

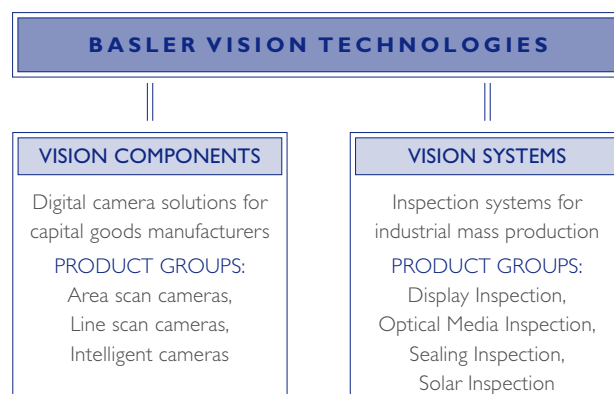
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Key figures

in € million	2006	2005	+/- in %
Income statement			
Sales	52.1	45.0	+16
Gross result	27.3	22.2	+23
Gross margin (%)	52	49	+3
EBITDA	11.8	8.9	+33
EBIT	5.5	4.1	+34
Earnings before tax	4.9	3.6	+36
Net Result	3.0	2.4	+25
Number of shares (m)	3.5	3.5	–
Income/loss per share (euros)	0.85	0.68	+25
Balance sheet			
Total assets	45.4	41.2	+10
Current assets	20.3	18.1	+12
Tangible assets	2.6	2.6	–
Equity	25.0	22.0	+14
Equity ratio (%)	55	53	+2
Debt capital	20.5	19.3	+6
Debt ratio (%)	45	47	–2
Cash flow			
Cash flow from operating activities	8.6	7.9	+9
Cash flow from investing activities	–8.1	–9.0	–10
Cash flow from financing activities	–0.6	1.2	–150
Employees			
Number of employees	303	311	–3
Employees in Research and Development (%)	30	30	–
Employees in Germany	259	269	–4

Corporate structure





▲ Basler's CEO, Mr. Dietmar Ley, receives the "Ort im Land der Ideen" (place in the country of ideas) award from Deutsche Bank representatives



German President Horst Köhler and the representatives of the 365 "places in the country of ideas" attend the initiative's annual reception in Berlin.

► The open day was well frequented. Several thousand visitors enjoyed the beautiful weather that graced the family event and watched the games held in the context of the 1st Basler RoboCup match. The winning team were the FU Fighters from the Freie Universität Berlin.



[!] Basler – a “Landmark in the Land of Ideas”

In 2006, Basler was honoured as “Landmark in the Land of Ideas”. “Germany – Land of Ideas” is a joint site promotion initiative of the Federal Government of Germany and the German economy, represented by the Federation of German Industries (Bundesverband der Deutschen Industrie – BDI) and leading German companies who wanted to present Germany as a broad-minded, competitive and forward-looking country in the year of the FIFA World Cup. Numerous cooperation partners from science, the government, culture and society – including the Foreign

Office, the Goethe Institute and several Federal States – contributed to this initiative. “365 Landmarks in the Land of Ideas” is one of five main projects of the initiative.

“We are honoured that we were chosen as a figurehead to represent Germany in the context of this nationwide campaign.”

Dietmar Ley,
Chief Executive Officer

From 1 January to 31 December 2006, every day one winner presented itself to the public with an event. The result was the biggest series of events ever held in Germany. The 365 Landmarks

were not geographical locations. A Landmark in the Land of Ideas can be any place where ideas are developed, promoted or preserved. The jury chaired by Prof. Dr. Martin Roth, General Director of the State Art Collections of Dresden, selected the 365 Landmarks from over 1,200 applicants.

In its capacity as Landmark in the Land of Ideas, Basler opened its doors for any-one interested on 26 August 2006. The undoubted highlight of the day was the first “Basler RoboCup” – a robot soccer tournament where teams from various German universities had their self-built robotic soccer players compete with each other on a 4 m x 5 m pitch. The day was rounded off by guided tours around the Company premises and information about industrial image processing technology.



Our vision and our mission

Vision Technology is the driving force of technical progress in industrial, medical, scientific and other consumer applications. It will make production more efficient and medical care more effective. It enables a more sustainable use of our resources and will also make our private lives more comfortable.

Our mission is to become the world's leading Vision Technology company through innovative & easy-to-use products that make our customers more competitive.

Contents

2	Preface by the Management Board
7	New Product Ideas
12	Share
16	Management Report
26	Financial Statements 2006
32	Notes
44	Audit Opinion
45	Corporate Governance
46	Report of the Supervisory Board
48	Service



Preface by the Management Board

Ideas to fuel Growth

Dear shareholders, business partners and friends,

One of the key strengths of Basler is the wealth of ideas that come from our employees. Their resourcefulness and their ingenuity, their visionary yet pragmatic thinking and their creative acumen will continue to drive us to achieve our growth goals. The results of their creative exuberance can be seen in new products, optimized processes and better forms of communication. As the Management Board it is thus one of our main concerns to create a climate in which our employees are free to constructively and creatively implement their ideas for the benefit of all who participate in our corporate success.

With its staff of more than 300 employees, Basler is one of Europe's biggest Vision Technology companies. Roundabout 30% of our employees work in research and development, forming the largest idea-pool for this technology in Europe.

As one of the 365 companies selected for the Federal Government's "Land der Ideen" (Land of Ideas) initiative, we were able to present the sheer wealth of our ideas to a broad public in the year of the World Cup. We are proud of this, but we are also aware that ideas are not an end in themselves but need to be translated in terms of hard cash. And we have succeeded in doing just this: in the course of the past business year our turnover has risen by 16% from € 45.0 million in 2005 to € 52.1 million. Our net profit has even risen by 25% to € 3.0 million. These results demonstrate that Basler has fared much better than all the rest of the Vision Technology market which showed a growth rate of under 10% in 2006.

A major part of our employees' creativity goes into the development of new products. In 2006 we have once more invested over 14% of our turnover in research and development. Last year the share of turnover for new products less than 24 months old was once again higher than the target figure of 50%. New products are the motor that drives our corporate growth, both now and in the future.

Our company boasts two business units: with our Vision Systems we offer inspection systems for use in the mass production of flat screens, optical storage media, rubber seals and solar wafers. Vision Components, on the other hand, develops and markets digital camera solutions and intelligent cameras for industrial applications (as in the electronics and semiconductor industries) and non-industrial applications (as in medical and traffic technologies).

With this constellation, and with our universally applicable core technology, we are able to address the needs and requirements of a broad number of industry sectors simultaneously. We can pave the way to, and access, new and

„Our customers benefit from the exceptional creativity that forms the basis of Basler's success; we will strengthen this positive development on a profitable basis.“

Dietmar Ley, Chief Executive Officer

highly promising markets as we did last year with the solar energy market. In this way we can continue to unfold our growth strategy whilst also diversifying our activities to protect our core business against changes in cycles of demand and the fluctuations in turnover they bring about.

In 2006 our two business units have shown disparate types of development. Turnover from Vision Systems stagnated vis-à-vis 2005, at € 28.8 million compared to € 29.1 million for 2005. The divisional operative result came to € 1.5 million – or 32% less than in the previous year where it was € 2.2 million. On the other

hand, our Vision Components business unit has had a highly successful year in 2006 with turnover increasing by 47% to € 23.3 million compared to € 15.8 million for 2005. Its EBITDA result even improved by 87% to € 4.3 million (2005: € 2.3 million).

Business with inspection systems for the flat screen industry – the area where we currently achieve our highest systems turnover – continued to flourish in 2006. In terms of our core business with inspection systems for screen glass for liquid crystal displays, over the past four years with our successful partnership with the two global leaders in this segment, we have installed over 100 systems and are the undisputed market leader.

What's more, in 2006 we also succeeded in positioning ourselves in a new market segment – inspection of color filter display glass. A first major order placed by one of the three global leaders in this segment, gives us every confidence that we shall continue to expand our business in this field in 2007.



In terms of inspection systems for optical storage media, we have forged ahead in preparing the future market for 3rd Generation media (High Density-DVD and Blu-ray®-discs). Even if the market has remained unchanged in the doldrums of a weak cyclical phase and turnover has stagnated compared to 2005, we have still been able to successfully position ourselves with numerous key customers as the provider of inspection systems for the new storage-intensive formats. This means that we now occupy an favourable vantage point from which to exploit the investments in production facilities for these new media to be expected from 2007/2008 onwards.

Business in 2006 with inspection systems for the rubber and elastomer industries has not matched our targets. The reason for the drop in turnover may be found in the reluctance of our customers to invest in the light of the delays experienced by major projects with the automotive industry. Our market share, however, still remains intact. In 2007 we expect a slight recovery in the investment activities of our customers.

With turnover growth of 47 %, our sales of components show a growth rate clearly outstripping that of the market. Basler is now one of the main global manufacturers of digital camera solutions for industrial applications. The main reason for this particularly welcome trend in 2006 is the accelerated pace at which technically obsolete analogue technology is being replaced by digital technology – a switch-over which owes a great deal to our innovative and reliable product portfolio. Alongside this, there has also been a steady demand from key sales markets like the semiconductor and electronics industries. At the same time past new developments have excited keen interest from customers and generated additional sales. In 2006, for instance, we received our first major order for the “Basler eXcite” intelligent camera which we developed back in 2005.

With a broad range of new products in the Vision Components division we are also expecting a further surge in growth for 2007. At the leading European trade fair for the Vision Technology industry, held in November 2006 in Stuttgart, we used our innovation campaign to unveil over 40 new camera models all built on one common platform. Our two families of camera – the “Basler scout” and the “Basler pioneer” - both feature the new Gigabit Ethernet connectivity standard and thus drastically simplify the switch-over to digital camera technology for our customers. All our new products are leaders in their respective fields in terms of the price-performance ratio, and thus provide our customers with a solid commercial incentive to change over to modern digital camera technology. Our presentation found a strong and positive customer resonance by the end of the year.



In the past fiscal year Basler shares have increased in value by 16% (from € 11.40 to € 13.22 as of 31 December 2006). Comparable indices like the TecDAX have fared better in an extremely positive stock exchange environment. Given this climate, we have once more extended our Investor Relations activities and intensified our contacts with investors. We have revised our Equity Story and secured the services of further partners on the capital market. These measures should contribute to ensuring that the price of Basler shares in 2007 once more shows an above market increase as it has done in the past.

With our gaze turned to the future, we agree with Max Weber who once wrote that “Only on the basis of hard work does the idea generally germinate”. The ideas that we develop are neither pulled out of thin air nor should serve as pure ends in themselves. They are hard won, offer tangible customer benefits and thus constitute the basis on which our continued profitable growth is founded. We feel ourselves to be well prepared for 2007 and the coming years. The new product developments we unveiled in 2006 have already excited considerable customer interest and our innovation pipeline is packed with a host of innovative product ideas. At the same time we do not cease to consider new ways of making our organization more efficient in its structure and operations, and of further improving our communication. And finally we are structurally investigating openings for achieving additional growth with new forms of business and new partners. With all this in our sights, we look forward once more to clearly improving our turnover in 2007.

We would like to thank you for the interest you have shown in our company and for the confidence you have placed in us.


Dietmar Ley


John P. Jennings


Peter Krumhoff



VISION SYSTEMS

Our inspection systems guarantee the highest level of inspection security in the production process and help our customers optimise their manufacturing processes.

[!] New Product Ideas

A system that checks solar cells for cracks. Equipment that inspects flat glass for the production of TFT displays. Camera solutions that are easy to connect. And a camera that is unrivalled for its speed. During the last few years, these new product ideas aroused our customers' interest and formed the basis of the company's growth.

As one of the leading global vision technology companies we address many different application markets in the industry, healthcare and science sectors. Vision Technology is based on the recording of optical information (e.g. visible light, infrared light, x-rays) by cameras, the automatic processing and evaluation of image data and the production of a situation-related decision by respectively programmed computers.

The technology used is a cross-sectional discipline involving a number of basic technologies that can be combined and implemented according to the task at hand. This includes camera production, lighting technology, computer production, software and mechanical construction. A well functioning vision system distinguishes itself by the optimum interplay between the respective technical disciplines for the benefit of customer and market-relevant solutions. Our approximately 100 developers are working on the development of the individual disciplines relevant for our company and are consolidating our expertise in the vision technology field. This enables our distribution and marketing units to offer products and solutions that are fully adjusted to the needs of our customers.

Our approximately 100 developers are consolidating our expertise in the vision technology field.

Our products are concentrated in two business sectors: firstly, turnkey systems – “vision systems” – that carry out quality inspection tasks in the industrial production field, and secondly “vision components” – the development of digital camera solutions for capital goods manufacturers in the fields of industrial mass production, healthcare technology and traffic control.

Safe and efficient – vision systems optimise production

Having to hold their ground in the face of global competition, commodities manufacturers are under massive cost pressure. They employ vision systems both for quality inspection purposes and for the optimisation of production processes. Rising production efficiency leads to an increase in manufacturers' competitiveness. The actual functioning of vision systems follows a set process: image acquisition, image pre-processing and image evaluation.

During the image acquisition process, the camera produces a digitalised image of the scene. The aim is to produce the most useful representation of the object for the respective inspection function. In the case of TFT flat glass inspection for example, the glass must be lit and screened such that all relevant surface and embedded defects are detected without fail.

During the image pre-processing stage, the image data are prepared for the subsequent image evaluation. In the case of high performance applications, such as TFT flat glass inspection, it is often necessary to reduce the data volume delivered by the cameras before commencing the actual image evaluation in order to guarantee full inspection of the glass in the available inspection time. In this example image pre-processing fulfils the function of locating suspect areas in the camera image and transferring these exact image data to the actual image evaluation process. The use of this technology reduces the to be analyzed data volume by more than 90%.



Our color filter inspection systems are integrated in the display production process and inspect the color filters applied to flat glass. Color filters are responsible for the color displayed in the finished flat screens.

During the image evaluation stage, the pre-processed image data are analysed and actions that depend on the result of the analysis are initiated. For example, during the inspection of a Blu-ray® disc, the new optical storage medium, defects are classified during image evaluation and assessed according to their extent and number. Should any of the defect criteria exceed a preset limit, the Blu-ray® disc receives a deficient evaluation and is rejected. Should several successive storage media be rejected, a serial defect may exist and the production line is stopped.

Besides simple good/bad sorting, the result of the image evaluation can also be used for automatic optimisation of the production process (so-called yield management). In this context, the production line settings are automatically corrected on the basis of the inspection result before the defect exceed set limits. This leads to a general avoidance of the production of defect parts which, in turn, increases production efficiency.

Tracking the fracture – micro crack inspection in the photovoltaic industry

In 2006, we presented innovative inspection systems for the photovoltaic industry to the public. The solar industry is one of the fastest growing markets worldwide. By 2020 turnover generated by solar companies in Germany alone is expected to quadruple compared to today (to over € 15,000 billion).

Exploding demand for solar wafers and modules has led to scarcity and hence rising prices of the raw material silicon. Manufacturers of solar wafers (=solar semiconductor discs) are therefore using the raw material as efficiently as possible and are forced to reduce the number of rejects during production. To achieve this, manufacturers are making increasingly thin raw wafers in order to produce ever larger numbers from the available silicone. At 200 micro meters thickness, these thin wafers are equally efficient but significantly more unstable and more prone to break than their thicker predecessors.

In conjunction with the market leaders in the flat glass TFT sector, we have developed inspection systems that perfectly meet our customers' requirements.

Against this background, our fully automated vision systems, which are integrated into the production process, fulfil an important function: the raw wafers are recorded within the process cycle, line by line, by high resolution cameras. With an accurateness of 50 µm or 50 thousandth millimeters, the thin wafer is inspected for so-called "micro cracks" that interrupt crystalline structures and may lead to fractures in the wafer at subsequent production stages. By way of comparison, the human eye can only discern structures of 100 µm and above. Should a raw wafer exceed a certain frequency of micro cracks, its early rejection may avoid further refining and further production costs. In this way our solutions support manufacturers of solar wafers in their efforts to reduce raw material consumption by using thinner raw wafers and increasing capacity use of their highly capital-intensive production facilities.

Keeping a keen eye on flat screen monitors

Our inspection systems for the flat screen industry offer similar benefits: flat screen monitors are produced in several stages. The initial raw material consists of high-quality flat glass that is less than one millimeter thick and is subsequently cut into the future format of the end product (e.g. PC monitors, TVs, mobile phone or PDA displays). During further production stages, the flat glass is refined and combined with various functional layers, such as color filters.

All along the manufacturing process, manufacturers are facing the challenge of meeting private consumers' snow-balling demand for ever larger unblemished flat screens that must be manufactured in the shortest possible time while their production costs must be reduced. To achieve this aim, manufacturers not only build additional factories but also increase production efficiency per se. Inter alia, they are increasing the formats of the manufactured flat glass. The bigger the initial glass, the higher the number of flat screen units that can subsequently be cut. This raises the ultimate output of each production line. The dimensions of the glasses are increasing in so-called generations. A few years ago, the first generation of flat glass had a format of 0.3 m x 0.4 m. Today, 9th generation glass already measures 2.4 m x 2.8 m.

During the years we have been working with the two market leaders in the field of flat glass manufacture for TFT displays, we have developed inspection systems that are perfectly adjusted to customer requirements. In contrast to conventional procedures, the inspection now takes place "in-line", i.e. without interrupting the production processes. This method saves both costs and time. With the help of a special air-cushion conveyer concept, the substrates move past our inspection system without being touched or soiled.

Furthermore, due to their modular structure, our systems can be scaled in almost any way required by the user. Both the number of digital cameras and the computer capacity can be adjusted to the size of the glasses that are being manufactured. For the inspection of 5th generation glass (1.1 m x 1.3 m) 12 cameras are being used while the inspection of the 9th generation glass requires up to 42 cameras. In larger systems this leads to the duplication of the data volume recorded per time unit, which requires an extremely high processing performance. This computer can process a maximum data volume of up to 4.7 gigabytes per second or 60 DVDs per minute.

A clever connection: GigE Vision

Within the short period of eight years, our Vision Components division has established itself among the three leading global suppliers of digital industrial cameras. On the one hand, the customers of our over 200 different camera products consist of capital goods manufacturers who equip their systems with industry-proof cameras and sell them on to end customers. On the other hand, cameras are bought by end customers who use them for various tasks (inspection, measuring, sorting or controlling) in their production environment.



The polarizer foils applied to the flat screen are inspected for purity. These foils pool the light and focus it more strongly on the observer. This saves energy costs and increases battery performance in the case of mobile applications, such as notebooks.



Our inspection systems can recognize minuscule cracks, so-called "micro cracks", on solar wafers, which are not visible to the naked eye.



The Basler *vario 2* inspects entire surfaces of up to nine so-called o-rings per second.

The Basler *sprint* camera is four times faster than any competitive camera.

Due to our extensive portfolio of cameras of various resolutions (up to 4 mega pixel) and image frequencies (up to 500 images per second), we have gained a leading market position. We intend to expand and consolidate this position with our new Basler *scout* und Basler *pioneer* camera families which we introduced at the end of 2006. The over 40 new cameras are all based on the innovative GigE Vision data interface. As a member of various standardisation bodies, Basler played an important role in the definition and technical development of the interfaces.

The new GigE Vision standard uses the proven Gigabit Ethernet data transfer standard which is frequently applied in computer networks. This standard provides a very high data rate as well as a cable length of up to 100 m allowing our customers to use a cost-effective cable to transfer large data volumes over great distances. In addition, the new camera families are based on a large and consistently conceptualised set of product variations and are compatible in terms of controls and size. As a consequence, our customers do not need to do a lot of integration work when a new camera model is used for the first time.

Fast – faster – sprint

The industrial production of split products, such as paper or plastic foils, is based on production speeds of several hundred meters per minute. In order to inspect the material quality within the process cycle, manufacturers of inspection systems depend on extremely fast and light-sensitive cameras. Last year, we developed a high-speed line scan camera, Basler *sprint* – a further highlight for exactly these applications. In contrast to conventional area scan cameras, line scan cameras are not based on two-dimensional image sensors but on one single sensor line, similar to photocopiers or document scanners. The key element of the Basler *sprint* family is the new high-speed sensor that

was developed under the auspices of Basler. The sensor facilitates 140,000 exposures per second which makes it four times faster than any competitive product.

Besides its exceptional speed, Basler *sprint* distinguishes itself by its excellent light sensitivity. Where high production and sorting speeds are required, very little light is available per individual exposure even if the brightest light sources are used.

Hence the image sensor of Basler *sprint* was developed with exceptional light sensitivity based on an innovative pixel structure. Basler *sprint* offers further options that make life easier for users: with the help of special software customers can focus on one particularly important image detail. This reduces the volume to be processed and leads to another further substantial increase in the image recording speed.

Basler's industrial cameras of the latest generation are powerful and easy to integrate into clients' applications.



VISION COMPONENTS

Digital camera solutions –
used for all technical
applications that require
high-quality, simple inte-
gration and an extensive
product range.

A share with great growth potential

In an extraordinarily positive stock market environment, the share price of Basler AG went up 16% in 2006, lagging slightly behind the development of similar indices. Thanks to positive business prospects and additional Investor Relations (IR) activities we expect the share to perform well again in 2007.

2006 was an exceptionally good year for the stock market. The DAX index rose by 22% from 5410.24 to 6596.92 reflecting the positive assessment of the future growth prospects of the German economy. This was beneficial in particular also to small and medium-sized enterprises in the S- and MDAX and the technology stocks in the TecDAX. For instance, the TecDAX rose by 25% from 596.61 to 748.32 in the course of the year.

The Basler share opened at a price of € 11.40 in 2006 and quoting at € 13.22 at the end of the year which corresponds to a value increase of 16%. The participation of new investors pushed the share price up to € 14.50 at the beginning of the year. After that it moved within a narrow range initially. Reports about a major order for new products in the field of flat screen inspection brought the share price to its yearly high of € 15.15 whereupon it came down again as a result of profit-taking. Finally, the share price moved within a narrow margin between € 12.00 and € 14.50 until the end of the year.

We continued to further develop our IR work in 2006. The measures taken included a complete revision of our Internet presence by adding new information and improved service features. For instance, investors can now access current analysts' studies or have automatic reminders sent to them of future financial dates of Basler.

New investors and a major contract buoyed up the Basler share at the start of the year. Despite profit-taking, the price stabilised at a high level in the second half of the year.

We have also been developing our direct communication with investors in 2006. In addition to a number of road shows with institutional investors in Frankfurt, Zurich and Paris, the Management Board took part in four different investor conferences in Hamburg, Munich and Frankfurt – including the German Equity Forum of Deutsche Börse AG in November. We explained the annual and quarterly financial statements to interested investors and analysts in four conference calls. Many investors availed themselves of the opportunity also in 2006 to contact the IR team directly by telephone or email.

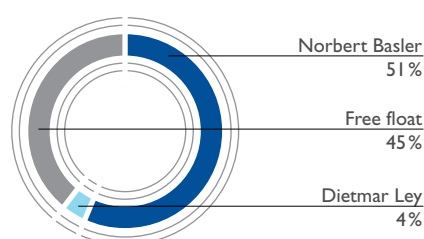
Due to our intensified IR efforts, more analysts resumed coverage of Basler in 2006. Our Company is currently being monitored by five analysts from different banks and research firms (previous year: 3). The current recommendations can be found at www.baslerweb.com/share under "Analyst Studies".

The Annual General Meeting was held on 8 May 2006 in Hamburg at the Chamber of Commerce. The 104 shareholders present represented 65% of the voting capital and gave their consent to the Management's proposals for the agenda by at least 99.5% of the votes present.

For 2007, we have initiated further measures to achieve a better ranking of Basler in the capital market. This included, for instance, a thorough review of Basler's equity story which now introduces the Company to investors in an even clearer and more focussed manner. Moreover, we have appointed another designated sponsor to provide additional liquidity for trading. The designated sponsors currently retained are regularly rated AA, i. e. awarded the highest rating, by Deutsche Börse.

With a price-earnings ratio (2006) of 15, Basler is rated relatively low, taking into account that the share is a growth stock. Similar companies are rated much higher although their business results are very similar. Thanks to the measures taken and the investments made, we expect the Basler share to perform well in 2007 and ultimately also the company to perform better than the relevant indices such as the TecDAX.

Shareholding structure



Contact

If you have any questions, please do not hesitate to contact our Investor Relations department:

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Tel 04102-463 0
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www.baslerweb.com/share

Regular information

If you would like to receive regular information e-mail, please use our contact form at www.baslerweb.com/share/ or contact the Investor Relations department.

Basic information regarding the Basler share

ISIN:	DE0005102008
SE code:	BSL
Prime sector:	Industrials
Industry group:	Advanced industrial equipment
Market segment:	Prime Standard/Regulated Market
Designated sponsors:	Close Brothers Seydler AG, equinet AG
Number of shares issued:	3,500,000
Member of the following indices:	CDAX, Prime AllShare, Technology AllShare, GEX*

* GEX is the indicator for the stock-market performance of small and medium-sized enterprises.

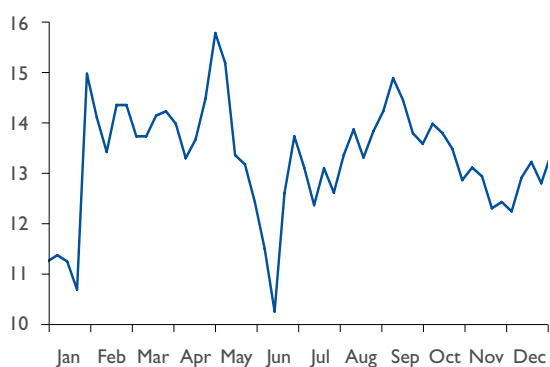
Ratios concerning the share price

	2006	2005	2004	2003
Market capitalisation in million € (as per 31 December)	46.27	40.1	52.5	37.8
Year-end price in € (as per 31 December)	13.22	11.45	15.00	10.80
Peak price in € during the year	15.15 (05,05)	18.29 (07,02)	15.75 (05,10)	15.80 (04,11)
Low in € during the year	10.60 (26,01)	11.00 (22,12)	10.50 (29,03)	2.11 (28,02)
Development over the year	+16%	-23%	+43%	+238%

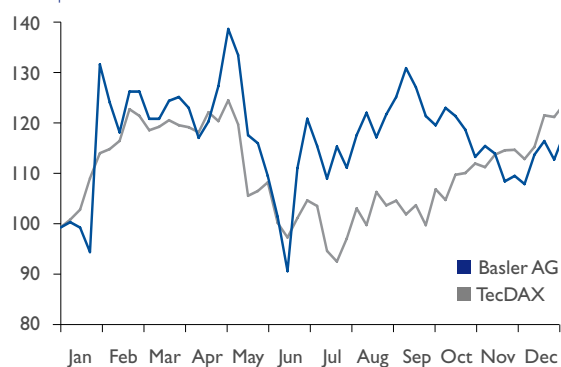
Directors' Dealings

Date	Person subject to disclosure requirements	Position	Transaction	No. of units	Price in €
05.07.2006	John P. Jennings	CCO	Purchase	2,000	13.00

Absolute performance of the Basler share in 2006



Relative performance of the Basler share in 2006 compared with TecDAX



Further information on this subject is available on the Internet at www.baslerweb.com/share.



MANAGEMENT REPORT AND FINANCIAL STATEMENTS

16 | Management Report

26 | Financial Statements 2006

32 | Notes

44 | Audit Opinion

45 | Corporate Governance

46 | Report of the Supervisory Board

Management Report

I. MANAGEMENT REPORT

I.1 Corporate structure

Basler has two divisions that operate in the Vision Technology market:

- Vision Systems develops and markets turnkey quality inspection systems for mass production in various industries.
- The second business division, Vision Components, develops and sells digital camera solutions for original equipment manufacturing customers (manufacturers of capital goods) in the market segments of machine vision, medical engineering and intelligent traffic systems.

I.2 Business environment and sector development

I.2.1 Macroeconomic environment

The upswing in the global economy continued in 2006. A weaker business cycle in the US and to a lesser degree also in Japan lead to a slowdown in growth in the course of the year. This was also not compensated by accelerated expansion in Euroland. In the emerging markets, the sharp rise in output continued, with even stronger growth in China during the first half of the year while the other newly industrialised countries in East Asia saw a slight slowdown in growth at the bottom line. As a whole, the effective gross domestic product is estimated to have increased by 3.7% worldwide in 2006 (DIW 2006).

The upturn in the German economy has improved significantly this year. Although exports continue to rise, this upturn is more and more driven by domestic demand. The effective gross domestic product grew by 2.5% in 2006.

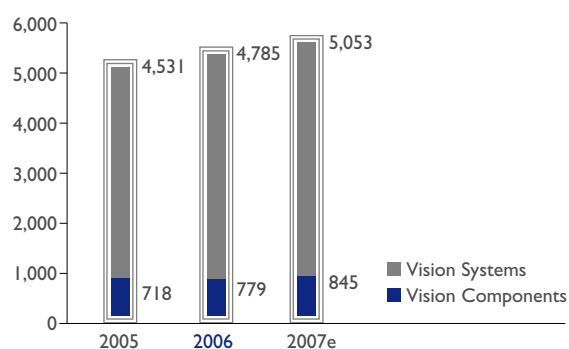
I.2.2 Global market development: machine vision

The Vision Technology market continued its growth also in 2006. The US machine vision umbrella organisation, the Automated Imaging Association (AIA), estimates that the total 2006 turnover in vision systems generated by all machine vision companies totalled US\$ 4.8 thousand million worldwide. This corresponds to a 7% increase (2006: US\$ 4.5m). Applications in the field of industrial mass production account for the biggest part of this turnover. For 2007, the organisation expects a further 6% increase to US\$ 5.1 thousand million. The growth in total turnover in vision components has been estimated at 9% for 2006 and again at 9% for 2007 (cf. graph).

The global machine vision market is mainly concentrated in the highly industrialised regions of North America, Europe and Asia Pacific. According to the AIA statistics, the latter is also the biggest regional market for industrial image processing with 37%. At 28% and 26%, the Europe and the US rank second and third, respectively. The rest of the world accounts for approx. 10% of global machine vision sales.

In addition to the ever growing Vision Technology applications in industrial mass productions, new fields of application arise continually due to the advancement of technology and decrease in prices. Consequently, the Vision Technology market still has a large growth potential.

Development of global turnover in the Vision Technology market in million € (Source: AIA 2006)



1.3 Trend analysis of financial performance indicators

1.3.1 Sales development and order levels

Consolidated revenues increased by 16 %

In fiscal year 2006, Basler Group's sales increased by 16 % to € 52.1m (Basler Group 2005: € 45.0m).

Vision Components sales level increased significantly

Vision Components generated € 23.3m with its products in 2006, thus increasing its turnover by more than 47 % (2005: € 15.8m).

Thereby the broad innovation campaign that was launched in 2004 has achieved full success. In addition, the growth was supported by the ever growing demand from one of the most important market segments today – the semiconductor and electronics industry. This enabled the Company to further consolidate its excellent position in the growing market for industrial digital cameras. Basler Vision Components is currently the fastest growing manufacturer in this market.

Inconsistent development of sales

volumes in Vision Systems

The Vision Systems division recorded turnover of € 28.8m for 2006, matching last year's level (2005: € 29.1m).

The situation regarding the individual product groups is as follows:

Although the expenditure of the flat screen industry for new manufacturing equipment was high again in 2006 due to fast technological advancement, the investment volume fell slightly short of the extremely high level of the past two years. Nevertheless, the Display Inspection

division (inspection systems for the flat screen industry) was able to significantly increase its sales once more in 2006. This was due to the Company's successful entry into the market segment of color filter inspection. This is a fully automated technology for inspecting the color filter layers used to display different colors on flat screens.

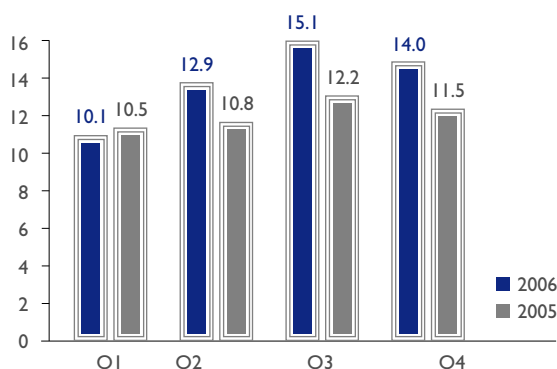
Investing activities in the optical disc industry has decreased further in 2006 compared with last year which was already weak. The reason for this was first an increase in the raw material for optical storage media which the manufacturers of these media could not pass on to their customers. Furthermore, the market launch of the new Blu-ray® disc (BD) or High-Density DVD (HD-DVD) was delayed. As a whole, this resulted in a decrease in equipment orders in 2006 compared with 2005.

The sealing industry also spent less on new inspection equipment last year than in the years before. The reason for this was the fact that major projects of the automotive industry, the main customer for seals inspected by our systems, were postponed. As a result, the sales volume of the Sealing Inspection division slightly decreased as a whole.

Fluctuating quarterly sales due to major orders

Sales experienced fluctuations from quarter to quarter during the fiscal year just ended, reflecting the increasing percentage of sales generated by inspection systems for the flat screen industry. Due to the high average order volume and the relatively small number of projects which bring along high volumes of individual orders, the accounting for such major orders has a significant impact on the quarterly sales figures. Q3 was the quarter with the highest sales volume with € 15.1m (Q3/2006: € 12.2m).

Development of turnovers by quarters in 2005 and 2006
 in million €



Well-balanced customer structure

As in the previous years, the customer structure is well-balanced. In 2006, the largest single customer accounted for 8% of sales (2005: 11%). The three largest customers had a share in sales of 19% in 2006 (2005: 23%), and the largest ten customers accounted for 34% (2005: 33%).

High level of incoming orders

The volume of incoming orders showed an increase of 22% compared with the previous year and amounted to € 57.5m (2005: € 47.0m). This means that the volume of incoming orders grew faster than the sales volume. Both business divisions have contributed to this positive development.

Vision Components accepted orders worth € 24.7m in 2006. This corresponds to an increase of 48% compared with 2005 (€ 16.7m) and is mainly due to the launch of new products and the generally positive market environment.

Vision Systems achieved a volume of incoming orders worth € 32.8m in 2006 which constitutes a slight 8% increase (2005: € 30.3m).

1.3.2 Earnings position

Exponential growth in earnings

The good income situation of the Basler Group in fiscal year 2006 is mainly due to improved productivity accompanied by strong revenue growth. Although earnings before taxes increased by 23%, the total costs rose only by 9% which means that earnings grew more than sales.

In 2006, the Group earnings before taxes amounted to € 27.3 million – 23% higher than in 2005 (€ 22.2m). The Company improved its gross margin significantly to 52%

(2005: 49%). Operating expenses rose by 19% from € 19.6 million (2005) to € 23.4 million. The biggest cost increase among operating expenses was attributable to sales and marketing. These expenses increased from € 7.4m in 2005 to € 9.4m (cf. Fig. 4). The main reason for this increase was investments in the sales and marketing structures of the component business.

For the entire year 2006, the net result amounted to € 3.0 million (2005: € 2.4m), corresponding to € 0.85 per share (2005: € 0.68 per share). This corresponds to a net margin of 6% (2005: 5%). Based on the development of sales volumes, the third quarter was the strongest quarter with a net result of € 1.5m (Q3/2005: € 1.2m). In the fourth quarter, non-recurring special effects were recorded under cost of materials which were attributable to a changeover in the production of printed circuit boards according to new statutory provisions regarding component groups and soldering methods. Due to the fact that many new products were launched whose development was completed in the fourth quarter, depreciation/amortisation increased as well.

1.3.3 Financial position

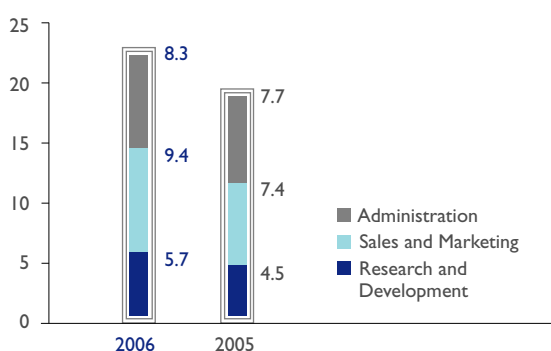
Aims and principles of financial management

The financial management of Basler AG is aimed at satisfying the need for capital so as to keep a reasonable balance between maturity risk, lender assessment and cost of capital. Accordingly, the time-to-maturity factor of the financing scheme is rather sound: 99% of the non-current assets of the Basler Group is covered by equity (previous year: 95%). The current assets cover 180% of the current liabilities (previous year: 196%).

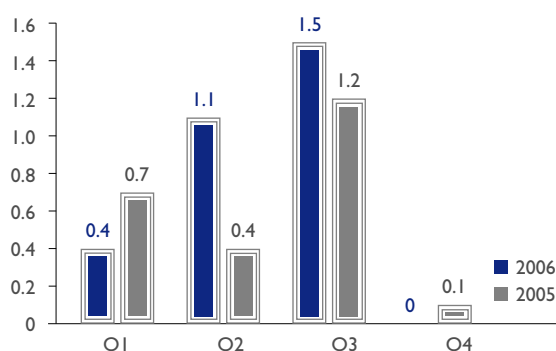
Sources and costs of financing, rating

For the financing of working capital, loan commitments have been obtained from the primary banks for a total of € 9.9m by 31 December 2006 of which € 4.0m has

Development of operating expenses in 2005 and 2006 in million €



Earnings after tax by quarters in 2005 and 2006 in million €



been utilised (utilisation in 2005: € 4.1m). This provides sufficient financing reserves for any short-term purchasing peaks induced by orders.

The capital cover of the fixed assets (excluding deferred taxes) remained almost unchanged at 152% (2005: 151%). At the same time, the equity ratio increased slightly in 2006 (55%) compared with the previous year (2005: 53%). With this ratio we are within our target corridor because both our creditworthiness and the financing of assets are secured at reasonable costs.

The operating cash flow amounted to € 8.6m in the fiscal year just ended (previous year: € 7.9m) which corresponds to 17% of sales (previous year: 18%). After net investments in an amount of € 8.1m (previous year: € 9.0m), the free cash flow amounts to € 0.5m (previous year: € -1.1m).

1.3.4 Net worth position

Sound balance sheet

The net worth position of the group was sound again in the fiscal year just ended. All in all, the net distributable profit of the group increased by 10% to € 45.4m until 31 December 2006 (31 December 2005: € 41.2m). The equity ratio amounted to 55% (31 December 2005: 54%).

Based on the trend in earnings, the equity capital increased by 13% to € 24.9m by 31 December 2006 (31 December 2005: € 22.0m). In order to finance this growth, current liabilities increased from € 9.2m (31 December 2005) to € 11.3m (31 December 2006).

1.3.5 Composition of subscribed capital

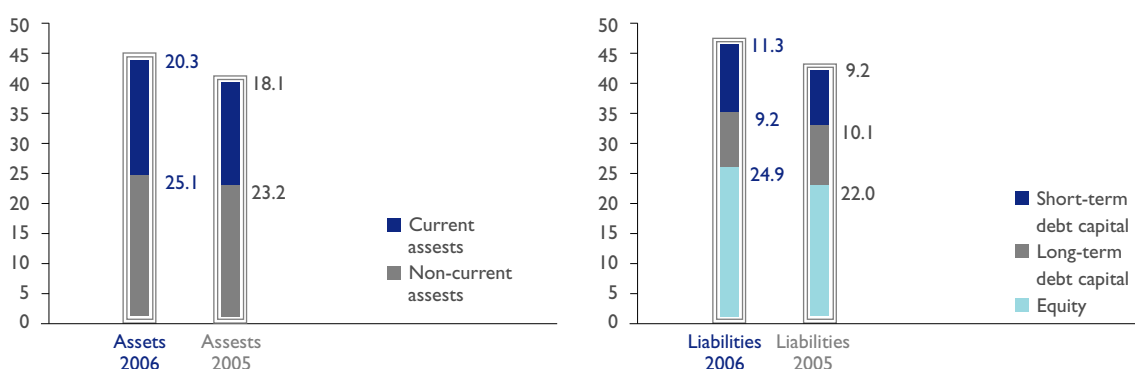
No voting rights were reported to the Company from the shares to be allocated to free float which would exceed the statutory reporting thresholds.

2. INVESTMENTS AND FINANCING

Development work is stated on the asset side at production cost and depreciated in accordance with the applicable regulations. The depreciation period was chosen to be three years. In the event that certain indications exist, the capitalised development work items are examined as to the degree to which they have maintained their value (impairment tests). For this purpose, the net present value of the cash flows to be expected from the business divisions are compared with the net value of the assets from own developments. If the cash flows to be expected were lower than the net value stated on the balance sheet, extraordinary valuation adjustments would have to be made. The impairment tests for fiscal year 2006 did not result in any extraordinary valuation adjustments.

The focus of the investing activities was on the further development of the Company's own product portfolio. For instance, investments were made in development projects worth € 6.7m of own expenses (2005: € 7.2m) and € 0.2m (2005: € 0.4m) of third-party development costs. Furthermore, € 0.4m (2005: € 0.4m) was invested in software and other intangible assets such as patents. € 0.8m (2005: € 1.1m) was invested in tangible assets, mainly for IT hardware and production equipment.

Balance sheet structure in 2005 und 2006 in million €



3. TREND ANALYSIS OF NON-FINANCIAL PERFORMANCE INDICATORS

3.1 Research and development

Our core business strategy and its resulting success on the market is based on an innovative product portfolio. Our continuous development work is focussed on the needs of our customers and takes into account the most recent technical trends.

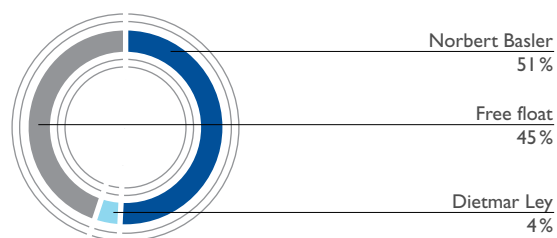
In 2006, both of our divisions launched new products on the market. Vision Components launched an innovation campaign with over 40 new products over the years. With the new product families "Basler scout" and Basler pioneer", we offer our customers the biggest product portfolio currently available of cameras using the new data transfer standard "Gigabit Ethernet". This new standard in whose definition and technical development Basler was significantly involved in several standardisation bodies enables our customers to solve image processing tasks at a medium performance level at lower costs and more easily than before while being flexible in their choice from a wide range of product variants designed consistently according to a modular concept. Moreover, our new cameras are the most compact models in their performance category.

The first systems for inspection of color filters could be installed in the Vision Systems division. The color filters are applied to glass substrates in the early stages of the flat-screen production process and are responsible for the color quality of the image in the finished flat screen display. Due to its groundbreaking concept and record performance, this inspection system represents an important innovation for the flat-screen industry. The first inspection systems for the new Blu-ray storage media formats have been tested just as successfully at some of our key customers and first devices have been sold.

Thus this division is well-positioned to participate in the mass production of these new formats which is expected from the middle of 2007 onward. The focus of our development work relating to the inspection of rubber and elastomer products was on the revision of our premium product "Basler vario2" which is able to inspect products even faster and is capable of adapting itself even more flexibly to the inspection requirements.

Since the third quarter of 2006, the Vision Systems division has expanded its business activities to include inspection solutions for the photovoltaics industry. With these products, we offer manufacturers of raw wafers, wafer-based solar cells and thin-film modules fully automatic solutions integrated into the production process for important quality control tasks which until now could not be automated. The main benefit of the products is an increase in efficiency and a reduced consumption of silicon which is difficult to procure. The solar industry is one of the fastest growing markets in the world. Sales of solar enterprises are expected to quadruple to more than € 15,000 million by 2020 in Germany alone. The fast growing demand for silicon as a raw material has led to a shortage and a consequential price rise that makes more efficient use of the raw material an essential factor for the success for a solar manufacturer. This is where the Basler inspection systems for solar wafers and wafer-based solar cells come into play: Using leading in-house component technology in the field of cameras, computers and software, the Basler inspection systems are capable of sorting out defective raw wafers and solar cells, thus preventing any unnecessary further refinement. At the same time, the test systems supply valuable data which can be used to continuously improve production facilities. In this way, the Basler solutions support the manufacturers in their efforts to reduce consumption of raw materials by using thinner raw wafers and to improve the overall output of very capital-intensive production facilities. First orders for solar wafer inspection systems from globally leading solar cell manufacturers have already been received. At the end of fiscal year 2006, a first order for the supply of an inspection system for thin-film solar modules was also acquired. Based on these pilot orders, increasing sales of solar inspection systems are expected in fiscal year 2007.

Composition of subscribed capital



In the year under review, the expenditure for research and development (fully absorbed costs) decreased by 6% to € 7.4m (2005: € 7.9m), thereby accounting for 14% of sales (2005: 18%). This continues to place Basler in the top echelons of Vision Technology companies worldwide.

Patents secure Basler's innovation activities and form an important part of our technological strategy. At the end of 2006, a total of 13 patents (some of them worldwide) had been granted (2005: 15), a further 22 had been applied for (2005: 15) and one utility model (so-called "minor patents") had been confirmed (2005: 3).

3.2 Locations

In the third quarter 2006, we added our own distribution office in Japan to our Asian activities. Being the biggest single market for Vision Technology, Japan represents a highly promising sales territory in particular for products of the Vision Components division. Especially the local machine builders of the semiconductors and electronics industry are attractive potential customers for our high-quality camera solutions.

Together with the existing locations in Singapore, Taiwan, China and South Korea, this is Basler's fifth Asian location.

3.3 Employees

Slight decrease in the number of employees

Basler is committed to providing family-friendly policies and procedures for its staff. One indication of this is the high percentage of employees who work under a wide variety of part-time schemes. In order to facilitate comparison, employee numbers are stated in fulltime equivalents here.

The number of Basler employees decreased slightly in the year under review and amounted to an average of 303 employees, representing a 2% drop from the previous year (2005: 311 employees). The turnover of employees continued at a low level of 0.3% in the fiscal year just ended (2005: 1.4%). The breakdown according to regions is as follows: The Ahrensburg headquarters had an average of 259 employees (2005: 269). An average of 15 was employed in Exton (USA) during the same period (2005: 14) and 18 in Taiwan (including the representative office in Shanghai) (2005: 18). 9 employees worked in Singapore (2005: 8) and 2 in Korea (2005: 2).

Staff structure focuses on research and development

As of 31 December 2006, the largest number of Basler's staff were working in the R & D area (30%, 2005: 30%); in production & logistics, the figure was 22% (2005: 22%) and in sales & marketing 35% (2005: 35%). 13% work in administration (2005: 13%) (including all management functions).

As at 31 December, a total of 8 trainees in both the technical and the commercial areas and four students from Wirtschaftsakademie Kiel were employed. This corresponds to a trainee quota of 4%.

3.4 Management Board

The composition of the Management Board did not change in fiscal year 2006. The Articles of Association of Basler AG provide as follows for the appointment and removal of Management Board members:

"Members of the Management Board shall be appointed, their appointment shall be revoked and service contracts with members of the Management Board shall be entered into, amended and terminated by the Supervisory Board. The same applies for the appointment of a Management Board member as chairman and of further Management Board members as Deputy Chairpersons."

The powers of the Management Board regarding the issuance or repurchase of own shares are stipulated in the Articles of Association as follows:

"The Management Board is authorised, subject to approval by the Supervisory Board, to increase the registered share capital of the company by 16 June 2008 by issuing up to 1,750,000 new no-par value bearer shares against cash and/or non-cash contributions either once or several times by a total of € 1,750,000.00. The shareholders shall be entitled to the statutory subscription right in this event.

However, the Management Board is authorised, subject to approval by the Supervisory Board, to exclude subscription rights of the shareholders for fractional amounts. Furthermore, the Management Board is authorised, subject to the Supervisory Board's approval, to exclude the subscription right of the shareholders against non-cash contribution for the purpose of offering the new shares of the Company to third parties against non-cash contri-

bution for the purpose of acquiring companies or participating interests in companies or claims against the Company or any company associated with it. The exclusion of the subscription right by the Management Board subject to the Supervisory Board's approval is also admissible if the capital increase against cash contributions does not exceed 10% of the share capital of € 3,500,000.00 and the issue price is not significantly lower than the stock market price of the share already listed having the same features at the time of final determination of the issue price (Sec. 203 Para. 1 Sentence 1 in conjunction with Sec. 186 Para. 3 Sentence 4 AktG). The stock market price is the arithmetic average of the closing prices of the Company's share in the electronic trading system XETRA on the Frankfurt Stock Exchange or in any successor system during the last ten trading days prior to exercising the power of attorney.

The Management Board shall be authorised, subject to the consent of the Supervisory Board, to stipulate the further details of the capital increase and the conditions for issuance of the shares, notably the issue date."

4. RISK REPORT

As a technology company, Basler AG is subject to a number of risks. Medium-sized companies like Basler cannot influence or control general fundamental risks. Consequently, risk management is primarily an entrepreneurial task for us that consists of controlling risks on the one hand and exploiting opportunities on the other. The Management and the employees are responsible for optimizing the probability of occurrence of these two factors for the benefit of the company.

4.1 Integrated risk management system

Internal control system

The core of our internal control system is a sensible, impermeable division of functions which is ensured by our organizational structure, job descriptions and procedures. The functions are defined in our certified quality management manual and compliance is checked regularly. Given the size of the company and the certified operational control mechanisms, an internal audit department is not required.

Our IT infrastructure security concept is constantly being refined and regularly checked by an external agent. This also applies to compliance with data protection regulations.

Controlling

Strategic, operative and functional controlling is performed in all business divisions. It is based on regular strategy checks and the preparation of balanced scorecards and product road maps. These lead to the systematic formulation of long- and short-term objectives at division level or cost division level.

The achievement of objectives (target/actual comparison) is checked at all management levels in the context of regular meetings where control measures are agreed upon whose effectiveness is also checked.

Early warning systems

Information regarding future developments is documented, exchanged at all levels in regular meetings, reports and minutes and evaluated where appropriate. This system ensures that the risk relevance of both internal and external information is examined at an early stage and that the results can be translated into action at group level.

4.2 Risks of the legal environment

Basler's risks arising from its environment consist of the development of its target markets, its competition and the capital market.

In the year just ended, competition on the Vision Technology market remained intense. Basler's 2006 expenditure for innovation, sales, cost reduction and quality improvement and the respective expenses planned for the year 2007 take this level of competition into account. Due to these measures, Basler's competitive position improved already in 2006.

A general slowdown in the growth trend of the Vision Technology market does not seem to be likely in the near future; however, fluctuations in demand in individual client industries which can be substantial in some cases eclipse this general trend. Basler's sector mix, which has been implemented in the past few years through the company's multi-sector approach, has meanwhile reduced our dependence on individual markets (notably

the optical discs market). Furthermore, the increase in the components business which addresses a number of markets at the same time with standardised products generally contributes to greater risk diversity. Consequently, in case sales in one of our business activities decline, no risks challenging the continued existence of our company as a whole have to be expected. Nevertheless, sales and revenue figures may decline if important target markets such as the semiconductor and electronics industry grow more slowly or even decrease.

The high gross income margin which causes increases in earnings when sales are rising results in correspondingly earnings losses in this event. The company counteracts these individual risks, which cannot be influenced, with foresight tools and flexible cost structures. With respect to target market evaluation, both the management and the sales units make use of all available internal and external sources of information in order to identify imminent changes on the markets at the earliest possible moment and to be able to adequately respond to them.

The Vision Technology sector which is characterised by small and medium-sized enterprises is in the middle of a concentration process at the moment. Smaller companies are being acquired and bigger companies merge in order to create further market opportunities and growth potential. Being one of the biggest Vision Technology companies in Europe, Basler is watching this process carefully and will act as player rather than as target when the need arises. Given the current shareholder structure, a hostile take-over can almost be excluded. However, we continuously monitor our shareholder structure closely and at all times in order to identify any significant shifts.

4.3 Operating risks

Customer satisfaction is often an indicator of the existing risk level with respect to declining sales and earnings. Consequently, our marketing and development activities focus on the determination of customer value. Also in 2006, Basler carried out customer satisfaction surveys in both divisions and optimizes its marketing mix not least on the basis of the respective results.

The availability of existing or new know-how is particularly important in a growth-orientated enterprise. Basler regularly prepares staff plans in order to cover its demand either internally or through external partners. In addition, development and performance talks are held regularly to strengthen staff loyalty at all levels.

Well-timed high-quality product development represents the backbone of any successful technology company. In the development field, procedures and responsibilities are clearly defined and we have introduced planning tools which contribute towards the completion of the vast majority of development projects within the planned time and cost frame.

Rapidly changing technology markets challenge companies to adjust capacities swiftly and efficiently to fluctuating requirements. Our flexible working hour model enables us to compensate fluctuations in the level of orders. Consequently, we are – within certain limits – in a position to "breathe" in unison with the market.

In individual cases, the availability of high-quality technological components that have to be procured externally plays an important role for the delivery times of our products. Continuous monitoring and analysis of procurement markets is thus a critical competence for technology companies. In addition, we need to know which external components must be available when and in what quantity. In the past few years, we have developed procedures to deal with these two tasks and have thereby shortened our delivery times and enhanced our compliance with delivery schedules. However, increasing expectations among our customers require us to continually improve key figures in these areas.

It has become a standard requirement among our customers that the quality of our products and procedures has to be checked and ensured according to an integrated quality management system. Since 2001, we have had DIN ISO 9000/2000 certification and are audited once every year by external auditors. In addition, we carry out internal audits in the course of a year to check and improve our procedures.

An essential component of successful product policy is the establishment and maintenance of a brand image. BaslerVision Technologies' name and logo are registered trademarks and are thus protected against illegal use.

4.4 Financial risks

In the case of export-orientated companies, fluctuations in foreign exchange rates affect market performance and earnings before taxes. 73 % of our sales volume is generated outside the euro zone. Consequently, exchange rates have an influence on our corporate result. In order to limit the risks associated therewith, the transaction volume generated in foreign currencies is appropriately secured by hedging the foreign exchange risk.

No tax risks affecting liquidity can be seen. Should a reform of company taxation result in a significant tax reduction, this causes a non-recurring, not liquidity-affecting, negative tax result due to the adjustment of deferred tax assets.

Liquidity is ensured by strict receivables management. Basler's distinctly formulated and strictly administered receivables management system enables the company to ensure the availability of the required liquid funds as well as the ability to plan forthcoming investments.

Transparent monthly reporting and a stable balance sheet structure also contribute towards the limitation of financial risks. These two factors are supported by an early detection system in the form of continuous 15-month sales and financial planning for all divisions as well as an extensive system of key figures. These measures facilitate successful and well-timed discussion of financial requirements with our lenders who generally proceed to provide the required funds. Our banking partners are also involved in our partnership concept for suppliers and service providers. These are subject to certain selection criteria and evaluations as well as permanent monitoring of their performance and suitability for partnership. This reduces the risk of loans being called in at short notice by credit institutions who are frequently subject to strategic changes.

4.5 Strategic risks and opportunities

Basler's corporate strategy focuses on the further development of the growth market of Vision Technology which continues to expand. Since replacement technologies are currently not to be seen, the corporate strategy risk is deemed to be low.

In the context of a group-wide checking and planning procedure, the business models of the divisions are reviewed on a regular basis. The result of these reviews forms the basis for a balanced scorecard system (BSC) which defines assessable strategic goals for each unit and measures to achieve them. Corporate and division strategies as well as the BSC system form the starting point for the development of a four-year plan as well as the budget for the forthcoming fiscal year. The budget is prepared in quarterly intervals for the next 15 months. This procedure ensures that strategic risks are identified in due time and enables the company to implement counter-measures at an early stage.

An essential element of risk management is to early identify opportunities that are opening up in the field of Vision Technology, to check their viability and to quickly submit them for decision on the measures to be taken on the basis of financial key figures. In addition, this is done in the "New Business Development" units based within each of the divisions. These identify, examine, select and develop potential future activities. This includes both organic development of new activities and potential acquisitions.

4.6 Overall risk

We have weighted all risks identified to date according to their probability of occurrence and have covered them with compensatory measures. They do not represent obvious challenges to the company's survival. At present, no additional risks jeopardizing the continued existence of the company are discernable.

No other events of particular significance that cannot be allocated to the ordinary course of business and are not described in the management report have occurred.

5. POSTSCRIPT REPORT

No relevant events have occurred after closing date.

6. FORECAST REPORT

Outlook

The German government's Council of Experts for the Assessment of the Overall Economic Development estimates that the global economy will remain stable and

continue to grow in 2007 and 2008. Analyses by the US American Automated Imaging Association and by the German Machinery and Engineering Association VDMA indicate that the global Vision Technology market will grow again in 2007 and 2008 by 9%. Moreover, it is to be expected in important sales markets for Vision Technologies that the investing activities in equipment and machinery will show a corresponding stable growth, although there may be considerable cyclical fluctuations in individual industries.

The strategy pursued by the Vision Components division is based on gaining further market shares by launching new versions of existing products as well as completely new products. Special emphasis will be laid in this context on sales markets which show an exponential dynamic growth. In addition, distribution in promising peripheral markets is to be intensified even further.

Within the Vision Systems division, we intend to expand our market share in the TFT display inspection equipment field. In 2007 and 2008, besides further developing our current core business, we intend to approach new customer groups with our new solution for the inspection of color-filters which was successfully tested in 2006. From today's point of view, the optical storage media market is expected to maintain its current investment caution throughout the first six months of 2007. We expect substantial sales in inspection systems for the manufacturing of the new Blu-ray®-disc format to be generated in the first half of the year. These formats have a storage capacity of up to 47 GByte and will be used to archive new data-intensive content for high-resolution television (HD-TV) in the future. For activities concerning inspection systems for the rubber industry, we expect a moderate increase in sales in 2007 after the losses in sales we suffered in the fiscal year just ended due to the weak market. The planned growth is to be achieved by enhancing our distribution efforts. First significant sales are expected to be generated in 2007 by the new business with inspection systems for the solar industry.

All in all we expect another two-digit growth in sales in 2007 and 2008 due to the planned launches of new products and the enhancement of distribution efforts. However, the launch of new products will also be accompanied by higher depreciation on the respective development costs.

The expected increase in sales is one reason why we think that a high profitability with a pre-tax margin of 8% – 10% can be achieved despite the unchanged high expenses on development and higher depreciation volumes. Besides the increase in earnings before taxes due to a growth in sales, we also intend to cut manufacturing costs from their 2006 level. In this context, we will combine cost-cutting measures in development and administration with an optimisation of supply management and manufacturing processes. Our planned business development will go hand in hand with a stable liquidity situation. A stable, positive free cash flow is expected in each case.

Expenditure on fixed assets will continue to focus on furniture, fixtures and equipment, infrastructure and intangible assets. The investment volume will be slightly higher than in 2006.

Also in 2007 and 2008, the management will pursue its strategy of serving the growth market of Vision Technology with innovative and easy to use products, thereby growing profitably and faster than the market. Basler is well-prepared also for the future to successfully implement this strategy.

7. REPORT ACCORDING TO SECTION 312 AKTG

In accordance with Section 312 of the German Stock Corporation Act (Aktiengesetz – AktG), we have prepared a report concerning our relationships with affiliated companies. The following declaration by the Management Board concludes this report:

“We hereby declare that, with respect to the legal transactions listed in the report regarding the company's relationships with affiliated companies and persons, Basler AG, Ahrensburg received adequate consideration given the circumstances we were aware of at the time when these legal transactions were entered into. The company neither implemented nor failed to implement other measures as defined by Section 312 AktG.”

Ahrensburg, January 19, 2007

Basler AG
 Management Board

Consolidated profit and loss statement (according to IFRS)

in € thousand	Note	01.01.–31.12.2006	01.01.–31.12.2005
Sales	5	52,122	44,973
Cost of sales		– 24,864	– 22,808
Gross profit		27,258	22,165
Sales and marketing expenses		– 9,429	– 7,380
General and administrative expenses		– 8,293	– 7,721
Research and development			
Costs		– 7,401	– 7,860
Capitalization of intangible assets		6,700	7,184
Deduction for depreciation on capitalized intangible assets		– 4,979	– 3,823
Research and Development expenses balanced		– 5,680	– 4,499
Other income	6	1,651	1,567
Operating result		5,507	4,132
Interest results	7	– 626	– 503
Result before income taxes		4,881	3,629
Income taxes	8	– 1,921	– 1,249
Group net income for period		2,960	2,380
Number of shares		3,500,000	3,500,000
Income/loss per share €		0.85	0.68
Number of shares (diluted)		3,714,285	3,714,285
Effect on earnings to be taken into account for dilution from convertible bond (thousand €)		75	75
Fully diluted income/loss per share €		0.82	0.66

Consolidated cash flow statement (according to IFRS)

in € thousand	01.01.–31.12.2006	01.01.–31.12.2005
Group net profit	2,960	2,380
Depreciation of fixed assets	6,245	4,798
Payments for interests	494	440
Increase/decrease in provisions	– 41	– 1,099
Change in deferred taxes	1,814	1,105
Invalid payments changes in shareholders' equity	16	9
Result from disposal of equipment	24	26
Inventories	– 632	2,729
Trade receivables	– 1,469	– 1,217
Other assets not attributable to investing or financing activities	– 217	65
Advanced payments received	– 393	– 1,000
Accounts payable	166	– 121
Increase/decrease of interest liabilities from shareholder loans	0	0
Other liabilities not attributable to investing or financing activities	– 320	– 254
Cash flow from operating activities	8,647	7,861
Revenue from disposal of equipment	21	168
Purchase of equipment	– 8,132	– 9,154
Cash flow from investing activities	– 8,111	– 8,986
Free cash flow	536	– 1,125
Cash received by bank loan	– 100	1,600
Payments of interest	– 494	– 440
Cash flow from financing activities	– 594	1,160
Changes in cash and cash equivalents affecting liquidity	– 58	35
Cash and cash equivalents at beginning of period	3,326	3,291
Cash and cash equivalents at end of period	3,268	3,326
Cash and cash equivalents at end of fiscal year		
Cash and cash equivalents	3,268	3,326
Payments for taxes	0	38

Consolidated balance sheet (according to IFRS)

Assets in € thousand	Notes	31.12.2006	31.12.2005
Long-term assets			
Fixed assets	10		
Tangible assets		2,585	2,643
Other intangible assets		1,318	1,117
Capitalization of development		12,487	10,785
Total fixed assets		16,390	14,545
Deferred tax assets	11	8,703	8,613
Total long-term assets		25,093	23,158
Current assets			
Cash and cash equivalents	12	3,268	3,326
Short-term receivables	13		
Trade accounts receivable		5,326	4,908
Accounts out of Percentage of Completion		4,155	3,104
Total short-term receivables		9,481	8,012
Inventories	14		
Finished goods and commodities		1,364	1,282
Work in process and semi-finished goods		1,030	736
Raw materials and supplies		4,140	3,859
Merchandise		229	253
Total inventories		6,763	6,130
Other receivables and financial assets	15	830	615
Total		20,342	18,083
Total assets		45,435	41,241

Liabilities in € thousand	Notes	31.12.2006	31.12.2005
Shareholders' equity	17		
Subscribed capital		3,500	3,500
Capital reserve		1,268	1,268
Equitation of currency exchange		114	97
Accumulated earnings		20,066	17,106
Total shareholders' equity		24,948	21,971
Liabilities			
Long-term liabilities			
Silent partnership		1,023	1,023
Convertible bond		0	2,727
Long-term liabilities to banks	19	511	526
Long-term liabilities to shareholders		0	30
Deferred tax liabilities	16	7,655	5,751
Total long-term liabilities		9,189	10,057
Short-term liabilities			
Convertible bond		2,727	0
Short-term liabilities to banks	19	4,000	4,100
Notes payable to shareholders' equity		170	136
Advance payments received		135	528
Trade liabilities		1,758	1,592
Other liabilities	20	577	884
Tax provisions	18	151	436
Other provisions	18	1,780	1,537
Total short-term liabilities		11,298	9,213
Total		20,487	19,270
Total liabilities		45,435	41,241

Consolidated fixed assets (according to IFRS)

in € thousand	Acquisition costs					As at 31.12.2006
	As at 01.01.2006	Additions	Disposals	Transfers	Foreign exchange- differentials	
Tangible assets						
Land and buildings on third-party land	385	22	– 4	0	0	403
Technical plant and equipment	3,725	416	– 886	460	– 11	3,704
Other furniture, fixtures and equipment	2,513	105	– 58	2	17	2,579
Assets under construction	468	272	0	– 462	0	278
Total tangible assets	7,091	815	– 948	0	6	6,964
Intangible assets						
Software, trademark rights, patents and licences	1,923	411	– 80	32	– 3	2,283
Finished own developments	9,483	2,866	– 2,941	5,040	– 1	14,447
Own developments in progress	5,887	3,834	0	– 5,040	0	4,681
Payments for third-party developments	557	206	0	– 29	1	735
Total intangible assets	17,850	7,317	– 3,021	3	– 3	22,146
	24,941	8,132	– 3,969	3	3	29,110

Consolidated statement of changes in shareholders' equity (according to IFRS)

in € thousand	Subscribed capital	Capital reserve	Exchange equalisation
Equity as at 1 Jan. 2005	3,500	1,268	90
Difference from currency conversion			7
Net profit for the year			
Equity as at 31 Dec. 2005	3,500	1,268	97
Difference from currency conversion			17
Net profit for the year			
Equity as at 31 Dec. 2006	3,500	1,268	114

Depreciation					Net carrying values		
As at 01.01.2006	Additions	Disposals	Transfers	Foreign exchange- differentials	As at 31.12.2006	As a 31.12.2006	Previous year
131	37	– 2	0	– 1	165	238	254
2,752	558	– 876	– 1	5	2,438	1,266	973
1,565	257	– 47	2	– 1	1,776	803	948
0	0	0	0	0	0	278	468
4,448	852	– 925	1	3	4,379	2,585	2,643
1,363	414	– 80	3	0	1,700	583	560
4,585	4,979	– 2,921	0	– 2	6,641	7,806	4,898
0	0	0	0	0	0	4,681	5,887
0	0	0	0	0	0	735	557
5,948	5,393	– 3,001	3	– 2	8,341	13,805	11,902
10,396	6,245	– 3,926	4	1	12,720	16,390	14,545

Income generated	Total
14,726	19,584
	7
2,380	2,380
17,106	21,971
2,960	17
	2,960
20,066	24,948

Notes to the consolidated Financial statement as at 31.12.2006

I. GENERAL INFORMATION

I. The company

Ahrensburg, Germany-based Basler AG and its subsidiaries develop, manufacture and sell artificial Vision Technology. The company's quality assurance systems and components play a key role in the optimization of industrial manufacturing processes.

The Group operates in four different markets: optical storage media, rubber and elastomer, flat-screen display and vision components. It has subsidiaries in the USA (Basler Inc.), Taiwan (Basler Vision Technologies Inc.) and Singapore (Basler Asia Pte. Ltd.). Besides its domestic turnover, Basler predominantly generates sales in the USA and in Asia. The company's main customers are industrial undertakings.

Since 23 March 1999, Basler AG has been listed at the Frankfurt stock exchange. Basler AG is obliged to the Prime Standard regulations.

2. Compliance with IFRS

The consolidated financial statements of Basler AG have been prepared according to the IFRS rules taking into account all standards and interpretations as used in the EU.

Unless otherwise specified, all amounts are stated in thousand euros (k€).

3. Scope and method of consolidation

3.1 Scope of consolidation

All major subsidiaries directly or indirectly controlled by Basler AG pursuant to IAS 27 have been included in the consolidated financial statements.

Companies under common control within the meaning of IAS 31 (joint ventures) are accounted for using proportional consolidation.

Significant associates are accounted for using the equity method according to IAS 28 if significant influence can be exercised on them.

An overview of subsidiaries and shareholdings is provided under no. 28 below.

3.2 Harmonisation

The financial statements to be consolidated of Basler AG as parent company and the subsidiaries included in the consolidation have been prepared using uniform accounting and valuation methods.

3.3 Use of estimates

The preparation of consolidated financial statements in accordance with IFRS requires the management to make estimates and assumptions regarding the recognition and amount of assets and liabilities, the disclosure of contingent assets and liabilities as at the reporting date and regarding the amount of turnover and expenses reported during the period under review. The actual results may deviate from these assessed values.

3.4 Currency conversion

The functional currency of the subsidiaries is the currency of the respective country, except for Basler Asia Pte. Ltd. whose balance sheet is prepared in euros. Consequently, on the balance sheet date, assets and liabilities were converted into euros using the applicable exchange rate on the reporting date. Turnover and expenses were converted using the average exchange rate of the reporting period. Accumulated exchange rate gains and losses are reported as a separate component of the equity capital.

Business transactions denominated in foreign currencies in the individual financial statements of the consolidated companies were converted at the exchange rate applicable on the reporting date of the transaction. In fiscal year 2006, gains amounting to k€ 303 (previous year: k€ 439) and losses of k€ 496 (previous year: k€ 202) arose respectively. The gains are reported under Other Operating Income and the losses under General Administrative Expenses in the respective annual financial statements.

Transactions within the European Union are recorded using the applicable fixed euro exchange rates. Further relevant exchange rates are listed below:

	Exchange rate as per 31.12.2006	Exchange rate as per 31.12.2005
1 €	US-Dollar 1.317	US-Dollar 1.1797
1 €	New-Taiwan-Dollar 43.0276	New-Taiwan-Dollar 39.02881

	Average exchange rates 2006	Average exchange rates 2005
1 €	US-Dollar 1.2556	US-Dollar 1.24410
1 €	New-Taiwan-Dollar 40.9007	New-Taiwan-Dollar 40.0674

Source: Exchange rates of the European Central Bank with the exception of the new Taiwan dollar which is based on the Interbank spot rate.

3.5 Capital consolidation

Capital consolidation is performed according to the purchase method which provides for the acquisition costs of the shareholding to be applied against the proportionate equity capital at the time of acquisition. Assets and debts of the subsidiaries are stated at their fair value, provided the fair values to be applied are higher than the respective book values.

3.6 Intra-group balances

All intra-group profits and losses, sales revenues, expenses and income as well as accounts payable and receivable and/or provisions are eliminated. Tax deferrals according to IAS 12 are applied on consolidation adjustments impacting the revenue results.

4. Accounting and valuation methods

Income and expenses are recorded in the period in which they arose. Customer production contracts (construction contracts) are reported according to the percentage-of-completion method (PoC method). The applicable percentage of completion is determined on the basis of the cost-to-cost method. Contracts are either recorded on the asset side under "Receivables from PoC" or under the liability side under "Liabilities from PoC". Where the accumulated performance exceeds the advance payments, contracts are recorded on the asset side; in the opposite case, they are recorded on the liability side.

Accounts receivable and other financial assets are recorded on the asset side at acquisition costs as at the settlement date. Should the recoverability of an account receivable be at risk, specific valuation adjustments are made to it.

Where the fair value of **financial assets** and debts is applied or stated, it is generally determined on the basis of the market or stock-exchange value. Should no active market exist, the fair value is determined on the basis of acknowledged methods of financial mathematics.

Raw materials and supplies, merchandise as well as unfinished and finished products are stated under **inventories**, unless they are attributable to a customer order. They are stated at acquisition cost on the basis of average prices or at production cost. In addition to the prime costs, the production costs include appropriate portions of the necessary material and indirect production costs as well as depreciation due to manufacturing which is directly attributable to the production process. Lower net selling prices will be written down. Interest on borrowed capital is not stated on the asset side.

All inventories at the Ahrensburg site and the accounts receivable have been assigned by way of collateral to the banking consortium.

Tangible assets are generally valued at acquisition or production cost reduced by scheduled straight-line depreciation. The useful life applied for this purpose corresponds to the expected period of use of the assets within the company. Residual values have been neglected in the calculation of depreciations due to insignificance. Revaluations of the tangible fixed assets have not been performed.

Scheduled depreciation of tangible fixed assets is mainly based on the following useful lives:

Asset	Useful life in years
Fixtures installed by the lessee	3 to 14 years (end of the lease agreement)
Technical equipment and machinery	3 to 5, 7 and 10
EDP equipment and systems	3 to 5

Intangible assets acquired against remuneration, mainly software, are stated on the asset side and depreciated over their scheduled useful life of three years.

Development costs for future products from which Basler will probably receive a benefit in the future are stated on the asset side at production cost and depreciated as scheduled over their useful life of three years using the straight-line method. The development of platforms on the basis of which numerous individual products are developed is amortised over five years on a regular basis using the straight-line method. In accordance with IAS 36, the value maintained by the company-produced intangible assets is monitored.

Liabilities from financing lease agreements are stated at the net present value of the lease payments at the time of conclusion of the contract while other liabilities are reported at the repayment value and/or at amortised costs.

Net financial debt has been reported at its amortised cost. This includes the silent partnership, due to banks and the convertible bond's proportion of borrowed capital.

A **lease** is classified as operating lease if essentially all risks and opportunities associated with ownership therein remain with the lessor.

Deferred taxes are formed pursuant to IAS 12 for valuation differences between the tax balance sheets of the individual companies and the consolidated financial statements. Tax-loss carry-forwards which are likely to bring a benefit in the future are stated on the asset side in the amount of the deferred tax claim.

The **cash flow statement** is prepared in compliance with the provisions of IAS 7. The cash flow statement is divided into operating, investing and financing activities. The cash-flow statements are prepared in accordance with the indirect method.

Convertible bonds are divided into their equity and their debt capital component pursuant to IAS 32.31 et seq. and reported accordingly.

The operating cash flow comprises the cash flows from the operating business and the investing activities.

II. ITEMS OF THE ANNUAL FINANCIAL STATEMENTS

PROFIT AND LOSS STATEMENTS

5. Sales revenues

The sales revenues amounting to k€ 52,122 (previous year: k€ 44,973) include revenues from customer orders determined according to the PoC method in the amount of k€ 3,387 (previous year: k€ 3,894).

6. Other operating income

Other operating income comprises:

	2006 k€	2005 k€
Rental income	917	847
Currency exchange gains	303	439
Income from the release of provisions	155	208
Other	276	73
	1,651	1,567

7. Financial result

	2006 k€	2005 k€
Interest income	19	15
Interest paid	– 645	– 518
	– 626	– 503

8. Earnings taxes

Both taxes paid or owed on income/revenues and deferred taxes are stated as earnings taxes.

Any income obtained is stated as negative amount.

	2006 k€	2005 k€
Current taxes from consolidated companies	77	170
Deferred taxes from consolidated companies (income)	1,844	1,079
Tax expense/income	1,921	1,249
Deferred taxes from losses carried forward	414	– 857
Deferred taxes from temporary differences	1,430	1,936
Deferred tax expense/income	1,844	1,079

9. Additional information

9.1 Production contracts

The accumulated costs of production contracts in progress on the reporting date amount to k€ 3,622 (previous year: k€ 2,189), the accumulated profits reported amount to k€ 4,316 (previous year: k€ 2,362).

9.2 Unscheduled depreciation/amortisation of fixed assets

	2006 k€	2005 k€
Tangible assets	0	0
Intangible assets	0	295
	0	295

The valuation adjustment for pre-year intangible assets refers to capitalised developments no longer used.

9.3 Personnel costs

	2006 k€	2005 k€
Wages and salaries	16,552	15,986
Social security contributions	3,097	2,981
	19,649	18,967

9.4 Cost of materials

	2006 k€	2005 k€
Expenses on raw materials and supplies, purchased goods	17,969	14,369
Expenses on purchased services	361	463
	18,330	14,832

BALANCE SHEET

10. Development of fixed assets

As at 31 December 2006, Basler used fully depreciated fixed assets representing an acquisition value of k€ 2,829 (previous year: k€ 3,062).

For more details on the development of fixed assets, reference is made to the separate explanation.

11. Deferred tax

	31.12.2006 k€	31.12.2005 k€
Deferred tax assets		
from tax-loss carry forwards	7,026	7,440
Inventories	1,352	817
Other	325	356
	8,703	8,613
Deferred tax liabilities		
Capitalization of development	4,662	4,027
Receivables	2,964	1,700
Other	29	24
	7,655	5,751

The following is a breakdown of the effective tax burden which is calculated using the German corporate income tax rate of 26.38% plus trade tax taking into account the respective deduction of tax relief, thereby resulting in a combined statutory tax rate of 37.34%:

Tax reconciliation	2006	2005
Net profit for the year before income taxes	4,881	3,629
Applicable tax rate (%)	37.34	37.34
Tax expense expected	1,823	1,355
Tax rate deviations		
Effects from foreign subsidiaries	11	3
Tax irrelevant expense/income	89	- 109
Actual tax expense/income	1,921	1,249
Effective tax rate (%)	39.36	34.42

As per 31 December, the following tax loss carry forward existed (in k€):

	2006	2005
Germany, corporation tax	18,824	19,940
Germany, trade tax	18,612	19,893
USA, federal level	157	187
Singapore	0	0
Taiwan	80	0

The tax loss carry forward in Germany applies for an indeterminate period of time. Due to the statutory situation, out of the total loss carry forward, a maximum of k€ 1,000 plus 40% of the excess tax profit can be utilised per year.

The tax loss carry forwards from the USA are limited until 2026.

The tax loss carry forwards in Taiwan are limited until 2011.

12. Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and in banks in an amount of k€ 3,268 (previous year: k€ 3,326).

13. Receivables

Receivables include k€ 7,938 (previous year: k€ 4,551) of receivables arising from PoC. Advance payments received total k€ 3,996 (previous year: k€ 1,975) from which k€ 3,783 (previous year: k€ 1,447) have been deducted under receivables arising from PoC.

The value of receivables was adjusted by k€ 13 (previous year: k€ 56). In fiscal year 2006, valuation adjustments credited to income amounted to k€ 18 (previous year: k€ 91).

14. Inventories

As per 31 December 2006, inventories included valuation adjustments of k€ 1,934 (previous year: k€ 1,698), including k€ 236 for fiscal year 2006 (previous year: k€ 452).

Finished products and merchandise are devices made available to customers temporarily for testing and demonstration purposes or on a loan basis worth k€ 637 (previous year: k€ 558). This manner of reporting facilitates the handling of the future sale to the customer. Devices used for demonstration purposes over an extended period of time, e. g. for trade fairs and exhibitions, are stated under fixed assets and are written off over their useful life which amounts to three years.

15. Current financial assets, tax refund claims and accruals and deferrals

Other assets are composed as follows:

	31.12.2006 k€	31.12.2005 k€
Tax receivables	326	316
Deferred charges	119	119
Advance payments made	53	0
Derivative financial instruments	22	0
Other	310	180
	830	615

Net carrying values are similar to the actual cash value.

16. Operating leasing

The company building and parts of the furniture, fixtures and equipment are used under operating leases. The future rental and leasing payments based on non-cancellable operating leases and rentals amount to a minimum of:

Fiscal year	k€
2007	2,517
2008–2011	9,350
From 2012	15,338

During the year under review, the rent/leasing expenses amounted to k€ 2,719 (previous year: k€ 2,590).

Basler will receive at least the following rental payments per year from subleasing the office building in Ahrensburg under contracts that have been concluded and are non-cancellable:

Fiscal year	k€
2007	485
2008–2011	450
From 2012	9

17. Equity

17.1 Subscribed capital

The registered share capital of the company amounts to € 3,500,000 and is divided into 3,500,000 no-par-value shares. The shares are in bearer form.

The shares of Basler AG have been listed at the Frankfurt stock exchange since 23 March 1999.

17.2 Capital reserve

The capital reserve contains mainly the share premium from the capital increase carried out in the context of the IPO in 1999.

17.3 Authorised capital

According to § 4 (3) of the Basler AG Articles of Association, the Management Board is authorised, subject to approval by the Supervisory Board, to increase the registered share capital of the company by 16 June 2008 by issuing up to 1,750,000 new no-par value bearer shares against cash and/or non-cash contributions either once or several times by a total of € 1,750,000.00. The shareholders shall be granted a subscription right for this purpose. However, the Management Board is authorised, subject to approval by the Supervisory Board, to exclude subscription rights of the shareholders for fractional amounts.

17.4 Contingent capital

The Contingent Capital I amounting to € 350,000 was allocated to the "1999 plan" and "2000 plan" share option schemes which have lapsed because the conditions were finally not met.

The authorized but unissued capital II amounting to € 215,000 serves to guarantee the refunding rights associated with the convertible bond. The general shareholders' meeting had decided in favour of the issuance of this bond on 1 July 2005.

18. Development of short-term provisions

	01.01.2006	Differences from currency conversion	Allocations	Accumulation	Utilisation	Releases	31.12.2006
Personnel costs	776	22	1172		754	22	1,194
Commissions	266	-2	158		184	70	168
Taxes	436	1	150		434	2	151
Warranty	139		163		139		163
Legal and consultancy costs	95		95		90	5	95
Other	261		122		167	56	160
	1,973	21	1860	0	1,768	155	1,931

The provisions for personnel costs were made mainly for profit-participation bonuses for the reporting year, for holiday leave carried forward and for flexi-time balances.

The tax provisions were made for the tax burden on the profit/loss for the reporting year and any previous years.

19. Financial liabilities

Basler reports the following financial liabilities (k€):

Description	Interest condition	Interest rate	End of term	Repayment sum
Silent partnership	Fixed	12%	31.12.2011	1,023
Convertible bond	Fixed	4%	31.07.2007	3,000
Loans	Fixed	12%	30.03.2012	511
Fixed-rate loan advances	Fixed	5.15%–5.73%	10.01.2007–27.03.2007	4,000

The fair values of the above financial liabilities, the accounts payable and the other liabilities are very close to the reported book value.

The convertible bond's equity proportion amounting to k€ 273 was determined on the basis of an effective interest rate of 7.5% p.a.

20. Derivative financial instruments

As a company acting on global markets, Basler is exposed to a number of market risks. In order to reduce currency risks, Basler uses forward exchange dealings. As these dealings are intended as security for underlying operating transactions, their term is less than one year in each case.

The following items existed as at the respective balance-sheet dates (in k€):

	31.12.2006	31.12.2005
Nominal volume	3,100	2,000
Fair value		
Positive	22	–
Negative	–	30

Valuation is carried out according to the Mark-to-Market method. Positive fair values are stated under short-term other assets and negative fair values under short-term other financial liabilities.

The maximum risk of default corresponds to the book values entered in the balance sheet (reduced by the valuation adjustments taken into account as at the balance sheet date, if any) of each financial asset, including derivative financial instruments. As the contractual partners for derivatives are renowned financial institutions, it can be assumed that the liabilities under derivative transactions will be met.

CASH FLOW STATEMENT

21. Credit lines

Credit lines in an amount of k€ 9,900 were available to Basler as at the balance-sheet date. k€ 4,000 of these had been utilised in the form of fixed-rate loan advances.

III. ADDITIONAL INFORMATION

22. Type and management of financial risks

22.1 Derivative financial instruments

As at the balance sheet date, US dollar forward transactions in an amount of k€ 3,100 with a residual term of less than one year were in place for exchange hedging. The positive fair value according to the market valuation stated under other assets amounted to k€ 22.

22.2 Risk of counter-party default

Basler continuously monitors its customers' credit standing using internal and external assessments. In addition, the risk associated with trade receivables is reduced to some degree by the fact that the company's regular customers are highly diversified. Furthermore, the company operates a clearly defined process to follow up on outstanding receivables. A credit-line structure supported by the ERP system with documented escalation levels is used to limit the risk even further.

23. Segment report

23.1 Primary segmentation

Basler has two divisions that operate in the vision technology market:

- Vision Systems develops and markets turn key quality inspection systems for mass production in various industries.
- The second business division, Vision Components, develops and sells digital camera solutions for original equipment manufacturing customers (manufacturers of capital goods) in the market segments of machine vision, medical engineering and intelligent traffic systems.

The company's products are mainly developed on its premises in Ahrensburg and are sold through a direct distribution structure, through the subsidiaries (USA, Singapore and Taiwan) and through independent distributors in Europe, North America, Australia, Japan and Asia.

The information contained in the overviews has been taken directly from the internal reports that are used for management purposes by the company's highest operative decision-makers. The company does not evaluate individual segments on the basis of financial liabilities and respective interest expenses for internal control purposes; consequently, the segment reports do not include such evaluations.

Segment assets are direct operating receivables, inventories and the fixed assets used for the company's business operations.

Segment liabilities are the advance payments received attributable to business operations, trade liabilities as well as provisions.

The business developed as follows during the reporting year (all amounts stated in k€):

	Vision Systems		Vision Components		Reconciliation		Whole Group	
	2006	2005	2006	2005	2006	2005	2006	2005
Segment revenues	28,831	29,133	23,291	15,840	0	0	52,122	44,973
Segment results (EBIT)	1,454	2,219	4,303	2,255	-250	-344	5,507	4,130
Segment assets	15,901	17,398	11,868	8,873	4,864	2,416	32,633	28,687
Segment liabilities	188	503	70	72	-123	3,082	135	3,657
Segment investments	3,982	5,212	3,409	2,982	741	961	8,132	9,155
Segment depreciations	3,505	2,765	1,840	1,255	900	778	6,245	4,798

23.2 Secondary segmentation

Basler's secondary segmentation is based on the place of production.

	Europe		Reconciliation		Group	
	2006	2005	2006	2005	2006	2005
Segment revenues	52,122	44,973	0	0	52,122	44,973
Segment assets	27,769	26,271	4,864	2,416	32,633	28,687
Segment investments	7,391	8,194	742	961	8,133	9,155

24. Number of employees

The average number of employees in each functional area is shown in the table below:

	2006	2005
Manufacturing	69	72
Distribution	112	114
Development	96	97
Administration	47	46
	324	329

Basler is committed to providing family-friendly policies and procedures for its staff. One indication of this is the high percentage of employees who work under a wide variety of part-time schemes. In fulltime equivalents, the distribution is as follows:

	2006	2005
Manufacturing	65	68
Distribution	106	109
Development	92	95
Administration	40	39
	303	311

25. Remuneration of auditors

In 2006, the company paid its auditors, BDO Deutsche Warentreuhand Aktiengesellschaft, a fee of € 51,859.30 (previous year: € 77,228.53) exclusively for audit procedures.

26. Related persons

The following affiliated persons hold shares in the convertible bond issued in 2004:

	Amount in €
Nicola-Irina Basler	1,496,698.00
Monika Proske-Ley	333,200.00
Peter Krumhoff	63,798.00

The applicable conditions are the same as those applying to third parties.

27. Shares

	Number of shares 31.12.2006
Management Board	
Dr.-Ing. Dietmar Ley	135,282
Dipl.-Ing. (MBA) John P. Jennings	2,000
Dipl. Betriebswirt Peter Krumhoff	500
Supervisory Board	
Norbert Basler	1,800,000
Konrad Ellegast	3,000

28. Board of Management and Supervisory Board

28.1 Management Board

In 2006, the Management Board consisted of the following members:

Dr. Dietmar Ley, Ahrensburg	CEO, Product Development and Personnel
John P. Jennings, Ambler, USA	Product distribution and foreign subsidiaries
Peter Krumhoff, Großhansdorf	Finance and Production

28.2 Supervisory Board

The Supervisory Board consisted of the following members in 2006:

Norbert Basler	Chairman of the Supervisory Board Master's degree in engineering
Bernd Priske	Deputy Chairman of the Supervisory Board (until 8 May 2006) Master's degree in business studies, member of the Management Board of M.A.X. Automation AG, Dusseldorf
Konrad Ellegast	Deputy Chairman of the Supervisory Board (since 8 May 2006) Ordinary Supervisory Board member (until 8 May 2006) Consultant
Prof. Dr. Eckart Kottkamp	Ordinary Supervisory Board member (since 8 May 2006)

Further assignments of the Supervisory Board members in 2006

Norbert Basler

Member of the Supervisory Board of Kuhnke AG, Malente
Supervisory Board member of Plato AG, Lübeck

Konrad Ellegast

Member of the Supervisory Board of Technotrans AG, Sassenberg
Member of the Advisory Board of C. Mackprang Jr. GmbH & Co. KG, Hamburg
Member of the Advisory Board of RIBE Richard Bergner Verbindungstechnik GmbH, Schwabach

Prof. Dr. Eckart Kottkamp

Chairman of the Supervisory Board of Hako-Werke GmbH, Bad Oldesloe
Chairman of the Advisory Board of Hako Holding GmbH & Co. KG, Bad Oldesloe
Chairman of the Advisory Board of Mackprang Holding GmbH & Co. KG, Hamburg
Chairman of the Supervisory Board of Lloyd Fonds AG, Hamburg
Supervisory Board member of Deutsche Steinzeug Cremer & Breuer AG, Alfter-Witterschlick

28.3 Remuneration of the Management Board and Supervisory Board members

In 2006, the members of the Management Board received the following remuneration (in EUR):

	Base/fixed salary	Performance-related bonuses for 2006	Total
Dr. Dietmar Ley	158,276.48	33,773.53	192,050.01
John P. Jennings	150,149.76	31,836.47	181,986.23
Peter Krumhoff	141,392.48	29,610.28	171,002.76

As in the previous year, the total remuneration of the Management Board members amounted to k€ 39 in 2006.

29. Breakdown of participating interests

In addition to Basler AG, the following companies have been included in the consolidated financial statements through full consolidation:

	Interest held %	Equity k€	Net profit for the year k€
Basler Inc., Exton/USA	100	7	-293
Basler Asia Pte, Ltd., Singapore	100	602	364
Basler Vision Technologies Taiwan Inc., Taipeh/Taiwan	100	-512	-213

Further participating interests are not held.

30. Corporate Governance

The company has made its Declaration of Compliance with the German Corporate Governance Code which is mandatory under Section 161 of the German Stock Corporation Act (Aktiengesetz – AktG). The declaration is available to shareholders on the company's website at www.baslerweb.com.

Audit Opinion

We have audited the consolidated financial statements of Basler Aktiengesellschaft, Ahrensburg, – consisting of balance sheet, income statement, notes, cash flow statements and statement of changes in equity – and the Group management report for the business year from 1 January to 31 December 2006. The preparation of the consolidated financial statements and the Group management report in accordance with the International Financial Reporting Standards (IFRS), as adopted by the EU, and the additional provisions stated in Section 315a Para. 1 HGB are the responsibility of the Company's legal representatives. Our responsibility is to express an opinion on the consolidated financial statements and the Group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with Section 317 HGB and the German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer in Deutschland (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with German principles of proper accounting and in the Group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and evaluations of possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the Group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of the companies included in consolidation, the determination of the companies to be included in consolidation, the accounting and consolidation principles used and significant estimates made by the legal representatives, as well as evaluating the overall presentation of the consolidated financial statements and the Group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion based on the results of our audit the consolidated financial statements are in compliance with the IFRS, as adopted by the EU, and the additional provisions stated in Section 315a Para. 1 HGB and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with German principles of proper accounting. The Group management report is in accordance with the annual financial statements and provides on the whole a suitable understanding of the Group's position and suitably presents the chances and risks of future development.

Lübeck, 2 February 2007

BDO Deutsche Warentreuhand
Aktiengesellschaft Wirtschaftsprüfungsgesellschaft

Dr. Probst	ppa. Beecker
Auditor	Auditor

Corporate Governance

The Board of Management and the Supervisory Board of Basler AG declare that the recommendations issued by the "Government Commission of the German Corporate Governance Code" published by the Federal Ministry of Justice in the official section of the electronic Federal Gazette (eBundesanzeiger) have been and are being complied with. This Code presents essential statutory regulations for the management and supervision of German listed companies and contains internationally and nationally recognised standards for good and responsible governance. Its purpose is to promote the trust of international and national investors, customers, employees and the general public in the management and supervision of listed German stock corporations.

By this declaration of undertaking, the Board of Management and the Supervisory Board want to demonstrate to the public that they intend to implement responsible corporate management and control so as to increase shareholder value. This measure is to build and enhance trust among current and future shareholders, customers, other interested members of the public and employees.

Declaration of conformity pursuant to Sec. 161 of the German Stock Corporation Act

The Board of Management and the Supervisory Board hereby declare that the recommendations of the Government Commission of the Corporate Governance Code as amended on 12 June 2006 have been complied with during fiscal year 2006 and that said recommendations will be complied with in the future. The following recommendations are excepted:

Clause 5.3 – Formation of committees by the Supervisory Board

The Supervisory Board does not form any committees. The Supervisory Board of Basler AG comprises three members. This size enables efficient work to be done in all matters of the Supervisory Board whilst the generally accepted minimum size for a committee is a membership of three.

Clause 5.4.7. – Compensation of members of the Supervisory Board

Remuneration of members of the Supervisory Board is set forth in the Articles of Incorporation. Special consideration is given to the remuneration of the chair and deputy chair of the Supervisory Board. However, in the light of the current level of fixed remuneration, the company does not intend to add a variable component to the remuneration of members of the Supervisory Board.



For the Board of Management
Dr. Dietmar Ley (CEO)



For the Supervisory Board
Norbert Basler (Chairman)



Norbert Basler,
Chairman of the Supervisory Board

Report of the Supervisory Board

Dear Shareholders,

During fiscal year 2006 which has just ended, the Supervisory Board fulfilled the tasks incumbent on it by law and the company's articles of association which consisted of monitoring and advising the Management Board in its management activities. The Management Board provided the Supervisory Board with written and oral reports on the economic position of Basler AG, its foreign subsidiaries and its divisions on a monthly basis and discussed the business and economic situation in detail with the Chairman of the Supervisory Board. In fiscal year 2006, four scheduled meetings took place which were attended by all Supervisory Board members: On 23 February 2006, 8 May 2006, 20 September 2006 and 14 December 2006.

Due to the limited size of the Supervisory Board (three members), committees as defined by Section 171 Para. 2 Sentence 2 of the German Stock Corporation Act (Aktiengesetz – AktG) were not formed.

The Management Board and the Supervisory Boards cooperate closely for the benefit of the company. This cooperation is based on open discussions and mutual trust. The Management Board consulted with the Supervisory Board on the company's strategic orientation and kept it informed on the progress of implementation. The Supervisory Board participated in all decisions of fundamental importance to the company. The Management Board regularly informed the Supervisory Board of all relevant issues concerning business development and the company's risk situation. The Chairman of the Supervisory Board is in regular contact with the CEO and was informed by him of all current developments and extraordinary events. The Supervisory Board approved all transactions that were subject to its approval according to the law and the articles of association. This involved decisions and measures of fundamental importance to the company's net asset, financial and income position. Inter alia, the following issues were dealt with in the fiscal year just ended:

- Discussion and adoption of the 2005 annual financial statement and of the proposals for the general shareholders' meeting
- Cyclical and market-specific developments and their effects on the company's earnings and turnover situation
- Revision of the Company vision, mission and strategy
- Consultation on the revision of the Company philosophy
- Development of new business and through new strategic partnerships or acquisitions
- Organisational reorientation of the Group
- Planning and budgeting for the segments and within the entire group
- Commitment to the Corporate Governance Codex

BDO Deutsche Warentreuhand Aktiengesellschaft Wirtschaftsprüfungsgesellschaft which was appointed auditor of the annual financial statements by the general shareholders' meeting on 8 May 2006 was instructed by the Chairman of the Supervisory Board to carry out the audit by a letter of 11 December 2006. The auditor attended the Supervisory Board meeting on 1 March 2007 during which the annual financial statements presented were discussed and delivered a report regarding the main results of his audit.

The auditors BDO Deutsche Warentreuhand AG, Lübeck, audited the accounting records, the annual financial statements as at 31 December 2006 and the management report of Basler AG as well as the consolidated financial statements as at 31 December 2006 and the consolidated management report, found them in conformity with the law and the articles of association and issued them with an unqualified audit certificate. The Supervisory Board took note of the audit results and approved them.

Within the scope stipulated by law, the Supervisory Board also reviewed the annual financial statements, the consolidated financial statements, the management report and the consolidated management report. No objections were raised. The Supervisory Board approved and thereby adopted Basler AG's annual financial statements as prepared by the Management Board.

In accordance with the Corporate Governance Code, the Supervisory Board regularly reviewed the efficiency of its work and enhanced it in connection with useful changes to the preparation and design of documents of these meetings.

The Supervisory Board members do not act as consultants to, or hold officer positions in, executive bodies of clients, suppliers, lenders or other business partners. Consequently, conflicts of interest did not arise during the past fiscal year.

The auditor of the annual financial statements audited the management report concerning relationships to affiliated companies which had been prepared in accordance with Section 312 AktG, and issued the following audit certificate:

"Having carried out our audit and evaluation in accordance with the applicable regulations, we hereby confirm that

- the actual information given in the report is correct and
- with respect to the legal transactions recorded during the year under review, the company's performance was not inadequately high"

The Supervisory Board also took note of and approved this audit report as prepared by the auditor. After drawing the final conclusion of its own audit, it declared that no objections had arisen as to the explanations by the Management Board regarding the relationships to affiliated companies.

In the fiscal year just ended, the composition of the Supervisory Board changed. At the meeting on 8 May 2006, Mr. Bernd Priske, CEO of M.A.X. Automation AG in Düsseldorf, resigned from his office. For his remaining term of office, Prof. Dr. Eckart Kottkamp of Grosshansdorf was appointed to the Supervisory Board instead.

In the fiscal year just ended, the Company was able to increase its revenues and earnings significantly and to acquire promising potential for the future, inter alia with new products and with its entry into the solar business. This was made possible by strong performance and a high level of commitment among the employees, the management and Management Board of Basler AG. The Supervisory Board would hereby like to thank the entire staff, the management and the Management Board of Basler AG for their excellent work during the past fiscal year.

Ahrensburg, March 2007
For the Supervisory Board



Norbert Basler – Chairman of the Supervisory Board

Events

FINANCIAL EVENTS

14.03.2007	Release of full year results 2006
09.05.2007	Release of Q I results 2007
21.05.2007	Annual general meeting, Hamburg, Germany
08.08.2007	Release of Q2 results 2007
07.11.2007	Release of Q3 results 2007

TRADESHOWS AND CONFERENCES

Vision Systems

13. – 15.03.2007	FPD – Shanghai, China
16. – 19.03.2007	GUTECH 2007 – Montichiari, Italy
15. – 17.05.2007	MEDIA-TECH Expo – Long Beach, USA
04. – 06.07.2007	FPD Expo – Taipeh, Taiwan
03. – 07.09.2007	EU PVSEC – Milan, Italy
16. – 18.10.2007	Rubber Expo 2007 – Cleveland, USA

Vision Components

22. – 24.03.2007	Vision Show China – Shanghai, China
11. – 13.06.2007	Vision Show China – Peking, China
12. – 14.06.2007	Robotics & Vision Show – Chicago, USA
17. – 20.06.2007	Semicon West – San Francisco, USA
25. – 27.09.2007	Vision Show France – Paris, France
06. – 08.11.2007	Vision Show – Stuttgart, Germany
05. – 07.12.2007	ITE – Yokohama, Japan

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This Annual Report is also available in German. In the event of conflicts the German language version shall prevail.

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