Thales sites or for the transfer of equipment from one site to another and fully integrates the eco-design concept into the development of its new products to reduce the environmental footprint of Thales and the customers who use its products in all areas where it is technically and economically viable.

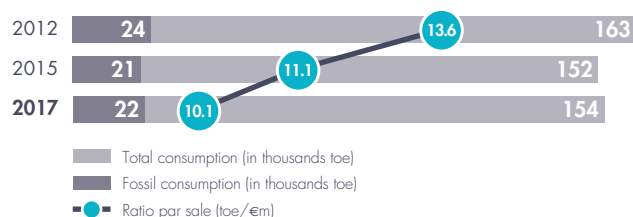
### 5.2.3.1.3 Energy consumption

Aware of the energy challenge, Thales sets goals to reduce energy consumption, which has declined even with production increases on the sites that consume the most energy (in 2017: increase in capacity, new facilities and/or site extension).

	2012-2015*	2015*-2017
Energy consumption (toe/€k)	-7%	1%

\* At constant scope of consolidation over the period.

### ➤ CHANGE IN ENERGY CONSUMPTION \*



\* At constant 2012 scope.

To achieve this energy efficiency, various audits have been conducted at some of the sites with the highest consumption. These have given rise to reduction programmes being rolled out at all Group sites. The actions taken are mainly connected to lighting, office equipment, heating, air conditioning and process-related equipment. Thales is redoubling its efforts to manage parameters such as heating temperature, plant operating schedules and the replacement of energy-intensive equipment.

At the same time, some Group entities have taken steps towards ISO 50001 certification for energy management systems. At end-2017, 33 entities were ISO 50001-certified, representing 26% of the Group's workforce.

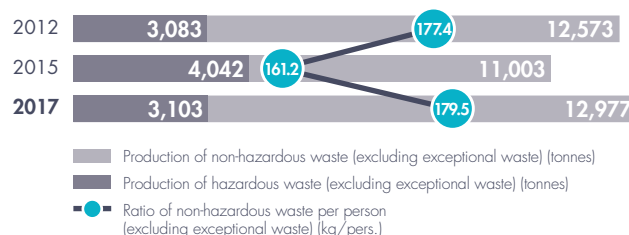
The Group's carbon footprint has also been reduced by restricting the use of fossil fuels (gas, fuel oil and coal), with their consumption in relation to sales continuing to fall in 2017 (down 7% compared with 2012). The percentage of electricity from renewable sources now represents 17% of electricity consumption.

## 5.2.3.2 Waste prevention and management

### 5.2.3.2.1 Preventing waste production; recycling, reusing, recovering and eliminating waste

In view of its waste targets, Thales has sought to reduce the quantity of waste it produces since 2012, as well as the amount sent to landfill and recycling.

### ➤ CHANGE IN WASTE PRODUCTION



The increase in the production of non-hazardous waste in 2017 is thanks to a multi-year cycle for the disposal of process sludge and metals on the Mulwala site, and to multiple works on the sites generating exceptional quantities which could not be segregated from those produced through the sites' activities.

As a result of measures taken since 2007, 83% of all waste (excluding exceptional waste) was recovered and 51% was recycled in 2017.

To achieve this, various measures related to selective waste sorting, the search for recycling channels or optimum treatment channels and campaigns to change habits and behaviour (printing policy and reusing cardboard and other packaging, for example) have been introduced. These measures are aimed at reducing waste production and improving waste treatment.

For instance, the amount of waste paper and packaging fell by 9% and 2.5% respectively compared to 2012, with the Group increasingly adopting a digitisation policy.

Certain Group sites reuse packaging either for procurement on Thales sites or to transfer equipment from one site to another.

Hazardous waste has also been a specific target. Dedicated areas for collection and storage have helped to manage this type of waste prior to disposal. The quantity of such waste has decreased consistently since 2015.

### 5.2.3.2.2 Food waste

Food services companies manage the corporate restaurants at the majority of Thales sites. It is therefore their responsibility to communicate about eating habits and food waste management which are strongly encouraged to reduce food waste.

At the few sites in charge of their own food services, communication campaigns targeting employees have been carried out.

## 5.2.3.3 Land use

The Group considers environmental criteria when choosing locations for its sites, looking at climate and geological risks, the impact of its activities on the human and natural environment, and land use. The objective is to optimise compatibility between the Group's activities and the environment. Some activities, such as pyrotechnics, require a specific site due to the risks they generate and need to be bounded by extensive security areas and suitable geology. These areas account for approximately 80% of areas occupied by the Group (two sites in Australia and one in France). However, steps are taken to enhance their ecological value either by promoting biodiversity or by converting them into pasture or farm land. Due to their activity, the majority of other Group sites tend to be in industrial areas (53% of land area excluding pyrotechnics sites).

Soil erosion is another factor taken into account, locally via impact studies and associated control measures where required by the context.

For the past 20 years, the Group has also been engaged in an extensive pollution risk assessment programme for soil and groundwater (See Section 5.2.1.4.3). Action and control plans are developed for this purpose.

## 5.2.4 Fighting climate change

### 5.2.4.1 Commitment to climate

Climate change is a major challenge which Thales wishes to address in a consistent manner by reducing its CO<sub>2</sub> emissions at source, as well as by contributing to a better understanding of climate impacts and a reduction in its customers' emissions and those of civil society, thanks to its innovative solutions or through the design of eco-responsible solutions.

Since 2015, to assert its commitment to combating climate change, Thales, along with a number of other large companies and international organisations, has signed the "Business Proposals for COP21<sup>(1)</sup>", the aim of which is to confirm corporate commitments on climate. Thales has also exhibited its innovative solutions to combat climate change at the Galerie des Solutions (solutions exhibition) in Paris in 2015, at the COP22 in Marrakesh in 2016 and, through the signature of the French Business Climate Pledge<sup>(2)</sup> (11 December 2017), the Group recently confirmed its desire and commitments to combating climate change.

Moreover, since 2005, Thales has chosen to communicate in a totally transparent way about its climate strategy to the Carbon Disclosure Project<sup>(3)</sup>, an association which aims to inform the investment decisions made by its institutional members, by telling them about the consequences

of climate change for companies. In 2017, Thales's rating remained A- for its "climate change" performance, confirming its position as one of the best-performing companies listed.

### 5.2.4.2 Reduction of greenhouse gas emissions from operations

To measure its greenhouse gas emissions, for over 10 years Thales has developed a methodology that is consistent with its operations and is based on the Greenhouse Gas Protocol created by the World Resources Institute (WRI) and the World Business Council for Sustainable Development (WBCSD). The main material sources identified have been evaluated (see table below). Working methods are in place to evaluate other sources that could be material, such as procurement of products and services and use of goods and services produced (see Section 5.2.4.3.1). Thanks to this, in 2017 the mapping of emissions for scope 3 was completed and the reliability of methods put in place was assessed. This work will continue in 2018.

	2017	2016	2015	2012
Scope 1 <sup>(a)</sup>	85,563	81,870	87,720	96,845
Scope 2 <sup>(b)</sup>	136,114	134,372	136,451	153,312
<b>Sub-total (1+2)</b>	<b>221,677</b>	<b>216,242</b>	<b>224,171</b>	<b>250,157</b>
Business travel	77,355	80,898	79,012	81,238
<b>TOTAL (in tonnes)</b>	<b>299,032</b>	<b>297,140</b>	<b>303,183</b>	<b>331,395</b>
Use of products and services sold <sup>(c)</sup>	563,483			

The Scopes combine CO<sub>2</sub> emissions (calculated with emission factors from the GHG Protocol 2012) relating to:

(a) Gas, coal, fuel oil, substances, mobile energy sources.

(b) Electricity and steam.

(c) Not included in the total as only part of the scope is covered.

In order to reduce its CO<sub>2</sub> emissions, Thales is increasing efforts specifically with regard to energy, substances and transportation.

Refurbishing and renovating certain buildings to higher ecological standards and changing equipment and consumption habits are all measures taken to improve energy efficiency and thereby help to reduce direct CO<sub>2</sub> emissions. Environmental criteria are incorporated in the selection of buildings, new locations and equipment (architecture, materials, building management system, comfort, access, etc.), as is the case for the new Thales (parent company) head offices in Paris, Thales Austria GmbH, Thales USA Inc and Thales Deutschland GmbH, which are certified compliant with the LEED and BREAM standards and where energy performance has been optimised. The energy efficiency of industrial processes has also been optimised where possible.

Along with energy, products with high global warming potential, used mainly in refrigeration systems, are subject to monitoring and reduction plans. Several sites have replaced a number of high-emission refrigerants with equipment containing lower-emission refrigerant fluids.

Particular attention is paid to sulphur hexafluoride (SF<sub>6</sub>). This gas, used in a specific industrial process to insulate electronic tubes during

high-voltage tests, has very high global warming potential. It is used by very few sites; those that do use it have implemented ambitious plans to reduce emissions, such as manufacturing tubes without using SF<sub>6</sub> or modifying equipment using this gas. They have also rolled out training and awareness campaigns for employees concerned by the environmental impact of SF<sub>6</sub> and/or implemented specific monitoring of incoming and outgoing SF<sub>6</sub> by workshop. This helped reduce emissions by 71% between 2012 and 2017. In 2017, SF<sub>6</sub> only accounted for 11% of CO<sub>2</sub> emissions due to refrigerant fluids.

Thales is also increasing its initiatives to reduce emissions from business travel by making use of a travel policy, modern information technologies, carpooling, electric vehicles and travel diagnostics and by highlighting the benefits of alternative means of transport to its employees and efficient communication tools. These initiatives led to a reduction in CO<sub>2</sub> emissions of 4% and 26%, respectively, for company vehicles and rental vehicles between 2015 and 2017.

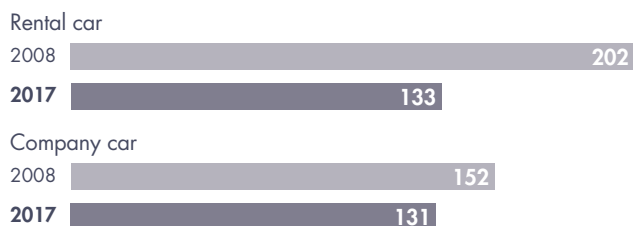
Through its employment policy, Thales also promotes the development of solutions for smart solutions to promote carpooling, the use of public transport and cycling.

(1) Business Proposals for COP21: proposals signed by 59 companies which committed to contributing to the low-carbon transition by demanding constructive dialogue between states and companies, a carbon price to be set, increased investments in the research of low-carbon solutions and a step up in R&D and innovation.

(2) French Business Climate Pledge: on the eve of the One Planet Summit on 12 December 2017, 91 French companies of all sizes and from all sectors announced the signature of a shared commitment to climate. Each of these companies put forward its actions as a committed player in the fight against global warming.

(3) Carbon Disclosure Project: an international non-profit organisation, which enables companies, cities, states and regions to measure and manage their environmental impacts, and investors and policy-makers to make more informed decisions by explaining to them the consequences of climate change.

### ➤ AVERAGE VEHICLE CO<sub>2</sub> EMISSIONS (G/KM)



## 5.2.4.3 Contribution to fighting climate change

### 5.2.4.3.1 Innovative climate solutions

Worldwide economic development, increasing urbanisation and changing lifestyles all have an impact on smart requirements in terms of travel, connectivity and resource management. At the same time, climate change has serious consequences for the planet and for the lives of its inhabitants.

Society, which is becoming increasingly technological, faces new environmental challenges as regards energy, air quality, noise, climate change, biodiversity and other issues, which governments, municipalities, economic and scientific operators and citizens must address, while offering an improved work/life balance.

Thales therefore puts innovation at the heart of its strategy, developing equipment that combines innovative technologies and a reduction in the environmental footprint. To achieve this, Thales leverages its technical expertise and its capacity for innovation in order to understand the environment, support the development of air traffic and create the right conditions for sustainable mobility and communication, and smart cities, while reducing the environmental footprint.

Section 5.2.6 discusses how Thales's solutions contribute to environmental protection and particularly to initiatives to combat and adapt to climate change. Because Thales supplies numerous solutions to clients for integration in other systems (B2B), it is difficult to measure their specific environmental footprint – particularly as concerns CO<sub>2</sub> – as the conditions of use and decommissioning are unknown. Examples include equipment embedded on board aircraft and trains. However, impact analysis based on environmental studies (simplified life cycle assessments) has been conducted on a wide variety of equipment produced by Thales using "average" hypotheses of the above-mentioned conditions. It emerged that the use phase accounts for around 90% of environmental impacts, with this impact strongly influenced by the equipment's long service lifetime. Work conducted during the design phase to improve energy efficiency and to reduce the weight of equipment built into mobile systems are the two main drivers in reducing their environmental impacts.

Working methods are in place to analyse this footprint including CO<sub>2</sub> emissions (see Section 5.2.6) and the translation of these elements into technical requirements allows for them to be taken into account in engineering and development phases. In addition, practices relating to eco-design have been defined and are currently being rolled out through the framework.

### 5.2.4.3.2 A key player in major programmes

Thales is present in the space market as well as the air, rail and road transport markets and is positioned as a key player in major national, European and international programmes such as:

#### Clean Sky

Thales is a founding member of the European aeronautics research program Clean Sky, whose environmental goals for 2020 include a 50% reduction in CO<sub>2</sub> emissions, an 80% reduction in NO<sub>x</sub> (nitrogen

oxide) emissions, a 50% reduction in perceived noise and a green life cycle for products (design, manufacture, maintenance and disposal/recycling).

In particular, Thales is leading a Clean Sky research initiative entitled "Systems for Green Operations" which should optimise aircraft fuel consumption by improving flight trajectories, in particular during the take-off and approach phases.

As part of Thales's activities, changes in cockpits, electricity generation, simulators, air traffic and satellite communication are all stakeholders in these European studies. Paper-based studies and demonstrator parts have been carried out for theoretical assessments of potential gains.

Based on models developed by the aircraft manufacturer, the results can be used to estimate and test changes arising from this programme for CO<sub>2</sub> savings in the aircraft with new materials and software on board or on the ground to generate results for all of the programme's stakeholders.

#### SESAR

In the air traffic sector, the European SESAR programme, in which Thales is a key player, should provide a response to the challenges posed by the doubling of air traffic and the tenfold improvement in flight safety by 2020, while reducing the fuel consumption of commercial aircraft by 5%, CO<sub>2</sub> emissions per flight by 10% and acoustic emissions from aircraft at take-off and landing by 20 decibels.

In particular, Thales is developing software for a flight management system to optimise descent and climb phases, in collaboration with air control, leading to a reduction in the consumption of kerosene. Ground stations will handle air traffic with new applications, based on information provided by the avionics system, to optimise the flow of aircraft descents and climbs.

#### Copernicus

Thales remains heavily involved in Copernicus, the European space programme. Formerly known by the acronym GMES (Global Monitoring for Environment and Security), the programme aims to provide Europe with an autonomous Earth observation and monitoring capability thanks to continuous, independent and reliable access to data in the areas of the environment and security. This involves monitoring of the marine environment, the atmosphere, land and climate change, as well as support for emergency and safety interventions. For its space component, the programme relies mainly on a constellation of *Sentinel* satellites.

#### ETCS

ETCS stands for the European Train Control System. It simplifies train operation, makes signalling smarter and more reliable, and ensures optimal safety. Thales has been a key player in defining and implementing this European standard, and continues to offer innovative solutions that comply with this standard.

#### Shift²rail

Aiming to convert a significant share of road users to rail, this European initiative reflects the policy goal of achieving a 60% reduction in greenhouse gas emissions by 2050. It also aims to make rail travel more attractive and to integrate it with other modes of transport. Thales is one of the programme's eight founding members.

#### GALILEO and EGNOS

GALILEO is a European project for a satellite-based positioning system (radio navigation). The EGNOS service is designed to improve GPS accuracy and also offers the Safety Of Life service, which can be used in civil aviation. From the outset, Thales has been a major player in both programmes.

#### Electric-Taxiing with SAFRAN

Thales and Safran Landing Systems joined forces to optimise the energy conversion of the Electric-Taxiing system. Electric-Taxiing allows an aircraft to taxi independently without the use of its engines and without the need for a tug tractor, thanks to electric motors located in the main wheels. The saving achieved in terms of fuel and CO<sub>2</sub> emissions of 3,000 single-aisle aircraft fitted with this technology, is equivalent to

that produced by one million cars. The ATRU (Auto Transformer Rectifier Unit) extremely high-powered transformer designed and developed by Thales will be offered to airlines on an optional basis and as a priority for single-aisle aircraft.

#### 5.2.4.3.3 Defining international standards

Thales encourages its partners to adopt a responsible attitude regarding climate change. To illustrate its commitment, Thales is joint chair of the Carbon working group of the French Aeronautics and Space Industry Group GIFAS and is participating in the greenhouse gas working party of the International Aerospace Environmental Group (IAEG) to define international emissions accounting standards.

#### 5.2.4.3.4 Partnerships

Thales is also engaged in partnerships with other industry players as well as research laboratories.

The industrial chair dedicated to the challenges of greenhouse gas emission monitoring systems, inaugurated in December 2011, is a perfect example of this. It brings together scientific partners such as the French Climate Sciences and Environment Laboratory (LSCE), the French Atomic Energy Commission (CEA), the University of Versailles Saint-Quentin-en-Yvelines (UVSQ) and the French National Centre for Scientific Research (CNRS) along with industrial partners such as Véolia Eau and Thales Alenia Space.

A true innovation hub, the Joint Research Unit in Urban Sciences (UMR-SU), inaugurated in Quebec City in 2015, brings together the complementary skills of academics, manufacturers, planners and urban managers. Managed and hosted by Thales Research & Technology, this one-of-a-kind research laboratory aims to develop smart solutions

for the city of tomorrow in areas such as sustainable mobility, management of drinking water and wastewater, electricity, urban spaces and infrastructure, with the city of Quebec providing public facilities for field tests.

### 5.2.4.4 Adapting to climate change

The approach adopted by Thales for adapting to climate change is designed to reduce the Group's vulnerability to such related impacts as extreme weather (storms, floods, etc.), seismic events or resource scarcity.

Over the past several years, Thales has assessed the exposure of Group sites to natural disasters as part of annual site visits focused on prevention. This analysis consists not only of identifying the potential risks of flooding, storms and earthquakes, but also of identifying the consequences of these events in terms of environmental impact, property damage, business continuity, etc.

Thales has thus mapped its risks related to water at around 160 sites worldwide. The analysis of existing and future risks included the social dimension (access to water and sanitation, availability of water for local inhabitants), economic aspects (conflict of use) and environmental concerns (water consumption relative to the level of water stress in the river basin). The risk was scored based on a series of indicators, using international data to ensure a uniform assessment. This mapping process revealed that 10 sites were located in vulnerable zones. The majority of them are offices, whose low water consumption only has a very minor impact.

Thales is currently looking into extending this analysis to the mapping of its critical suppliers and to be in a position to assess its exposure to the risk of natural disasters for its supply chain.

## 5.2.5 Protection of biodiversity

The preservation of species, their habitat and ecosystems, the preferential use of areas dedicated to flora and the protection of historical and natural heritage are taken into account in all decisions with a view to contributing to environmental protection.

As early as 2006, Thales drew up a preliminary inventory of its sites in France near or within protected areas for flora and fauna and their habitat and, on certain sites, assessed the impact of activities on biodiversity and the degree of dependence on the ecological services provided by nature.

At the same time, Thales embarked on biodiversity risk mapping at 140 sites in 26 countries in order to obtain, as part of a macroscopic approach, a homogeneous overview of Group sites situated in the most vulnerable areas in terms of biodiversity. The indicators defined are used to analyse the risks for any project and integrate constraints for future developments, within a 2-km radius of sensitive sites.

Although the overall impact of the Group's activities on biodiversity is low, flora and fauna are of particular concern and the Group encourages its sites and employees to preserve and promote actions to protect biodiversity.

Various initiatives are taken across the world, and inventories are carried out at some sites by volunteers or in partnership with local authorities or biodiversity protection agencies, and ad hoc management measures are put in place.

Several Australian sites have put in place a habitat management plan which partly involves enclosing several natural habitat areas to control access to herds. This helps to reestablish the natural biodiversity and restore the region's original characteristics. Some species of flowers and animals have been registered on the site as well as some protected habitats such as that of the flying squirrel.

Other sites will focus on outdoor features to preserve the natural habitat and protect fauna (with bird boxes, feeders, species survey by an expert, etc.) or to re-establish native species, thereby guaranteeing a balance of habitats in terms of biodiversity, and offering a relatively safe and protected habitat for a wide variety of plants, fungi and animals.

Furthermore, as part of the grouping together of two of its sites near Bordeaux, France, between 2015 and 2017 Thales built a new 16-hectare site in line with the Avoid-Reduce-Mitigate principle. The impact of the new site on biodiversity informed its location and building procedures. Environmental compensation measures put in place during the site's construction continue to apply, in addition to a management plan for green areas which was also introduced.

For sites with large areas of plains or forests, particular precautions are taken for fauna and flora by promoting environmentally-gentle natural techniques for mowing and grazing and by eliminating phytosanitary products.

At other sites, employee awareness will be raised through photographic exhibitions of the forest, agroforestry and the species present on the site; programmes with bee-keepers; a register of species and a dedicated online review.

## 5.2.6 Solutions to support the environment

### 5.2.6.1 Environment and products

Continuous efforts are made to incorporate the environment into the entire product life cycle from cradle to grave while maintaining the strictest standards of security, safety and reliability expected by the Group's customers. The systems and high-tech products and services offered to the aeronautics, space, defence, transport and security markets are fully equipped to limit their environmental impact but are sometimes hard to square with this approach due to high technical constraints.

Nevertheless, Thales is committed to a responsible, proactive approach aimed at limiting as much as possible the impact of its products and services on the environment in order to comply with the increasing number of regulations along with the demands of the market and civil society. This is true of products that are eco-designed, i.e. that have an improved life-cycle environmental impact, or solutions with features that support the environment, for example by providing an understanding of extreme weather events.

Incorporating environmental factors into design generates the creativity and dynamism needed to make progress and to promote green innovation in areas such as developing new materials, saving energy and reducing weight.

To help in this approach, Thales applies skills throughout the Global Business Units (see Section 5.2.1.2.).

The Group's guidelines integrate the environmental aspect, from bids to product policies, design, development, maintenance and end-of-life phases. To ensure regulatory compliance, anticipate future regulations and requirements in this area, and guarantee traceability during the life cycle by looking ahead to dismantling, Thales is developing methods and tools to help product designers and architects make responsible choices and access environmental information. Resources include guides, questionnaires, checklists, computers and dedicated software tools such as the database on hazardous substances in components, regularly updated following regulatory changes, such as in REACH, or environmental impact analyses. Practices linked to the eco-design approach are defined in the engineering framework and made available to developers.

One example in the area of medical imaging are the developments carried out on a pre-treatment unit, in relation to the detector part, which led to a reduction in mass of 30% and in consumption of 70% between versions 1 and 3. Projections for 2018 and beyond aim for this mass to be phased out completely through integration of the software into the customer's computer and for consumption to be divided by three.

Thales is also a key player in national, European and international programmes to reduce the environmental footprint of products (see Section 5.2.4.2).

Lastly, Thales has been selected to take part in the European Space Agency's GreenSat study. This study is focused on the eco-design of a satellite to reduce its environmental impacts as much as possible. The study will include material aspects and manufacturing processes, as well as methods for the management of operations and the implementation of a mission in space. The eco-design approach will be compared to the conventional design approach, to estimate differences in the environmental impacts and in the costs and planning. Thales also takes into account requirements allowing it to prioritise the reduction of environmental impacts by looking to the future. As part of the Scorpion-EBMR programme, baseline conditions for the initial version were established and will be used to define targets for improvement during changes in the system.

### 5.2.6.2 Eco-responsible products and innovation

Several group companies are engaged in various initiatives to reduce the environmental impact of commercial and military products starting from the design stage. A number of product lines already incorporate strict environmental criteria assessed during life cycle analyses.

Thanks to its capacity for innovation, which is central to its strategy, Thales develops breakthrough technologies and new architecture that help to promote "green" innovation.

One example is *Stratobus* (a project launched in 2016), an autonomous geostationary stratospheric platform designed for a wide range of applications such as border and maritime surveillance, boosting GSM network capacity for public events and augmenting GPS over areas of dense traffic. This platform offers tangible environmental benefits. It runs on solar energy only and does not require a launcher to be put into position. It is made from recyclable subsystems and the use of hydrogen or helium considerably reduces the risk of pollution in the event of an accident. It is designed among other things to harness the sun's rays in all seasons and features a number of technological innovations, such as a power generation system coupling photovoltaic panels to a solar power amplification system patented by Thales and an energy storage system based on an ultra-lightweight regenerative fuel cell. The project underwent a review by the interested parties in November 2017, who confirmed its feasibility.

The Reality H helicopter simulator can reduce the number of flight hours and energy consumption (five times lower than the previous generation model). This gain has been achieved through the development of a simulator motion system, based on electric power rather than on a hydraulic system and offering much better performance without the risk of pollution. Life cycle analysis has led to the use of lighter, recyclable materials, as well as a reduction in size and weight, thus enabling easy transportation and lower CO<sub>2</sub> emissions.

Thales also lends its support to encourage the deployment of renewable energies. Wind farms interfere with civil aviation, defence and weather radars by creating a masking effect and triggering false alarms. This problem has led many countries to defer their plans to build wind farms. To address this situation, Thales has developed a material that absorbs broadband radiofrequency.

This material reduces the Equivalent Radar Surface (ERS) of the objects coated with it, attenuating or eliminating the interference. The radar signature of wind turbines is reduced by 99%. This solution has now been added to an existing solution consisting of a series of algorithms enabling radars to determine whether an echo has been sent by an aircraft or a wind turbine, thus reducing the risk of transmitting erroneous information to air traffic controllers.

In transport, Thales offers a predictive maintenance system to metro network operators, consisting of a data analysis service in the Cloud thanks to a secure platform. When they deviate from the norm, warnings are triggered, and recommendations are made as to the best course of action to take. This helps to improve reliability and reduce maintenance impacts.

Thales is also careful to identify replacement products if a substance presents a risk or might be banned. A dedicated programme has been launched to manage this issue, in light of the potential impact a ban on certain chemicals could have on the Group's processes and products. Conducted internally or with industrial partners, substitution surveys are intended to validate the characteristics and implementation processes of a new substance and to ensure that the product will continue to perform as expected. In some cases, it is necessary to redesign products and interfaces and rescope industrial tools.

In the case of chromatates for example, Thales carried out the qualification, for its applications, of more than 30 alternative industrial processes and verified the capacity of its subcontractors to manage these processes to meet its requirements. Thales set aside €5 million for this work and for the deployment of replacements in equipment and systems to reduce the use of authorisations under the REACH regulation.

### 5.2.6.3 Innovative solutions for the environment

#### 5.2.6.3.1 Understanding the environment

Thales is a key player in space-based Earth observation programmes, providing high-resolution optical and radar imaging systems that promote a better understanding of climate change and more effective environmental monitoring. The Group, in partnership with global agencies, contributes to most European climate missions, and is positioned in:

- the collection of essential information for climate forecasts and monitoring of the general status of plant life: topography of the surface of the oceans, ice floes and land surfaces; observation of ocean currents, pollution and marine life; the increasing temperature on the surface of the sea and land; and the overall status of vegetation to better manage its development (Sentinel 3 satellite);
- observation and anticipation of extreme, sometimes violent weather events, (hurricanes, floods, etc.), and long-term monitoring of climate change via *Meteosat* satellites;
- greenhouse gas monitoring, particularly carbon dioxide. This monitoring specifically includes the pinpointing of anthropogenic sources and the study of carbon sinks, and how they evolve in response to climate change. The complementary nature of the French (*Microcarb*) and European (*CarbonSat*) space-based observation initiatives means that all monitoring goals can be addressed.

As an example, the Poseidon technology, developed by Thales Alenia Space in partnership with CNES, has significantly modified the tools used in the world of oceanography. The accuracy of measurements has highlighted the thermohaline circulation of the world's oceans – an energy transport system as regards the global climate – as well as the rise in sea levels due to global warming. All satellites in the Jason mission are fitted with a Poseidon altimeter. Jason 3 focuses for instance on measuring the height of the oceans that supply the monitoring and prediction models for climate change.

For the future, the KaRin project, born out of a collaboration between NASA/JPL-CNES-Thales Alenia Space, should result in the delivery of a wide-swath radar interferometer, a key element in the SWOT (Surface Water and Ocean Topography) altimetry mission. This will ultimately allow for the use of hydrology to measure the topography of bodies of fresh water, lakes and flood zones with a surface area as small as 250x250 sq. m and rivers as narrow as 100m, and following on from the Poseidon altimeters, to measure the level of oceans with better global coverage.

#### 5.2.6.3.2 A cleaner sky

From flying to air traffic management, for over 30 years, Thales has developed features that improve performance and lower the environmental impact during all flight phases:

- navigational aids to optimise flight paths, take-off and landing phases in particular and taxiing that take weather conditions into account, thus reducing noise, emissions and consumption;
- systems for more fluid air traffic management with less waiting time in airport stacks;
- solutions to supply electric power to a number of aircraft systems which were previously supplied with hydraulic or pneumatic energy;
- lighter, less bulky and more efficient equipment.

These initiatives help to reduce kerosene consumption, carbon footprint, and nitrogen oxide emissions as well as to improve reliability while reducing maintenance costs.

An example of this is the Flight Management System (FMS), which calculates the optimal flight path according to aircraft data, weather conditions and the desired arrival time, while ensuring less noise, fewer emissions and lower consumption during take-off, ascent, cruise, descent and approach.

New avionics system architectures help reduce energy consumption, limiting the amount of on-board equipment and making it more compact so that it is easier to transport, thereby cutting CO<sub>2</sub> emissions. The integrated modular avionics featured on the A380 made it possible to streamline computing requirements and reduce the weight of hardware by 15-20% while increasing computing capacity and the useful life of equipment.

Through its participation in these programmes, Thales integrates the taking into account of its customers' increasingly high demands to reduce environmental impacts.

#### 5.2.6.3.3 Sustainable mobility

In today's increasingly urbanised world, creating sustainable conditions for urban mobility and inter-city travel is one of the most effective ways to reduce CO<sub>2</sub> emissions. Thales plays an important role in this by supplying transport operators with systems that optimise operational efficiency while limiting their environmental impact. Thales solutions provide:

- simpler access to transport with interconnected public transit that allows passengers to use different modes within and between towns and cities, at regional or national level, with a single ticket;
- smoother traffic flows thanks to urban traffic management systems that make it possible to regulate vehicle flows and handle trouble spots in real time. This means that motorists spend less time in their cars, use less fuel and produce fewer CO<sub>2</sub> emissions;
- a reduction in power consumption on underground lines, allowing underground operators to address environmental protection concerns while lowering their operating costs;
- an increase in the capacity of the existing main line network and reduced travel time, while ensuring compatibility between the various European rail networks.

For example, the Green SelTrac® CBTC solution reduces a train's energy consumption by 15% by loading efficient speed profiles into the train's on-board system. Algorithms are used to limit energy-intensive stop/start cycles and to switch off power so that trains run on their accumulated power whenever possible. For a standard underground line, CO<sub>2</sub> emissions are reduced by around 14,000 tonnes per year, equivalent to taking 6,000 cars off the road. To date, Thales's solution Thales Green SelTrac® CBTC operates more than 85 lines in more than 40 cities.

The ATSoft Energy Saving solution takes advantage of interactions between trains to save energy by optimising real-time traffic management: use of slow speed profiles when the operating circumstances permit and optimisation of current recovery from train braking by synchronising the acceleration of some trains with the braking of others.

#### 5.2.6.3.4 Smart Cities

Data analysis makes cities more efficient. Thales's solutions collect data on such parameters as water and energy consumption, subscriptions to various public and private services, and transport users, allowing city authorities to improve residents' quality of life and reduce their environmental footprint. Through its data analysis solutions, Thales helps city planners and managers:

- leverage the gigantic data reservoirs of the connected city – smartphones, street lighting, transport, billboards, access to public

places, surveillance cameras, etc. – to better understand and anticipate the needs of residents and offer them services that make their lives easier;

- inform users via traffic information systems, giving motorists and train passengers information on traffic conditions in near-real time;
- manage day-to-day operations more effectively and facilitate the coordination of the various players, especially in the event of an emergency. These solutions also improve the environmental efficiency of cities with regard to water and energy consumption, transport use, etc.

For example, the PRESTO electronic system, designed and developed by Thales, allows residents of the Greater Toronto Area to travel using the various means of public transport (train, underground, bus) using a single ticket, in the form of an electronic contactless card that can be

used across the entire network. Statistical analysis applied to the data collected gives an insight into mobility across this vast area, meaning that supply can be tailored to actual needs, new services can be created and the use of public transport can thereby be encouraged.

Thales contributes to the Hyderabad programme (India) to become a “green” city, in particular by supplying to the new metro system opened in 2017 CBTC (Communication Based Train Control) and ISC (Integrated Communications and Supervision) systems, for the very first time in the country. This environmentally friendly metro should reduce carbon emissions both through using zero emission electricity and by limiting high-emission road transport.

Going even further, Thales Research & Technology Quebec hosts and manages the Joint Research Unit in Urban Sciences (UMR-SU), which aims to identify needs and new technologies in the city of tomorrow.

## 5.2.7 Environmental indicators

The table below contains a number of items for assessing trends in Thales's environmental performance on a comparable basis. In 2017, the scope comprised 28 countries and 155 sites. This scope represents 97% of sales and 98% of the Group's workforce.

2015 is the base year for the 2016-2018 goals.

This chapter was subject to a fairness review by Mazars. In Section 5.4 "Independent third-party report on consolidated human resources, environmental and social information published in the management report," the opinion provides moderate assurance concerning the indicators in the table below.

	Units	2008-2015 change (at constant 2008 scope)	2015	2016	2017	2015-2017 change
<b>Energy</b>						
Electricity consumption	Thousand toe	-12%	131 <sup>(b)</sup>	131	132	1%
Per sales electricity consumption	Toe/€k	-27%	9.57 <sup>(b)</sup>	9.1 <sup>(b)</sup>	8.65	-9%
Fossil energy consumption	Thousand toe	-38%	21	21.9	21.9	4%
Per sales fossil energy consumption	Toe/€k	-48%	1.54	1.52	1.44	-6%
Total energy consumption	Thousand toe	-17%	154 <sup>(b)</sup>	155 <sup>(b)</sup>	156	1%
Per sales total energy consumption	Toe/€k	-31%	11.2 <sup>(b)</sup>	10.7	10.2	-9%
<b>Water</b>						
Water consumption	Thousand cu. m	-26%	1,540 <sup>(b)</sup>	1,587 <sup>(b)</sup>	1,593	3%
Per sales water consumption	Cu. m/€m	-39%	112.3 <sup>(b)</sup>	110.3 <sup>(b)</sup>	104.4	-7%
<b>Waste</b>						
Total waste production <sup>(a)</sup>	Tonnes	-24%	15,045 <sup>(b)</sup>	14,967 <sup>(b)</sup>	16,080	6.9%
Per sales total waste production <sup>(a)</sup>	Kg/€m	-36%	1.10 <sup>(b)</sup>	1.04 <sup>(b)</sup>	1.05	-3.9%
Ratio of non-hazardous waste <sup>(a)</sup>	%		73	75.3 <sup>(b)</sup>	81	10.3%
Non-hazardous waste per person <sup>(a)</sup>	Kg/pers	-29%	161.2 <sup>(b)</sup>	159.7 <sup>(b)</sup>	179.5	11.3%
Non-hazardous waste recycling rate	%	45%	64	50 <sup>(b)</sup>	55	-14.6%
Hazardous waste recycling rate	%	-45%	19	24.8	32	68.8%
<b>Industrial discharge</b>						
Industrial wastewater discharge	Thousand cu. m	-1%	562 <sup>(b)</sup>	652	595	6%
Air emissions	Tonnes	-30%	917	993	923	1
<b>CO<sub>2</sub></b>						
CO <sub>2</sub> emissions from energy use	Thousand tonnes CO <sub>2</sub>	-23%	187	187 <sup>(b)</sup>	188	1%
Per sales CO <sub>2</sub> emissions from energy use	Kg CO <sub>2</sub> /€m	-36%	14	13	12	-9%
CO <sub>2</sub> emissions linked to Kyoto Protocol substances and R22	Thousand tonnes CO <sub>2</sub>	-23%	35	27	30	-14%
O/w CO <sub>2</sub> emissions linked to SF <sub>6</sub>	Thousand tonnes CO <sub>2</sub>	-78%	6.7	1.6	3.4	-49%
CO <sub>2</sub> emissions from transport (Group-wide)	Thousand tonnes CO <sub>2</sub>	-1%	79	81	77	-2%
Per sales CO <sub>2</sub> emissions from transport	Kg CO <sub>2</sub> /€m	-17%	5.8	5.6	5.07	-12%
<b>CO<sub>2</sub> Scopes according to GHG Protocol</b>						
Scope 1 (gas, fuel oil, coal, substances, mobile energy sources)	Thousand tonnes CO <sub>2</sub>	-35%	88	82	86	-2%
Scope 2 (electricity, steam)	Thousand tonnes CO <sub>2</sub>	-13%	136	134	136	0%
Scope 3 (business travel by air, rail, road)	Thousand tonnes CO <sub>2</sub>	-1%	79	81	77	-2%
<b>TOTAL SCOPES 1, 2 AND 3</b>	<b>THOUSAND TONNES CO<sub>2</sub></b>	<b>-17%</b>	<b>303</b>	<b>297</b>	<b>299</b>	<b>-1%</b>
<b>TOTAL SCOPES 1, 2 AND 3 PER SALES</b>	<b>KG CO<sub>2</sub>/€M</b>	<b>-31%</b>	<b>22</b>	<b>21</b>	<b>20</b>	<b>-12%</b>
<b>Other disclosures</b>						
ISO 14001-certified entities			117	120	124	
Staff concerned as percentage of total workforce	%		90%	89%	89%	

(a) Excluding exceptional waste.

(b) Adjustment of 2015 scope following the resale of a site.

## 5.2.8 Environmental reporting rules

### 5.2.8.1 Scope

The consolidation scope of environmental data is based on the financial consolidation scope. However, due to restricted activity and/or workforce or the absence of operational control by Thales, certain establishments have not been included.

In connection with this report, the 2017 indicators are provided at constant scope with 2015.

#### 5.2.8.1.1 Criteria

Only companies meeting the following criteria are included:

##### Equity interest and operational control

- Thales equity interest of 50% or more;
- Thales exercises operational control over the company.

Companies and joint ventures not meeting the above criteria are not included in Thales' environmental reporting.

##### Activity/workforce

- "Company/site" involved in an industrial activity (surface treatment, painting, pyrotechnics, shipbuilding, etc.) irrespective of the number of employees;
- "Company/site" involved in a semi-industrial activity only (testing, integration, R&D, etc.) with more than 50 employees;
- "Company/site" involved in a tertiary activity only (head office, service facility, sales office, etc.) with more than 100 employees.

##### Environmental Management System

All "companies/sites" that are ISO 14001 and/or EMAS-certified are included in the scope irrespective of the criteria related to activity.

#### 5.2.8.1.2 Changes in scope

- Disposals/acquisitions: company to be included as soon as one full calendar year has been completed and if the company meets the scope selection criteria.
- New business: company to be included as soon as one full calendar year has been completed and if the company meets the scope selection criteria.
- Inter-site transfers: data taken into account in the reporting:
  - of the departure site from 1 January Y to the date of transfer,
  - of the arrival site from the date of transfer to 31 December Y.
- Intra-Group merger: integration of data for the absorbed entity for the period from 1 January Y to the date of absorption into the data of the absorbing entity.

### 5.2.8.2 Reporting procedure

The Group-wide reporting system includes an environmental reporting procedure with instructions for each successive stage of data entry, validation and consolidation. It also defines the roles of each person involved and includes the recording of data (traceability, archiving, etc.).

### 5.2.8.3 Indicators

Environmental concerns change over time. Environmental performance indicators therefore have to evolve to stay abreast of developments and reflect the Group's policy priorities. Different interpretations of certain indicators can lead to conflicting data from different countries. Thales is therefore adapting the indicators to make the environmental reporting system more efficient, building on lessons learned from previous years and refocusing the reporting effort on current and future environmental concerns. The indicators are described in the reporting tool. Information is also available on the calculation of the carbon footprint.

#### 5.2.8.3.1 Reporting tool

An environmental reporting and management tool for the entire scope of consolidation of the Thales group is available on the corporate intranet. This tool consolidates the data from each entity, country and geographic area, and for the Group as a whole. It checks data consistency and suggests country-specific units of measurement, conversion factors, etc. The same tool provides access to the rules for data entry, validation and consolidation defined in the reporting procedure.

#### 5.2.8.3.2 Analysis of performance

For easier analysis of environmental data, the Group reporting system incorporates the following principles:

- changes in scope specifically related to disposals and acquisitions. For each family of indicators, a gross figure is given (e.g. water consumption in cubic metres) and a ratio supplements the information to take account of changes in scope (e.g. water consumption per person);
- Group targets are set for a given period. During that period:
  - changes in performance are assessed on a like-for-like basis (i.e. at constant scope of consolidation),
  - coefficients such as emission factors for CO<sub>2</sub> emissions are constant;
- if emission factors are modified at the start of a new period, the performance data for the reference year are recalculated using the new coefficients;
- the principles and methods for reporting on data are described in the methodological guides to environmental reporting and calculation of CO<sub>2</sub> emissions, which are available in the Group reporting system.

## 5.3 SOCIAL INFORMATION

The Group's strong commitments, formalised in its Code of Ethics, attest to its desire to act responsibly. Certain actions undertaken by Thales in connection with its corporate responsibility policy target other stakeholders than its own employees.

### 5.3.1 Territorial, economic and social impact of the Group's activities

#### 5.3.1.1 The Group's regional policies in France

The Group's regional policy relies on the quality of its relations with economic, social and academic players and local institutions and communities. Whenever to the greatest extent possible, its sub-contractors, suppliers and industrial partners are chosen locally in order to support regional business.

In France, Thales aims to mobilise all of the relevant players in its labour pools in order to develop Regional Workforce and Skills planning. This strategy takes into account the specific characteristics of the regions in question as well as Thales' local challenges. The Group agreement to promote professional development and employment through proactive initiatives signed on 26 April 2013 actively supports local action by creating a Commission on regionalism and relying on a Group Anticipation representative, as part of a joint organisation, to coordinate the Thales Regionalism community and monitor regional actions.

The policy is based on a knowledge of each labour pool, key players, and three priority areas of focus:

- Skills maintenance and development;
- Professional integration of young people, education and training;
- Co-development of the industrial fabric and open innovation.

In France, Thales has thus created nine labour pools in order to better coordinate its action. Within each labour pool, a correspondent coordinates regional actions in cooperation with the local and regional authorities, social and economic players, and Thales's Engineers for Schools seconded to academies, universities, schools and training centres.

In France, Thales also makes use of a dedicated local economic development company, G ris Consultants, which assists, in collaboration with the Anticipation representative, with the roll-out of the Group agreement for professional development and employment through anticipation initiatives, by coordinating the network of Thales Engineers for Schools and supporting Group employees to take over or start a business (62 new projects in 2017). G ris Consultants also conducts HR engineering experiments to develop the performance and skills of Thales's suppliers and more generally of SME/SMI in labour pools, to support the professional development of employees from large companies, and to facilitate the integration of young people into the local industrial fabric.

For this purpose, G ris Consultants coordinates the *Pass'Comp tences* inter-company outreach tool, the Shared Learning Path initiative (in connection with *Fondation Innovation Pour les Apprentissages* – Innovation for Learning Foundation (FIPA)), and, through Thales's Shared Training Service offers the implementation of Thales methodology known as *Trans'Faire* – tailored transfer of skills between a mentor and a mentee – in French SME/SMI.

More specifically, the *Pass'Comp tences* initiative is designed to stimulate SME development by assigning them voluntary expert employees from large companies (Thales, Schneider Electric, etc.) for pivotal assignments lasting between 12 and 18 months, which create local employment and wealth. Offers (profiles of voluntary expert employees from large companies) and requests (SME/SMI/start-up) for skills are constantly updated on the [www.pass-competences.net](http://www.pass-competences.net) website, in addition to numerical projections by CEOs (the creation of 816 new jobs and combined wealth estimated at  185m by 2020) and the results observed since the initiative's launch in 2012

(35 placements: 28 involving Thales employees, 6 from Nokia and 1 from Schneider Electric).

In 2017, there were 10 new placements involving Thales employees.

The rollout of the *Pass'Comp tences* initiative continues in the region of Occitanie, and was launched in April 2017 in Nouvelle-Aquitaine with funding from the region's economic services.

In addition, G ris Consultants, in partnership with Thales HR teams, assists the professional integration of work study employees:

- by promoting the "Shared Learning Path" initiative;
- by inviting SME with open positions (23 SME requested submitted more than 147 job offers in 2017) to Thales's annual forum for Top Interns and Work-Study Employees;
- by coordinating Thales's participation in the "Altern'UP 2017" contest under the aegis of the FIPA: four employees at the end of work-study programmes who submitted a total of three projects were selected to participate in the *Creativ'Week* during which they were trained in key topics for business creation and had the opportunity to improve their business model in a collaborative, dynamic and inspiring way. At the end of the contest, Thales awarded the Innovation prize to the winner selected by the judging panel;
- G ris Consultants also shares its expertise with large companies and local authorities in order to provide assistance, in the form of advice and innovative financial engineering, to SME and SMI that create long-term positions in regions impacted by the loss of industrial jobs. The revitalisation projects led by G ris Consultants since 2009 have led to the creation of nearly 4,800 jobs in France (including 210 in 2017) with approximately 700 SME and SMI.

#### 5.3.1.2 Group initiatives to support people with disabilities

In France in 2017, the Group continued its partnerships for the training and guidance of young people with disabilities, with highlights including:

- a new partnership with the University of Rennes to be added to those existing with the Universities of Orleans, Tours and Lille as well as with the  le-de-France university communities, Pierre & Marie Curie University (UPMC Paris), the University of Nice Sophia-Antipolis (UNICE), the University of Bordeaux 1, the University of Toulouse, and the University of Western Brittany (UBO Brest);
- in line with the many existing agreements already signed with educational authorities designed to help high school students with disabilities to access higher education and monitor students with disabilities, work is ongoing to establish an agreement with the educational authority of Aix-Marseille and Bretagne. These agreements cover almost all the labour pools where Thales is present;
- the partnership with Paris-Est Cr teil University to set up an inter-university diploma (IUD) in disability representation in the public or private sector continued. 21 students received the diploma in 2015, 22 in 2016 and 26 in 2017;
- Thales continued to be involved in the development of the Hanvol non-profit organisation, whose mission is to find jobs for people with disabilities in the field of aeronautics;

- the Group also continued its involvement in the agreements to implement software architecture and information system engineering courses at Vocational Rehabilitation Centres (CRP) in Millau and Mulhouse.

Thales also participates in the implementation of innovative projects based on technologies developed within the Group in order to provide practical assistance to people with disabilities. Initiatives include:

- the “Eyeschool” system, which enables young visually-impaired people to have what the teacher writes on the board transferred to their computers and documents distributed in class to be vocalised. In line with the assessment report by France’s Education Ministry in 2015 encouraging the expansion of the scheme in schools and universities, Thales continued its action in this area by assisting visually-impaired school and university students;
- the GUIDEO guidance system, which helps a blind or visually-impaired person to move autonomously through a building using a smartphone (the system was tested on the Gennevilliers site);

- in 2012, Thales participated, in cooperation with AFNOR, in implementing the “OK Pilot” tool for a company to self-audit its compliance with the disability-friendly standard and to define the necessary action plans for improvement.

The Group also stepped up its local involvement in SME through initiatives such as those put in place, in the department of Hauts-de-Seine, with a partnership agreement, signed on 9 December 2016, with the aim of supporting SME through large groups in the implementation of their employment policy for people with disabilities.

The Group’s expertise and commitment with regard to disabled employment have been widely recognised, as evidenced by the 2016 appointment of Thales Mission Insertion Director to French national consultation committee for people with disabilities (*Conseil National Consultatif des Personnes Handicapées* – CNCPH) and national committee for the fund for disabled employment in the public sector (*Comité National du Fonds d’Insertion des Personnes Handicapées dans la Fonction Publique* – FIPHFP) in his capacity as an expert.

## 5.3.2 Fair business practices

### 5.3.2.1 Anti-corruption

Corruption represents a major risk for multinationals, particularly those with export operations. It exposes these companies, as well as their employees and managers, to criminal and civil sanctions and can be very harmful in terms of reputation.

At the end of the 1990s, in order to protect itself from these risks, Thales introduced a corruption risk prevention policy, which is being continually improved. This policy is regularly reviewed and the provisions are constantly adapted to take into account legislative and regulatory developments, in particular the entry into force in June 2017 of the French law on transparency, the fight against corruption and modernisation of the economy (known as the Sapin II law).

The policy is based on an integrity programme, the various components of which are integrated into the operational procedures, and supported by a dedicated organisation.

#### 5.3.2.1.1 An integrity programme adapted to the new legislative environment

Thales launched a review of its integrity programme to bring it into line with recent legislative developments, in particular the French Sapin II law.

The integrity programme is based on:

- clearly stated, shared principles. The zero tolerance policy concerning all acts of corruption has the full support of Group corporate management. With a foreword by the Chairman and CEO, the Code of Ethics expressly reiterates this principle. The Code of Ethics in addition to a range of thematic guides (gifts and hospitality, conflicts of interest, lobbying, etc.) published in several languages, are made available to all employees on the Group intranet;
- a code of Conduct which defines the types of conduct that are prohibited as they may be construed as acts of corruption or influence peddling. It applies to all employees of the Group. It has been incorporated into the internal regulations of the Group’s French companies and is in the process of being rolled out to its foreign subsidiaries;

- an alert system available to all Group employees (permanent employees, casual employees and external staff);
- risk mapping;
- an assessment of the main commercial partners. In particular, Thales strictly supervises the use of agents and consultants by means of a detailed procedure, which provides for in-depth upstream checks and controls (due diligence) backed by an analysis of the risk factors at play, and for all appropriate declarations and undertakings on the part of these agents or consultants. This procedure is regularly reviewed and was updated in 2017;
- a training plan for exposed employees, consisting of face-to-face sessions and e-learning modules;
- accounting control procedures.

#### 5.3.2.1.2 Clear operational measures

The pillars of this integrity programme are integrated into the different operational processes of Thales’s reference system (Chorus 2.0). From the preliminary phase of a project, these processes which govern the management of offers and projects also provide for action plans to mitigate business risks, with a particular focus on anti-corruption and the management of health, safety and environmental impacts. In addition, the provisions of the integrity programme are also built into purchasing and subcontracting processes. As a result, the players in the supply chain are also stakeholders in the integrity policy: at the end of 2017, close to 12,700 suppliers and subcontractors in the portfolio pledged to adhere to the terms of Thales’s Purchasing and Corporate Responsibility Charter.

Using risk mapping and rigorous internal control, the Group’s Audit, Risks & Internal Control Department conducts regular compliance and integrity audits on the various components of the model and their implementation.

### 5.3.2.1.3 A dedicated organisation

The Group's corruption risk prevention policy is underpinned by a dedicated organisation. Thales has governance bodies and an organisational set-up designed to establish, manage and monitor the implementation of regulations with regard to the prevention of corruption risks, as well as to instil a culture of corporate responsibility throughout the Group.

Confirming the central role played by ethics and corporate responsibility in the Group's strategy, Thales created an Ethics & Corporate Responsibility Committee in 2001 composed of representatives from the support functions and the main countries where the Group operates. Its tasks are focused on three areas: (i) Strategy: contributing to defining Thales's policy on ethics and corporate responsibility; alerting and making ethical recommendations with regard to the standards and procedures concerning sales, environmental, human-resource-related and social issues; (ii) Ownership: ensuring that the internal codes are kept up to date and implemented within Thales; defining training objectives and suitable means of communication; coordinating and monitoring the Country Ethics Committees and ethics officers; (iii) Sharing: holding discussions amongst its members on good practices, experiences and the ethical issues submitted to it.

The Group's Ethics & Corporate Responsibility Committee is chaired by the Group Secretary & General Council. In 2017, the Committee met three times.

The Ethics and Corporate Responsibility Department is responsible for the Group's actions in terms of ethics and responsibility, coordinating the relevant people within the Group, addressing and ensuring that the ethical issues submitted to it are handled and followed up correctly, through an *ad hoc* committee where necessary.

Ethics officers ensure that the Code of Ethics and its principles are disseminated throughout all the Group's units and specifically to new hires. Their role consists of overseeing staff training and awareness-raising, responding to questions concerning the application of the Code of Ethics and the code of Conduct, and bringing the Group's ethics policy into line with local customs and legislation.

The Thales corruption risk prevention policy has been recognised by stakeholders. In 2017, for the first time, Thales was ranked the company which has developed the most advanced corporate responsibility policy in the world in the "Aerospace & Defence" sector by the Dow Jones Sustainability Index (DJSI).

The Group is also ranked in the top four European companies in the Defence companies anti-corruption index published by the NGO Transparency International in 2015 (the year of publication of the last rankings of this type). Finally, the Group has renewed its support for the principles of the United Nations Global Compact and was one of 447 companies to obtain Global Compact Advanced level for their Communication on Progress in 2017.

### 5.3.2.1.4 An alert mechanism

Since 2004, Thales has put in place an alert mechanism available to all Group employees, in addition to the existing alert channels, namely the hierarchical route and the employee representation bodies and, where applicable, specific alert mechanisms in certain countries.

This mechanism is under review in order to bring it into line with the requirements of the Sapin II law, the new European regulation on personal data protection which will enter into force on 25 May 2018 and law 2017-399 on the duty of care of parent companies and subcontracting companies.

## 5.3.2.2 Consumer health and safety

Thales's products, technologies and services are aimed primarily at governmental customers in the "B2G" (Business to Government) positioning, in particular in the Defence and Security segments, or at private "B2B" (Business to Business) customers, notably in the aeronautics, space and railway transport segments.

## 5.3.3 Relations between Thales and its stakeholders

### 5.3.3.1 Customer relations

Customer confidence is central to Thales's commitments and one of its key values. The very or core nature of Thales's activities requires a sustainable relations and commitment. Thales must act as a strategic partner towards its customers, understanding their challenges, strategic objectives and operational needs. Thanks to its policy of ensuring a local presence, based on offering customers proximity, attentiveness and support in the long term, it has established itself as a major industrial player in its "traditional" countries with the ability to expand its presence in high-growth countries.

#### 5.3.3.1.1 An organisation which promotes customer relations

Thales's organisation is designed to develop a relationship as close as possible to the environment and the business activity of its customers:

- a global setup, providing a local presence, both commercially and in terms of operational capacity;
- a global network of 250 Key Account Managers (KAM) dedicated to managing customer relations, covering all the different organisations and activities of the Group;
- business Lines building a strategy and a range of products, systems and services tailored to the needs and strategic developments of markets and customers;
- a marketing organisation, which drives coherence between Thales's offer and the requirements of the market and customers;

- project and support teams at the ready to respond to contractual requirements and operational needs, working in close collaboration with customers and partners;
- a Quality and Customer satisfaction organisation to support the teams and monitor customer interests.

#### 5.3.3.1.2 Regular measurement of customer satisfaction and confidence

For Thales, assessing the satisfaction and confidence of its customers is a key indicator of its operational performance and a source of constant progress.

For this purposes, Thales is equipped with a global system for gauging and managing the quality of customer relations based on:

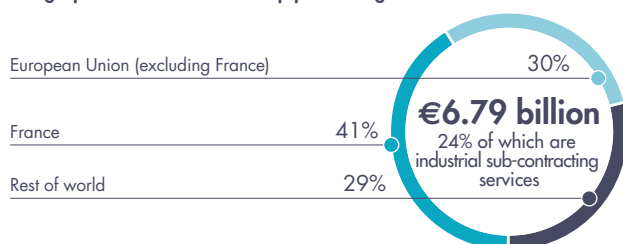
- a satisfaction survey schedule with a frequency of 18 months to 2 years;
- a network of independent consultants across a hundred countries to meet customers and take stock of relations;
- a centralised digital platform for customer data and feedback;
- indicators and analysis on the different market segments, types of customers, product lines, etc.;
- action plans coordinated by account managers to respond to the specific issues of each customer;
- transverse analyses, which can detect weak signals and showcase advantages and differentiating factors as well as recurring customer expectations for use in performance plans.

The global scope of this approach is appreciated by customers, who clearly see Thales's desire to forge relationships based on trust and cooperation, constantly striving to better respond now and in the future to their key challenges.

In 2017, the survey conducted on a representative panel of 1,900 contacts from 620 customer accounts in 100 countries, covering all of the Group's Defence and Civil activities established that 74% of the Thales customers asked stated to be satisfied or highly satisfied with Thales; while 84% of customers asked confirmed that they would be prepared to recommend Thales.

### 5.3.3.2 Supplier relations: a responsible approach

#### Geographic breakdown of Group purchasing in 2017



#### 5.3.3.2.1 A recognised purchasing policy

The aim of the Thales purchasing policy is to work with a bedrock of efficient, reliable suppliers, capable of helping the Group achieve its sales objectives while complying, in particular, with export control requirements and with environmental, financial, ethical and social obligations as well as national and international regulations.

This policy is based on ten responsible purchasing practices specified in the Responsible Supplier Relations Charter, of which Thales has been a signatory since 2010. The aim of the charter is to develop a balanced relationship based on trust between suppliers and customers in the knowledge and respect of their respective rights and obligations. To this end, the Group has also appointed an internal mediator to act between suppliers with a view to trying to resolve potential conflicts which could arise in connection with its contractual relations with its partners; the Thales internal mediator's actions are also in line with the initiatives carried out by the mediator of the aeronautics and space sector driven by GIFAS (*Groupement des Industries Françaises Aéronautiques et Spatiales*).

Confirming its commitments in this area, in 2012 Thales was one of the very first large groups to be awarded the "Responsible Supplier Relations Label" by the Médiation des Entreprises (business mediator) and the Conseil National des Achats (French Purchasing Board). Awarded for a period of three years for the French perimeter, this label singles out companies committed to forging a structured collaborative relationship based on mutual respect. To obtain this label, a prior external audit of purchasing procedures and action plans must be carried out; the various audits conducted on an annual review (2013, 2014, 2016 and 2017) or triennial renewal (2015) basis have, since it was first obtained, consistently confirmed the award of this label to Thales.

#### 5.3.3.2.2 Involve suppliers in an approach based on collaborative innovation

As part of its Purchasing strategy, Thales also develops a collaborative innovation approach with its suppliers. This involves quarterly meetings for discussion between the representatives of the Group Purchasing and Research & Technology Departments to identify the best players, classify them in relation to the Group's requirements and be in a position to launch with them analysis, studies upstream or PoC (Proof of Concept); this approach has the potential to identify critical innovations and/or technological breakthroughs in both the military and civil fields. An internal application was also developed in 2017 to assess the potential in terms of R&T and the offer of innovative start-ups and SMEs to Thales's prescribers and buyers; at the end of December 2017 almost 500 start-ups had already been added to the database.

In parallel, Thales organises or participates in dedicated events which are an opportunity to meet players in innovation such as the Thales InnovDays (showcasing micro-enterprise, SME and start-up partners involved in ongoing projects) or the Thales Open Innovation Day (event organised with the Pôle Minalogic which was a springboard for some fifty European start-ups during pitches or BioB meetings). Thales is also involved in many incubators, such as Starburst, the number one worldwide Aerospace start-up accelerator. Finally, since 2012, Thales has signed the "Innovative SME charter" and has actively participated in several multi-sectoral actions taken by its signatories (primarily publicly-funded French companies) to help SME in their innovation projects and contribute to their future development.

In line with this initiative, Thales has also shown its commitment to France's Ministry of the Armed Forces through a bilateral agreement. This initiative, known as the "SME Defence Pact", is primarily aimed at improving the access of SME to defence markets and establishing a balanced partnership between SME and industry champions such as Thales; actions are reviewed regularly and at different levels in conjunction with those involved. In France, Thales works with more than 3,000 SME and mid-cap companies representing a commitment in the amount of more than €1.7 billion in 2017.

#### 5.3.3.2.3 Strengthening links with SME

Since its creation in 2010, the Group has also been heavily involved with the organisation Pacte PME and still sits on its Board of Directors. As part of a proactive initiative to develop good practices, Pacte PME aims to facilitate the growth of SME and the emergence of new mid-cap companies. In 2017 for instance, the Group actively participated (design, implementation and support) in an experimental reinforcement programme for thirty SME from the aeronautics and space sector, in particular on subjects relating to growth and competitiveness. Several Pacte PME partners also contributed to the implementation of this programme such as Adiver, Airbus, GIFAS, the ASTech competitiveness pole, Business France, Comité Richelieu and Safran.

Since 2013, Pacte PME has produced a supplier relations quality barometer for its "subcontracting company" members, with the objective of involving the latter in an on-going improvement approach. In 2015, 2016 and 2017, the barometer conducted on behalf of Thales, of a panel of 330 suppliers, highlighted a very high level of satisfaction with the quality of relationships developed between the Group and its partners.

Finally, Thales is heavily involved in GIFA Industrial Performance programme aimed at improving performance of the French supply chain in terms of delivery and quality, improving the subcontracting company/supplier relationship, boosting the competitiveness of SME in the sector and developing employment in the industry. In 2017, 300 companies across France, grouped into clusters of five and seven suppliers and led by a subcontracting company, were set in motion; as part of this initiative, Thales steered seven clusters in Rhône-Alpes Auvergne, Bretagne, Île-de-France, Normandie, Nouvelle Aquitaine, Provence Alpes Côte d'Azur and Pays de Loire, comprising a total of around fifty suppliers. The initial stages of this programme generated excellent results, with 97% of the SME seeing a significant improvement

in their performance measured via one of the following criteria: punctuality, lead time delays and quality.

### 5.3.3.3 Duty of care of parent companies and subcontracting companies (law 2017-399)

Since September 2001, the date of publication of Thales's first Code of Ethics, the Group has paid particular attention to the conduct of its suppliers. This initiative was reinforced in 2003 when Thales formally joined the United Nations Global Compact initiative (see below). Thales also applies the OECD Guidelines for multinational companies. These define the criteria for the responsible conduct of companies in the areas of employment and business relations, environment, anti-corruption, consumer interests, science and technology, competition and taxation. In addition, since 2008, as part of these commitments, the Group has asked its suppliers to respect the ten principles stipulated, particularly those relating to Human Rights, employment law and environmental protection.

During 2017, the implementation of law 2017-399 of 27 March 2017 on the duty of care of parent companies and subcontracting companies has been discussed during meetings of the Ethics Corporate Responsibility Committee giving rise to the launch of ad hoc working groups.

This chapter specifies the actions undertaken for many years by Thales which will be integrated into the global duty of care plan to be approved during 2018 and presented in the 2018 Registration Document.

#### 5.3.3.3.1 Action undertaken in terms of duty of care

##### Action to support Human Rights and fundamental freedoms

Thales signed the United Nations Global Compact in 2003 and complies with its ten principles relating to Human Rights, labour standards and environmental law inspired by the Universal Declaration of Human Rights and the International Labour Organization's Declaration on Fundamental Principles and Rights at Work. These ten principles are applied on the basis of agreements and best practices which ensure the Group's business activities are compliant with responsible conduct. As proof of the relevance of the actions taken in terms of corporate responsibility, in 2017, for the sixth year in a row, Thales achieved the Advanced level of the Global Compact differentiation programme which, with its 21 specific criteria, is the highest reporting and performance standard for responsible development. It should be noted that the Advanced level programme required an external evaluation, which Thales successfully passed in a peer review. Finally, of the 9,668 companies that are members of the Global Compact, only 447 obtained the Global Compact Advanced level in 2017, including 83 French companies.

Thales also extends its own commitments in this area to its suppliers (see 5.3.4.1.4 below).

In order to ensure strict export control, both at a national and international level, Thales has put in place a global organisation and constantly reinforces its internal measures and procedures. This strong commitment is intended to protect the national security of democratic States and specifically to contribute to the fight against the spread of weapons of mass destruction. Accordingly, Thales and other European Aerospace and defence companies support the United Nations Arms Trade Treaty, which came into force in late 2014.

Since 2004, Thales has also ceased all activity in the field of cluster munitions, opting to respond in a proactive manner to the expectations of the NGOs involved in the field of Human Rights issues, as well as anticipating the principles and definitions of the Convention on Cluster Munitions.

Finally, as part of a multi-stakeholder dialogue, Thales takes part in numerous working groups on Human Rights, specifically aimed at improved consideration of the United Nations' guidelines relating to Human Rights (known as the Ruggie Principles).

##### Action to promote the environment

For many years, Thales has applied a responsible environmental policy. To this end, Thales has established and updated an environmental risk analysis based on the activities carried out, scientific and technical developments and new challenges, which is in line with an overall procedure to manage these risks. The Group is also working to secure ISO 14001 certification for the industrial sites of subsidiaries across the world. To date, 124 sites covering 89% of the Group's workforce are certified. See Chapters 5.2.1.3 and 5.2.1.4.1 for more information.

##### Action related to personal health and safety

With the health and safety of its employees a key priority for the Group, risk analysis has also been conducted in these areas for many years, aimed at ensuring that employees are not exposed to specific risks and analysing and anticipating the impact of new regulations. Risk mapping consolidates an overview of areas for improvement, which are addressed via action plans both at Group level and locally. Coordinated by the Risk Assessment Committee, the process to manage these risks likely to affect employees is monitored regularly. See Chapter 5.1.5.2 for more information.

##### Values shared with our suppliers and subcontractors

Thales's strong attachment to respecting the principles of corporate responsibility with regard to suppliers was conveyed in 2017 through the continued deployment of the Purchasing and Corporate Responsibility Charter. Through this charter, the Group asks its suppliers across the world to adhere to its Corporate Responsibility approach and to respect both the principles of its Code of Ethics and those of the Global Compact and the OECD. In particular, Thales raises their awareness to the issue of conflict minerals and the non-use of toxic substances.

The companies concerned are also encouraged to fill in a self-assessment questionnaire composed of sixteen questions: nine relating to labour standards, three to environmental protection, two to governance, one to business ethics and one to export control.

At end-2017, nearly 12,700 Thales suppliers (21% more than in 2016) had signed the Purchasing and Corporate Responsibility Charter and completed the self-assessment questionnaire. On this basis, overall supplier performance in terms of environmental, social and governance (ESG) criteria was rated 8.3 on a scale of 10.

#### 5.3.3.3.2 Other aspects of the duty of care plan

##### Risk mapping related to the duty of care

The main risks related to Thales's activities are presented in Chapter 1.1.2 of this document entitled "Risk factors". Some of these risks are suitable for inclusion in the mapping of duty of care-related risks, in other words related to severe abuses of Human Rights, and damage to the health and safety of people and the environment. Also contributing to this mapping will be the mechanisms to measure environmental risks or damage to the health and safety of people, as discussed above (See Chapter 5.2.1.4.2).

Thales has set up an ad hoc working group which assumes the main roles concerned, to supplement, if necessary, this risk mapping in collaboration with other stakeholders, particularly within professional bodies. This risk mapping will be used as a reference for the rollout of the duty of care plan.

##### Alert mechanism

The mechanism described in Section 5.3.2.1.4 above, open to employees and third parties, is under review to incorporate potential alerts in line with the law on the duty of care and will be finalised in 2018 in conjunction with the representative trade unions.

### 5.3.3.4 Thales initiatives with non-profit organisations

#### 5.3.3.4.1 Actions by the Thales Foundation in 2017

Through its foundation, launched in 2014, Thales is an innovative force for the good of humanity and contributes to a response to the challenges faced by society. To achieve this, the Thales Foundation (the Foundation) draws on the commitment of Thales's employees, who can devote their motivation and skills to the benefit of the two overall themes chosen by the Foundation: education and humanitarian aid.

In the area of education, the Foundation develops projects relating to science and innovation in teaching methods, prioritising children and their teachers in order to increase students' interest, curiosity and abilities in science. The goal is to give young people a taste for innovation and to make them more agile in an increasingly fast-changing world.

The Foundation is also involved in projects aimed at anticipating and reducing the impact of natural and environmental disasters. Through these actions, the Foundation helps to mitigate the vulnerability of populations located in risk areas by supporting risk prevention and preparedness and field mission programmes.

In three years, the Thales Foundation has supported more than 40 partners and 50 projects in around fifteen countries across the world, including 14 projects in 2017. The projects and actions of the Foundation have benefited from the voluntary support of 180 Group employees in 3 years.

#### 5.3.3.4.2 Eight new employee projects supported in six countries in 2017

As part of the annual call for projects devoted to projects submitted by Group employees, eight organisations obtained financial support. Of these projects, six of them with an educational theme focus primarily on combating and correcting the impact of social and economic inequalities on educational success thanks to education on entrepreneurship or teaching on digital technology and IT. Two humanitarian risk projects were also launched in Sri Lanka and Nepal with the aim of helping local populations to prepare for the risks of natural disasters to limit human and material damage.

These projects had an impact on close to 15,000 young people and adults made aware of the different tools and methods to ensure their continuity. Encouraged by the Foundation, some twenty Group employees offered voluntary support to these projects.

#### FOCUS: THREE WINNING PROJECTS IN THREE COUNTRIES

##### A mobile makerspace to learn by building a drone in France

The Apprentis d'Auteuil foundation supports and trains young people with serious social, family and educational issues within 200 establishments in France.

**Project:** deployment of a mobile teaching cart containing the technological tools to carry out practical work and build a drone, thereby encouraging access to new technologies and an interest in key issues for 180 underprivileged high school students from 5 establishments in Occitanie.

##### Lessons and IT resources for the Vellai Thamarai school in India

Thanks to the support of the organisation Vellai Thamarai France, the Vellai Thamarai school in India works to promote the education and integration of a large underprivileged village community of Tamil Nadu.

**Project:** implementation of lessons and IT equipment allowing the schoolteachers to become familiar with digital tools and 160 young pupils to receive an induction in IT.

#### A coastal green belt to fight against natural disasters in Sri Lanka

The Consortium of Humanitarian Agencies (CHA) coordinates humanitarian projects aimed at offering all Sri Lankans equal opportunities in terms of development.

**Project:** creation of environmentally-friendly plant barriers offering the best chance of protection against the impacts of natural disasters and helping to fight drought in the island of Kayts, which has a population of over 10,000.

#### 5.3.3.4.3 Les Savanturiers de l'ingénierie et du numérique: continuation of the pilot learning through research programme

In September 2017, the Foundation renewed its support for the third year running of the *Savanturiers de l'ingénierie et du numérique* pilot engineering and digital technology programme. This approach based on learning through research, conducted in class and sponsored by Thales engineers, relies on the methods and ethics of research as a model for collaborative, ambitious learning methods. Students and teachers are supported by mentors to carry out their research and scientific project, transforming their classroom into a makeshift research laboratory.

#### FOCUS: THE "SAVANTURIERS" YOUNG RESEARCHERS CONFERENCE IN 2017

To close the programme for the academic year, the *Savanturiers* classes were invited to present the results of their research work during end-of-year conferences in Cannes and Gennevilliers.

Year 5 and Year 6 (CM1-CM2) students from Anatole France school in Gennevilliers, supported by three young Thales engineers, captivated the auditorium with a presentation of their project: they gave a step-by-step explanation of the construction and programming of a robot capable of dancing to music, while underlining all the qualities they had gained from this exercise, such as teamwork and perseverance. They orchestrated demonstrations and answered questions from their classmates, as well as sharing their insight into the world of business by talking about their visit to the Thales Gennevilliers site and the Group's activities.

Richard Merra, Deputy Mayor of Gennevilliers, attested to the success of the programme: *"I found this second edition of the Savanturiers to be even richer than the last one. There was notable pleasure from both the students and adults whose contributions went far beyond their professional remit. Thales's engineers play a major role. The students feel it, they love to feel the importance of their success through the eyes of others."*

#### 5.3.3.4.4 Round Off Your Pay: a supplemented collection for five non-profit organisations

Launched in May 2016, the "round off your pay" initiative, designed by the social outreach company microDON, allows every Thales employee in France to support one of five charitable projects presented, by donating the cents from their pay every month, with an optional additional donation of up to €10 per month. All donations are paid to the charities, with Thales committing to match employees' contributions up to an annual ceiling. The micro-donations are obligation-free and participants can at any time change or cancel their donation or choice of project.

During 2017, this innovative outreach tool was used by 3,300 employee micro-donors within the Group's French companies, raising €240,000 to support the following five charitable projects:

- *Planète Urgence* project to distribute school kits in several African countries;
- *Aide et Action* project to create a learning platform and teaching tools to educate students in France and Senegal about community values;
- *Bibliothèques Sans Frontières* project to send “Ideas Box” media kits to children in low-income neighbourhoods in the South of France;
- *Télécoms Sans Frontières* project to re-establish communication networks following humanitarian crises;
- *Pour Un Sourire d'Enfant* to combat school dropout in Cambodia.

Led by government-approved non-profit organisations, these five projects enable the Foundation to support initiatives that spread its values and address social challenges. The Foundation commits to promoting and monitoring each project to help it to achieve its objectives in terms of funding and results on the ground.

#### ANTICIPATION IN THE PROVISION OF SUPPORT TO EMERGENCY INTERVENTIONS BY TÉLÉCOMS SANS FRONTIÈRES IN 2017

As soon as they are alerted to a natural disaster or humanitarian crisis, the teams of Télécoms Sans Frontières (TSF) are deployed in less than three hours to REACH the ground and put in place crucial communication systems for the coordination and management of rescues and the dispatch of humanitarian aid. In addition to providing support to humanitarian players, TSF offers free calls to populations to communicate with and contact their loved ones.

In 2017, Thales’ “round-off” collection contributed to three important TSF missions in Madagascar (Cyclone Enawo), in Saint-Martin and Saint-Barthélemy (Hurricane Irma) and in Dominique (Hurricane Maria). The reinstatement of telecommunications benefited more than 450 aid and humanitarian workers and more than 7,500 families.

#### 5.3.3.4.5 Other international examples of local engagement initiatives

Many Group companies also support local and national organisations, particularly in the areas of education and outreach to the underprivileged or people with disabilities. They offer them financial and material support and invite Group employees to volunteer for the different charitable projects or actions. In many countries, a range of projects increase Thales’s contribution to education in science, technology, engineering and mathematics<sup>(1)</sup>.

##### Australia

Thales Australia has significantly increased its impact with five new projects to promote access for young people to science, technology and the digital world, allowing them to learn by doing, to play their part in technology and to work towards careers in industry and technology. These actions benefit from the support and volunteering of Thales employees and promote links between education and industry.

The main partnership was signed with the Commonwealth Scientific and Industrial Research Organisation (CSIRO) for three years, in relation to two programmes conducted in Australian schools. The aim is to support students in developing scientific thinking, the ability to conceive and conduct research work, to solve problems and to communicate effectively. Thanks to Thales’s involvement, they gain a better understanding of the industrial world and of the importance of science and technology.

A programme providing an introduction to computer programming, CoderDojo, allows young people aged 7 to 17 to take free workshops run by employee volunteers during the weekends on a Thales site.

Robot Obedience School is a learning platform which allows children as young as six to programme robots. P-Tech is a mentoring programme to guide young people towards university studies and boost their employability. Subs in schools gives high school students the opportunity to work on a project to create a guided submarine in class.

##### Canada

As is the case every year, employees took action through campaigns of donations matched by Thales Canada for United Way to support families in difficulty.

##### China

Thales China Enterprise Management Co. Ltd. renewed its partnership with the Cedar Foundation, an organisation which supports students from isolated or underprivileged areas. Students had the opportunity to take part in visits to Thales premises, professional development workshops and a mentoring programme to support them in their integration into the workplace.

##### United States

Thales USA gave its support to the innovative Iridescent Technovation Challenge programme: this international competition for young women (high school students) is aimed at developing their entrepreneurial and leadership skills. The participants are invited to identify an issue in their community, to develop a mobile application to solve it, then to communicate and transform their ideas into a viable business activity.

The partnership with the Team America Rocketry Challenge was renewed, allowing for the participation and selection of students for this international rocket launch competition which involves 4,000 students every year wishing to pursue a career in science.

Thales USA employees also contributed to voluntary mentoring actions, a collection of educational supplies for the organisation Boys Town and food items for a social centre in Arlington.

##### Mexico

Following on from the support provided by the Thales Foundation in 2016, in Mexico, Thales Mexico and the SUM Foundation organised a new training session on innovation to support 60 young women aged between 14 and 21 to design and develop a project which responds to an issue in their community. This educational innovation project is an opportunity to help these young women from problem neighbourhoods to develop useful skills for future job roles, and in particular to offer them access to the world of science.

Following the powerful earthquake which hit Mexico in September 2017, causing almost 230 deaths, Thales supported actions to offer aid to victims of the Mexican Red Cross through donations of money, medication and food items.

##### Netherlands

More than 60 visits of Thales sites in the Netherlands were organised in 2017 to welcome more than 1,000 students and school pupils with a view to encouraging them to consider a career in industry and technology.

Thales Netherlands actively supported the participation of a team of international students in the World Solar Challenge Australia, an innovative challenge focused on the issue of sustainable technological development and improved performance: advised and coached by Thales experts for two years, the team had the opportunity to design and build its own solar-powered vehicle to compete in the race in Australia.

##### United Kingdom

Thales’s aim in the United Kingdom is to inspire, inform and involve young people through initiatives aimed at offering them the necessary skills and knowledge to make an informed decision as to their personal and professional choices.

(1) STEM education, in English-speaking countries.

In 2017, Thales UK worked with more than 45 schools and colleges to organise activities to meet their needs, and in support of young people within its local communities. As a partner of the Primary Engineers programme, Thales UK supported the training of 40 teachers to implement long-term scientific projects in primary schools in the south-east of England. As part of the Tomorrows Engineers programme, Thales took part in various events of the Big Bang, a major national event to raise awareness on science and engineering which is attended by more than 70,000 young people each year.

Through a partnership with the UK organisation of voluntary scientific ambassadors (STEM volunteers), Thales UK rallied more than 200 employees trained to promote opportunities in science and technology in the United Kingdom.

#### Singapore/Cambodia, the Philippines, Vietnam

Thales Asia continued its partnership with Passerelles numériques, an organisation which offers underprivileged young people in Cambodia, the Philippines and Vietnam access to a qualified job in the new technology sector. Through this partnership, Thales funded the education of 20 students for two years until they achieved their IT diploma in addition to outreach leave assignments for employees wishing to offer their skills to the organisation.

### 5.3.3.5 Partnerships with professional, international and non-governmental organisations

Through partnerships with numerous organisations, Thales has been able to share its best practices with other companies, to anticipate changes in regulations and standards, and to promote the conditions for equal competition among the players in its business segment.

In this regard, Thales works closely with numerous bodies, including:

- the United Nations, and specifically the UN Global Compact; in 2017, for the sixth year running, Thales achieved Global Compact Advanced level in the UN Global Compact differentiation programme; Thales confirms its involvement in this initiative through its regular involvement in the work of the “Global Compact Advanced” club and the *Droits Humains* (Human Rights) club of the Global Compact France;
- the Organisation for Economic Cooperation and Development (OECD);
- the European Commission;

- the International Chamber of Commerce (ICC);
- the Mouvement des Entreprises de France (the French employers’ confederation (MEDEF)): International Committee, CSR Committee, Ethics and Guiding Principles Committee, Economic Intelligence Committee, Internationalisation Committee, Sustainable Development Division;
- the Association Française des Entreprises Privées (the French Association of Private Companies (AFEP));
- French investor relations association CLIFF;
- the Aerospace and Defence Industries Association of Europe (ASD);
- the Aerospace Industries Association of America (AIA);
- the *Groupe des Industries Françaises Aéronautiques et Spatiales* (the Group of French Aeronautic and Space Industries (GIFAS));
- the US-based ethics and integrity body Defense Industry Initiative (DII);
- various forums set up by the main British companies in the defence industry, including UK National Defence Business Ethics Forum, ADS Supply Chain 21 Task Force, Institute of Business Ethics;
- the Ethics Network Australian Defence Industry (ENADI);
- the *Observatoire sur la Responsabilité Sociétale des Entreprises* (Centre for Corporate Social Responsibility (ORSE));
- *le Cercle d’Éthique des Affaires* (Business Ethics Circle (CEA));
- the International Aerospace Environmental Group (IAEG), board member;
- the *Association pour la promotion de la Conformité Réglementaire Santé Sécurité Environnement* (Association for the Promotion of Compliance with Health, Safety and Environmental Regulations (ACORES)).

Thales plays an active role in the work of these organisations.

The Group is also a founding member and joint chair of the International Forum on Business Ethical Conduct (IFBEC), whose last worldwide forum took place in Washington in October 2017.

In the United States, in 2002, Thales was the first non-US company to sign the Defense Industry Initiative. In the United Kingdom, the Group’s UK subsidiary was one of the first members of the UK National Defence Business Ethics Forum (formerly known as the Defence Industry Anti-Corruption Forum), set up by the main defence companies present in the country and by the industry’s professional associations.

Thales also pursues a policy of regular, high-quality dialogue with its stakeholders, including the financial community, socially responsible investment funds, ratings agencies and non-financial analysts.

Finally, Thales maintains regular contact with NGOs such as Transparency International, particularly on matters related to business ethics, and Amnesty International and Saferworld on the question of Human Rights.

## 5.3.4 Social indicators

Description	2017 data	Comments/References
Number of operational entities that assessed risks of corruption	111	Corruption risk, just like the other major risks on the Group's risk map, is an integral part of the overall Thales risk management system. As part of the Group's self-assessment and internal control policy, the 111 main operational entities conducted a self-assessment of their exposure to the risk of corruption and, in certain cases, defined an action plan with a view to continually improving the system. See the section on Internal control and risk management – Ongoing improvement process – <b>Self-assessment and ongoing improvement of corporate risk management</b> .
Communication and training with regard to anti-corruption policies and procedures	1,035	The benchmark training is delivered by multilingual trainers who are specialists in the field of ethical business conduct. Lasting four hours, the course takes place either on the Thales Learning Hub campuses across the world or directly on site. Other ad hoc training is also given in specific environments, such as for senior executives and country teams. In addition, an e-learning programme comprising three 30-minute modules (in French, English and German) is available to all Group employees, with the potential addition of country initiatives; 2,500 learners completed one or more modules in 2017.
Proven cases of corruption and measures taken	None	Since 2004, a global professional alert mechanism has been in place within Thales. During 2017, this mechanism was reviewed with a view to meeting the requirements of the Sapin II law, the new European regulation on personal data protection which will enter into force on 25 May 2018 and law 2017-399 on the duty of care of parent companies and subcontracting companies. Certain countries in which Thales has a significant presence have supplemented this system with a local whistle-blowing system, notably the United Kingdom, the United States and Australia. None of the incidents reported in 2017 concerned a proven case of corruption.

The overall system is completed by Thales's active participation in various initiatives in the fight against corruption. Thales also actively participates in national professional organisations (including MEDEF, GIFAS and ADS<sup>(1)</sup>) and international organisations (Business Ethics committee of ASD<sup>(2)</sup>, ICC<sup>(3)</sup>, B20<sup>(4)</sup>, IFBEC<sup>(5)</sup>, etc.) dealing with business ethics, and has an active presence within the working groups of intergovernmental organisations (OECD, United Nations, etc.).

(1) Association of UK Aerospace, Defence Security & Space Industries.

(2) Aerospace and Defence Industries Association of Europe.

(3) International Chamber of Commerce.

(4) International business community bringing together 22 employer organisations.

(5) International Forum on Business Ethical Conduct.

## 5.4 REPORT BY THE INDEPENDENT THIRD PARTY ON THE CONSOLIDATED HUMAN RESOURCES, ENVIRONMENTAL AND SOCIAL INFORMATION INCLUDED IN THE MANAGEMENT REPORT

*This is a free English translation of the Independent third party's report issued in French and is provided solely for the convenience of English-speaking readers. This report should be read in conjunction with, and construed in accordance with, French law and professional standards applicable in France.*

To the Shareholders,

In our capacity as independent third party, certified by COFRAC number 3-1058 (scope available at [www.cofrac.fr](http://www.cofrac.fr)), and member of the Mazars network of one of the Company's statutory auditors, we hereby report to you on the consolidated human resources, environmental and social information for the year ended 31 December 2017, included in the management report (hereinafter named "CSR Information"), pursuant to Article L. 225-102-1 of the French Commercial Code (*Code de commerce*).

### Company's responsibility

The Board of Directors is responsible for preparing a company's management report including the CSR Information required by Article R. 225-105-1 of the French Commercial Code in accordance with the reporting criteria used by the Company (hereinafter the "Reporting Criteria"), summarised in the management report and available on request from the Company's head office.

### Independence and quality control

Our independence is defined by regulatory texts, the French Code of Ethics (*Code de déontologie*) of our profession and the requirements of Article L. 822-11-3 of the French Commercial Code. In addition, we have implemented a system of quality control including documented policies and procedures regarding compliance with the ethical requirements, French professional standards and applicable legal and regulatory requirements.

### Responsibility of the Independent Third-Party

On the basis of our work, our responsibility is to:

- attest that the required CSR Information is included in the management report or, in the event of non-disclosure of a part or all of the CSR Information, that an explanation is provided in accordance with the third paragraph of Article R. 225-105 of the French Commercial Code (Attestation regarding the completeness of CSR Information);
- express a limited assurance conclusion that the CSR Information taken as a whole is, in all material respects, fairly presented in accordance with the Guidelines (Conclusion on the fairness of CSR Information).

It is however not our responsibility to attest compliance with other legal dispositions where appropriate, in particular those included in Article L. 225-102-4 of the French Commercial Code (vigilance plan of parent companies) and law n° 2016-1691, dated December 9th, 2016, said Sapin II (fight against corruption).

Our work involved 9 persons and was conducted between end of October 2017 and February 2018 during a 14 week period.

We performed our work in accordance with the French professional standards and with the order dated 13 May 2013 defining the conditions under which the independent third party performs its engagement and with ISAE 3000<sup>(1)</sup> concerning our conclusion on the fairness of CSR Information.

### I. Attestation regarding the completeness of CSR Information

#### Nature and scope of our work

On the basis of interviews with the individuals in charge of the relevant departments, we obtained an understanding of the Company's sustainability strategy regarding human resources and environmental impacts of its activities and its social commitments and, where applicable, any actions or programmes arising from them.

We compared the CSR Information presented in the management report with the list provided in Article R. 225-105-1 of the French Commercial Code.

For any consolidated information that is not disclosed, we verified that explanations were provided in accordance with Article R. 225-105, paragraph 3 of the French Commercial Code.

We verified that the CSR Information covers the scope of consolidation, i.e., the Company, its subsidiaries as defined by Article L. 233-1 and the controlled entities as defined by Article L. 233-3 of the French Commercial Code within the limitations set out in the methodological note, presented in the Sections 5.2.8 "Environmental reporting rules" and the "Methodological note" of Sections 5.1 in the management report.

### Conclusion

Based on the work performed and given the limitations mentioned above, we attest that the required CSR Information has been disclosed in the management report.

### II. Conclusion on the fairness of CSR Information

#### Nature and scope of our work

We conducted about forty interviews with the persons responsible for preparing the CSR Information in the departments in charge of collecting the information and, where appropriate, responsible for internal control and risk management procedures, in order to:

- assess the suitability of the Guidelines in terms of their relevance, completeness, reliability, neutrality and understandability, and taking into account industry best practices where appropriate;
- verify the implementation of data-collection, compilation, processing and control process to REACh completeness and consistency of the CSR Information and obtain an understanding of the internal control and risk management procedures used to prepare the CSR Information.

We determined the nature and scope of our tests and procedures based on the nature and importance of the CSR Information with respect to the characteristics of the Company, the human resources and environmental challenges of its activities, its sustainability strategy and industry best practices.

Regarding the CSR Information that we considered to be the most important<sup>(2)</sup>:

- at Group level, we referred to documentary sources and conducted interviews to corroborate the qualitative information (organisation, policies, actions), performed analytical procedures on the quantitative information and verified, using sampling techniques, the

calculations and the consolidation of the data. We also verified that the information was consistent and in agreement with the other information in the management report;

- at the level of a representative sample of entities selected by us<sup>(1)</sup> on the basis of their activity, their contribution to the consolidated indicators, their location and a risk analysis, we conducted interviews to verify that procedures are properly applied, and we performed tests of details, using sampling techniques, in order to verify the calculations and reconcile the data with the supporting documents. The selected sample represents on average 56% of headcount considered as material data<sup>(4)</sup> of social issues and between 22% and 76% of quantitative environmental data considered as material data of environmental issues.

For the remaining consolidated CSR Information, we assessed its consistency based on our understanding of the Company.

We also assessed the relevance of explanations provided for any information that was not disclosed, either in whole or in part.

We believe that the sampling methods and sample sizes we have used, based on our professional judgement, are sufficient to provide a basis for our limited assurance conclusion; a higher level of assurance would have required us to carry out more extensive procedures. Due to the use of sampling techniques and other limitations inherent to information and internal control systems, the risk of not detecting a material misstatement in the CSR information cannot be totally eliminated.

## Conclusion

Based on the work performed, no material misstatement has come to our attention that causes us to believe that the CSR Information, taken as a whole, is not presented fairly in accordance with the Guidelines.

Paris-La Défense, 5 March 2018

The Independent Third-Party

**Mazars**

Anne-Laure Rousselou  
Partner

Edwige Rey  
CSR & Sustainable development Partner

(1) ISAE 3000 – Assurance engagements other than audits or reviews of historical financial information.

(2) **Environmental Information:** Electricity consumption, Annual fossil energy consumption, Water consumption, GHG (greenhouse gas) emissions: GHG emissions from energy consumption (CO<sub>2</sub>), GHG emissions from substances (CO<sub>2</sub>), GHG emissions from transportation (business travels – CO<sub>2</sub>); Industrial Wastewater Discharges, Common waste production (excluding exceptional items), hazardous waste production (excluding exceptional items), common waste recovery (%), hazardous waste recovery (%).

**Human Resources Information:** Global workforce as 31/12/2017, Women/men breakdown (%), workforce by age, Recruitments, Redundancies, Total number of training hours, Absenteeism rates, Actions in favor of gender equality, Attractiveness policy, professional development of employees

**Social information:** Overall performance of suppliers in ESG responsibility, Communication and training on policies and procedures in the fight against corruption, Part of class A suppliers evaluated on HSE criteria, Number of sites that have been subjected to an assessment of risks of corruption and substantial risks identified, Global organization for listening and managing the quality of customer relation

(3) **Environmental Information:** Thales Communications & Security, Thales Alenia Space (Rome), Thales Alenia Space (Charleroi), Thales Underwater Systems (Templecombe Hub), Thales Land Australia (Mulwala), Thales Electron Devices (Thonon), Thales Communications & Security (Laval), TDA Armements (La Ferté), Thales Research & Technology (Palaiseau).

In addition to environmental information (fuel consumption and GHG emissions from substances (CO<sub>2</sub>)): TED Vélizy

**Human resources Information:** Legal entities of Thales France and Thales Canada

**Social Information:** law/Human Resources Department, Ethics & Corporate Responsibility Department, Relationship suppliers Director, Quality & Customer Satisfaction Department

Détailler les sites concernés dans le corps du rapport ou en note de bas de page

(4) See environmental information considered to be the most important.

## 5.5 TABLE OF RECONCILIATION (ARTICLES L. 225-102-1 AND R. 225-105-1 OF THE FRENCH COMMERCIAL CODE)

In accordance with the Articles L. 225-102-1 and R. 225-105-1 of the French Commercial Code on transparency obligations for companies on social and environmental matters, Thales provides information in its management report on the Group's social, environmental and societal issues. An independent verifier issued a declaration of inclusion and a limited assurance report on consolidated social, environmental and societal information.

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# DECLARATION FROM THE PERSON RESPONSIBLE FOR THE REGISTRATION DOCUMENT

I hereby certify that, after having taken all reasonable measures to this effect, to the best of my knowledge, the information contained in this Registration Document is accurate and does not omit any material fact.

I certify that, to the best of my knowledge, the financial statements have been prepared in accordance with applicable accounting standards and give a fair view of the assets, liabilities, financial position and results of the Company and of all the entities taken as a whole included in the consolidation, and that the management report included on page 8 a fair view of the development and performance of the business and financial position of the Company and of all the entities taken as a whole included in the consolidation, as well as a description of the main risks and uncertainties to which they are exposed.

I have received a letter from the statutory auditors confirming that they have completed the work they undertook to audit the information related to the financial situation and the financial statements included in this document, as well as a review of this document in its entirety.

The historic financial information presented in this Registration Document is the subject of reports from the statutory auditors. The report on the consolidated financial statements for 2017 on pages 80 to 83 has been issued without reservation and the parent company financial statements report for 2017 on pages 116 to 118 has been issued without reservation and include one observation. The reports on the consolidated financial statements for 2015 and 2016, included by reference in this 2017 Registration Document, were issued without reservation.

Paris-La Défense, 30 March 2018

**Patrice Caine**  
Chairman and CEO

# EUROPEAN CROSS-REFERENCE TABLE

## (ANNEX 1 OF THE EUROPEAN REGULATION NO. 809/2004)

To facilitate reading of this Registration Document, the following European Cross-Reference table allows the identification of the main information required by Annex 1 of the European Regulation No. 809/2004.

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# CHANGES MADE TO 2017 REGISTRATION DOCUMENT STRUCTURE

Pursuant to Order No. 2017-1162 of 12 July 2017 and Decree No. 2017-1174 of 18 July 2017<sup>(1)</sup>, the following changes were made to the structure of the Thales Registration Document for financial year 2017:

- the description of internal control and risk management procedures, which appeared in the Chairman's Report (Section 3.2.2 of the 2016 Registration Document, p. 137 and thereafter) has been moved in the Group Management Report, to Section 1.1.3 of the 2017 Registration Document;
- conversely, the Corporate Governance Report, which now replaces the Chairman's Report, includes in its Section 3.2.2 all compensation factors for company representatives, which are listed in Section 3.5.1 of the 2016 Registration Document;
- similarly, this Corporate Governance Report, in Section 3.2.1.6 of the 2017 Registration Document, includes certain factors previously included in the Group or parent company management report, i.e.,
- the summary table of current valid delegations granted by the general shareholders' meeting with regard to capital increases (Section 4.3.3.9 of the 2016 Registration Document,
- a detailed description of the principal factors likely to have an impact in the event of a public offering (Section 4.3.3.10 of the 2016 Registration Document);
- the description of any agreements entered into between Thales subsidiaries and related parties<sup>(2)</sup>, if they do not correspond to current agreements entered into under normal conditions (included under Section 4.4 of the 2016 Registration Document).

This new Section 3.2.1.6 also sets forth the specific conditions for shareholder participation in the general shareholders' meeting, which for the sake of consistency, now include most elements of Section 4.2 "General Shareholders' Meetings" of the 2016 Registration Document. The remainder of the text of this former Section 4.2, relating to statements involving exceeding statutory thresholds, is included in Section 4.1 (general company information) of the 2017 Registration Document, Section 4.2 "General Shareholder Meetings" of the 2016 Registration Document, has not been retained in the 2017 Registration Document, and Section 4 of the latter has been renumbered.

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(1) Order and decree providing various measures for simplification and clarification of the reporting obligations for which companies are responsible.

(2) Agreements entered into directly or through an intervening third party between, on the one hand, a company representative or shareholder holding a percentage of voting rights greater than 10% of a company, and, on the other hand, another company in which the former directly or indirectly holds more than half the share capital.

# ANNUAL FINANCIAL REPORT RECONCILIATION TABLE

To facilitate reading of the Registration Document, the following table allows the identification of information that constitutes the Annual Financial Report in accordance with Article L. 451-1-2 of the French Monetary and Financial Code and Article 222-3 of the AMF General Regulations.

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