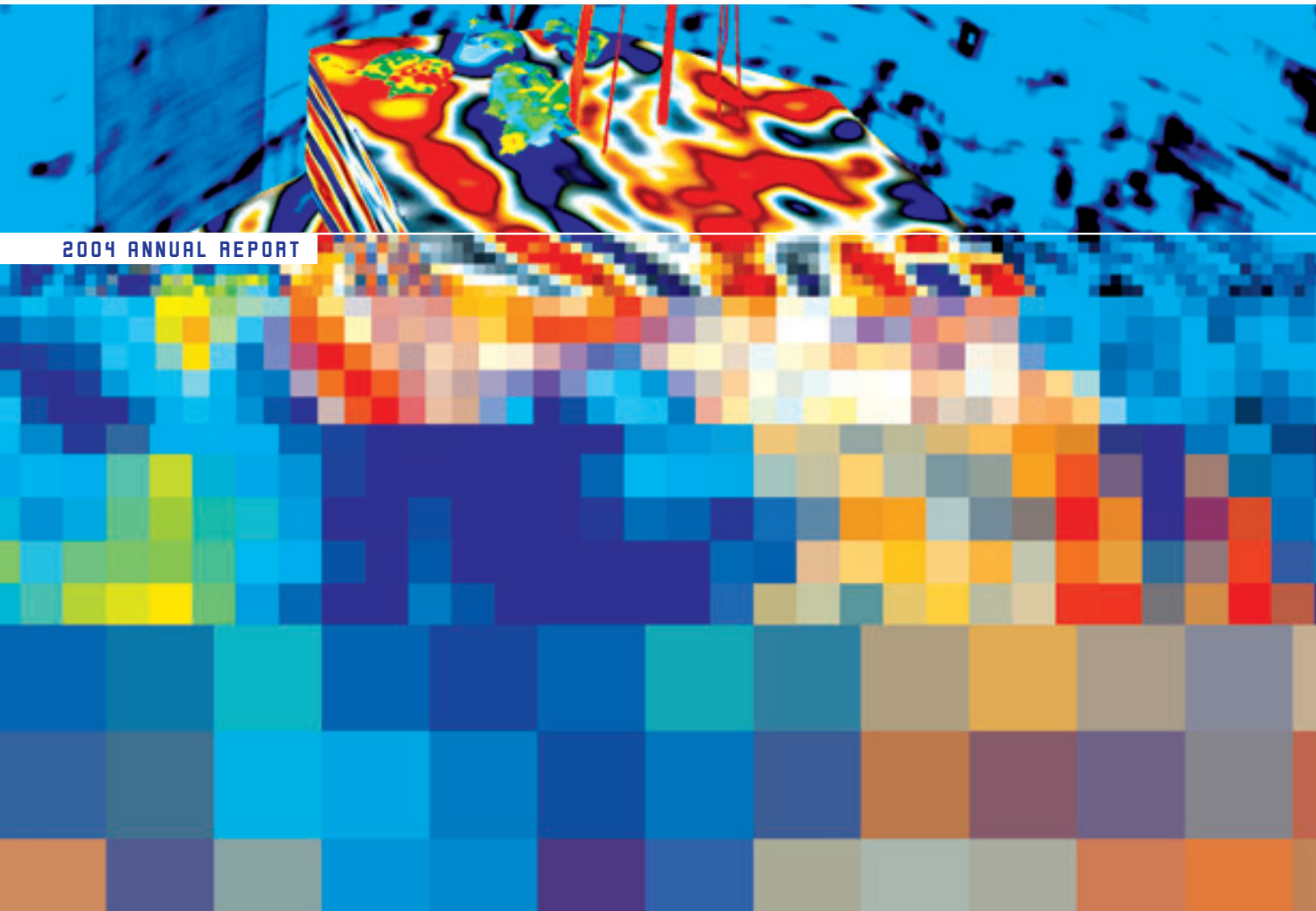




GIVING SEISMIC A WHOLE NEW IMAGE

2004 ANNUAL REPORT



THE REVOLUTION CONTINUES

The year 2004 transformed I/O. Following the acquisitions of Concept Systems and GX Technology, I/O moved beyond its 35-year legacy of being an equipment manufacturer for the global seismic contracting industry. By integrating these well-respected entities into the I/O family, we have collectively created the world's first, technology-focused seismic solutions company. I/O is committed to leading the global oil & gas industry into the next era of seismic imaging – Digital Full-wave – by developing the solutions needed to address the most difficult geophysical challenges worldwide.

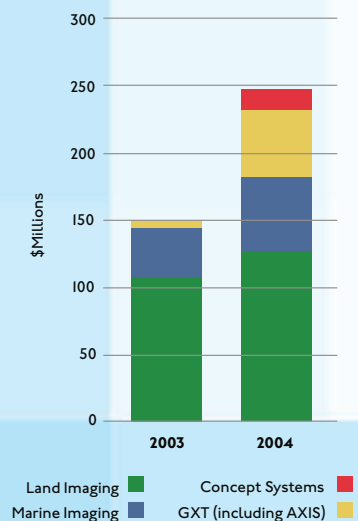
I/O has developed, acquired, and deployed advanced technology solutions that are vital for leading the E&P industry into the Digital Full-wave era. These include software and services for designing customized 3-D and 4-D seismic surveys. Digital sensors for advanced imaging on land and on the seabed. Seismic acquisition platforms and data management software that provide step-change improvements in field operational efficiencies both onshore and offshore. Processing solutions that enhance the quality and resolution of the final seismic image. And services across the seismic workflow that enable oil & gas companies and seismic acquisition contractors to better apply, and gain a competitive advantage from, our broad portfolio of technologies at all stages of the hydrocarbon reservoir lifecycle.

I/O begins 2005 as a new company poised to tackle the challenges and capture the opportunities of a new era in seismic imaging. Our mission at I/O is clear – to give seismic a whole new image. The revolution continues.

MILESTONES

- Raised more than \$200 million in growth capital
- Completed the acquisitions of Concept Systems and GX Technology
- Increased revenues 65% to \$247 million
- Improved gross margins to 29% (from 19% in 2003)
- Launched new platforms for land and seabed acquisition
- Sold \$30+ million in VectorSeis®-based systems (50% increase from 2003)
- Achieved record performance in our Sensor and Concept Systems businesses
- Concluded the sale of our Applied MEMS™ business to Colibrays

REVENUE PER BUSINESS SEGMENT





LETTER TO SHAREHOLDERS

I began last year's letter by stating that a journey of a thousand miles begins with a single step. In 2004, we took several giant leaps forward. As with any journey, we had a couple of unanticipated setbacks along the way. On balance, we made solid progress in executing against the vision our management team formulated in the summer of 2003. With hydrocarbon demand increasing and supply pressures mounting, we remain confident in the need for a new era of seismic imaging technology to enable oil & gas companies worldwide to meet their exploration and production objectives. And we, along with several thought leaders in the E&P industry, believe digital full-wave imaging will provide the breakthroughs necessary to find, develop, and produce hydrocarbons more effectively and efficiently.

The acquisitions of Concept Systems and GX Technology (GXT) were our most significant developments of 2004. These two companies are well recognized in the E&P industry for their advanced technologies and service offerings. By bringing them both into the I/O family, we believe we now possess the foundation of hardware, software, and survey design and processing services needed to deliver against our full-wave strategy. We're already benefiting from these acquisitions today. Our technical teams are hard at work on a series of projects to integrate our existing offerings and to develop the next generation of seismic imaging solutions that should benefit both oil & gas companies and seismic contractors alike in the years ahead.

As important as these acquisitions were to I/O, there were many other noteworthy developments during the year. We deployed new acquisition systems in both the land and marine environments. We saw continued uptake in VectorSeis sensor technology. Several of our businesses had record years. And we continued to lay the foundation for growth and operational improvement.

In transitioning from 2004 to 2005, we are moving from a year of building our strategic foundation via acquisitions and launching new technologies to a year focused upon business execution. I'm confident in our vision for the company, but realize we have a significant amount of work to do to turn our view of what's possible into solid business performance. Operationally, the last half of 2004 was disappointing since we didn't deliver our desired financial results. In retrospect, most of our issues were related to initial technical issues with our new system introductions and business development challenges related to creating market pull for our full-wave offerings. I believe these issues are transitional in nature and are being adequately addressed as we progress into 2005.

I am encouraged by the amount of progress we've made in such a short period of time. Is there more to be done? Absolutely. My team and I are committed to executing against the plans we have drawn up and to delivering against the goals we have set. Continuing the turnaround of our equipment business, especially in Land Imaging Systems, and more tightly integrating Concept Systems and GXT into the I/O family, are at the top of our list. As with any endeavor, there will be challenges along the way. I assure you that we will do everything within our means to anticipate and address these in a timely, effective manner.

For those of you with the time and interest to learn more, over the next several pages I'll describe where we've been and where we're going as I/O continues Giving Seismic a Whole New Image™.

Thank you for your ongoing support of my team and their ambitious efforts.

Robert P. Peebler
PRESIDENT & CEO



STATE OF THE INDUSTRY

IN LAST YEAR'S SHAREHOLDER'S LETTER, I PROVIDED YOU WITH AN IN-DEPTH PERSPECTIVE ON THE SUPPLY-DEMAND DYNAMICS WITHIN THE GLOBAL E&P INDUSTRY AND HOW I THOUGHT THEY MIGHT IMPACT THE SEISMIC SECTOR. LET ME SUMMARIZE THE MAJOR THEMES HERE AND TELL YOU WHAT'S CHANGED, FOR BETTER AND FOR WORSE. I'LL START FIRST BY REFLECTING ON KEY THEMES FROM THE PERSPECTIVE OF THE OIL & GAS COMPANIES.

- Escalating global demand for hydrocarbons, with China and India leading the charge
- Mounting supply pressures as new discoveries become smaller and decline rates of both new and existing fields increase in many hydrocarbon basins
- Rising oil and gas prices
- Persistent geopolitical uncertainties, especially in the former Soviet Union and Middle East
- Increasing finding and development costs

Over the last year, there has been little change to these macro themes. If anything, the trends have become more favorable for I/O and our peers in the seismic sector.

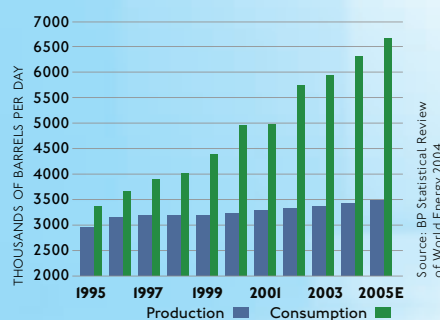
Take China, for example. While there is some talk of the Chinese economy cooling, any slowdowns that do occur will be off a torrid 8-10% GDP growth rate sustained over the last decade. By contrast, most Western economies grow at 3-4% each year. As Chinese consumers amass more wealth, one of their first discretionary purchases will be an automobile. We've done some back-of-the-envelope calculations that indicate fuel for automobiles in China could increase global demand for oil by 10-15 million barrels per day over the next decade. China's energy requirements, not just for gasoline but for all forms of energy, explain why the Chinese-backed oil & gas companies have been so active on the international stage, forging deals with Iran, Russia, Angola, Australia, Venezuela, and the Sudan (among others) to secure hydrocarbon supplies.

On the supply front, there has been little change to the generally held perspective in the industry that each incremental barrel becomes harder to find and more costly to develop. This isn't to say that there won't be new

discoveries and rounds of activity, even in fairly mature regions like the onshore U.S. But most known hydrocarbon basins have been fairly well picked over and the industry finds itself in a push towards deeper waters offshore or in a scramble for resource access in the former Soviet Union, Africa and the Middle East.

However, the risks associated with these areas are high. Witness the reduction in direct foreign investment in Russia following the Yukos ordeal, continued concerns about terrorist activity, the uncertain stability of the government in Saudi Arabia, and attempts at stabilizing Iraq. While the fallout from these risks can impact I/O's

CHINA'S OIL DEMAND IS OUTSTRIPPING SUPPLY



business in an unfavorable way from quarter to quarter, we stand to benefit over the long-term. Why? Primarily because the emerging markets contain roughly 90% of the world's oil and gas reserves and many of these regions are under-imaged when it comes to seismic. When the supermajors, like BP and ConocoPhillips, sign joint venture deals with Russian oil & gas companies to explore and develop hydrocarbons, we stand to benefit as they acquire and process new seismic data in the region. A similar up-cycle will begin soon in Libya. And, hopefully, one will begin in Iraq over the next 2-3 years. From the perspective of I/O, these trends are our friends.

Let me reflect for a moment on the impact of these trends, and other industry factors, from the viewpoint of the seismic acquisition contractors and I/O. Again, the news is generally favorable.

- E&P capital spending plans have increased for 2005
- Equipment utilization and prices are beginning to strengthen
- New seismic acquisition capacity is being added both onshore and offshore
- A technology upgrade cycle is beginning, especially in the marine segment

Most of the major oil & gas companies have released their plans for capital expenditures in 2005. In general, we're seeing increases of 8-10% across the board. That's the good news. However, a significant portion of the planned increase is targeted at development drilling to take advantage of high oil and gas prices. While this won't create a step-change increase in seismic activity in the near-term,

the channeling of funds by the E&P companies towards production projects will do little to address the looming global supply-demand gap I mentioned earlier. The silver lining for I/O from this capital allocation will likely be a sustained period of fairly

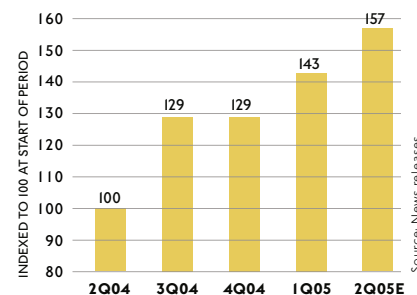
high commodity prices and a steady increase in seismic activity over the longer term as E&P companies reallocate budgets towards exploration and reservoir development, including 4-D seismic applications.

A number of segments in the oil field service sector, including seismic, are showing signs of increasing utilization. As is generally the case, price increases soon follow. In the seismic sector, we're beginning to see a tightening in the 2-D marine vessel market with much of the fleet signed up to longer term contracts. The 3-D acquisition markets appear to be tightening in both the North Sea and the Gulf of Mexico, as changes to the

fiscal regime and looming lease expirations drive new cycles of activity among both existing players and potential new entrants. The marine acquisition segment seems to be recovering more quickly than the land acquisition segment, which still suffers from excess crew and equipment capacity in many regions.

However, even land is showing signs of strength. Several contractors have added, or plan to add, capacity. In

LAND CREW DEPLOYMENT TRENDS Major North American Contractor

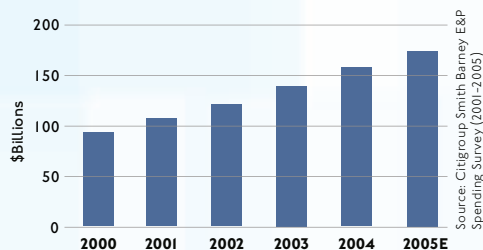


some cases, the additions are substantial. One of the largest contractors plans to double the number of land crews they deploy around the world by the end of 2005. While this is generally good news for I/O, our biggest challenge will be to make the case that these new crews should be mobilized using the next generation of full-wave technology rather than either pulling stacked equipment from inventory or extending their installed base by purchasing new, but outdated, technology.

I/O is poised to benefit from a technology upgrade and replacement cycle, especially in the marine segment. During the seismic down-cycle that started in the late 1990's, many marine contractors lacked the funds to update their vessel fleets with the latest technologies or froze capital programs as they contemplated mergers that never materialized. The harsh marine acquisition environment takes its toll on the best of equipment and we now have signs that several players see the need to begin a fairly significant and sustained retooling. The oil & gas companies appear to be putting pressure on the contractors to make this happen since the latest generation of marine streamer technologies - including digital source controllers, low-noise streamers, acoustic positioning gear, and streamer control systems - significantly improve the quality of 3-D and 4-D seismic images as well as the efficiency of vessel operations.

While there are still risks and uncertainties, I/O generally stands to gain as the seismic sector begins a long-anticipated rebound. For the first time in nearly a decade, the tide is once again rising in the seismic business and, as our contractor customers' business improves, so should ours.

GROWING WORLDWIDE E&P EXPENDITURES



VISION FOR FULL-WAVE

OUR FUNDAMENTAL VISION IS TO LEAD THE OIL & GAS INDUSTRY INTO THE NEXT ERA OF SEISMIC IMAGING, WHICH WE CALL DIGITAL FULL-WAVE. SINCE MODERN SEISMOLOGY BEGAN IN THE 1920'S, THERE HAVE BEEN TWO ERAS. THE 2-D ERA WAS THE FIRST, LASTING FROM THE 1920'S THROUGH THE EARLY 1980'S WHEN THE SECOND ERA – THE ERA OF 3-D SEISMIC – BEGAN. EACH OF THESE ERAS HAVE BEEN UNDERPINNED BY A MYRIAD OF INNOVATIONS IN ACQUISITION EQUIPMENT, SOFTWARE, AND SEISMIC DATA PROCESSING TECHNIQUES AND SUPPORTED BY COMPLEMENTARY INNOVATIONS IN COMPUTING AND INTERPRETATION SYSTEMS.

Seismic technology continues to serve the E&P industry well, providing a view thousands of feet beneath the surface of the Earth and allowing geoscientists to identify new sources of hydrocarbons ahead of the drill bit. In recent years, geophysicists have begun to design surveys and acquire 3-D data in what is sometimes referred to as time-lapse (or 4-D) seismic. As promising as these time-lapse techniques can be in revealing changes in a hydrocarbon reservoir across the explore–appraise–develop–produce lifecycle, 4-D seismic is fundamentally a series of repeat 3-D surveys conducted over an extended period of time.

While there have been significant enhancements to the underlying technologies since the 3-D era began nearly 25 years ago, current 3-D seismic suffers from several limitations:

- Measures ground motion in a single direction using a mechanical, coil-spring geophone
- Captures only a portion of the full seismic wavefield (the pressure or P-wave)
- Under-samples the subsurface because of equipment and economic constraints
- Assumes the Earth is homogeneous or isotropic

In a number of cases, these limitations don't necessarily constrain the utility of the seismic image. When

geophysicists are attempting to locate large, well-defined structures or to capture a single image early in the life of a reservoir, 3-D seismic is usually good enough.

However, as subsurface reservoir targets become deeper, more subtle, or more structurally complex, or when geophysicists want to delineate rock and fluid properties (and movements) within reservoirs, conventional 3-D seismic may no longer suffice. As more and more of the world's hydrocarbons are located in these types of reservoirs and as the need grows to optimize hydrocarbon production through every possible tool (including 4-D seismic), the E&P industry needs an entirely new approach and a new technology toolkit.

This is where digital full-wave seismic comes in. We, along with several thought leaders in our industry, believe that digital full-wave will underpin the third era in seismology. Why? Because we believe digital full-wave addresses the limitations of traditional 3-D seismic highlighted earlier. Let me explain.

To develop an image of a reservoir thousands of feet below the surface, geophysicists send acoustic energy into the Earth. This energy reflects off individual rock layers and eventually makes its way back to the surface where it is recorded with highly sensitive sensors. Since the 1920's, the sensor design has certainly evolved, but it



Analog geophone

still centers upon the coil-spring geophone. The springs in thousands of geophones vibrate in response to the reflected energy, after which highly advanced signal processing techniques are used to determine where the reflected energy came from in the subsurface. The problem is that most geophones are designed to record energy in only one direction (up and down), yet reflected energy is coming from all directions.

If the reflected energy can be recorded in three directions rather than one (what geophysicists would refer to as a vector), more data is captured, the chances of determining where the reflected energy came from in the subsurface is improved, and a more accurate image can be developed. This is the technology that underpins VectorSeis, our three-component digital sensor based on advanced MEMS (micro-electro-mechanical systems) technology.

VectorSeis brings benefits that extend beyond just recording seismic data in three directions. It captures the energy from the full seismic wavefield, revealing a more holistic, accurate image of the subsurface. When seismic energy travels through the Earth, it does so in multiple forms.

Since the 1920's, only one form of wave energy (what geophysicists call the P-wave) was recorded in most seismic acquisition programs. Until recently, seismic sensor technology didn't allow cost-effective recording of the full-wave data. In addition, many geophysicists didn't exactly know how to measure or process the other waves and they were effectively removed as noise during the signal processing step.

These other waves (especially the shear or S-wave) contain valuable information about the subsurface. By removing this information, insights into structure, lithology (rock type), and fluid locations were lost. Since VectorSeis can be deployed either on land or on the seabed, it has application in both onshore and offshore acquisition environments. And we believe VectorSeis' ability to capture shear wave information, which is especially valuable in detecting fluid types and movements, should make VectorSeis the sensor of choice for time-lapse 4-D seismic applications.

Beyond enhancing the subsurface image, VectorSeis also delivers improved field efficiencies during acquisition. Geophones are typically deployed in arrays, with 6 to 128 geophones per recording station (there are generally 2,000 or more recording stations on a land survey). VectorSeis is a single-point recording sensor, meaning that only one VectorSeis sensor is needed per recording station. These features allow VectorSeis to be more rapidly deployed and moved by land acquisition crews during field operations. Our customers get the dual benefits of improved images in shorter periods of time.

I/O's vision for full-wave is about more than just the sensor. It's also about how surveys are designed, how the data is acquired in the field, and how the data is processed. VectorSeis is a key enabler in survey design, field acquisition, and data processing. It is a bit of our secret sauce. But our vision for full-wave is not defined by VectorSeis alone.

Let me give you an example involving survey design. Conventional seismic surveys are designed in what we call a shoebox configuration. This means they are long in one dimension and shorter in another, which is a vestige of the acquisition platforms that the sensors are connected to and the traditional practices of acquisition crews in the field. The shoebox is effectively imposed by the limitations of acquisition equipment, whether used by a land crew or on a streamer vessel. The problem with the shoebox is that it tends to over-sample seismic data in one direction (the long axis) and under-sample seismic data in another. In many cases, this design is sub-optimal.



Exterior of VectorSeis sensor



Interior of VectorSeis sensor

An analogy might be looking at a television screen in which the resolution is really high in the middle of the screen, but distorted as you looked at the edges near the top and bottom.

One of our key goals is to develop survey design software, provide value-added expert services, and reconfigure our acquisition platforms so that oil & gas companies and contractors have the ability to deploy technology in a manner that is highly customizable to the subsurface imaging task at hand. By using our MESA® survey design software, single-point VectorSeis sensors, and our VectorSeis System Four® land acquisition platform, our customers have the ability to design and execute highly-tailored seismic programs that are Image-Driven™, not equipment-constrained.

A key reason to move away from the shoebox design is to be better able to account for velocity changes in the subsurface that are a function of compass direction, or azimuth. Conventional 3-D surveys effectively ignore these azimuthal velocity changes and assume that the Earth is homogeneous or isotropic in all directions. Geophysicists will readily acknowledge that this is a faulty assumption, as rocks are buried and compacted in the subsurface with a certain orientation, much like the grain in a wood tabletop. The problem with the conventional assumption of homogeneity is that seismic waves will travel faster in the direction with the grain than they do when traveling against it. If not accounted for, these azimuthal velocity changes distort the subsurface image.

To be able to properly account for this velocity anisotropy, a geophysicist has three requirements. The first is a survey that is shaped more like a square than a rectangle. In the short direction of the rectangle, there typically isn't enough distance (or offset) to be able to record and account for these velocity changes across the entire 360-degree azimuth range. So survey design is critical. The second is a highly accurate three-component sensor like VectorSeis that captures the full seismic wavefield across a very high signal bandwidth.

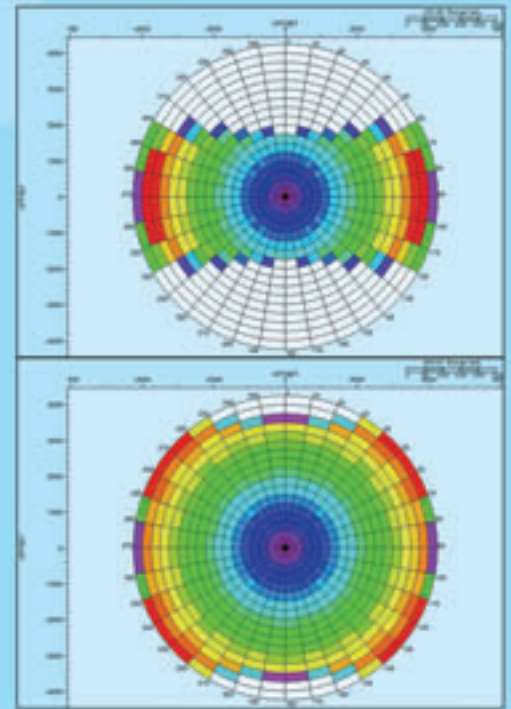
The third is an anisotropic processing technique. AZIM™, developed by our AXIS Geophysics group in Denver, is considered to be one of the leading products in this area and has been used by one of the supermajors to reprocess nearly their entire onshore North American seismic data library.

We've come a long way in articulating our full-wave vision, evangelizing it within the E&P industry, and commercializing the early technologies necessary to deliver real value to our customers. We have more work to do in this area, especially in developing processing algorithms that can take advantage of the full-wave data captured by VectorSeis. Nonetheless, in a variety of reservoir settings and acquisition environments that span the globe, the oil & gas companies are beginning to acknowledge the potential for digital full-wave seismic. And not just tomorrow, but today.

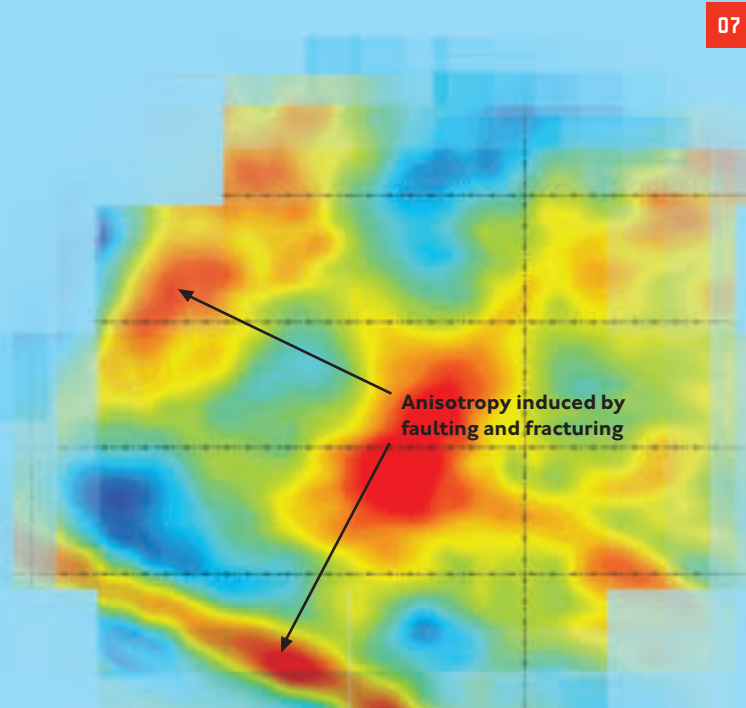
One of the most promising trends for I/O and the industry is that many of the more intractable imaging problems lend themselves to full-wave solutions. Full-wave works especially well when there are abrupt velocity changes that occur in the near-surface layer. These velocity changes are generally caused by things like permafrost, sand dunes, and desert hard pan. The fact that a large portion of the world's remaining hydrocarbons exists in the Arctic and Middle East bodes well for full-wave technologies in these areas.

Full-wave also works well in detecting fluid movements and in removing ambient sources of noise, like those caused by drilling and production operations. This provides a potentially large addressable market for full-wave in time-lapse 4-D seismic within producing oil & gas fields. With the recovery factors for many reservoirs still less than 50%, many E&P companies view 4-D seismic as an important tool for reservoir management and improved recovery.

Finally, full-wave is well suited to identifying subtle properties within reservoirs, including fractures and thin, gas-filled sand-shale sequences. As more of the world's hydrocarbons are produced from these types of reservoirs, we expect full-wave technologies to benefit and become more widely applied.



Subsurface data coverage for conventional shoebox (top) and wide azimuth (bottom) survey designs



AZIM anisotropic processing to detect reservoir fractures



TRANSFORMING THE COMPANY VIA ACQUISITION

ACQUISITIONS HAVE ALWAYS PLAYED AN IMPORTANT ROLE IN THE GROWTH OF I/O. HOWEVER, WE BELIEVE THAT NO PREVIOUS ACQUISITION IN OUR COMPANY'S HISTORY WAS AS STRATEGICALLY IMPORTANT AS EITHER THE CONCEPT SYSTEMS OR GX TECHNOLOGY TRANSACTION. BY COMPLETING BOTH ACQUISITIONS IN THE SAME YEAR, WE TRANSFORMED THE COMPANY AND CAPTURED TWO KEY TARGETS WE IDENTIFIED IN OUR COMPREHENSIVE STRATEGY REVIEW DURING 2003.

I/O IS NO LONGER AN EQUIPMENT MANUFACTURER SELLING ONLY HARDWARE TO THE SEISMIC ACQUISITION CONTRACTORS. INSTEAD, WE HAVE BECOME THE WORLD'S FIRST TECHNOLOGY-FOCUSED SEISMIC SOLUTIONS COMPANY WITH A RICH PORTFOLIO OF HARDWARE, SOFTWARE, AND SERVICES THAT ADD VALUE TO BOTH SEISMIC ACQUISITION CONTRACTORS AND, PERHAPS MORE IMPORTANTLY, TO THE ULTIMATE USERS OF THE SEISMIC IMAGES – THE OIL & GAS COMPANIES.

I'D LIKE TO TELL YOU A LITTLE BIT ABOUT EACH COMPANY, WHAT THEY DO, AND HOW THEY FIT INTO OUR BROADER CORPORATE STRATEGY. LET ME BEGIN WITH CONCEPT SYSTEMS, WHICH I/O ACQUIRED IN FEBRUARY 2004.

CONCEPT SYSTEMS

Concept Systems Limited is a 21 year-old company based in Edinburgh, Scotland. Concept Systems has approximately 80 employees whose backgrounds span key disciplines such as geoscience, engineering, applied mathematics, and computer science. The inclusion of professionals with mathematics and computational science training reflects Concept Systems' original mission to provide advanced navigation solutions to operators of marine streamer vessels in a pre-GPS (global positioning system) world. Imagine the complexity of trying to figure out where a streamer vessel was in the ocean, along with the miles of streamer cables towed behind it. Bringing mathematical solutions to this challenging problem via software and services is what gave Concept Systems its foundation and cemented its relationships to both vessel operators and the oil & gas companies.

Over time, Concept Systems extended their offerings to include integrated data management software for the marine streamer vessel fleet. On a modern seismic vessel, there are numerous technology subsystems

associated with locating and navigating the boat, determining the position of the streamers behind it, locating the air gun energy sources (along with synchronizing the firing of these energy bursts), and recording reflected energy on hydrophones towed behind the streamers. Figuring out what equipment is where, and matching up source energy and recorded energy in both time and place, is an extremely challenging task.

Concept Systems develops the software, and provides services on-board the vessel, to help streamer vessel operators acquire, quality control, and integrate data from all these disparate subsystems in a highly reliable, cost-effective manner. Concept Systems' leading market share is a testament to its stature and importance in modern marine streamer acquisition operations.

As the time-lapse 4-D seismic market continues to grow, so too will the importance of Concept Systems. The most critical element on a 4-D survey is repeatability from one survey to the next. This requires minimizing variations from survey to survey so that the only thing

changing is the signature of the reflected energy caused by fluid movements in the reservoir. To do this, the vessel and its streamers must be in effectively the same place each time, and heading in the same direction in each survey. The air guns need to fire in effectively the same location, and be towed in the same direction. This perhaps sounds easier said than done. Concept Systems is effectively the autopilot for the entire 4-D operation, making sure the vessel and its equipment are on course and shooting/recording in the optimal location every time on every survey, quality controlling the operation, and making the adjustments necessary to keep things on track according to the plan provided by the oil & gas company.

Concept Systems has a number of attractive growth platforms moving forward, some of which they have already begun to capitalize on. For instance, they have taken their competence in the marine streamer area and extended it to the marine seabed market through a product called Gator, which has become the de facto standard for data integration among seabed acquisition contractors. They have also begun a similar extension into land acquisition with a product called Scorpion. Additionally, they have a successor product for their marine streamer offerings (called Orca), which should be commercially available later in 2005.

All of these products are available as stand-alone software offerings to the global acquisition contractors, and we intend to continue this philosophy. Simultaneously, we have begun efforts in the streamer, seabed, and land segments to imbed key features of Concept Systems software into our acquisition platforms. We believe this tight integration, between software and hardware, will extend the functionality and appeal of our offerings in the marketplace.

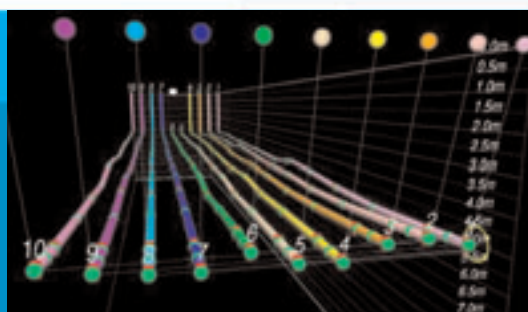
The analogy here is similar to the tight relationships that existed between Microsoft, Intel, and Compaq as the PC market took off in the late 1980's and early 1990's. All players were effectively open standards companies. But their tight alignment allowed them to develop products with additional functionality, which operated in

a more seamless way and could be delivered more rapidly to the market than their competitors.

We also believe Concept Systems has an exciting services opportunity to act as a technical advisor on the front-end of 4-D seismic programs, helping the oil & gas companies determine which assets in their portfolio will best respond to time-lapse seismic, optimize the design of surveys for repeatability, and assist in the evaluation and selection of appropriate technologies. For the past four years, Concept Systems has been funded by oil & gas companies to develop and deploy the technologies these companies need to unlock the potential of 4-D. During this time, Concept Systems has consulted on approximately fifty 4-D projects around the world. Looking ahead, we believe a back-end services opportunity exists associated with integrating and quality-controlling data before it is passed along to the seismic data processing phase, as well as in managing and storing the large volume of time-lapse seismic data.

GX TECHNOLOGY

GX Technology is a 16 year-old company based in Houston, Texas. The GXT group has more than 200 full-time employees, many of whom are advanced degree holders in geophysics, supplemented by a team of technical contractors whose numbers vary depending on project activity levels. The company's original mission was to provide advanced depth imaging services to oil & gas companies with operations in the Gulf of Mexico (GoM). The GoM was the real proving ground for the processing technique known as pre-stack depth migration (PreSDM), which is used to image complex subsurface structures such as those abutting salt domes, that are highly faulted, or that have extreme dips in the reservoir bedding layers. PreSDM is used to map reflected seismic energy into the right location in the subsurface both laterally and vertically. The technique involves building complex velocity models that convert the reflected travel time of seismic waves to depth, is extremely computational-intensive, and requires substantial expert intervention and iteration to perform properly.



Real-time streamer positioning display (Concept Systems)

As one of the leaders in PreSDM, GXT has an estimated 20% share in the GoM depth imaging market and is generally considered to be number one or two by their customers on dimensions such as technical sophistication and customer service. GXT's client list includes supermajors, independents, and national oil companies, many of whom have been long-standing customers. Trust-based relationships have been forged with many of these oil & gas companies and their geographic scope of operations have created a pull for GXT PreSDM services in other locations, including London, Aberdeen, and Calgary. We plan to open at least three additional processing centers in 2005 (in Venezuela, Angola, and Nigeria) based upon customer requests for local presence and significant commitments of future work. Since national oil companies control the majority of the world's hydrocarbon reserves, we believe it is critical to extend our international presence in order to be closer to this important customer segment.

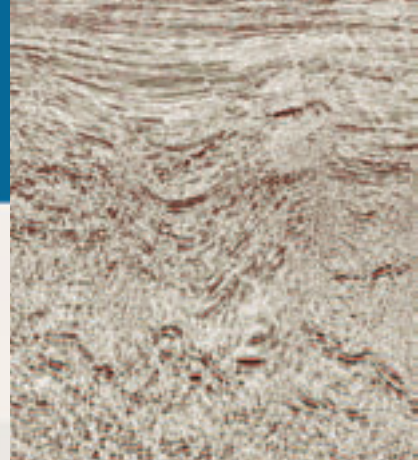
Following our acquisition of GXT, we aligned our Denver-based GMG/AXIS group with GXT. The synergies in this realignment were significant. AXIS focused primarily on processing seismic data acquired onshore and had developed a special expertise in azimuthal velocity analysis, which is the ability to understand how acoustic waves travel within the Earth as a function of their direction of propagation. Prior to the transaction, AXIS had a limited presence in marine data processing and also lacked the scale and capability for undertaking PreSDM.

GXT focused primarily on processing seismic data acquired offshore and had developed a special expertise in tomographic velocity analysis, which is the ability to understand how acoustic waves travel spatially within the Earth without consideration of their direction of propagation. When we put AXIS and GXT together, we get significant synergy and scale. We can now process data both onshore and offshore. In addition, I believe we possess the best "whole Earth" velocity analysis capability in the industry because we can now help geophysicists determine acoustic wave velocities both spatially and as a function of direction. Since velocity modeling is so critical to PreSDM, being the best whole Earth velocity modeler should allow GXT to extend its leadership in this critical imaging area and be prepared to participate in what many expect will be considerable market growth as PreSDM becomes more commonplace in many land-based reservoirs.

Our AXIS and GXT processing teams are already working extremely well together. They have made a step-change improvement in the effectiveness and computational efficiency of the algorithm used to enhance the P-wave



Reservoir pore pressure prediction from high resolution velocities



PreSDM data from GulfSpan imaging subsurface to 18,000 meters (60,000 feet)

data acquired by VectorSeis (a technique called Vector Filtering), have a project underway to dramatically reduce the cycle time associated with processing seismic data, and have pursued and won several joint commercial opportunities.

This is just the beginning, however. PreSDM is an integral part of the workflow for processing full-wave data. The P-waves and S-waves are both traveling at different velocities within the subsurface. To successfully merge and interpret the individual wavefields, one needs to tie them to a common depth point in the subsurface using a process called registering. While the theory to do this exists, and some modest pilot processing projects have been undertaken by ourselves and others to validate the concept, additional work must be done to make comprehensive full-wave processing cost effective. We have added additional resources to the separate efforts that both GXT and AXIS had in this area prior to the acquisition, combined the R&D teams onto a single development path, and charged the team with commercializing a value-added workflow for full-wave processing by the end of 2006.

While there are many things to do between here and there, this is an incremental development process that will deliver insights and benefits along the way. In fact, our full-wave processing team is already working with datasets acquired during the 2003-04 acquisition season for several of our oil & gas company customers and delivering insights that are helping them to adjust their investment decisions and drilling programs.

As part of its growth strategy since 1996, GXT developed a unique approach in the seismic industry that has spawned two new business lines beyond project-based PreSDM services. In line with GXT's Image-Driven approach, GXT geoscientists work closely with their counterparts in the oil & gas companies to define the nature of the imaging challenge at hand, determine what portfolio of acquisition and processing technologies would optimize the desired image, and then design the survey accordingly. This is a consultative, trust-based model that has served both GXT and its customers well.

One of the unique features about the model is that GXT outsources the actual seismic acquisition to established marine seismic contractors, which allows GXT to assume a value-added project management role while avoiding the ownership of capital-intensive vessels, acquisition equipment, and seismic crews. This lets GXT focus on value-adding technologies rather than logistics and field operations, ignore temptations to make recommendations based on utilizing directly-owned vessels and crews, and stay aligned with the imaging interests of its oil & gas company customers.

The first business line generated by GXT's Image-Driven model is called Integrated Seismic Solutions (ISS). ISS is an end-to-end offering in which GXT designs the survey, specifies the technologies to be used, project manages the acquisition contractor, processes the data, and renders final seismic images. While ISS is available on either a proprietary or multi-company basis, the majority of ISS projects undertaken to date have involved multiple oil & gas companies.

These multi-client projects are not speculative, but programs in which GXT has received pre-committed funding from two or more oil & gas companies. The companies that underwrite the ISS programs generally receive favorable pricing terms and preferential access to the seismic images for a designated period, but GXT retains resale rights to the seismic data and is able to resell it to others. As a result, the ISS business effectively creates another business line for GXT – reselling licenses of its seismic data library.

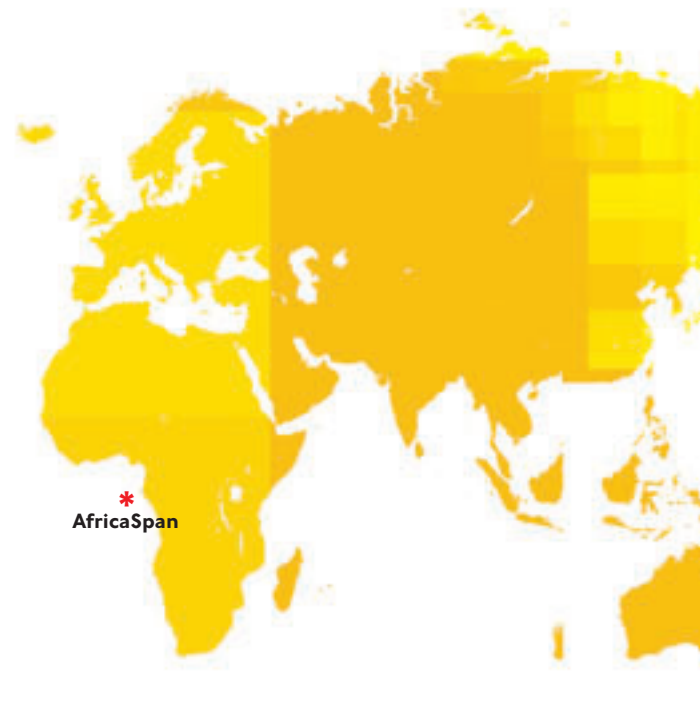
There is a tremendous, self-reinforcing synergy here. GXT's competence in PreSDM enables them to deliver

highly differentiated images from the competition. When existing customers enter a new geography, are planning for a lease sale, or are about to execute a costly development program, they commission an ISS program. After the exclusivity period ends, GXT can resell the data library licenses to others, including those who have never been significant clients. If these clients become comfortable with the data quality, they might then commission GXT to carry out stand-alone PreSDM projects. And this virtuous cycle begins again.

GXT has already begun to execute on this self-reinforcing business model. Their original work in the Gulf of Mexico led to the creation of a data library called GulfSpan, which helps oil & gas companies understand the deep geology of the GoM petroleum system. A significant number of GulfSpan licenses have been sold since the data became available in 2003, with several license buyers becoming PreSDM customers of GXT. Since that time, GXT has replicated the 'Span' model in several other key hydrocarbon regions including Trinidad, West Africa, and Eastern Canada. Additional Spans are in the detailed planning stages worldwide.

As a consequence, GXT is a critical engine for the future growth of I/O. Ideally, if we can use GXT's oil & gas company relationships to access the customer, evangelize (where appropriate) about the benefits that full-wave acquisition and processing can bring to the resolution of the final image, and secure full-wave ISS surveys around the world, we have a real opportunity to accelerate the adoption of full-wave imaging. By having GXT as part of the I/O family, we believe we can jointly shape the next era in seismic technology.

Current library of GXT regional Spans





ACCOMPLISHMENTS IN 2004

BEYOND THE ACQUISITIONS OF CONCEPT SYSTEMS AND GXT, AND THE SUBSEQUENT TECHNOLOGY AND ORGANIZATIONAL INTEGRATION EFFORTS, I/O ACCOMPLISHED A GREAT DEAL IN 2004. I WOULD LIKE TO HIGHLIGHT OUR MAJOR ACCOMPLISHMENTS IN FOUR AREAS:

- Raised capital to grow the business
- Improved operating performance
- Introduced new products
- Expanded customer relationships

RAISED CAPITAL TO GROW THE BUSINESS

In December 2003, I/O completed a \$60 million offering of Convertible Senior Notes. The proceeds from this capital markets transaction helped to strengthen our balance sheet and provided the funds necessary to complete the acquisition of Concept Systems in February 2004. The Concept Systems transaction was funded through a combination of \$36 million in cash, excluding acquisition costs, and 1.68 million shares of I/O common stock, valued at \$10.8 million.

We raised additional capital through a \$150 million secondary offering of our common stock in June 2004, which was used to fund the acquisition of GXT and for working capital.

IMPROVED OPERATING PERFORMANCE

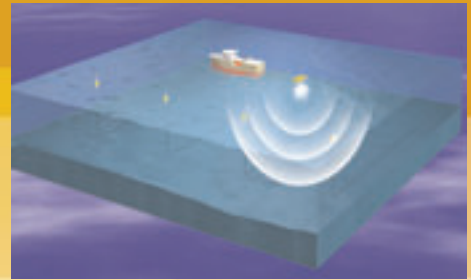
In 2003, I/O generated revenues of \$150 million, gross profits of \$27.8 million, and an operating loss of \$21.3 million. Our consolidated gross profit margin was only 19%, which is too low for a company providing important products and services with a high technology content. We would prefer our gross product margins be at least in the 30's in order to support our ongoing high technology R&D efforts.

We worked hard to change those numbers during 2004. We continued our efforts to strengthen our procurement, manufacturing, and supply chain processes and focused our sales teams on improving the mix of high-value

products and on negotiating higher prices for all of our offerings. As a result, we improved gross profit margins to 29%. With revenues increasing to \$247 million as a result of organic growth and acquisitions, our company ended the year with gross profits of \$72 million, an increase of 157% versus 2003.

Our Sensor, Concept Systems, and Marine Imaging business units were strong contributors to these results. Sensor, with annual revenues of approximately \$50 million, is the world's leading manufacturer of high-performance geophones, which remain the dominant seismic sensor in the marketplace. In 2004, Sensor had a record year for revenues and profitability and closed what we believe is the largest single sale in the history of the geophone industry with a Chinese seismic contractor.

Concept Systems also had a record year, again as measured on both revenues and profitability on a pro forma basis. They benefited from increasing strength in the marine streamer segment, sales of Gator software licenses to seismic contractors who acquire seabed-based surveys, and ongoing growth in their services business. The fact that Concept Systems managed to deliver these strong results in the same year they were



acquired by I/O is a testament to the strength of their product offerings and management team.

In 2004, our Marine Imaging Systems Division (MISD), which develops technologies for both towed streamer and seabed acquisition, saw revenues increase by 53% to \$55 million. Part of this increase was generated by the sale of our first VectorSeis Ocean redeployable seabed system, but we also saw strengthening in our legacy DigiCOURSE® business lines associated with towed streamer control and positioning technology. MISD gross margins also increased to 36% in 2004 (from 30% in 2003). If we exclude the \$5 million write-off of the receivable associated with the Russian contractor Large, a subsidiary of Yukos, MISD delivered \$10 million in operating income to the corporation (which compares to a slight loss in 2003).

Even though they did not achieve the overall financial results forecasted for 2004, our Land Imaging Systems Division significantly improved their profitability compared to 2003. Gross profits increased \$14.4 million to \$20.7 million versus the previous year as gross profit margins improved to 27% (from the single digits in 2003).

We continue to focus on improving our operational performance in all business lines. I'll comment more on our efforts in this regard later, but did want to highlight the outsourcing of our Applied MEMS business to the Swiss technology firm Colibrys as one example of our efforts to continually improve our operating performance. While we remain convinced that MEMS-based sensors like VectorSeis will increasingly become the sensors of choice for seismic imaging in the oil & gas business, we also believe that continuous improvements in the design and manufacture of the core MEMS technology will be required. Colibrys has developed breakthrough MEMS-based technologies for other industries. By combining forces with a MEMS specialist like Colibrys, we felt I/O would be better positioned to leverage the development insights from other products and industries, improve gross margins on VectorSeis-based seismic imaging systems, and reduce future investment requirements to sustain technology leadership in MEMS.

INTRODUCED NEW PRODUCTS

In 2004, we introduced three major products into the marketplace:

- VectorSeis Ocean, our redeployable seabed acquisition platform
- The digital-analog version of our System Four land acquisition platform
- New processing techniques for pre-stack depth migration (PreSDM)

In April 2004, I/O delivered our first commercial, VectorSeis-based system for seabed acquisition. This redeployable platform, called VectorSeis Ocean, integrates several proprietary I/O technologies including VectorSeis digital sensors, a buoyed recorder, and a patented noise-reducing cable system. These technologies are designed to enable oil & gas companies to acquire full-wave seismic data from the low noise environment of the seabed much more cost effectively than competing ocean bottom cable (OBC) systems. Our launch partner, Reservoir Exploration Technology (RXT, formerly known as Terra Seismic Services), has been operating VectorSeis Ocean since late summer for a supermajor in the bays of southern Louisiana and on the Gulf of Mexico shelf.

As with any new seismic acquisition platform, there have been a few unanticipated start-up difficulties that are being addressed as needed, while improvements are being incorporated into the next series of systems as prioritized by our customer. We are encouraged that our launch system has demonstrated that field productivity goals can be met when the system is fully functional. Both we and RXT look forward to the positive impact we believe it will have on the future OBC market.

Perhaps the best news in our early commercialization phase is the data quality from VectorSeis Ocean has been very encouraging. The acquired full-wave data has enabled the customer to image through gas clouds in the shallow subsurface and, in combination with GXT's advanced PreSDM, better resolve the steeply dipping reservoir beds that abut the many salt domes in the area. We are excited about the potential for this product and look forward to additional sales in markets both within and outside of the Gulf of Mexico.

BGP's recently purchased VectorSeis System Four - in staging and testing

In July 2004, Trace Energy Services became the first commercial customer for a version of our System Four land acquisition platform that we call A/C (analog cable). The name is a bit of a misnomer, as System Four A/C is actually both analog and digital. The product offers hybrid functionality that enables contractors to acquire seismic data using either analog geophones or digital full-wave VectorSeis sensors – in virtually any combination or configuration – even on the same survey. This flexibility is important to many of our contractor customers who see the market interest in digital full-wave imaging, but are uncertain of the pace of the transition as the seismic industry moves from one era to the next. By deploying System Four, these contractors capture the productivity benefits associated with our next-generation System Four platform architecture irrespective of the type of sensor used. They then can switch back and forth between geophones and VectorSeis from survey to survey or, better still for I/O, acquire what are called test patches of VectorSeis data within a predominantly geophone-acquired survey. Once the data from the patches is processed, oil & gas company customers are able to make side-by-side comparisons of the imaging improvements delivered by VectorSeis in the reservoir horizon of interest.

Our GXT group developed several key technologies during 2004 that extend the company's reputation as a leading provider of high-end seismic data processing algorithms. One of these technologies is called 3-D Surface-Related Multiple Elimination (SRME). 3-D SRME is a tool that removes multiples from data acquired in the marine environment (multiples are effectively reflections of source-generated acoustic energy that bounce between the seabed and the ocean's surface). In many cases, multiples obscure the intended subsurface target, making their removal vital for accurate seismic imaging. The results achieved to date through the use of 3-D SRME have been encouraging, particularly in the Gulf of Mexico and the North Sea. GXT has already won several processing contracts with oil & gas companies based on its capabilities in this technology. Since the next 2-3 years will be characterized by high lease turnover (and reprocessing activity both before and after lease relinquishment), we believe that GXT continues to be

well positioned at the high-end of the advanced imaging services market.

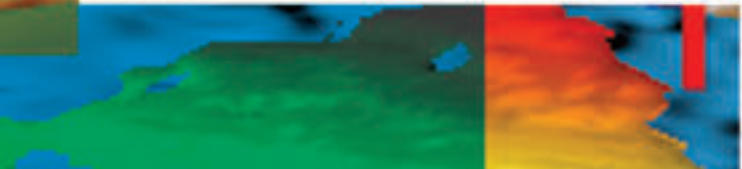
EXPANDED CUSTOMER RELATIONSHIPS


A key facet of our game-changing strategy for the seismic sector is to work in new and different ways with the contractors and the oil & gas companies. For I/O, this entails reaching out to a broader set of potential customers than had been the case when we were only an equipment manufacturer. It also involves being highly innovative commercially, both in terms of how we identify opportunities and how we structure sales, partnerships, and the like. In 2004, we expanded our efforts to broaden and deepen our relationships with key customers around the world.

On the contractor front, we continued our efforts with the integrated global incumbents, the Chinese contractors, and the regional specialists. The integrated global incumbents – WesternGeco, Veritas, PGS, and CGG – remain important customers for I/O, especially in the towed streamer area. Since these four players comprise 60% or more of the capacity in the highly concentrated marine streamer business, we feel reasonably well covered as we continue to grow and develop these relationships. We are also striving to cement our relationships with the smaller, but fast growing, players like Fugro Geoteam and contractors from China and Russia.

The land acquisition business is structured quite differently from marine. Because the barriers to entry are lower, land acquisition is a far more fragmented segment. The top four integrated global incumbents have approximately 40 crews operating around the world, representing about 20% of the total number of crews currently operating (according to the February 2005 edition of World Geophysical News).

The Chinese contractor BGP, now the largest land contractor in the world, has an estimated 20% share in the land market (perhaps even as high as 33% if some of the smaller, hard-to-account-for crews operating in China are included). BGP continues to be a very important customer for I/O, especially for our land acquisition technology. They currently operate several System Four platforms for





both domestic and international use. During 2004, they purchased new systems and expanded existing ones. These include System Four platforms operating in 100% VectorSeis mode and others that are digital-analog compatible. At the end of the year, BGP was operating one System Four in VectorSeis mode with a spread layout that was equivalent to nearly 19,000 channels of live capacity, which we believe represents a channel-count record for land seismic acquisition.

The regional specialists have proven to be important land equipment buyers in recent years. Companies like Trace in North America and Bashneftegeofizika in Russia have carved out unique, capability-based regional strongholds. Since approximately half of the land acquisition market is comprised of regional specialists, we intend to focus on partnering with the leaders to drive full-wave technologies into particular regions and acquisition segments. This includes working with new entrants, like RXT in seabed acquisition, who offer a new mindset and operating model, as well as a shared aspiration to change the game in seismic through new technologies.

On the oil & gas company front, we continue to focus on creating demand for our products and services with the ultimate end-users of the seismic image. Apache has been delighted with our work acquiring and processing VectorSeis full-wave data in Canada, with President and CEO, Steve Farris remarking that VectorSeis delivered “the best data I’ve ever seen from Canada.” We continue to work closely with Apache on the data acquired already in North America and to identify new imaging opportunities around the world.

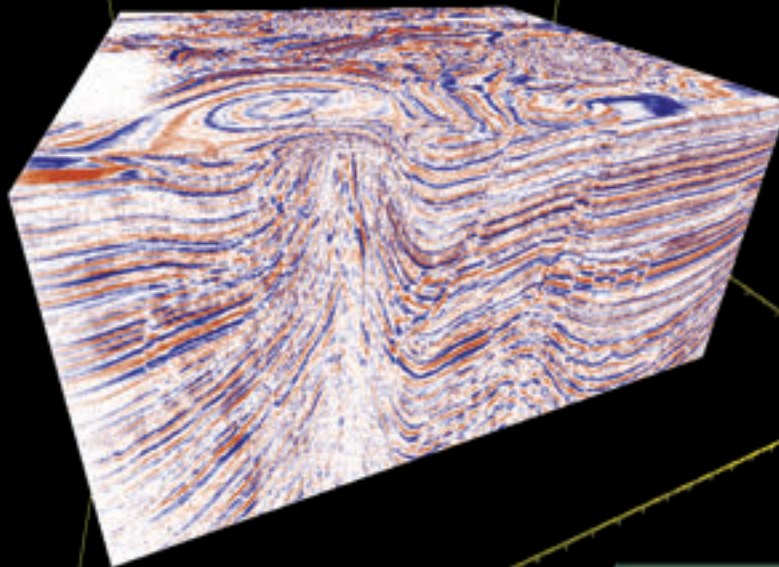
We also continue to work with other major oil & gas companies. We hosted one supermajor for a technology day during which one of their senior geophysicists commented, “We believe full-wave is now a tractable seismic technology, representing the best path forward in geophysics over the next decade.” This same company is working with us on the design of next-generation land imaging technologies and we were encouraged that they recently signed up as the lead underwriter for one of GXT’s new Span surveys in West Africa. It appears that they also will be one of our anchor clients in the two seismic processing centers we will be opening in Angola and Nigeria in 2005.

A second supermajor, which has been a long-standing client of GXT, has engaged us about the potential for full-wave technologies on both land and the seabed. They introduced us to their joint venture partner in Russia and we worked together, along with a regional specialist contractor, to design several VectorSeis pilot surveys for their most challenging reservoirs to image. Late in the year, we also were awarded our first contract with an asset team located in North Africa, which will be piloting AZIM for fracture detection. If this test proves successful, we would hope to extend our work to a broader range of full-wave imaging technologies spanning hardware, software, and services.

Recently, my land imaging team and I hosted a dozen senior geophysicists from a third supermajor at an all-day workshop. The discussion focused on the theory, benefits, and applications of full-wave imaging and the need for a fundamental rethink for how land seismic surveys are designed, acquired, and processed. While it’s too soon to determine how this relationship will unfold, I believe we will have an opportunity to work together to identify and execute one or two targeted full-wave land acquisition pilots in the months ahead.

These are just some of the types of projects we are working on in order to demonstrate the value of full-wave imaging with the oil & gas companies. Compared to where we were 18 months ago, I/O has made significant progress in connecting with key decision makers at all levels in these E&P firms and in evangelizing about the merits of full-wave imaging.

The acquisitions of Concept Systems and GXT have helped us in many of these dialogues. For one thing, we now can talk about a rich collection of imaging technologies, not just equipment. Second, we can leverage the relationships and track records both Concept Systems and GXT have within the E&P sector. Third, we have gained the scale needed to make it onto the preferred bid lists of the major oil & gas companies. Individually, I/O, Concept Systems, and GXT may have been too small to qualify. Together, we are a force to be reckoned with. Do we have more to do in this area? You bet. But we have made definite progress in a short time.



PRIORITIES FOR 2005

EVEN THOUGH WE DIDN'T END 2004 EXACTLY AS WE HAD PLANNED, I THINK IT'S IMPORTANT TO REMIND OURSELVES OF TWO FUNDAMENTAL REALITIES THAT WE FACE AS WE LOOK TO THE FUTURE.

16 First, I/O is still in the midst of a turnaround in its legacy equipment business. When I took the helm in 2003, the company was bleeding cash, had missed a technology cycle or underinvested in some businesses, and was lacking basic management infrastructure in many areas. I hired a top-notch team to drive change throughout the company and, by and large, they have delivered. But the process of change sometimes happens slower than any of us would like. Deeply rooted challenges can sometimes rear up and bite us. We all hope that most of these have been addressed and we are surprised less often in the quarters ahead, but I suspect that we still have challenges ahead just getting the basics completely in place.

The second reality is that, in the midst of this turnaround, we made two transformational acquisitions. I explained why we bought Concept Systems and GXT earlier in this letter. They were integral to our ability to deliver on the full-wave vision. Unfortunately, we didn't have the luxury of time in making either of these acquisitions. Both companies were effectively "in play" when we put them on our radar, forcing us to pursue the transactions sooner than we may have planned in an ideal scenario. Since they were such important assets for us to have, and there weren't any other alternatives, we had to act opportunistically. As a result, in a period of less than four months, we added two new entities to the I/O family, which was already undergoing a significant turnaround.

On the whole, the integration process for both Concept Systems and GXT has been a smooth one. Our teams are working well together and the technical synergies we saw are present and being acted upon. Yet, we're all still learning from one another. I believe that we, as a collective family of companies, have the people, the technologies, and the aligned vision to unlock the value of the Digital Full-wave era in seismic.

In 2005, I/O has two overarching goals. The first is to deliver consistent profits to our shareholders. The second is to continue driving the adoption of full-wave technologies, including VectorSeis. To achieve these goals, we have identified four critical objectives:

- Managing the commercialization of new products
- Restoring the growth trajectory at GX Technology
- Advancing the technology integration of Concept Systems and GX Technology
- Strengthening our sales organization and process

MANAGING THE COMMERCIALIZATION OF NEW PRODUCTS

Let me briefly highlight the products we have in the pipeline for 2005.

Concept Systems is targeting the release of Orca for the third quarter. Orca is the successor product for towed



streamer navigation and integrated data management. It combines the functionality of existing software packages while adding additional features that will benefit the vessel operator. By using Orca on towed streamer operations, seismic acquisition in the marine environment will be more efficient and vessel operators will be able to review their manpower requirements, while possibly saving costs and reducing HSE risks. Orca will also offer several modules that are important in ensuring the repeatability of time-lapse 4-D surveys by more tightly integrating across navigation, source control, and streamer control subsystems.

At about the same time, our DigiCOURSE group will be releasing a product called DigiFIN™ for advanced streamer control. DigiFIN will allow vessel operators to control the lateral position of streamer cables in the water, enabling them to be towed closer together without the threat of tangling and facilitating faster line changes (or turns) as each line of a survey is acquired. The tighter streamer spacing will improve image quality for the oil & gas companies, while the reduced threat of tangles and more rapid line changes will improve operational efficiencies of the streamer acquisition process.

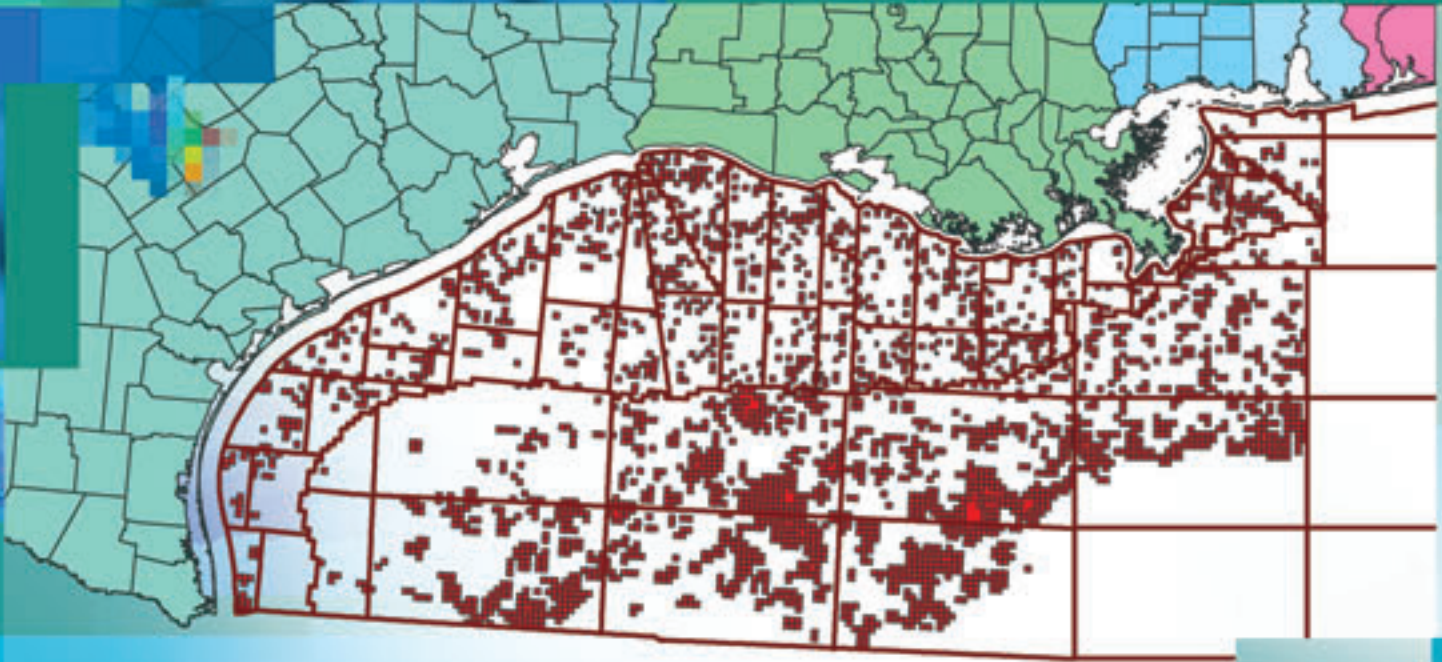
DigiFIN will join two other Digi products that are already in the marketplace – DigiSHOT® for enhanced digital control of marine air-gun energy sources and DigiRANGE II™ for highly accurate and cost effective acoustic position

determination of the streamer cables in the water. The combination of DigiFIN, DigiSHOT, and DigiRANGE II gives a vessel operator the toolkit needed for acquiring highly repeatable marine surveys, the most critical factor in time-lapse 4-D programs. As a result, this three-product toolkit, which we're calling Digi4D, has the potential to become an integral part of most marine streamer vessels as the number of 4-D surveys continues to grow.

In our Land Imaging Systems Division, we have a "special forces team" working on a variant of our System Four land acquisition platform. While borrowing significantly from the advanced System Four architecture, this product will contain features that should enhance productivity in certain land acquisition environments. We don't view it as a replacement to System Four, but as an extension of our line. I'll tell you more about this as we get closer to launching it later in the year.

RESTORING THE GROWTH TRAJECTORY AT GX TECHNOLOGY

We faced several unanticipated challenges with GXT following the acquisition. GXT's proprietary processing business slowed unexpectedly in the second half and we had several multi-client ISS Span surveys slip beyond 2004 due to delays in governmental permitting. Perhaps our biggest short term challenge involved being too dependent on GXT's data library business in the second half. Although we have learned to expect ebbs and flows



in the mix of these three elements of their business, we want to achieve a better balance than we did over the last six months of the year.

Some of the challenges resulted from changes in the market that we are adjusting to. For instance, many of the oil & gas companies now appear to be reacquiring data in the Gulf of Mexico in anticipation of upcoming lease sales rather than reprocessing old datasets. While this may ultimately help drive demand for proprietary processing, it will also defer the demand by several quarters until the data is acquired. I also believe, however, that several of the challenges are internal. Perhaps the biggest is that GXT's management team was involved in the process of selling their company for nearly a year. With the acquisition now behind them, they have become fully focused on running the business and recapturing operational momentum.

Our GXT management team is moving quickly to address the challenges across several fronts. The first priority is to reduce the backlog of our Houston Processing Center (HPC), which has notably increased in the first quarter of 2005. The nature of PreSDM requires an enormous amount of computing infrastructure and a team of dedicated professionals to process, quality control, and render images from the seismic data. The HPC is the core of GXT's

processing infrastructure given the company's legacy focus on the Gulf of Mexico region. In addition to serving external customers in the oil & gas companies, the center also serves an internal customer – GXT's Integrated Seismic Solutions (ISS) group. The ISS group designs and delivers proprietary and multi-client seismic surveys around the world, and relies upon the HPC for its processing needs.

We believe many of the ISS permits that were delayed in late 2004 will be issued during the first half of 2005, increasing the utilization and profitability of the HPC. In addition, GXT is working to extend relationships with several existing customers, and to introduce selected new ones, in order to expand the imaging business for external processing projects. Given the anticipated increases in demand for PreSDM in the Gulf of Mexico as leases expire and change hands among the oil & gas companies over the next few years, and the fact that several core GXT customers are discussing alliance-type relationships for PreSDM services, we believe HPC activity levels will be robust in the quarters ahead.

Our second priority is to continue to build the international foundation of GXT. One aspect of this is to get the permitting issues resolved for international ISS programs. Doing this will generate both near-term income as images from the ISS programs are delivered

to their underwriters and long-term income as data library licenses are resold once the underwriters' exclusivity period ends.

In addition, we plan to expand the international footprint of GXT early in 2005. At the request of several core customers, GXT has been asked to open centers in Nigeria, Angola, and Venezuela for advanced PreSDM and other imaging services. These center openings are associated with commitments of work from existing customers, so we feel the risk of opening them is manageable. The centers will provide a base to expand from in these important petroleum-producing countries, add to GXT's existing international presence in Calgary, London, and Aberdeen, and diversify our revenue streams.

ADVANCING THE TECHNOLOGY INTEGRATION OF CONCEPT SYSTEMS AND GX TECHNOLOGY

I/O has already benefited from the acquisitions of Concept Systems and GXT. These companies, filled with remarkable people and technologies, have already helped lay the groundwork for future growth in the era of Digital Full-wave seismic.

It's important to remember that we acquired Concept Systems and GXT for their technologies and innovative people. Making sure we continue to maintain an environment that preserves or enhances their motivation is paramount to our collective success. I took this approach with both Concept Systems and GXT, allowing them ample flexibility to operate as they always had, while making some moves on the technology front to begin the process of sharing ideas about new product directions and the development of seismic solutions that integrated best-in-class elements from across our portfolio of hardware, software, and services.

Concept Systems delivered a record year in terms of revenue and operating income on a pro forma basis. Our managers and technical personnel are collaborating well on topics ranging from strategy development to joint opportunity pursuit. We have a number of cross-group projects underway with ambitious objectives. And several of the projects are already beginning to show results in areas like full-wave processing, "intelligent hardware," 4-D solutions, and cycle time reduction across the seismic workflow.

STRENGTHENING OUR SALES ORGANIZATION AND PROCESS

Legacy parts of the company, especially our Land Imaging Systems Division, had a tough time anticipating the demand for their products in 2004. Several factors underpin this. One is the challenge of forecasting the market adoption of a new technology cycle like full-wave seismic, along with the products that underpin it like VectorSeis. The second is the challenge of forecasting customer adoption of new products in existing categories. Although we believe System Four is a breakthrough land acquisition platform, it is competing against an entrenched competitor that has a significant installed base around the world. That will take some time and hard-nosed, "in the trenches" sales efforts to undo. The third is to successfully execute our strategy of creating demand pull with the oil & gas companies for new full-wave technologies like VectorSeis and System Four.

To meet these challenges, we are taking several actions. First, we have most recently brought in a new Vice President of Global Sales and Business Development in our Imaging Systems Group. This individual has extensive experience in packaging and selling complex solutions, grounded in new technologies, within the E&P sector and especially to the oil & gas companies. He has been charged with creating end-user demand pull for full-wave systems within the oil & gas company segment as well as with attracting and developing a talented pool of consultative salespeople who can assist him in these efforts.

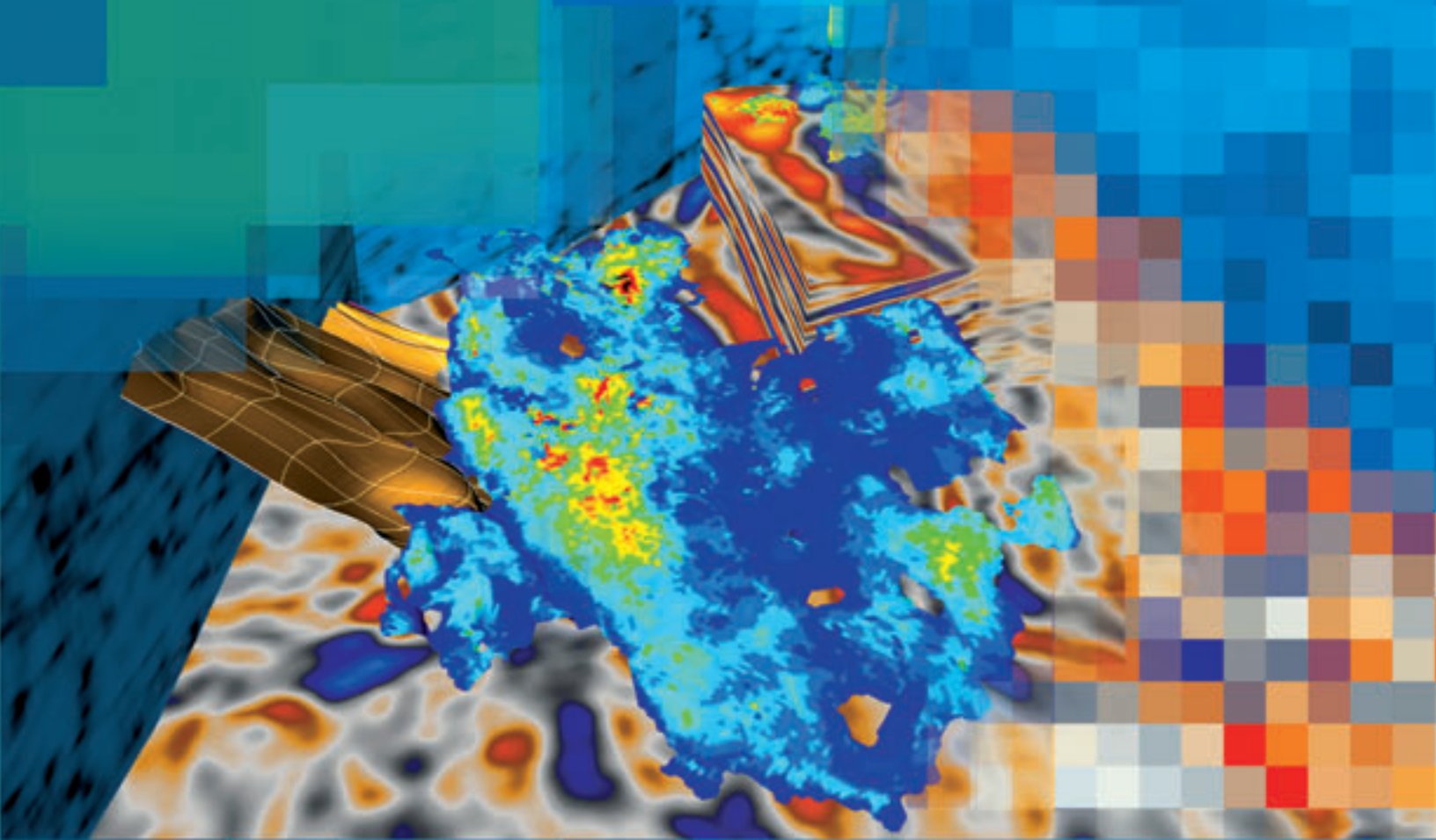
Second, we have begun to restructure our sales teams within the Imaging Systems Group to more clearly focus on our two customer segments. One group will focus on the oil & gas companies, evangelizing about the imaging benefits that full-wave can deliver among senior executives, asset team leaders, and geophysicists. This team is oriented more towards the 6-12 month window in our long-term sales cycles and will focus on the consultative, strategic, solutions sale. A second group will focus on the contractors, dealing more with sales over the next 90 days for specific products and services. While both groups will work together to ensure alignment within regions, across targeted customers, and on specific sales in the pipeline, we



believe the separation of our sales team into two well-defined channels will better align our efforts with the distinct requirements of our customer base.

Third, we are continuing our efforts related to training and sales tool utilization. On the training front, we are executing against an intensive, multi-quarter, skills-enrichment program that includes modules in consultative selling, presentation skills, negotiations, and account planning. In mid-2004, we licensed the Salesforce.com software package to assist us with tracking our sales pipeline more rigorously. Once fully implemented and embraced by our salespeople, we believe Salesforce.com will provide a vehicle for more accurately forecasting future revenues and gross profits on a risk-weighted basis. Our efforts in this regard are part of the general theme of infrastructure high-grading I mentioned earlier as part of our overall turnaround initiative. This isn't an excuse for the magnitude of our challenge or the pace of our change, simply a statement that reflects the reality of our position at the end of 2004.

What we have also come to fully appreciate is that our business results are difficult to predict, primarily as a result of the timing of big-ticket sales for data library licenses and land or seabed acquisition platforms. While we recognize that refined business development practices and sales forecasting techniques should improve our accuracy moving forward, we believe we (and our shareholders) will be better served by focusing more on annual goals and results versus focusing on quarter-to-quarter projections.



SUMMARY

The year 2004 continued the revolution of a company and of an industry.

My management team made significant progress in turning around the equipment business of the legacy I/O. We launched new products, increased revenues year-on-year, and improved our gross profit margins significantly. We also completed the acquisitions of both Concept Systems and GXT, transforming our company into a broad-based seismic solutions provider with the technologies needed to deliver upon our vision for digital full-wave imaging.

We have now laid the foundation for future growth as oil & gas companies invest more in resource exploration and development, as the seismic sector begins its long-anticipated rebound, and as the era of Digital Full-wave imaging begins to emerge. There remains much for us to do. I am confident, however, that we are on the right course. As the industry accelerates its transition from the 3-D era to the era of Digital Full-wave, I/O should be poised to benefit as should you, our shareholders.

SELECTED FINANCIAL DATA

The selected consolidated financial data set forth below with respect to our consolidated statements of operations for the years ended December 31, 2004, 2003, 2002 and 2001, the seven months ended December 31, 2000 and the fiscal year ended May 31, 2000, and with respect to our consolidated balance sheets at December 31, 2004, 2003, 2002, 2001 and 2000 and May 31, 2000 have been derived from our audited consolidated financial statements. Our results of operations and financial position have been affected by acquisitions of companies and significant charges during the periods presented, which may affect the comparability of the financial information. For information on our acquisitions and a tabular presentation of significant charges, see Notes 2 and 2I, respectively, of *Notes to Consolidated Financial Statements*. This information should not be considered as being necessarily indicative of future operations, and should be read in conjunction with Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and the notes thereto included elsewhere in the Annual Report on Form 10-K for the fiscal year ended December 31, 2004.

	Years Ended December 31,				Seven Months ended December 31,	Year Ended May 31,
	2004	2003	2002	2001	2000	2000
	(In thousands, except per share data)					
STATEMENT OF OPERATIONS DATA:						
Net sales	\$ 247,299	\$ 150,033	\$ 118,583	\$ 212,050	\$ 78,317	\$ 121,454
Cost of sales	175,705	122,192	101,018	139,478	59,582	109,329
Gross profit	71,594	27,841	17,565	72,572	18,735	12,125
Operating expenses (income):						
Research and development	19,611	18,696	28,756	29,442	16,051	28,625
Marketing and sales	23,758	12,566	11,218	11,657	5,506	8,757
General and administrative	29,748	16,753	19,760	19,695	8,127	21,885
(Gain) loss on sale of assets	(3,980)	(291)	425	—	—	—
Impairment of long-lived assets	—	1,120	6,274	—	—	—
Goodwill impairment	—	—	15,122	—	—	31,596
Amortization of goodwill	—	—	—	3,873	2,157	6,732
Total operating expenses	69,137	48,844	81,555	64,667	31,841	97,595
Income (loss) from operations	2,457	(21,003)	(63,990)	7,905	(13,106)	(85,470)
Interest expense	(6,231)	(4,087)	(3,124)	(695)	(627)	(826)
Interest income	1,276	1,903	2,280	4,685	4,583	4,930
Fair value adjustment and exchange of warrant obligation	—	1,757	3,252	—	—	—
Impairment of investment	—	(2,059)	—	—	—	—
Other income (expense)	220	685	(373)	574	176	1,306
Income (loss) before income taxes	(2,278)	(22,804)	(61,955)	12,469	(8,974)	(80,060)
Income tax expense (benefit)	701	348	56,770	3,128	1,332	(6,097)
Net income (loss)	(2,979)	(23,152)	(118,725)	9,341	(10,306)	(73,963)
Preferred dividend	—	—	947	5,632	3,051	4,557
Net income (loss) applicable to common shares	\$ (2,979)	\$ (23,152)	\$ (119,672)	\$ 3,709	\$ (13,357)	\$ (78,520)
Basic net income (loss) per common share	\$ (0.05)	\$ (0.45)	\$ (2.35)	\$ 0.07	\$ (0.26)	\$ (1.55)
Weighted average number of common shares outstanding	65,961	51,237	51,015	51,166	50,840	50,716
Diluted net income (loss) per common share	\$ (0.05)	\$ (0.45)	\$ (2.35)	\$ 0.07	\$ (0.26)	\$ (1.55)
Weighted average number of diluted shares outstanding	65,961	51,237	51,015	52,309	50,840	50,716
BALANCE SHEET DATA (END OF YEAR):						
Working capital	\$ 109,075	\$ 133,467	\$ 114,940	\$ 204,600	\$ 181,366	\$ 183,412
Total assets	479,116	249,204	249,594	387,335	365,633	381,769
Notes payable and current maturities of long-term debt	6,564	2,687	2,142	2,312	1,207	1,154
Long-term debt, net of current maturities	79,387	78,516	51,430	20,088	7,077	7,886
Stockholders' equity	314,512	133,764	152,486	331,037	325,403	335,015
OTHER DATA:						
Capital expenditures	\$ 5,022	\$ 4,587	\$ 8,230	\$ 9,202	\$ 2,837	\$ 3,077
Investment in multi-client library	4,168	—	—	—	—	—
Depreciation and amortization (other than multi-client library)	18,345	11,444	13,237	17,535	11,448	22,835
Amortization of multi-client library	6,323	—	—	—	—	—

CORPORATE INFORMATION

EXECUTIVE OFFICERS

Robert P. Peebler
President & Chief Executive Officer

Jorge Machniz
President, Imaging Systems Group

Michael K. (Mick) Lambert
President, GX Technology

J. Michael Kirksey
Executive Vice President & Chief
Financial Officer

Chris M. Friedemann
Vice President, Commercial Development

David L. Roland
Vice President, General Counsel &
Corporate Secretary

Michael L. Morrison
Controller & Director of Accounting

BOARD OF DIRECTORS

James M. (Jay) Lapeyre, Jr.
Chairman of the Board
President, Laitram L.L.C.

Bruce S. Appelbaum
Chairman, Mosaic Natural Resources

Theodore H. Elliott, Jr.
Chairman, Prime Capital Management Co.

Franklin Myers
Senior Vice President & Chief Financial Officer,
Cooper Cameron Corporation

S. James Nelson, Jr.
President, FSD Corporation
Retired Vice Chairman, Cal Dive International

Robert P. Peebler
President & Chief Executive Officer,
Input/Output

John Seitz
Co-CEO, Endeavour International Corp.

Sam K. Smith
Consultant, Private Investments

INVESTOR RELATIONS BY TELEPHONE, E-MAIL OR WEBSITE

Shareholders, securities analysts, portfolio managers or brokers seeking information about the Company are welcome to call Investor Relations at +1 281 933 3339. If you prefer, you may send your requests to the Investor Relations' e-mail address: ir@i-o.com. Recent news releases, financial information and SEC filings can be downloaded from the Company's website at www.i-o.com.

ANNUAL REPORT ON FORM 10-K

Input/Output's Annual Report on Form 10-K for the fiscal year ended December 31, 2004, although furnished as an integral part of this Annual Report to Shareholders, is also available upon request without charge from Input/Output, Inc., Attn: Investor Relations, 12300 Parc Crest Drive, Stafford, Texas 77477.

ANNUAL MEETING

The Annual Meeting of Shareholders of Input/Output, Inc. will be held at the Holiday Inn Southwest, 11160 Southwest Freeway, Houston, Texas 77031-3698, on May 4, 2005 at 10:30am CST.

STOCK TRANSFER AGENT

Computershare Investor Service LLC
2 North LaSalle St.
Chicago, Illinois 60602-3705
Tel: +1 312 588 4991

INDEPENDENT AUDITORS

PricewaterhouseCoopers LLP
1201 Louisiana, Suite 2900
Houston, Texas 77002-5678
Tel: +1 713 356 4000

CEO & CFO CERTIFICATES

The Company has included as Exhibit 31 to its Annual Report on Form 10-K for its fiscal year ended December 31, 2004 filed with the Securities and Exchange Commission, certificates of the Chief Executive Officer and Chief Financial Officer of the Company certifying the quality of the Company's public disclosure, and the Company has submitted to the New York Stock Exchange a certificate of the Chief Executive Officer of the Company certifying that he is not aware of any violation by the Company of New York Stock Exchange corporate governance listing standards.

A copy of the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission will be furnished without charge to any shareholder upon written request to the address listed above.

STATEMENT FOR PURPOSE OF FORWARD-LOOKING STATEMENTS

The information included herein contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements include statements concerning expected future financial positions, segment sales, results of operations, cash flows, funds from operations, financing plans, gross margins, business strategy, budgets, projected costs and expenses, capital expenditures, competitive position, product offerings, technology developments, access to capital and growth opportunities, future sales and market growth, and other statements that are not of historical fact. Actual results may vary materially from those described in these forward-looking statements. All forward-looking statements reflect numerous assumptions and involve a number of risks and uncertainties.

These risks and uncertainties include the timing and development of the Company's products and services and market acceptance of the Company's new and revised product offerings; risks associated with competitor's product offerings and pricing pressures resulting therefrom; the relatively small number of customers that the Company currently relies upon; the fact that a significant portion of the Company's revenues is derived from foreign sales; the Company's ability to successfully manage the integration of its acquisitions into the Company's operations; the risks that sources of capital may not prove adequate; the Company's inability to produce products to preserve and increase market share; collection of receivables; and technological and marketplace changes affecting the Company's product line. Additional risk factors, which could affect actual results, are disclosed by the Company from time to time in its filings with the Securities and Exchange Commission, including its Annual Report on Form 10-K for the year ended December 31, 2004.

The information contained herein includes references to trademarks, service marks and registered marks of Input/Output and our subsidiaries, as indicated. Except where stated otherwise or unless the context otherwise requires, the terms "VectorSeis," "MESA," "DigiCOURSE," "DigiSHOT," and "VectorSeis System Four" refer to our VectorSeis®, MESA®, DigiCOURSE®, DigiSHOT®, and VectorSeis System Four® registered marks, and the terms "AZIM," "DigiFIN," "DigiRANGE II," "Applied MEMS," "Giving Seismic a Whole New Image," and "Image-Driven" refer to our AZIM®, DigiFIN®, DigiRANGE II®, Applied MEMS®, Giving Seismic a Whole New Image®, and Image-Driven® trademarks and service marks.





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