



TORNOS HOLDING S.A., MOUTIER
CONSOLIDATED AND HOLDING FINANCIAL STATEMENTS 2008

Tornos Group

Report of the Statutory Auditor	4
Consolidated Financial Statements	7
Notes to the Consolidated Financial Statements	11

Tornos Holding S.A., Moutier

Report of the Statutory Auditor	52
Financial Statements	55
Notes to the Financial Statements	58
Proposed appropriation of available earnings	61

Report of the Statutory Auditor

to the General Meeting of

Tornos Holding S.A., Moutier

Report of the statutory auditor on the consolidated financial statements

As statutory auditor, we have audited the consolidated financial statements of Tornos Holding S.A., which comprise the income statement, balance sheet, statement of changes in equity, cash flow statement and notes (pages 7 to 50), for the year ended December 31, 2008.

Board of Directors' Responsibility

The Board of Directors is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with the International Financial Reporting Standards (IFRS) and the requirements of Swiss law. This responsibility includes designing, implementing and maintaining an internal control system relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error. The Board of Directors is further responsible for selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Swiss law and Swiss Auditing Standards as well as the International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers the internal control system relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control system. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements for the year ended December 31, 2008 give a true and fair view of the financial position, the results of operations and the cash flows in accordance with the International Financial Reporting Standards (IFRS) and comply with Swiss law.

Report on other legal requirements

We confirm that we meet the legal requirements on licensing according to the Auditor Oversight Act (AOA) and independence (article 728 CO and article 11 AOA) and that there are no circumstances incompatible with our independence.

In accordance with article 728a paragraph 1 item 3 CO and Swiss Auditing Standard 890, we confirm that an internal control system exists which has been designed for the preparation of consolidated financial statements according to the instructions of the Board of Directors.

We recommend that the consolidated financial statements submitted to you be approved.

PricewaterhouseCoopers SA



Michael Foley
Audit expert
Auditor in charge



Aude Joly
Audit expert

Neuchâtel, March 3, 2009

Enclosure:

- Consolidated financial statements (income statement, balance sheet, statement of changes in equity, cash flow statement and notes)

CONSOLIDATED INCOME STATEMENT

In thousands of CHF, except per share data

For the years ended December 31,	Notes	2008	2007
Gross sales		262'944	287'384
Rebates and discounts		-2'891	-2'128
Net sales		260'053	285'256
Cost of sales		-165'883	-169'907
Gross profit		94'170	115'349
Marketing and sales		-43'884	-45'725
General and administrative expenses		-21'102	-22'792
Research and development		-16'245	-16'899
Other income/(expenses) – net	8	154	2'813
Earnings before interest and taxes (EBIT)		13'093	32'746
Financial expenses – net	9	-576	-989
Exchange gains/(losses) – net		-4'254	-568
Income before income taxes		8'263	31'189
Income tax credit/(charge)	10	-2'221	3'948
Net income		6'042	35'137
Earnings per share	26		
– basic		0.42	2.42
– diluted		0.42	2.36
Earnings before interest and taxes (EBIT)		13'093	32'746
Depreciation and amortisation		6'758	6'597
Earnings before interest, income taxes, depreciation and amortisation (EBITDA)		19'851	39'343

The accompanying notes form an integral part of these consolidated financial statements.

CONSOLIDATED BALANCE SHEET

In thousands of CHF

As of December 31,	Notes	2008	2007
ASSETS			
Cash and cash equivalents	11	14'268	29'689
Trade receivables	12	48'457	52'487
Inventories	13	94'739	76'813
Other receivables and prepayments	14	16'160	17'011
Total current assets		173'624	176'000
Available-for-sale financial assets	15	1'787	–
Property, plant and equipment	16	43'009	40'297
Goodwill	17	2'873	–
Deferred tax assets	18	963	2'615
Total non-current assets		48'632	42'912
Total assets		222'256	218'912
LIABILITIES AND EQUITY			
Interest bearing loans and borrowings	19	7'359	1'052
Trade payables		29'093	19'765
Other payables	20	21'546	23'119
Current tax liabilities		193	295
Provisions	21	5'103	7'930
Total current liabilities		63'294	52'161
Interest bearing loans and borrowings	19	1'632	1'374
Retirement benefit obligations	22	2'141	1'451
Provisions	21	907	3'744
Deferred tax liabilities	18	539	3
Total non-current liabilities		5'219	6'572
Total liabilities		68'513	58'733
Total equity		153'743	160'179
Total liabilities and equity		222'256	218'912

The accompanying notes form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

<i>In thousands of CHF</i>	Ordinary shares (note 23)	Share premium	Treasury shares (note 23.3)	Retained earnings (note 24)	Currency translation difference	Total
At December 31, 2006	68'954	14'234	-84	36'718	-1'364	118'458
Currency translation difference					-303	-303
<i>Net income/(expense) recognised directly in equity</i>					-303	-303
Net income for the year				35'137		35'137
<i>Total recognised income/(expense) for the year</i>				35'137	-303	34'834
Issuance of new shares	5'966	1'676				7'642
Purchase of treasury shares			-1'986			-1'986
Share-based compensation				1'287		1'287
Other expense (note 23.3)				-56		-56
At December 31, 2007	74'920	15'910	-2'070	73'086	-1'667	160'179
Fair value gain/(loss) on available-for-sale financial assets (note 2.9)				-1'787		-1'787
Currency translation difference					-963	-963
<i>Net income/(expense) recognised directly in equity</i>				-1'787	-963	-2'750
Net income for the year				6'042		6'042
<i>Total recognised income/(expense) for the year</i>				4'255	-963	3'292
Issuance of new shares	168	46				214
Purchase of treasury shares			-9'195			-9'195
Sale of treasury shares			4'696	1'257		5'953
Reduction of par value of the shares (note 23.1)	-7'499	-81		230		-7'350
Share-based compensation				701		701
Other expense (note 23.3)				-51		-51
At December 31, 2008	67'589	15'875	-6'569	79'478	-2'630	153'743

The accompanying notes form an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT

In thousands of CHF

For the years ended December 31,	Notes	2008	2007
Net income		6'042	35'137
Adjustments for:			
Taxes		2'221	-3'948
Depreciation of property, plant and equipment	16	6'758	6'597
Gain on disposal of property, plant and equipment		-50	-2'773
Other non cash items		41	1'157
Decrease/(increase) in working capital:			
Trade receivables		8'055	-1'679
Other receivables		1'161	-3'885
Inventories		-12'398	-724
Trade payables		7'002	-2'583
Other current payables and provisions		-13'763	2'796
Interest expenses		104	47
Income tax paid		-624	-27
Income tax refund		-	880
Net cash provided by operating activities		4'549	30'995
Cash flow from investing activities			
Acquisition of subsidiaries – net of cash acquired		-4'826	–
Investment in available-for-sale financial assets		-3'574	–
Investment in property, plant and equipment		-6'715	-9'065
Disposal of property, plant and equipment		176	7'324
Interest received		201	224
Net cash used in investing activities		-14'738	-1'517
Cash flow from financing activities			
Repayments of borrowings, including finance lease liabilities		-1'103	-15'361
Proceeds from borrowings		6'883	578
Proceeds from issuance of share capital		214	7'642
Reduction of par value of shares – net	23.1	-7'350	–
Purchase of treasury shares	23.3	-9'195	-1'986
Sale of treasury shares	23.3	5'953	–
Payment of other financing expenses	23.3	-51	-56
Interest paid		-305	-295
Net cash used in financing activities		-4'954	-9'478
Net increase/(decrease) in cash and cash equivalents		-15'143	20'000
Cash and cash equivalents at beginning of year		29'689	9'849
Effects of exchange rate changes		-278	-160
Cash and cash equivalents at end of year		14'268	29'689

The accompanying notes form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

1 Activity and Group structure

Tornos Holding S.A. (the Company) is a company domiciled in Moutier, Switzerland. The Group is active in the development, manufacture, marketing and servicing of machine tools. The Group manufactures solely in Moutier and La Chaux-de-Fonds, Switzerland, and markets the product lines on a worldwide basis. The Group's operations outside of Switzerland principally include European countries, North America and Asia.

These consolidated financial statements have been approved for issue by the Board of Directors on March 3, 2009. These financial statements will be submitted for approval to the General Meeting of Shareholders on April 7, 2009.

2 Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These accounting policies have been consistently applied to all the years presented.

2.1 Basis of preparation

The consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS) and comply with Swiss law. The consolidated financial statements are prepared under the historical cost convention except that, as disclosed in the accounting policies below, certain items, including derivatives, are shown at fair value. All amounts set out in the consolidated financial statements are presented in Swiss francs (CHF), rounded to the nearest thousand (KCHF) unless otherwise stated.

The preparation of consolidated financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in note 4.

2.1.1 The following standard has been early adopted as of January 1, 2008:

IFRS 3 (amendment), "Business combinations" and consequential amendments to IAS 27 "Consolidated and separate financial statements". The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Costs directly attributable to the acquisition are charged to income. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

2.1.2 Amendments and interpretations to published standards effective in 2008

IAS 39 (amended), "Financial instruments: Recognition and measurement". The amendment allows the reclassification of certain financial assets previously classified as "held for trading" or "available for sale" to another category under limited circumstances. Various disclosures are required where a reclassification has been made. Derivatives and assets designated as "at fair value through profit or loss" under the fair value option are not eligible for this reclassification.

IFRIC 11, "IFRS 2 – Group and treasury share transactions". IFRIC 11 provides guidance on whether share-based transactions involving treasury shares or involving group entities (for example options over a parent's shares) should be accounted for as equity-settled or cash-settled share-based payment transactions in the stand-alone accounts of the parent and Group companies.

IFRIC 12, "Service concession arrangements". IFRIC 12 applies to contractual arrangements whereby a private sector operator participates in the development, financing, operation and maintenance of infrastructure for public sector services.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

IFRIC 13, "Customer loyalty programmes" (effective for annual periods beginning on or after July 1, 2008). IFRIC 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values.

IFRIC 14, "IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction". IFRIC 14 provides guidance on assessing the limit in IAS 19 on the amount of the surplus that can be recognised as an asset. It also explains how the pension asset or liability may be affected by a statutory or contractual minimum funding requirement.

IFRIC 16, "Hedges of a net investment in a foreign operation" (effective for annual periods beginning on or after October 1, 2008). IFRIC 16 provides guidance on hedging the foreign currency risk arising from net investments in foreign operations in accordance with IAS 39.

None of these amendments and interpretations have any impact on the Group's account.

2.1.3 *New standards, interpretations to existing standards and standards amendments that are not yet effective*

The Group has not early adopted any other new standards, interpretations to existing standards and standards amendments which need adoption by January 1, 2009, at the latest. The Group is currently evaluating the potential impact, if any, that the adoption of these new or amended standards will have on the Group's consolidated financial statements.

2.2 Consolidation

2.2.1 *Subsidiaries*

Subsidiaries are those companies in which the Company, directly or indirectly, holds an interest of more than 50% of the voting rights or otherwise has power to exercise control over the operations. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Acquisitions are accounted for using the purchase method. A listing of the Company's subsidiaries is set out in note 5.

2.2.2 *Balances and transactions eliminated on consolidation*

Intra-group balances and transactions, and any unrealised gains arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

2.3 Foreign currencies

2.3.1 *Functional and presentation currency*

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Swiss francs (CHF), rounded to the nearest thousand (KCHF) unless otherwise stated, which is the Company's functional and presentation currency.

2.3.2 *Foreign currency transactions*

Transactions in foreign currencies are translated to CHF at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to CHF at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated to CHF at the foreign exchange rate ruling at the date of the transaction.

2.3.3 *Financial statements of foreign operations*

The assets and liabilities of foreign operations are translated to CHF at foreign exchange rates ruling at the balance sheet date. The revenues, expenses and cash flows of foreign operations are translated to CHF at the average exchange rates prevailing during the reporting period. Foreign exchange differences arising on this translation are recognised directly in equity as currency translation difference.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

2.4 Revenue recognition

Revenues include sales of machines, spare parts and service costs which can be directly charged to customers. Sales are recognised on the full completion of the delivery or service (upon delivery of products or customer acceptance in the case of “bill and hold” sales, or performance of services), net of sales taxes and discounts, and after eliminating sales within the Group. Gross sales represent the binding amounts effectively invoiced to customers. Net sales represent gross sales net of rebates and discounts granted after billing.

2.5 Cash and cash equivalents

Cash and cash equivalents consist of cash balances and short-term liquid investments with original maturities of three months or less. They are stated at their nominal amounts.

2.6 Trade and other receivables

Trade and other receivables are initially recognised at fair value and subsequently measured at amortised cost using the effective interest rate method, less provision for impairment determined based on a review of all outstanding amounts at the year-end. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor and probability that the debtor will enter bankruptcy or financial reorganisation are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the estimated future cash flows. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement within general and administrative expenses. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables. Subsequent recoveries of amounts previously written off are credited against general and administrative expenses in the income statement.

2.7 Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

The cost of inventories is based on the weighted average principle and is composed of three categories: (a) materials and components (b) work in progress and (c) finished goods and spare parts.

The cost of inventories includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of overheads, except interest expenses, based on normal operating capacity.

2.8 Financial assets

The Group has only the following categories of financial assets: loans and receivables, available-for-sale financial assets and derivatives at fair value through profit or loss. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

2.8.1 Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Group's loans and receivables comprise cash and cash equivalents, trade receivables and other receivables in the balance sheet (see accounting policy 2.5 and 2.6).

Loans and receivables are carried at amortised cost using the effective interest method.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

2.8.2 *Available-for-sale financial assets*

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date (see accounting policy 2.9).

2.8.3 *Derivatives at fair value through profit or loss*

Financial assets at fair value through profit or loss are financial assets held for trading. Assets in this category are classified as current assets.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired.

2.9 **Available-for-sale financial assets**

Regular purchases and sales of these financial assets are recognised on the trade date – the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs. They are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets are subsequently carried at fair value.

Changes in the fair value of monetary and non-monetary securities classified as available-for-sale are recognised in equity. When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement as financial income. Interest on available-for-sale securities calculated using the effective interest method and dividends on available-for-sale equity instruments are recognised in the income statement as part of financial income when the Group's right to receive payments is established.

A significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

The fair values of quoted investments are always based on current bid prices.

2.10 **Derivative financial instruments and hedging activities**

Derivatives are initially recorded on the date they are entered into and subsequently carried at fair value in current assets or liabilities. The Group does not use hedge accounting. Changes in the fair value of derivative instruments are recorded in the period in which they arise on the various lines of the income statement to which they relate.

2.11 **Property, plant and equipment**

2.11.1 *Owned assets*

Property, plant and equipment are stated at cost less accumulated depreciation (see below) and impairment losses, if any (see accounting policy 2.14). Interest cost on borrowings to finance property, plant and equipment during the course of construction are capitalised.

2.11.2 *Subsequent expenditure*

Expenditure incurred to replace a component of an item of property, plant and equipment that is accounted for separately, including major inspection and overhaul costs, is capitalised. Other subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of property, plant and equipment. All other expenditure is recognised in the income statement as an expense as incurred.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

2.11.3 *Leased assets*

Leases with terms for which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Plant and equipment acquired by way of finance leases are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the leases, less accumulated depreciation (see below) and impairment losses, if any (see accounting policy 2.14).

Each lease payment is allocated between the liability and financial charges so as to achieve a constant rate on the finance balance outstanding. The corresponding lease obligations, net of financial charges, are included in interest bearing borrowings. The interest element of the finance charge is recognised in the income statement over the lease period.

2.11.4 *Depreciation*

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of items of property, plant and equipment. Land is not depreciated. The estimated useful lives are as follows:

■ Buildings	20–40 years
■ Installations	8–12 years
■ Machinery	8–12 years
■ Other equipment	3–10 years

The asset's residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate components.

2.12 **Goodwill**

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiaries at the date of acquisition. Separately recognised goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

2.13 **Intangible assets**

Internal research costs are charged against income as incurred. Internal development costs are capitalised as intangible assets only when there is an identifiable asset that will generate expected future economic benefits and when the cost of such an asset can be measured reliably. The Group does not currently have any such internal development costs that qualify for capitalisation as intangible assets. Development expenditure which does not meet the criteria above is recognised as an expense as incurred.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

2.14 Impairment

Assets that have an indefinite useful life, for example goodwill, are not subject to amortisation and are tested annually for impairment. The carrying amounts of the Group's other assets, other than inventories (see accounting policy 2.7), deferred tax assets (see accounting policy 2.15) and pension assets (see accounting policy 2.16), are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount, being the higher of the asset's net selling price and value in use, is estimated. For intangible assets that are not yet available for use, the recoverable amount is estimated at each balance sheet date. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement. Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

2.15 Income taxes

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet liability method on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future.

The amount of deferred tax recognised is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity or group of entities filing consolidated tax returns.

A deferred tax asset is recognised only to the extent that it is probable that sustainable future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

2.16 Employee benefits

The Group has established defined benefit and defined contribution plans around the world. The benefits of the defined benefit plans usually depend on one or more factors such as the number of years the employee was covered in the plan, age, pensionable salary and to some extent on the accumulated old age capital. The plans are either funded or unfunded. The assets of the funded plans are held independently of the Group's assets in separate trustee-administered funds.

The expense and defined benefit obligations for the material defined benefit plans in accordance with IAS 19 are determined using the Projected Unit Credit Method. This takes into account insurance years up to the valuation date. The valuations of the defined benefit obligations are conducted annually by independent actuaries. Valuation of pension assets is done annually, at market value.

Current service cost is recorded in the income statement for the period in which the services are rendered. Past service costs are recognised immediately in the income statement, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past service costs are amortised on a straight-line basis over the vesting period.

Actuarial gains and losses arising from changes in actuarial assumptions and experience adjustments in excess of the greater of 10% of the value of plan assets or 10% of the defined benefit obligation are charged or credited to the income statement over the employees' expected average remaining working lives.

In measuring pension assets, the Group applies IFRIC 14—The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction. The interpretation addresses the interaction between the limits on recognition of assets from defined benefit post employment plans and any minimum funding requirement of such plans. IFRIC 14 has to be applied retrospectively as of January 1, 2007. The application of IFRIC 14 had neither an impact on the balance sheet nor on the profit and loss account of the Group. Actuarial losses and unvested prior service cost of the current period are immediately recognized if they would result in an asset that is not controlled by the Group.

In Switzerland the pension fund is controlled by an equal number of representatives of the management and the employees. The parity of control implies that neither side individually controls the assets in the pension fund. Therefore, the Company cannot dictate on its own that any excess funds will be used for the benefit of the Company (i.e. to reduce future contributions). In addition, the only commitment of the Company is the payment of the monthly contribution to the pension fund which is based on each employee individual earnings.

Contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred.

2.17 Share-based compensation

The Group operates equity-settled, share-based compensation plans. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted. At each balance sheet date, the entity revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision to original estimates, if any, in the income statement, with a corresponding adjustment to equity.

2.18 Provisions

A provision is recognised in the balance sheet when the Group has a legal or constructive present obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

2.19 Interest bearing borrowings

Interest bearing borrowings are recognised initially at cost, less attributable transaction costs. Subsequent to initial recognition, interest bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest rate basis.

2.20 Segment reporting

The Group is engaged in the development, manufacture, marketing and servicing of machine tools. These products are mainly purchased by companies active in the electronic, automotive, connector, watch and medical engineering industries, as well as other specialised manufacturers of high-precision turned parts.

The products of the Group require similar materials and production processes. Management does not consider that there is currently a clear distinction of risks and returns among the products and therefore concluded that the Group operates in one business segment, i.e. machine tools.

In view of the foregoing, management has chosen the geographical segmentation for the purposes of the Group's primary segment reporting.

Switzerland is the domicile of the parent company and of the main operating and distribution companies. The Swiss operating companies conduct all development and manufacture activities. The subsidiaries located in the other European countries (France, Germany, Italy, Poland, Spain and the United Kingdom), the United States of America, China and in Hong Kong only have support or sales and distribution activities. This organisation has the effect that the risks and returns of each geographical location are dependent to a large extent on the operating companies in Switzerland. Management has identified four geographical segments, namely, Switzerland, Other European countries, North America and Asia. For the purpose of presenting net sales by location of customers, one other geographical segment, namely Rest of world, is identified.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

3 Financial risk management

3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: market risks, credit risk and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. The Group uses derivative financial instruments to cover certain risk exposures.

3.2 Market risks

3.2.1 Currency risks

Tornos S.A., the Swiss operating company of the Group, invoices its revenues to the subsidiaries and to customers located outside Switzerland in local currencies, mainly EUR and USD except Asia where it is mainly in CHF. Therefore, the currency risk remains with the Swiss operating company. Tornos S.A. converts the offer in those currencies at an exchange rate which is decided internally. An offer is only valid for 90 days, and only if the exchange rate between CHF and the other currency fluctuates by less than 5%. If the parity fluctuation exceeds 5%, a new price list in that currency is issued. If parity is stable, no foreign exchange contracts are entered into. If a revaluation of the CHF is expected, a review of the risk is done and, if necessary, foreign exchange contracts are entered into for all or a portion of the net position in each currency. Due to the anticipated devaluation of the CHF against the EUR at the end of 2008 Tornos S.A. hedged, in November 2008, the net exposure in EUR for the next 6 months.

On an annual basis, if the CHF had weakened/strengthened by 1% against the EUR, additional income/losses of some KCHF 470 would have resulted from the translation of the net monthly movements in EUR.

At December 31, 2008, if the CHF had weakened/strengthened by 1% against the EUR, additional exchange gains/losses of KCHF 344 would have resulted from the translation of all EUR denominated assets and liabilities, the majority of which being represented by trade receivables (2007: KCHF 357).

On an annual basis, if the CHF had weakened/strengthened by 1% against the USD, additional income/losses of some KCHF 145 would have resulted from the translation of the net monthly movements in USD.

At December 31, 2008, if the CHF had weakened/strengthened by 1% against the USD, additional exchange gains/losses of KCHF 47 would have resulted from the translation of all USD denominated assets and liabilities, the majority of which being represented by cash equivalents (2007: KCHF 110).

At December 31, 2008, if the CHF had weakened/strengthened by 1% against the JPY additional exchange gains/losses of KCHF 118 would have resulted from the translation of all JPY denominated assets and liabilities, being represented by trade payables (2007: NIL).

The Group has certain investments in foreign operations, whose net assets are exposed to foreign currency translation risks.

3.2.2 Interest rate risks

The Group is exposed to changes in interest rates on borrowings bearing interest at floating rates. At December 31, 2008 and 2007, the Group did not hold any derivative financial instruments in order to limit the interest rate exposure of the Group.

Since 2007, the Group became net cash and only a very limited amount of borrowings is subject to interest rate risk at December 31, 2008.

Risk on financial assets is not significant as the Group has only significant cash and cash equivalent positions and no other interest bearing assets.

3.2.3 Price risks

The Group is exposed to equity securities price risk because of an investment held by the Group and classified on the consolidated balance sheet as available-for-sale and holding of treasury shares.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

3.3 Credit risk

The Group sells to large customer bases dealing with different market segments and located on all the continents resulting in no significant concentration of credit risk. Each year, the largest customer, which is different every year, represents less than 3% of total gross sales. Sales to new customers are made after obtaining credit ratings from independent sources, obtaining up to 90% of sales price before shipment and/or selling it to leasing companies financing the final customer. Cash excess is maintained with UBS and ZKB.

3.4 Liquidity risk

Group treasury policy is to maintain flexibility in funding by keeping committed credit lines available (see note 19.1) as well as sufficient cash balances (see note 11). In times of an economic downturn and short work, liquidity requirements may increase and credit lines may be partly or fully utilised.

All financial liabilities are current except a portion of interest bearing loans and borrowings which is non-current (see note 19.3).

3.5 Fair values

The carrying amounts of the following financial assets and financial liabilities approximate their fair values: cash, trade receivables net of specific provisions for impairment, available-for-sale financial assets and trade payables, other receivables and payables, loans, short-term borrowings and long-term borrowings predominantly negotiated at variable interest rates.

3.6 Capital risk management

The financial policy of Tornos is that its business should be self-funded. Although a policy of permanent borrowing would help to boost the return on equity, that has been ruled out in view of the cyclical and volatile nature of the Group's business. Given the wide variances in business volumes in the short term, the working capital requirement can rise sharply when the economy is booming, with temporary spikes which can be as high as 20% of annual turnover. It then takes around 9 months for cash to flow massively back into the company. If the company does not hold adequate liquidity, some of the benefits of a cyclical upturn could be missed. To minimise this risk, a credit limit of up to 10% of annual turnover will be maintained, and a cash reserve, also up to 10% of full-year turnover, will be progressively built up.

Additionally, "minor" acquisitions, defined as those representing up to the equivalent of 5% of annual turnover, may be considered without calling an Extraordinary General Meeting of Shareholders to decide on the principle of the acquisition and how to finance it. A cash reserve may also be built up for this purpose.

Once these reserves have been accumulated, surplus cash will be distributed to shareholders in one form or another. The decision on whether to reduce the par value of the company's shares, undertake share buybacks or pay dividends will be made in the light of circumstances at the time. Hence, a certain amount of cash will also have to be retained for this purpose.

In view of the above three factors, the Group will seek to maintain a net positive cash position.

Apart from the "minor" acquisitions referred to above, a cash reserve for potential acquisitions will not be maintained, as the decision on the purchase and the way it is to be financed falls solely within the discretion of the shareholders.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

4 **Critical accounting estimates and judgements**

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. On an ongoing basis, management evaluates the estimates, including those related to provisions for warranty purpose and other provisions resulting from pending litigations as well as other present obligations of uncertain timing, inventory obsolescence, bad debts and the assessment of income taxes including deferred tax assets, retirement benefit obligations and the fair value of stock option grants. Management bases the estimates on historical experience and on various other assumptions that it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. Management believes the following critical accounting policies reflect the most significant judgements and estimates that are used in the preparation of the consolidated financial statements.

4.1 **Bad debts**

Allowances are made for estimated losses resulting from the inability of the customers to make required payments. If the financial conditions of the customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances might be needed.

4.2 **Inventory obsolescence**

Machines, including work in progress machines on the assembly floors, are reviewed individually and recorded at the lower of cost and estimated net realisable value based upon assumptions about future demand and market conditions.

For raw material, components, semi-finished goods and spare parts, the following inventory obsolescence and write-offs methodologies are applied for any slow moving or any otherwise obsolete inventory:

Raw material, components and semi-finished goods

For any article, the quantity of articles in stock cannot exceed 18 months of consumption based on the last 12 months of consumption. Any excess is fully provided for.

After 24 months without movement, the individual stock of articles is written off. Once written off, the articles are transferred to the spare parts department upon their request at nil value.

After 48 months without movement, the stock is physically disposed of after second opinion from the spare parts department.

In case of a machine phase out, all the related stocks of articles are fully written off.

Spare parts in the spare parts department

For any article, the quantity of articles in stock cannot exceed 36 months of consumption based on the last 24 months of consumption. Any excess is fully provided for.

After 36 months without movement, the stock of articles is written off.

After 72 months without movement, the stock is physically disposed of upon selective review.

If actual market conditions are less favourable than those projected, additional inventory write-downs may be needed.

At December 31, 2008, the provision for obsolescence would have decreased by KCHF 3'149 had six months been added to all above-mentioned obsolescence rules (2007: decrease of KCHF 1'986). On the opposite, it would have increased by KCHF 3'956 had six months been deducted on all above-mentioned obsolescence rules (2007: increase of KCHF 2'845).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

4.3 Deferred taxes

The Group's financial and operating performance, as well as that of its competitors, is significantly influenced by the short to medium term economic cycles.

In times of economic growth, customers will buy and even place speculative purchase orders. However, in an economic downturn, demand typically falls with customers often seeking to postpone deliveries or cancel orders.

Following the financial restructuring of 2002, the Group had unused tax losses carried forward at December 31, 2006 which, until June 30, 2007, had not resulted in the recognition of deferred tax assets. In 2007, the Group considered it had demonstrated that it can sustain profitability at a sufficient level to be able to use most of the available tax losses of the operating companies and has therefore activated the related deferred tax assets which qualified for recognition at December 31, 2007. In 2008, due to the economic downturn, the Group made valuation allowances on all the available tax losses which remained and matured in 2009 (KCHF 134). Other deferred tax assets on tax losses carryforwards which expire in the year 2010 or do not expire remained capitalised (KCHF 1'472).

Had the Group estimated that all available tax losses of the operating companies could be used, the effect would have been an additional income of KCHF 2'182 for the year ended December 31, 2008 (2007: KCHF 1'450).

4.4 Postretirement benefits and other long-term employee benefits

The Group has established defined benefit and defined contribution plans around the world. The benefits of the defined benefit plans usually depend on one or more factors such as the number of years the employee was covered in the plan, age, pensionable salary and to some extent on the accumulated old age capital. The plans are either funded or unfunded. The assets of the funded plans are held independently of the Group's assets in separate trustee-administered funds. The expense incurred under the defined benefit retirement plans is based upon statistical and actuarial calculations, and is impacted by assumptions on discount rates used to determine the present value of future pension liabilities, expected returns that will be made on existing pension assets, future salary increases as well as future pension increases. Furthermore, the independent actuaries of the Group use statistical based assumptions covering future withdrawals of participants from the plan and estimates on life expectancy. The actuarial assumptions used may differ materially from actual results due to changes in market and economic conditions, higher or lower withdrawal rates or longer or shorter life spans of participants. These differences could impact significantly the amount of pension income or expense recognised in future periods.

4.5 Warranty provision

Warranty provision of KCHF 4'966 reflects management assessment of warranty claims (December 31, 2007: KCHF 7'972). It is based on historical data as well as the level of sales. The total warranty provision takes into consideration all possible legally enforceable claims as well as actions undertaken for commercial reasons. Actual results may fluctuate significantly.

4.6 Other provisions and contingencies

Other provisions amounting to KCHF 1'044 principally comprise the expected costs of pending litigations as well as other present obligations of uncertain timing, the outcome of which may prove to be more or less favourable than management currently believes (December 31, 2007: KCHF 3'702).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

Several of the Group subsidiaries are parties to various legal proceedings which are an ongoing feature of the business of the Group. As a result, claims could be made against them which might not be covered by existing provisions or by insurance. There can be no assurance that there will not be an increase in the scope of these matters or that any future lawsuits, claims, including those resulting from tax inspections, proceedings or investigations will not be material. Management does not believe that during the next few years, the aggregate impact, beyond current provisions, of these and other legal matters affecting the Group could be material to the Group's results of operations and cash flows, and to its financial condition and liquidity.

5 Scope of consolidation

Subsidiaries

Name	Domicile	Purpose
Tornos S.A., Moutier	Switzerland	Production and sales
Tornos Holding France, St-Pierre-en-Faucigny	France	Holding company
Tornos Technologies France SAS, St-Pierre-en-Faucigny	France	Support services
Tornos Technologies Deutschland GmbH, Pforzheim	Germany	Support services
Tornos Technologies Italia Srl, Opera / MI	Italy	Support services
Tornos Technologies Poland Sp. z o.o., Warsaw	Poland	Support services
Tornos Technologies Iberica SA, Granollers	Spain	Support services
Tornos Technologies UK Ltd., Coalville	United Kingdom	Support services
Tornos Technologies U.S. Corp., Bethel CT	United States of America	Sales & services
Tornos Technologies Asia Limited	Hong Kong	Sales & support services
Tornos Technologies (HK) Limited, Hong Kong	Hong Kong	Sales & services
Tornos Technologies (Shanghai) Limited, Shanghai	China	Sales & services
Almac S.A., La Chaux-de-Fonds	Switzerland	Production & sales
Almatronic S.A., La Chaux-de-Fonds	Switzerland	Dormant

Tornos Holding S.A. holds 100% of the shares of Almac S.A., La Chaux-de-Fonds, Almatronic S.A., La Chaux-de-Fonds and of Tornos S.A., Moutier. All the other Group companies are direct or indirect wholly-owned subsidiaries of Tornos S.A., Moutier.

Changes in scope

2008

Almac S.A., La Chaux-de-Fonds, Switzerland, was acquired effective January 1, 2008, and is a wholly-owned subsidiary of Tornos Holding S.A. It develops, manufactures and markets CNC machining equipment for small, high-precision parts which are destined predominantly for watchmaking applications used in Swiss companies. Other customers come from the dental, medical and connector fields.

Almatronic S.A., La Chaux-de-Fonds, Switzerland, was acquired effective January 1, 2008, and is a wholly owned subsidiary of Tornos Holding S.A.

Tornos Technologies (Shanghai) Limited, Shanghai, was founded and registered on April 2, 2008, and is a wholly-owned subsidiary of Tornos S.A., Moutier. It is acting as a sales and services company in China.

Tornos Technologies (HK) Limited, Hong Kong, was founded and registered on July 29, 2008, and is a wholly-owned subsidiary of Tornos Technologies Asia Limited, Hong Kong. It is acting as a sales and services company in Hong Kong.

These are the only changes which took place in the scope of consolidation in the period under review.

2007

Tornos Technologies Poland Sp. z o.o., Warsaw, was founded on October 30, 2007, and is acting as a support services company in Poland. This is the only change in the scope of consolidation which occurred in the period under review.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

6 Expenses by nature	2008	2007
Personnel expenses (note 7)	-93'853	-93'962
Changes in inventories of finished goods and work in progress, raw materials and consumables used	-107'704	-108'453
Depreciation charges	-6'758	-6'597
Other expenses	-38'799	-46'311
Total cost of sales, marketing and sales, general and administrative and research and development expenses	-247'114	-255'323

7 Personnel expenses	2008	2007
Total personnel expenses	-93'853	-93'962
Of which:		
Defined benefit plans (note 22.2.1)	-4'002	-3'848
Defined contribution plans (note 22.3)	-180	-39

8 Other income/(expenses) – net	2008	2007
Gain on sale of land and buildings	–	2'852
Other – net	154	-39
Other income/(expenses) – net	154	2'813

9 Financial expenses – net	2008	2007
Interest income from third parties	201	224
Dividend income from third parties	63	–
Interest expenses to third parties	-306	-271
Bank charges and other financial expenses	-534	-942
Financial expenses – net	-576	-989

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

10 Income taxes

	2008	2007
Current income tax credit/(charge)	-494	583
Deferred tax credit/(charge)	-1'727	3'365
Income tax credit/(charge)	-2'221	3'948

The Group's expected tax expense for each year is based on the weighted average of the statutory corporate income tax rates, which in 2008 ranged between 8% and 37% (2007: between 8% and 42%), in the tax jurisdictions in which the Group operates. The reconciliation of the expected and the effective income tax expense is as follows:

	2008	2007
Income before income taxes	8'263	31'189
Expected tax expense	-1'162	-7'022
Weighted average applicable tax rate	14.1%	22.5%
Utilisation of previously unrecognised tax losses carryforwards	603	7'786
Effect of changes in tax rates	542	176
Use of/recognition of previously unrecognised deferred tax assets	252	3'676
Income taxes relating to prior years	-	980
Write-down of deferred tax assets/unrecognised tax losses	-968	-1'319
Effect of tax deductible expenses (taxable income) eliminated on consolidation	-1'577	-359
Expenses not deductible for tax purposes	-178	-276
Other effects	267	306
Income tax credit/(charge) recognised	-2'221	3'948

The expected tax expense is calculated at entity level since the Group does not file consolidated tax returns. As such, profits and losses generated by different entities cannot be offset against each other. Losses predominantly incurred in countries with higher tax rates and profits predominantly made in countries with lower tax rates resulted in a relatively low overall tax rate of 14.1% (2007: 22.5%).

11 Cash and cash equivalents

	2008	2007
Cash in hand and in current or call accounts	14'268	29'689

No bank balances are pledged as collateral for bank guarantees issued at December 31, 2008 (December 31, 2007: KCHF 2'574).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

12 Trade receivables

	2008	2007
Trade receivables	49'231	53'012
Less provision for impairment of receivables	-774	-525
Trade receivables – net	48'457	52'487

At December 31, 2008, trade receivables include amounts denominated in EUR equivalent to KCHF 26'846 (December 31, 2007: KCHF 36'200) and amounts denominated in USD equivalent to KCHF 2'895 (December 31, 2007: KCHF 2'604).

Trade receivables aging is as follows:

	2008	2007
Current	28'067	25'303
1 to 30 days overdue	8'569	9'446
31 to 60 days overdue	2'506	7'098
61 to 90 days overdue	2'313	2'558
91 to 180 days overdue	4'008	3'386
More than 180 days overdue	3'768	5'221
Trade receivables	49'231	53'012

The provision for impairment of receivable was determined based on reviews of all outstanding amounts at the year-end. Following those reviews, 80% of the provision for impairment of receivable for identified risks at December 31, 2008 is related to trade receivables classified under "more than 180 days" (December 31, 2007: all the provision related to trade receivables classified under "more than 180 days").

Net bad debt expense in 2008 was KCHF 236 (2007: KCHF 143). There are no significant concentrations within trade receivables of counterparty credit risk (see note 3.3).

13 Inventories

	2008	2007
Materials and components	38'800	30'024
Work in progress	26'261	27'703
Finished goods and spare parts	47'647	34'284
Total inventories – gross	112'708	92'011
Less allowance for obsolescence	-17'969	-15'198
Total inventories – net	94'739	76'813

Total obsolescence and write-offs charged to the income statement during the year 2008 amount to KCHF 3'675 (2007: KCHF 6'339).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

14 Other receivables and prepayments

	2008	2007
Derivative financial instruments	611	16
VAT receivable	8'802	8'110
Advances to suppliers	2'410	5'893
Other	4'337	2'992
Total other receivables and prepayments	16'160	17'011

In appropriate circumstances, the Group uses derivative financial instruments as part of its risk management and trading strategies (note 3.2.1). At December 31, 2008, the Group had entered into forward exchange contracts to sell KEUR 12'000 against KCHF 18'522 which were carried at fair value for KCHF 611 (December 31, 2007: KCHF 16).

15 Available-for-sale financial assets

Available-for-sale financial assets represent the acquisition during 2008 of 1'000'000 shares of JPY 1'000 each of Tsugami Corporation, Tokyo, Japan (Tsugami), a company listed on the Tokyo Stock Exchange.

Tsugami and the Group are two entities of similar size in the machine tool sector which signed a framework partnership agreement on February 15, 2008. The underlying logic of the agreement is that the two groups are complementary in terms of their product range and geographical markets, in which each of them holds a leadership position. Under the terms of the agreement, contracts will be signed in the future in a number of areas such as research and development, procurement, production and distribution. The first contract involves Tsugami producing entry-level single spindle machines for which the Group has supplied the specification and which it will then distribute through its own sales network. Under the second contract, Tsugami will distribute Tornos multispindle machines in Japan and Asia. To cement the links between the two groups and symbolise the importance of the alliance for the two partners, each entity has decided to acquire in the market one million shares in the other.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

16 Property, plant and equipment

	Land, buildings & installations	Building in construction	Machinery	Other equipment	Total
Cost					
At December 31, 2006	66'502	–	65'078	10'846	142'426
Additions	811	4'747	441	3'066	9'065
Disposals	-7'945	–	-587	-2'055	-10'587
Exchange differences	-102	–	3	40	-59
At December 31, 2007	59'266	4'747	64'935	11'897	140'845
Acquisition of subsidiaries (note 27)	4'080	–	332	496	4'908
Additions	1'049	1'831	895	2'940	6'715
Disposals	–	–	-32	-1'735	-1'767
Transfer between categories	6'450	-6'578	–	128	–
Exchange differences	-794	–	-46	-466	-1'306
At December 31, 2008	70'051	–	66'084	13'260	149'395
Accumulated depreciation					
At December 31, 2006	-32'612	–	-59'926	-7'401	-99'939
Charge for the year	-2'532	–	-2'158	-1'907	-6'597
Written back on disposal	3'646	–	548	1'842	6'036
Exchange differences	-8	–	-3	-37	-48
At December 31, 2007	-31'506	–	-61'539	-7'503	-100'548
Acquisition of subsidiaries (note 27)	-920	–	-220	-211	-1'351
Charge for the year	-2'443	–	-1'945	-2'370	-6'758
Written back on disposal	–	–	30	1'610	1'640
Exchange differences	283	–	39	309	631
At December 31, 2008	-34'586	–	-63'635	-8'165	-106'386
Carrying amounts					
December 31, 2007	27'760	4'747	3'396	4'394	40'297
December 31, 2008	35'465	–	2'449	5'095	43'009

Of which related to leased assets:

	Land, buildings & installations	Building in construction	Machinery	Other equipment	Total
Acquisition of subsidiaries					
December 31, 2007	–	–	–	–	–
December 31, 2008	–	–	55	280	335
Carrying amounts					
December 31, 2007	847	–	–	22	869
December 31, 2008	639	–	39	111	789

The fire insurance value of PP&E and inventories amounts to CHF 408 million (2007: CHF 375 million).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

17 Goodwill

Goodwill results from the acquisition of Almac S.A. and Almatronic S.A. in 2008 (note 27) which are considered as a separate cash generating unit (CGU).

The recoverable amount of a CGU is determined based on value-in-use calculations. These calculations use pre-tax cash flow projections based on financial budgets approved by management until 2012.

The key assumptions used for value-in-use calculations are as follows:

EBIT: 10%

Discount rate: 8.3%

Management determined budgeted gross margin based on past performance and its expectations of market development. The discount rates used are pre-tax and reflect specific risks relating to the CGU.

18 Deferred taxes

18.1 Deferred tax assets and liabilities

Following the financial restructuring of 2002, the Group had unused tax losses carried forward at December 31, 2006 which, until June 30, 2007, had not resulted in the recognition of deferred tax assets. In 2007, the Group considered it had demonstrated that it can sustain profitability at a sufficient level to be able to use most of the available tax losses of the operating companies and has therefore activated the related deferred tax assets which qualified for recognition at December 31, 2007. In 2008, due to the economic downturn, the Group made valuation allowances on all the available tax losses which remained and matured in 2009. The effect of KCHF 134 is included in the write-down of deferred tax assets in the tax expense reconciliation in note 10.

Deferred tax assets and liabilities are attributable to the following:

	2008		2007	
	Assets	Liabilities	Assets	Liabilities
Trade receivables	8	24	–	–
Inventories	–	309	–	–
Property, plant and equipment	51	1'220	54	896
Investments in subsidiaries	–	–	–	413
Trade and other payables	66	75	99	152
Retirement benefit obligations	259	25	98	17
Provisions	–	–	82	–
Borrowings	221	–	322	–
Tax losses carried forward	1'472	–	3'435	–
Tax assets/liabilities	2'077	1'653	4'090	1'478
Set off	-1'114	-1'114	-1'475	-1'475
Net tax assets/liabilities	963	539	2'615	3

Deferred tax assets and deferred tax liabilities were set off where there is a legally enforceable right to set off these taxes as they relate to the same tax authorities.

The decrease in the net deferred tax assets by KCHF 2'188 relates to the deferred tax expense recognised in the consolidated income statement (KCHF 1'727), to the acquisition of subsidiaries (KCHF 408) and to exchange differences (KCHF 53). There are no deferred taxes which have been recognised directly in equity.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

18.2 Unrecognised deferred tax assets

Deferred tax assets have not been recognised in respect of the following items:

	2008	2007
Deductible temporary differences	3'057	3'891
Tax losses carried forward	141'202	146'345
Total	144'259	150'236

The expiry dates of unrecognised tax losses carried forward are as follows:

	2008	2007
Year 2009	135'447	142'172
After 2009	4'880	2'864
Losses not subject to expiry	875	1'309
Total	141'202	146'345

Tax losses include CHF 134.7 million (December 31, 2007: CHF 142.2 million) relating to Tornos Holding S.A. expiring in 2009.

The deductible temporary differences for which no deferred tax asset has been recognised do not expire.

19 Interest bearing loans and borrowings

	2008	2007
<i>Current portion:</i>		
Current portion of credit facility	7'000	–
Mortgage	139	85
Other short-term bank borrowings	6	812
Short-term lease liabilities (note 19.6)	214	155
Current portion	7'359	1'052
<i>Non-current portion:</i>		
Long-term lease liabilities (note 19.6)	608	739
Mortgage	1'024	635
Non-current portion	1'632	1'374
Total interest bearing loans and borrowings	8'991	2'426

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

19.1 Credit agreements with banks

Mortgages are granted to subsidiaries at floating rates of 2.1% and 3.125% at December 31, 2008 (December 31, 2007: 6.625%).

On December 20, 2007, the Group concluded an Amended and Restated Facility Agreement with two of the banks which were already parties to the Credit Facility Agreement entered into on April 25, 2005. Under this Amended and Restated Facility Agreement the syndicate of banks grants to Tornos S.A. as borrower, with Tornos Holding S.A. acting as guarantor, a credit facility in the aggregate of CHF 32.5 million. Of this amount, CHF 20.0 million can be used for advances of up to 12 months and CHF 12.5 million for current overdrafts and the issuance of bank guarantees of up to 12 months. This Amended and Restated Facility Agreement which is valid until December 31, 2010 is subject to certain conditions and financial covenants related to total net debt to EBITDA and interest cover ratios as well as tangible net worth. All the conditions and financial covenants related to the Credit Facility Agreement were always met.

The interest charged on the advances is based on the LIBOR rate plus an applicable margin. The applicable margin ranges between 0.65% and 1.35% per annum and is based on the total net debt to EBITDA ratio. The Amended and Restated Facility Agreement is also subject to a commitment fee on the average undrawn and uncanceled amount of the Facility until the end of the availability.

19.2 Facilities

Below is a summary of the credit facilities granted by the banks:

	Term loan credit facility CHF million	Working capital facilities CHF million	Total CHF million
At December 31, 2007			
Available	20.0	12.5	32.5
Used	–	7.4	7.4
Interest rate	LIBOR + 0.65%		
At December 31, 2008			
Available	20.0	12.5	32.5
Used	7.0	7.3	14.3
Interest rate	LIBOR + 0.65%		

The term loan credit facility can be used for roll over periods up to 12 months. Of the amount used at December 31, 2008 CHF 2 million matured on January 12 and CHF 5 million on February 12, 2009 and were bearing interest at 1.36% and 1.61% respectively.

The working capital facility may be used in the form of overdraft on current accounts, stand-by letter of credits, performance and bid bonds, advance payment guarantees or similar instruments.

Additionally, the Group disposes through one of its affiliates of two credit lines with two banks for a total of CHF 3 million. These credit lines have not been used in 2008 and can be cancelled by the parties at any time without notice.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

19.3 Maturity schedule

	2008	2007
Within 1 year	7'359	1'052
Between 1 and 2 years	346	234
Between 2 and 5 years	841	783
Over 5 years	445	357
Total borrowings	8'991	2'426

19.4 Interest rate exposure

	2008	2007
At fixed rates	–	19
At floating rates	8'991	2'407
Total borrowings	8'991	2'426

19.5 Exchange rate exposure

The original currencies of the Group's borrowings are:

	2008	2007
Swiss franc	7'890	–
Euro	664	1'702
British pound	437	724
Total borrowings	8'991	2'426

To be consistent with the legal right of offset that each bank has over all bank accounts maintained by each company of the Group, the net position of all bank current accounts with each bank is the basis for classification as either cash and cash equivalents or borrowings.

19.6 Finance lease liabilities

	2008	2007
<i>Minimum lease payments</i>		
Within 1 year	261	194
Between 1 to 5 years	684	696
More than 5 years	–	130
Total minimum lease payments	945	1'020
Future finance charges on finance leases	-123	-126
Present value of finance lease liabilities	822	894
<i>Of which:</i>		
Due within 1 year	214	155
Between 1 to 5 years	608	612
More than 5 years	–	127

The majority of the finance lease liabilities of the Group carries an effective interest rate of 6.265% at December 31, 2008 (December 31, 2007: 5.84%).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

20 Other payables

	2008	2007
Advances received	9'208	8'883
Accrued employees remuneration	4'997	6'847
Payable to pension plans	8	2
Other payables and accrued expenses	7'333	7'387
Total other payables	21'546	23'119

21 Provisions

	Warranties	Restruc- turing	Other	Total
At beginning of year	7'972	356	3'346	11'674
Acquired through business combinations	525	–	–	525
Additional provisions	6'842	133	16	6'991
Utilised during the year	-10'356	-222	-114	-10'692
Released via income statement	–	–	-2'396	-2'396
Exchange differences	-17	-18	-57	-92
At end of year	4'966	249	795	6'010
			2008	2007
Current liabilities			5'103	7'930
Non-current liabilities			907	3'744
Total			6'010	11'674

Warranties

The Company gives a contractual one to two years warranty depending on the type of machines sold and undertakes to repair or replace items that fail to perform satisfactorily.

Restructuring

The movements in the provision for restructuring reflect principally changes in the organisation.

Other provisions

Other provisions include the expected costs of pending litigations as well as other present obligations of uncertain timing. Management reassessed the provision for other risks and further to new developments which occurred during the year under review, provisions of CHF 2.4 million were released through the income statement as the outcome of various present obligations foreseen at the end of the prior year is now considered to be more favourable than management originally believed.

22 Retirement benefit obligations

22.1 Description of pension schemes

Substantially all employees are eligible for retirement benefits. Among the benefit schemes are defined benefit plans as well as defined contribution plans. The locations with significant defined benefit plans are Switzerland, France, Germany, Italy and the USA.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

Retirement benefits are provided based on salary, years of service or an accumulated old age account. Some of the plans provide only lump sum benefits in the events of leaving the Group and retirement. The last actuarial valuation was performed as of December 31, 2008, by independent actuaries.

22.2 Defined benefit pension plans

22.2.1 Employee benefits expense

According to IAS 19, the following amounts are recorded in the income statement as employee benefits expense:

	2008	2007
Current service cost	3'041	3'586
Interest on obligation	4'411	3'774
Expected return on plan assets	-5'379	-5'307
Net actuarial losses recognised	2'065	1'931
Past service cost	-136	-136
Total employee benefits expense	4'002	3'848

22.2.2 Actual return on plan assets

	2008	2007
Actual return	-10'172	1'022

22.2.3 Changes in the present value of the defined benefit obligation

	2008	2007
Opening defined benefit obligation	134'440	138'421
Current service cost	3'041	3'586
Plan participants' contributions	3'618	3'356
Interest on obligation	4'411	3'774
Actuarial losses/(gains)	614	-5'936
Liabilities assumed in business combinations	4'435	-
Benefit payments and net transferrals through pension assets	-10'290	-8'299
Benefit payments by employer	-265	-400
Past service cost	-	87
Exchange differences	-237	-149
Closing defined benefit obligation	139'767	134'440

22.2.4 Changes in the fair value of plan assets

	2008	2007
Opening fair value of plan assets	131'646	132'107
Plan participants' contributions	3'618	3'356
Employer contributions	3'709	3'587
Assets assumed in business combinations	3'691	-
Benefit payments and net transferrals through pension assets	-10'290	-8'299
Expected return on plan assets	5'379	5'307
Gains/(losses) on assets	-15'551	-4'285
Exchange differences	-138	-127
Closing fair value of plan assets	122'064	131'646

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

The pension assets are composed of the following essential classes of assets at December 31,

	2008	2007
Equities	15%	21%
Bonds	50%	45%
Real estate	23%	22%
Qualified insurance policies	4%	1%
Others, including cash	8%	11%

No shares issued by the Group are included in the assets of the pension plans at December 31, 2008 and 2007. The Group rented apartments which belong to pension plans for KCHF 56 during 2008 (2007: KCHF 54). The expected company contributions for fiscal year 2009 amount to KCHF 3'800.

22.2.5 Amount recognised in the balance sheet

The net position of pension obligations in the balance sheet can be summarised as follows at December 31,

	2008	2007
Present value of funded obligation	138'834	133'705
Fair value of plan assets	-122'064	-131'646
Under funding	16'770	2'059
Present value of unfunded obligations	935	735
Unrecognised actuarial losses	-17'269	-3'177
Unrecognised past service cost	1'705	1'834
Net liability	2'141	1'451

22.2.6 Principal assumptions

The following principal assumptions form the basis for the actuarial calculation:

Calculation of defined benefit obligations at December 31,

	2008	2007
Discount rate	3.54%	3.31%
Future salary increases	1.93%	1.95%
Future pension indexations	0.11%	0.10%

Assumptions regarding future mortality experience are set based on advice in accordance with published statistics and experience in each territory.

Calculation of expenses:

	2008	2007
Discount rate	3.31%	2.82%
Expected return on plan assets	4.04%	4.05%

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

22.2.7 Actual development of obligations and assets

The following table shows how the actual development of obligations and assets for the benefit plans deviates from their expected development at December 31,

	2008	2007	2006	2005
Defined benefit obligation	139'767	134'440	138'421	136'086
Fair value of assets	-122'064	-131'646	-132'107	-127'878
Under funding	17'703	2'794	6'314	8'208
Experience gain / (loss) on plan liabilities	-2'868	-1'094	1'475	-1'820
Experience loss on plan assets	-15'551	-4'285	-1'042	-1'165

22.3 Defined contribution plans

During 2008, the Group contributed KCHF 180 (2007: KCHF 39) to defined contribution plans.

23 Share capital

23.1 Capital structure

	Issued registered shares	Treasury shares	Total shares in circulation
Issued and fully paid in at December 31, 2006	13'790'880	56'000	13'734'880
Issued for cash	1'193'035		1'193'035
Purchased		103'565	-103'565
Issued and fully paid in at December 31, 2007	14'983'915	159'565	14'824'350
Issued for cash	35'786		35'786
Purchased		658'854	-658'854
Sold		-338'855	338'855
Issued and fully paid in at December 31, 2008	15'019'701	479'564	14'540'137

During the year 2008:

- The General Meeting of Shareholders held on April 8, 2008 approved the proposal to reduce the share capital by reducing the par value of the shares by CHF 0.50 from CHF 5.00 to CHF 4.50 each and payment on June 30, 2008 to holders of the shares on June 27, 2008;
- 35'786 registered shares were issued and fully paid for at a price of CHF 6.00 further to the exercise of options granted under the 2004 Management and Board Participation Plan (MBP04). In addition, 7'271 options granted under the MBP04 were exercised on December 30, 2008 and issued and fully paid in January 2009;
- CHF 125'000 of the conditional share capital which was reserved for the issuance of shares upon the exercise of option rights which were granted to certain creditor banks in consideration of them waiving part of their claims in 2002 which could have been exercised until July 2007 being without object anymore was cancelled during 2008.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

As a result of the above, the following changes were made to the Articles of Incorporation of the Company during 2008:

- The share capital amounts to CHF 67'588'654.50 represented by 15'019'701 registered shares of CHF 4.50 each;
- The conditional share capital was reduced to CHF 4'000'743.00 which can be used for the issue of 889'054 registered shares of CHF 4.50 each to be fully paid to satisfy stock compensation plans in favour of eligible members defined by the Board of Directors.

During the year 2007:

- The General Meeting of Shareholders held on April 3, 2007, approved the issue of 900'000 conditional shares that may be used by the Board of Directors to satisfy the Management and Board Participation Plan 2007–2009 (MBP07);
- 150'410 registered shares were issued and fully paid for at a price of CHF 6.00 further to the exercise of options granted under the 2004 Management and Board Participation Plan (MBP04);
- 89'500 registered shares were issued and fully paid for at a price of CHF 11.39 each under the MBP07;
- 953'125 registered shares were issued and fully paid for at a price of CHF 6.00 further to the exercise of options granted to former creditor banks as compensation for their debt waiver in 2002.

As a result of the above, the following changes were made to the Articles of Incorporation of the Company during 2007:

- The share capital amounts to CHF 74'919'575 represented by 14'983'915 registered shares of CHF 5.00 each;
- The conditional share capital was reduced to CHF 4.7 million which can be used for the issue of registered shares of CHF 5.00 each to be fully paid to be allocated as follows:
 - For a maximum amount of CHF 0.1 million which is reserved for the issuance of shares upon the exercise of option rights which were granted to certain creditor banks in consideration of them waiving part of their claims in 2002 which could have been exercised until July 2007. This portion of the conditional capital which is now without object will be cancelled during 2008;
 - For a maximum amount of CHF 4.6 million which is reserved for the issuance of shares that may be used by the Board of Directors to satisfy stock compensation plans in favour of eligible members defined by the Board of Directors.

23.2 *Shares outstanding and rights attached to each class of shares*

As of December 31, 2008, the share capital consisted of 15'019'701 ordinary registered shares with a par value of CHF 4.50 each. The holders of the ordinary shares are entitled to receive dividends as declared by the meeting of shareholders and are entitled to one vote per share at the meetings of shareholders.

23.3 *Treasury shares*

Movements in treasury shares are as follows:

	2008		2007	
	Nb of shares	Amount	Nb of shares	Amount
At beginning of year	159'565	2'070	56'000	84
Purchases	658'854	9'195	103'565	1'986
Sales	-338'855	-4'696	–	–
At end of year	479'564	6'569	159'565	2'070

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

Treasury shares are valued at average purchase price. Sales of treasury shares during 2008 resulted in a gain of KCHF 1'257 booked directly in equity.

As from July 12, 2004, 50'000 of these shares were loaned to a third party for market-making purpose. The Company is charged a fixed fee for each share movement, any gains and losses resulting from the shares sold/bought being at the profit/expense of the third party. During the year 2008, total costs incurred totalled KCHF 51 (2007: KCHF 56).

23.4 Conditional share capital

The conditional share capital amounts to CHF 4 million and is reserved for the issuance of shares that may be used by the Board of Directors to satisfy stock option plans in favour of eligible members defined by the Board of Directors.

23.5 Significant shareholders

At December 31, 2008, Tsugami Corporation, Japan hold more than 5% of the share capital of the Company (December 31, 2007: 0%),

24 Retained earnings

Retained earnings include the following reserves which are not available for distribution:

	2008	2007
General reserves	4'442	1'964
Reserve for treasury shares	6'569	2'070

25 Stock compensation plans

There are two management and Board of Directors stock participation plans, namely the 2004 Management and Board Participation Plan (MBP04) and the Management and Board Participation Plan 2007–2009 (MBP07). Compensation expense is recognised in accordance of the provisions of IFRS 2 “Share-based Payment”, for options over the vesting period and for shares purchased immediately in the accounts as the shares do not need to be returned in case the employment contract is terminated. The expense recorded in the income statement spreads the cost of each option equally over the vesting period. Assumptions are made concerning the forfeiture rate which is adjusted during the vesting period so that at the end of the vesting period there is only a charge for vested amounts. Compensation expense of KCHF 701 was recorded for the year ended December 31, 2008 (2007: KCHF 1'287). Compensation expense arising from stock options outstanding at December 31, 2008 to be recognised in future periods amounts to KCHF 621 (December 31, 2007: KCHF 564).

25.1 Management and Board Participation Plan 2007–2009 (MBP07)

The General Meeting of Shareholders held on April 3, 2007, approved the issue of 900'000 conditional shares that may be used by the Board of Directors to satisfy the Management and Board Participation Plan 2007–2009 (MBP07). Under this plan, from 2007 to 2009, a maximum of 300'000 shares/options may be allocated each year to the participants by the Nomination and Compensation Committee. The possible participants are members of the Board of Directors as well as the management. Each participant chooses on grant date, within the number of shares/options allocated to him by the Nomination and Compensation Committee, to receive options free of charge, to purchase shares with a discount or a combination of receiving options free of charge and purchasing shares with a discount. As of December 31, 2008, a total of 470'000 shares/options

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

were attributed by the Nomination and Compensation Committee, of which 29'500 options were cancelled (December 31, 2007: 230'000 shares/options granted and 20'000 options cancelled respectively). Of the total amount, the participants elected to purchase 89'500 shares immediately and to receive 380'500 options under the stock option program as detailed below (2007: 89'500 shares and 140'500 options respectively).

25.1.1 *Stock purchasing program under MBP07*

Each participant has the right to purchase shares on May 1, 2007, 2008 and 2009 (within the number of shares/options allocated by the Nomination and Compensation Committee and not used for the stock option program). The purchasing price is the weighted average price paid at SWX within the 12 months (May 1 to April 30) preceding the purchase of the shares minus a discount of 25%. There is a restriction period of two years after purchasing the shares during which the shares are held in an escrow deposit. However, the shares do not need to be returned in case the employment contract is terminated and there is a take me along clause in case of a change of control transaction. In 2008, none of the participants elected to purchase shares at a price of CHF 14.75 (2007: 89'500 shares at a price of CHF 11.39). As a result, no expense was recorded in the income statement for the year ended December 31, 2008 (2007: KCHF 690).

25.1.2 *Stock option program under MBP07*

Each participant receives free of charge on May 1, 2007, 2008 and 2009, the number of options chosen (within the number of shares/options allocated by the Nomination and Compensation Committee and not used for the share purchasing program). The options vest after two years and can be exercised only in the third year. The exercise price is the weighted average price paid at SWX within the 12 months (May 1 to April 30) preceding the allocation of the options. A possible share capital reduction or dividend payment has no impact on the option rights according to this program as the exercise price will not be adjusted should these events take place in the future. Options not exercised generally need to be returned at the time the employment contract is terminated. However, they can be exercised without any restriction in case of a change of control transaction. Total expenses recorded in the income statement for the year ended December 31, 2008, amounted to KCHF 591 (2007: KCHF 234).

The fair value of the grants under the MBP07 stock option plan was estimated using the Black-Scholes valuation model with the following assumptions and values:

	2008 attribution	2007 attribution
Number of options granted	240'000	140'500
Grant date	May 1, 2008	May 1, 2007
Vesting period	2 years	2 years
Expiration date	April 30, 2011	April 30, 2010
Closing stock price at grant date	CHF 18.05	CHF 19.10
Exercise price	CHF 19.66	CHF 15.18
Expected life	2.5 years	2.5 years
Volatility	37.76%	31.28%
Expected dividend yield	2.77%	1.30%
Risk-free interest rate	2.30%	2.81%
Fair value of option at grant date	CHF 3.35	CHF 5.80
Expected turnover of personnel	-	-

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

A summary of activity under the MBP07 stock option plan, including weighted average exercise price, is as follows:

	2008			2007		
	Options	Exercise price (CHF)	Contractual life	Options	Exercise price (CHF)	Contractual life
Outstanding at January 1,	120'500	15.18		–		
Granted	240'000	19.66	3 years (April 30, 2011)	140'500	15.18	3 years (April 30, 2010)
Exercised	–			–		
Cancelled or expired	-9'500			-20'000		
Outstanding at December 31,	351'000	18.18		120'500	15.18	
Exercisable at December 31,	–			–		

25.2 2004 Management and Board Participation Plan (MBP04)

The General Meeting of Shareholders held on April 13, 2004, approved the issue of 450'000 conditional shares that may be used by the Board of Directors to satisfy stock purchase and option plan commitments set out below.

25.2.1 Share purchase plan under MBP04

Under the MBP04, eligible members selected by the Board of Directors were offered 150'000 registered shares at CHF 5.30 per share to be issued in three equal tranches over a three-year period. The purchase price was deemed equivalent to the fair market value at the date each eligible member contractually committed to purchasing the shares, hence no compensation expense has been calculated in respect of the above. As at December 31, 2008, 150'000 registered shares had been issued under the 2004 Management and Board Participation Plan (December 31, 2007: 150'000 registered shares).

25.2.2 Stock option plan under MBP04

Under the MBP04, eligible members selected by the Board of Directors were issued options to purchase registered shares at a strike price of CHF 6.00 per share. The terms and conditions with respect to options granted were determined by the Board of Directors who administered these plans. Options vest over two years and remain outstanding for periods not exceeding three years. A total of 300'000 options were issued under this plan, of which 228'717 options were exercised and 5'838 options were cancelled at December 31, 2008 (December 31, 2007: 185'660 options exercised and 5'838 options cancelled). Total expenses recorded in the income statement for the year ended December 31, 2008, amounted to KCHF 110 (2007: KCHF 364).

A summary of activity under the MBP04 stock option plan, including weighted average exercise price, is as follows:

	2008			2007		
	Options	Exercise price (CHF)	Contractual life	Options	Exercise price (CHF)	Contractual life
Outstanding at January 1,	108'502	6.00		264'750	6.00	
Exercisable at January 1,	14'340	6.00		64'750	6.00	
Granted	–			–		
Exercised	-43'057	6.00		-150'410	6.00	
Cancelled or expired	–			-5'838		
Outstanding at December 31,	65'445	6.00		108'502	6.00	
Exercisable at December 31,	65'445	6.00	Until April 30, 2009	14'340	6.00	Until April 30, 2008

The related weighted average share price at the time of exercise was CHF 11.13 in 2008 and CHF 19.56 in 2007.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

26 Earnings per share, basic and fully diluted

26.1 Basic

Basic earnings per share is calculated by dividing the net income attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares purchased by the Company and held as treasury shares (note 23.3).

	2008	2007
Net income attributable to equity holders of the Company	6'042	35'137
Weighted average number of ordinary shares in issue (thousands)	14'464	14'511
Basic earnings per share (CHF per share)	0.42	2.42

26.2 Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Company has one category of dilutive potential ordinary shares: share options. For the share options, a calculation is done to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

	2008	2007
Net income attributable to equity holders of the Company	6'042	35'137
Weighted average number of ordinary shares in issue (thousands)	14'464	14'511
Adjustments for share options (thousands)	43	372
Weighted average number of ordinary shares for diluted earnings per share (thousands)	14'507	14'883
Diluted earnings per share (CHF per share)	0.42	2.36

27 Business combinations

Effective January 1, 2008, the Group acquired 100% of the share capital of Almac S.A. and Almatronic S.A. These two companies are based in La Chaux-de-Fonds, Switzerland. Almatronic S.A. main customer was Almac S.A. The two companies' shareholding was diverse and consisted primarily of private individuals. The group of shareholders was formed in 1997 at a time when Almac S.A. was going through a particularly rough path. The group's aim was to recapitalise the company and get it back on track. This objective was seen through to fruition. Almac S.A. is thriving and there is no longer any call for the temporary shareholding initiative which was originally developed to keep the company afloat. According to the management of the two companies, the shareholders chose to trade in their shares to an industrial partner that would continue to develop Almac S.A. and Almatronic S.A. The Group has a key presence in a variety of market segments including automotive, medical, microtechnology (including watchmaking) and electronics. As mentioned above, Almac S.A.'s products are tailored to companies operating in the fields of microtechnology, medical and electronics – three of the four key market segments in which the Group is involved. With their complementary, non-competitive machines, the Group and Almac S.A. share the same target markets, allowing them to benefit from synergies in terms of sales and service networks. These acquired businesses contributed revenues of KCHF 23'579 and net profit of KCHF 1'954 for the year ended December 31, 2008.

The goodwill is attributable to the workforce of the acquired business and the significant synergies expected to arise after the Group's acquisition of both companies. No other intangible assets have been recognised as they are not considered to add any value to the Group.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

Almatronic S.A. operations being minor and mostly with Almac S.A., the assets and liabilities as of January 1, 2008, arising from the acquisition of both companies have been combined and are as follows:

	Fair value	Acquirees' carrying amount ¹⁾
Cash and cash equivalents	721	721
Trade receivables	4'205	4'205
Inventories	5'890	5'890
Other receivables and prepayments	400	400
Property, plant and equipment	3'557	2'004
Interest bearing loans and borrowings	-1'070	-1'070
Trade payables	-2'596	-2'596
Other payables	-5'506	-5'506
Current tax liabilities	-50	-50
Provisions	-525	-525
Retirement benefit obligations	-744	-
Deferred tax liabilities	-408	-229
Net assets acquired	3'874	3'244
Goodwill	2'873	
Total purchase consideration	6'747	
<i>Of which:</i>		
Cash	5'547	
Deferred payments	1'200	
Outflow of cash to acquire businesses, net of cash acquired:		
Cash consideration	-5'547	
Cash and cash equivalents in subsidiaries acquired	721	
Cash outflow on acquisition	-4'826	

¹⁾ The acquired companies were not using IFRS for reporting purpose. The acquirees' carrying amount related to retirement benefit obligations calculated in accordance with IFRS was not computed as work and costs involved to derive this information would have been disproportionate in relation to the benefit obtained for disclosure purpose only.

Costs directly attributable to the acquisitions and which amounted to KCHF 115 have been directly charged to income under General and administrative expenses.

28 Segment information

As described in note 2.20 above, management of the Group has chosen geographical segments for the purpose of primary segment reporting in accordance with IAS 14. The reportable segments identified are Switzerland, Other European countries, North America and Asia. For the purpose of presenting net sales by location of customers, one other geographical segment, namely Rest of world, is identified.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

28.1 *Net sales by location of assets*

	2008	2007
Switzerland:		
– To third parties	233'224	261'529
– To other segments	15'944	14'251
	249'168	275'780
Other European countries:		
– To third parties	79	1'173
– To other segments	-	25
	79	1'198
North America:		
– To third parties	24'115	21'295
– To other segments	447	-
	24'562	21'295
Asia:		
– To third parties	2'635	1'259
– To other segments	1'174	-
	3'809	1'259
Elimination	-17'565	-14'276
Total net sales	260'053	285'256

28.2 *Net sales by location of customers*

	2008	2007
Switzerland	76'427	50'765
Other European countries	128'568	164'674
North America	31'892	26'871
Asia	21'831	38'117
Rest of world	1'335	4'829
Total net sales	260'053	285'256

28.3 *Segment result (EBIT) by location of assets*

	2008	2007
Switzerland	12'272	33'573
Other European countries	1'459	1'522
North America	-2'128	-3'016
Asia	557	216
Total	12'160	32'295
Elimination	256	-49
Unallocated	677	500
Total EBIT	13'093	32'746

The transactions between Group companies are conducted based on internationally acceptable transfer pricing policies, thereby leaving reasonable margins at local subsidiary level.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

28.4 Segment assets

	2008	2007
Switzerland	202'526	215'240
Other European countries	8'010	14'265
North America	10'206	10'026
Asia	8'174	469
Total	228'916	240'000
Elimination	-5'697	-18'473
Unallocated assets:		
– Tax assets	-963	-2'615
Total assets	222'256	218'912

28.5 Segment liabilities

	2008	2007
Switzerland	49'080	56'258
Other European countries	4'450	18'464
North America	6'660	3'817
Asia	7'677	277
Total	67'867	78'816
Elimination	-9'077	-22'807
Unallocated liabilities:		
– Tax liabilities	732	298
– Interest bearing borrowings	8'991	2'426
Total liabilities	68'513	58'733

28.6 Depreciation of property, plant and equipment by segment

	2008	2007
Switzerland	-5'953	-5'771
Other European countries	-660	-685
North America	-120	-120
Asia	-25	-21
Total depreciation	-6'758	-6'597

28.7 Capital expenditure on property, plant and equipment and other intangible assets by segment

	2008	2007
Switzerland	8'956	7'603
Other European countries	455	941
North America	125	493
Asia	52	28
Total capital expenditure	9'588	9'065

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

29 Commitments and contingencies

29.1 Operating lease commitments

Operating lease liabilities, minimum lease payments

	2008	2007
Year 1	1'080	1'104
Years 2 to 5	1'570	2'060
After 5 years	-	147
Total minimum lease payments	2'650	3'311

29.2 Other commitments and contingent liabilities

As of December 31, 2008 the Group had entered into foreign exchange contracts to sell a total of KEUR 12'000 against KCHF 18'522 with maturities ranging between one and six months (2007: to sell a total of KEUR 28'800 against KCHF 47'246 with maturities ranging between one and twelve months).

There were no other commitments or contingent liabilities not in the ordinary course of business.

29.3 Assets pledged

At December 31, 2008 and 2007, the following assets were pledged to banks or leasing companies:

	2008	2007
Cash and cash equivalents	-	2'574
Land and buildings	4'134	2'135
Technical machinery & other equipment	150	22
Total assets pledged	4'284	4'731

At December 31, 2008, the total value of the pledged mortgage notes related to land and buildings amount to CHF 3.4 million (December 31, 2007: CHF 1.0 million).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

30 Related-party transactions

Remuneration consisting of fees, to non-executive members of the Board of Directors amounted to KCHF 543 in 2008 (2007: KCHF 570). Remuneration, consisting principally of salaries and bonuses, to the executive member of the Board of Directors and the members of Group Management totalled KCHF 3'211 in 2008 (2007: KCHF 3'100). As of December 31, 2008, the outstanding balances payable related to remuneration amounted to KCHF 351 (December 31, 2007: KCHF 715).

During the years under review, option rights have also been granted and exercised as follows:

	Non-executive members of the Board of Directors	Executive member of the Board of Directors and members of the Group Management	Total
Option rights outstanding at December 31, 2006	109'035	132'209	241'244
Granted during 2007	–	117'000	117'000
Exercised during 2007	-64'940	-69'235	-134'175
Cancelled during 2007	–	-25'838	-25'838
Option rights outstanding at December 31, 2007	44'095	154'136	198'231
Granted during 2008	40'000	160'000	200'000
Exercised during 2008	-7'735	-35'322	-43'057
Cancelled during 2008	-	-	-
Option rights outstanding at December 31, 2008	76'360	278'814	355'174

In addition, during 2008, neither the non-executive nor the executive members of the Board of Directors and the Group Management elected to purchase shares of the Company under MBP07 (2007: purchase of 40'000 shares and 43'000 shares respectively). Please refer to note 25 for further details.

As of December 31, 2008, the Board of Directors and Group Management also held 1'328'115 shares (8.8%) of the Company (December 31, 2007: 1'484'425 shares and 9.9%).

During 2008, sales to companies in which one of the directors of the Company holds a significant interest amounted to KCHF 767 (2007: sales of KCHF 603 and purchases of KCHF 12). Services provided by a company in which one of the directors of the Company holds a significant interest amounted to KCHF 108 (2007 : KCHF 103). These transactions were undertaken on an arms length basis. As of December 31, 2008, the related outstanding balances receivable and payable amounted to KCHF 9 and KCHF 8 respectively (December 31, 2007: KCHF 40 and KCHF 9 respectively).

No loans or advances were granted to related parties in 2008 and 2007.

Please also refer to note 22 for transactions with the pension funds.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

31 Board of Directors and General Management compensation disclosures as required by Swiss Law

31.1 2008

31.1.1 Compensation

In thousands of CHF unless otherwise stated

	Base compensation		Variable compensation		Other compensation ³⁾ (amount)
	Cash (amount)	Cash bonus ¹⁾ (amount)	Shares ²⁾ (number)	Stock options ²⁾ (number)	
Non executive members of Board of Directors					
François Frôté <i>(Chairman of BofD and chairman of Nomination and Compensation Committee and member of Audit Committee)</i>	200	-	-	8'000	21
Claude Elsen <i>(Deputy Chairman of BofD)</i>	90	-	-	8'000	10
Paul Haering <i>(Chairman of Audit Committee)</i>	120	-	-	8'000	13
Michel Rollier <i>(Member of Nomination and Compensation Committee)</i>	70	-	-	8'000	8
Hans-Otto Stenzel <i>(Until April 8, 2008)</i>	19	-	-	8'000	8
François Gabella <i>(As from April 8, 2008)</i>	44	-	-	-	5
Total non executive members of Board of Directors	543	-	-	40'000	65
Executive member of Board of Directors and General Management					
Raymond Stauffer ⁴⁾ <i>(Managing Director and CEO)</i>	645	75	-	30'000	101
Total other members of General Management	2'055	276	-	130'000	375
Total executive member of Board of Directors and General Management	2'700	351	-	160'000	476
Former member of the General Management in relation to his former capacity	160	-	-	-	29

¹⁾ The amounts represent the recorded expense for cash bonus for 2008, which will be paid out in May 2009.

²⁾ The number of shares and options reflected represent the number of shares and/or options granted during the year 2008 in accordance with the stock compensation plans and which are still vesting at December 31, 2008.

³⁾ These amounts comprise the Group share of payments to pension plans and other social security contributions.

⁴⁾ The cash remuneration of Mr Raymond Stauffer includes KCHF 60 related to his function of member of Board of Directors.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

31.1.2 *Loans and credits*

There were no loans and credits made to any current or former members of the Board of Directors or the General Management.

31.1.3 *Participations*

At December 31, 2008, the following number of participations were held by members of the Board of Directors and the General Management (including persons closely related to these members):

	Shares	Share options		
		Expiring 2009	Expiring 2010	Expiring 2011
Non executive members of Board of Directors				
François Frôté <i>(Chairman of BofD and chairman of Nomination and Compensation Committee and member of Audit Committee)</i>	182'567	7'272	-	8'000
Claude Elsen <i>(Deputy Chairman of BofD)</i>	47'218	7'272	-	8'000
Paul Haering <i>(Chairman of Audit Committee)</i>	49'518	7'272	-	8'000
Michel Rollier <i>(Member of Nomination and Compensation Committee)</i>	542'459	7'272	-	8'000
François Gabella	-	-	-	-
Total non executive members of Board of Directors	821'762	29'088	-	32'000
Executive member of Board of Directors and General Management				
Raymond Stauffer <i>(Managing Director and CEO)</i>	397'933	7'272	-	30'000
Philippe Maquelin <i>(COO and CFO)</i>	59'975	7'271	20'000	30'000
Philippe Jacot <i>(CTO)</i>	1'000	-	-	-
Carlos Cancer <i>(Head of Single Spindle Products)</i>	8'922	-	20'000	20'000
Roland Gutknecht <i>(Head of Almac Products)</i>	-	-	-	-
Willi Nef <i>(Head of Sales & Marketing)</i>	13'768	-	17'000	20'000
Bernard Seuret <i>(Head of Production)</i>	24'755	7'271	20'000	20'000
Sandor Sipos <i>(Head of Customer Service)</i>	-	-	20'000	20'000
Iwan von Rotz <i>(Head of Multispindle Products)</i>	-	-	-	20'000
Total executive member of Board of Directors and General Management	506'353	21'814	97'000	160'000
Former non executive member of Board of Directors				
Hans-Otto Stenzel <i>(Until April 8, 2008)</i>	99'794	7'272	-	8'000
Total former non executive member of Board of Directors	99'794	7'272	-	8'000

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

31.2 2007

31.2.1 Compensation

In thousands of CHF unless otherwise stated

	Base compensation		Variable compensation		
	Cash (amount)	Cash bonus ¹⁾ (amount)	Shares ²⁾ (number)	Stock options ²⁾ (number)	Other com- pensation ³⁾ (amount)
Non executive members of Board of Directors					
François Frôté <i>(Chairman of BofD and member of Nomination and Compensation Committee and Audit Committee)</i>	200	–	8'000	–	45
Claude Elsen <i>(Deputy Chairman of BofD and member of Nomination and Compensation Committee and Audit Committee)</i>	110	–	8'000	–	20
Paul Haering <i>(Chairman of Audit Committee)</i>	120	–	8'000	–	26
Michel Rollier <i>(Member of Nomination and Compensation Committee)</i>	70	–	8'000	–	31
Hans-Otto Stenzel <i>(Member of Nomination and Compensation Committee)</i>	70	–	8'000	–	10
Total non executive members of Board of Directors	570	–	40'000	–	132
Executive member of Board of Directors and General Management					
Raymond Stauffer ⁴⁾ <i>(Managing Director and CEO)</i>	549	215	30'000	–	110
Total other members of General Management	1'828	508	13'000	97'000	412
Total executive member of Board of Directors and General Management	2'377	723	43'000	97'000	522
Former member of the General Management in relation to his former capacity					
	–	–	–	–	21

¹⁾ The amounts represent the recorded expense for cash bonus for 2007, which, with the exception of KCHF 8, will be paid out in April 2008.

²⁾ The number of shares and options reflected represent the number of shares and/or options granted during the year 2007 in accordance with the stock compensation plans and which are still vesting at December 31, 2007.

³⁾ These amounts comprise the Group share of payments to pension plans and other social security contributions.

⁴⁾ The cash remuneration of Mr Raymond Stauffer includes KCHF 60 related to his function of member of Board of Directors.

31.2.2 Loans and credits

There were no loans and credits made to any current or former members of the Board of Directors or the General Management.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

31.2.3 Participations

At December 31, 2007, the following number of participations were held by members of the Board of Directors and the General Management (including persons closely related to these members):

	Shares	Share options		
		Expiring 2008	Expiring 2009	Expiring 2010
Non-executive members of Board of Directors				
François Frôté <i>(Chairman of BofD and member of Nomination and Compensation Committee and Audit Committee)</i>	182'567	–	7'272	–
Claude Elsen <i>(Deputy Chairman of BofD and member of Nomination and Compensation Committee and Audit Committee)</i>	112'218	–	7'272	–
Paul Haering <i>(Chairman of Audit Committee)</i>	46'518	–	7'272	–
Michel Rollier <i>(Member of Nomination and Compensation Committee)</i>	542'459	–	7'272	–
Hans-Otto Stenzel <i>(Member of Nomination and Compensation Committee)</i>	92'059	7'735	7'272	–
Total non-executive members of Board of Directors	975'821	7'735	36'360	–
Executive member of Board of Directors and General Management				
Raymond Stauffer <i>(Managing Director and CEO)</i>	397'933	–	7'272	–
Philippe Maquelin <i>(COO and CFO)</i>	59'975	–	7'271	20'000
Carlos Cancer <i>(Head of Single Spindle Products)</i>	8'922	–	7'271	20'000
Willi Nef <i>(Head of Multispindle Products)</i>	11'033	2'735	7'271	17'000
Michael Op de Hipt <i>(Head of R&D)</i>	2'267	–	–	–
Bernard Seuret <i>(Head of Production)</i>	20'885	3'870	7'271	20'000
Sandor Sipos <i>(Head of Customer Service)</i>	7'589	–	7'271	20'000
Total Executive member of Board of Directors and General Management	508'604	6'605	43'627	97'000

32 Risk assessment as required by Swiss law

Risks to which the Group may be faced are assessed by the Group Audit Committee on a regular basis. Each of the risks identified is evaluated in order to take appropriate preventive measures if necessary. The risk assessment summary is submitted to the Board of Directors of the Company for review and final approval. See note 3 for additional information related to financial risk management.

Report of the Statutory Auditor

to the General Meeting of

Tornos Holding S.A., Moutier

Report of the statutory auditor on the financial statements

As statutory auditor, we have audited the financial statements of Tornos Holding S.A., which comprise the income statement, balance sheet, statement of changes in equity and notes (pages 55 to 60), for the year ended December 31, 2008.

Board of Directors' Responsibility

The Board of Directors is responsible for the preparation of the financial statements in accordance with the requirements of Swiss law and the company's articles of incorporation. This responsibility includes designing, implementing and maintaining an internal control system relevant to the preparation of financial statements that are free from material misstatement, whether due to fraud or error. The Board of Directors is further responsible for selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Swiss law and Swiss Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers the internal control system relevant to the entity's preparation of the financial statements 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 entity's internal control system. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements for the year ended December 31, 2008 comply with Swiss law and the company's articles of incorporation.

Report on other legal requirements

We confirm that we meet the legal requirements on licensing according to the Auditor Oversight Act (AOA) and independence (article 728 CO and article 11 AOA) and that there are no circumstances incompatible with our independence.

In accordance with article 728a paragraph 1 item 3 CO and Swiss Auditing Standard 890, we confirm that an internal control system exists which has been designed for the preparation of financial statements according to the instructions of the Board of Directors.

We further confirm that the proposed appropriation of available earnings complies with Swiss law and the company's articles of incorporation. We recommend that the financial statements submitted to you be approved.

PricewaterhouseCoopers SA



Michael Foley
Audit expert
Auditor in charge



Aude Joly
Audit expert

Neuchâtel, March 3, 2009

Enclosures:

- Financial statements (income statement, balance sheet, statement of changes in equity and notes)
- Proposed appropriation of available earnings

INCOME STATEMENT

In thousands of CHF

For the years ended December 31,	Note	2008	2007
Dividend income from a subsidiary		10'000	-
Interest income from a subsidiary		1'279	1'435
Gain on sale of treasury shares	5	1'257	-
Financial income		63	-
Total income		12'599	1'435
Administrative expenses		-1'445	-1'242
Loss on valuation of treasury shares	5	-3'530	-
Financial expenses		-3	-3
Taxes other than on income		-122	-14
Total expenses		-5'100	-1'259
Net income for the year		7'499	176

The accompanying notes form an integral part of these financial statements.

BALANCE SHEET

In thousands of CHF

As of December 31,	Notes	2008	2007
ASSETS			
Cash and cash equivalents		31	428
Treasury shares	5	3'039	2'070
Group receivables		-	7'595
Other current assets		143	13
Total current assets		3'213	10'106
Investment in subsidiaries	2	70'547	65'000
Other investment	3	3'574	-
Loan to a subsidiary		20'700	22'500
Total non-current assets		94'821	87'500
Total assets		98'034	97'606
LIABILITIES AND EQUITY			
Accrued expenses		82	99
Group payables		1	-
Total current liabilities		83	99
Ordinary shares	4	67'589	74'920
Additional paid-in capital		15'956	15'910
Reserve for treasury shares		6'569	2'070
Retained earnings		7'837	4'607
Total equity		97'951	97'507
Total liabilities and equity		98'034	97'606

The accompanying notes form an integral part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

<i>In thousands of CHF</i>	Ordinary shares	Additional paid-in capital	Reserve for treasury shares	Retained earnings	Total
At December 31, 2006	68'954	14'234	84	6'417	89'689
Issuance of new shares (note 4)	5'966	1'676			7'642
Net income for the year				176	176
Transfer for treasury shares (note 5)			1'986	-1'986	-
At December 31, 2007	74'920	15'910	2'070	4'607	97'507
Issuance of new shares (note 4)	168	46			214
Reduction of par value of the shares (note 4)	-7'499			230	-7'269
Net income for the year				7'499	7'499
Transfer for treasury shares (note 5)			4'499	-4'499	-
At December 31, 2008	67'589	15'956	6'569	7'837	97'951

The accompanying notes form an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

1 Basis of preparation

The financial statements of Tornos Holding S.A., Moutier (the Company), are prepared in accordance with the provisions of the Swiss law and the Company's Articles of Incorporation.

2 Subsidiaries

Further to the acquisition of Almac S.A. and Almatronic S.A. in 2008 the Company has the following wholly-owned subsidiaries:

Name	Domicile	Share Capital	Purpose
Tornos S.A., Moutier	Switzerland	65'000	Production and sales
Almac S.A., La Chaux-de-Fonds	Switzerland	1'175	Production and sales
Almatronic S.A., La Chaux-de-Fonds	Switzerland	50	Dormant

3 Other investment

Other investment represent the acquisition during 2008 of 1'000'000 shares of JPY 1'000 each of Tsugami Corporation, Tokyo, Japan (Tsugami), a company listed on the Tokyo Stock Exchange which is carried at cost.

4 Share capital and conditional capital

During the year 2008:

- The General Meeting of Shareholders held on April 8, 2008 approved the proposal to reduce the share capital by reducing the par value of the shares by CHF 0.50 from CHF 5.00 to CHF 4.50 each and payment on June 30, 2008 to holders of the shares on June 27, 2008;
- 35'786 registered shares were issued and fully paid for at a price of CHF 6.00 further to the exercise of options granted under the 2004 Management and Board Participation Plan (MBP04). In addition, 7'271 options granted under the MBP04 were exercised on December 30, 2008 and issued and fully paid in January 2009;
- CHF 125'000 of the conditional share capital which was reserved for the issuance of shares upon the exercise of option rights which were granted to certain creditor banks in consideration of them waiving part of their claims in 2002 which could have been exercised until July 2007 being without object anymore was cancelled during 2008.

As a result of the above, the following changes were made to the Articles of Incorporation of the Company during 2008:

- The share capital amounts to CHF 67'588'654.50 represented by 15'019'701 registered shares of CHF 4.50 each;
- The conditional share capital was reduced to CHF 4'000'743.00 which can be used for the issue of 889'054 registered shares of CHF 4.50 each to be fully paid to satisfy stock compensation plans in favour of eligible members defined by the Board of Directors.

NOTES TO THE FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

During the year 2007:

- The General Meeting of Shareholders held on April 3, 2007, approved the issue of 900'000 conditional shares that may be used by the Board of Directors to satisfy the Management and Board Participation Plan 2007–2009 (MBP07);
- 150'410 registered shares were issued and fully paid for at a price of CHF 6.00 further to the exercise of options granted under the 2004 Management and Board Participation Plan (MBP04);
- 89'500 registered shares were issued and fully paid for at a price of CHF 11.39 each under the MBP07;
- 953'125 registered shares were issued and fully paid for at a price of CHF 6.00 further to the exercise of options granted to former creditor banks as compensation for their debt waiver in 2002.

As a result of the above, the following changes were made to the Articles of Incorporation of the Company during 2007:

- The share capital amounts to CHF 74'919'575 represented by 14'983'915 registered shares of CHF 5.00 each;
- The conditional share capital was reduced to CHF 4.7 million which can be used for the issue of registered shares of CHF 5.00 each to be fully paid to be allocated as follows:
 - For a maximum amount of CHF 0.1 million which is reserved for the issuance of shares upon the exercise of option rights which were granted to certain creditor banks in consideration of them waiving part of their claims in 2002 which could have been exercised until July 2007. This portion of the conditional capital which is now without object will be cancelled during 2008;
 - For a maximum amount of CHF 4.6 million which is reserved for the issuance of shares that may be used by the Board of Directors to satisfy stock compensation plans in favour of eligible members defined by the Board of Directors.

5 Treasury shares

Movements in treasury shares are as follows:

	2008		2007	
	Nb of shares	Amount	Nb of shares	Amount
At beginning of year	159'565	2'070	56'000	84
Purchases	658'854	9'195	103'565	1'986
Sales	-338'855	-4'696	-	-
At end of year	479'564	6'569	159'565	2'070

Treasury shares are valued at the lower of average purchase price and average quoted price during the month preceding the closing of the accounts. Sales of treasury shares during 2008 resulted in a gain of KCHF 1'257 (2007: NIL).

As from July 12, 2004, 50'000 of these shares were loaned to a third party for market-making purpose. The Company is charged a fixed fee for each share movement, any gains and losses resulting from the shares sold/bought being at the profit/expense of the third party. During the year 2008, total costs incurred totalled KCHF 51 (2007: KCHF 56).

NOTES TO THE FINANCIAL STATEMENTS

All figures are presented in thousands of Swiss francs (CHF) unless otherwise stated

6 Significant shareholders

At December 31, 2008, Tsugami Corporation, Japan hold more than 5% of the share capital of the Company (December 31, 2007: 0%).

7 Board of Directors and General Management compensation

The disclosures required by articles 663b^{bis} and 663c of the Swiss Code of Obligations on the Board of Directors and General Management compensation is reflected in note 31 of the consolidated financial statements.

8 Risk assessment

The disclosures required by articles 663b of the Swiss Code of Obligations on the risk assessment is reflected in note 32 of the consolidated financial statements.

PROPOSED APPROPRIATION OF AVAILABLE EARNINGS

In thousands of CHF

For the years ended December 31,	2008	2007
Retained earnings brought forward	4'607	6'417
Transfer to reserve for treasury shares	-4'499	-1'986
Effect of reduction of par value per share on treasury shares	230	-
Net income for the year	7'499	176
Available earnings	7'837	4'607

The Board of Directors proposes to the General Meeting of Shareholders the following appropriation:

In thousands of CHF

For the years ended December 31,	2008	2007
	Proposal	Actual
Available earnings	7'837	4'607
To be carried forward	7'837	4'607



TORNOS S.A.

Rue Industrielle 111 CH-2740 Moutier Phone +41 (0)32 494 44 44 Fax +41 (0)32 494 49 03 contact@tornos.com www.tornos.com