

achieving success

Ultra

Ultra Electronics Holdings plc Annual Report and Accounts 2004

ELECTRO



# achieving success

ULTRA ELECTRONICS IS A GROUP OF SPECIALIST BUSINESSES DESIGNING, MANUFACTURING AND SUPPORTING ELECTRONIC AND ELECTROMECHANICAL SYSTEMS, SUB-SYSTEMS AND PRODUCTS FOR DEFENCE, SECURITY AND AEROSPACE APPLICATIONS WORLDWIDE.

ULTRA, WHICH EMPLOYS 2,800 PEOPLE IN THE UK AND NORTH AMERICA, FOCUSES ON HIGH INTEGRITY SENSING, CONTROL, COMMUNICATION AND DISPLAY SYSTEMS WITH AN EMPHASIS ON INTEGRATED INFORMATION TECHNOLOGY SOLUTIONS. THE GROUP CONCENTRATES ON OBTAINING A TECHNOLOGICAL EDGE IN NICHE MARKETS, WITH MANY OF ITS PRODUCTS AND TECHNOLOGIES BEING MARKET LEADERS IN THEIR FIELD.

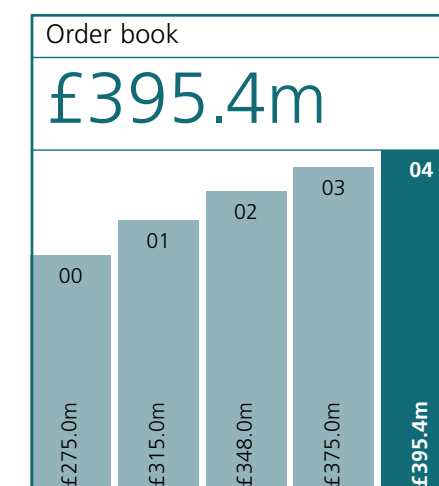
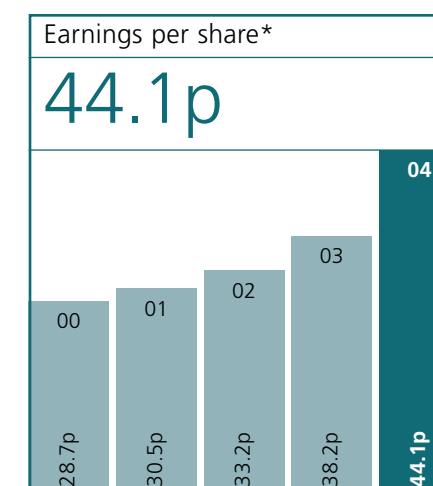
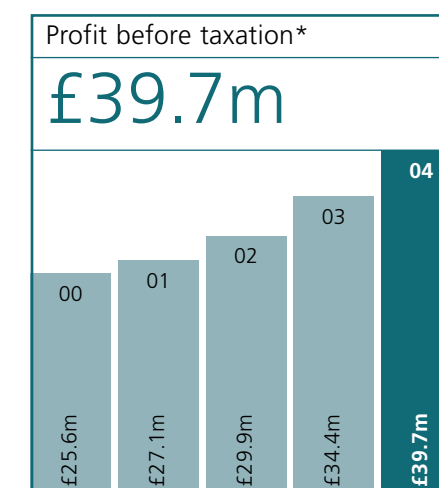
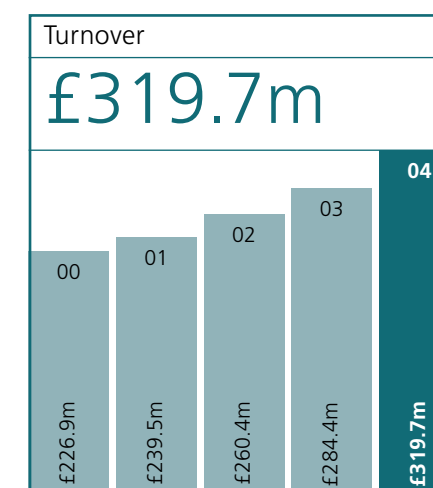
ULTRA'S PRODUCTS AND SERVICES ARE USED IN AIRCRAFT, SHIPS, SUBMARINES, ARMoured VEHICLES, SURVEILLANCE AND COMMUNICATION SYSTEMS, AIRPORTS AND TRANSPORT SYSTEMS AROUND THE WORLD. ULTRA ALSO PLAYS AN IMPORTANT ROLE IN SUPPORTING PRIME CONTRACTORS BY UNDERTAKING SPECIALIST SYSTEM AND SUB-SYSTEM INTEGRATION USING THE COMBINED EXPERTISE OF THE GROUP BUSINESSES.

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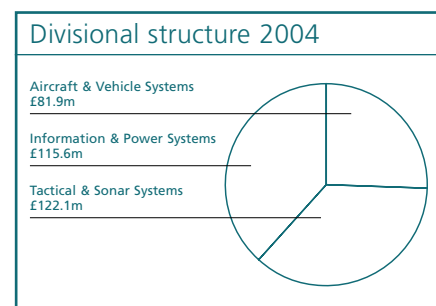


THE QUEEN'S AWARD  
FOR ENTERPRISE 2003  
FOR  
HIP-PAG  
AT PRECISION  
AIR SYSTEMS

	2004	2003	GROWTH
TURNOVER (£m)	<b>319.7</b>	284.4	+12.4%
PROFIT BEFORE TAXATION (£m)*	<b>39.7</b>	34.4	+15.5%
EARNINGS PER SHARE*	<b>44.1p</b>	38.2p	+15.4%
OPERATING PROFIT MARGIN*	<b>13.3%</b>	13.2%	
EMPLOYEES (AVERAGE NUMBER)	<b>2,678</b>	2,505	



\* Before amortisation of goodwill.  
In 2004 this amounted to £5.9m (2003: £4.9m).  
Statutory information after goodwill amortisation:  
operating profit £36.6m (2003: £32.7m), profit  
before tax £33.8m (2003: £29.5m) and earnings  
per share 35.2p (2003: 30.8p).



ULTRA ELECTRONICS SPECIALISES IN THE DESIGN, MANUFACTURE AND SUPPORT OF ELECTRONIC AND ELECTROMECHANICAL SYSTEMS, SUB-SYSTEMS AND PRODUCTS FOR AIRCRAFT, SHIPS, SUBMARINES, ARMoured VEHICLES, SURVEILLANCE AND COMMUNICATION SYSTEMS, AIRPORTS AND TRANSPORT SYSTEMS. IT IS ORGANISED INTO THREE DIVISIONS: **AIRCRAFT & VEHICLE SYSTEMS, INFORMATION & POWER SYSTEMS AND TACTICAL & SONAR SYSTEMS.**



AT THE HEART OF ULTRA'S SUCCESS IS ITS INVESTMENT STRATEGY. THE MANAGEMENT HAS A REAL EXPERTISE IN IDENTIFYING INVESTMENT OPPORTUNITIES THAT DELIVER GROWTH.

Aircraft & Vehicle Systems	Information & Power Systems	Tactical & Sonar Systems
<b>Sales £81.9m</b> (2003: £79.9m)	<b>£115.6m</b> (2003: £95.5m)	<b>£122.1m</b> (2003: £109.0m)
<b>Profit* £14.7m</b> (2003: £13.9m)	<b>£14.8m</b> (2003: £11.0m)	<b>£13.0m</b> (2003: £12.7m)
<b>CONTROLS</b> • Landing gear control and proximity sensing systems. Airframe de-icing and crack detection systems. Civil and military aircraft cabin quieting systems using active noise and vibration control technology. Propeller balancing systems. <b>DATTEL</b> • High integrity systems including safety critical software. Internet-based secure collaborative working environments and secure communication networks. <b>ELECTRICS</b> • Data management and vision control systems for armoured vehicles. Specialised control handles, high integrity switches and indicators. Lighting systems. Ruggedised cable harnesses. <b>MEASUREMENT SYSTEMS INC</b> • Displacement and force joysticks, hand grip controls, trackballs, encoders and simulation equipment. Cockpit equipment. <b>PRECISION AIR SYSTEMS</b> • High Pressure Pure Air Generators (HiPPAG) for cooling thermal imagers and infra-red sensors, and for pneumatic ejection of aircraft munitions. Sidewinder missile overhaul and repair.	<b>ADVANCED TACTICAL SYSTEMS</b> • (until 1 January 2005, Advanced Programming Concepts) Battlespace IT solutions. Software based data fusion and display systems for applications in military command, control, communications, computers, intelligence, surveillance and reconnaissance (C4ISR) systems. <b>AIRPORT SYSTEMS</b> • Airport IT system integration. IT services and solutions for airlines and airports: common use check-in, local departure control, weight & balance management systems, central database (UltraDB); flight information (UltraFIDS); management information (UltraMIS); passenger bag matching (UltraTrak); resource management (UltraResource); data acquisition and control (UltraControl). <b>COMMAND &amp; CONTROL SYSTEMS</b> • Optical and infra-red surveillance and tracking systems. Battlespace IT solutions. Geographical information management systems. Combat management systems. Multifunction command and control console systems. Weapon interface electronics. High integrity electronic control systems. <b>EMS</b> • Specialised power supplies and demagnetising systems for the electromagnetic silencing of naval vessels. Transformer rectifier units. <b>MANUFACTURING &amp; CARD SYSTEMS</b> • High integrity contract electronic manufacturing services. The Magicard range of identity card printers. <b>PMES</b> • High power solid state power conversion and control equipment. Naval data processing and distribution systems. Transit system power conversion and control. Multi-influence measurement and control systems for the management of complex signatures of naval vessels. Magnetic and electric field sensors. <b>SML TECHNOLOGIES</b> • Radar surveillance, navigation and safety systems for offshore platforms, naval, coastal and border surveillance and protection systems.	<b>DNE TECHNOLOGIES</b> • Military network communications equipment for voice, data, and video information. High-speed protocol converters and modems. <b>FLIGHTLINE SYSTEMS</b> • Sonobuoy telemetry receivers for maritime patrol aircraft and helicopters. Mechanical gyroscopes. Specialist military test equipment. <b>MARITIME SYSTEMS</b> • Passive sonobuoys and bathythermal buoys. Towed array sonars. High power sonar transducers. <b>OCEAN SYSTEMS</b> • Underwater acoustic countermeasures and systems. Torpedo defence systems. <b>SONAR &amp; COMMUNICATION SYSTEMS</b> • Active and passive sonobuoys. Sonobuoy receivers and acoustic processors for maritime patrol aircraft and helicopters. Ship sonar systems. Torpedo defence systems and countermeasures. Mine disposal systems. Submarine communication systems. Data link communication systems. Cryptographic equipment. <b>TACTICAL COMMUNICATION SYSTEMS</b> • High capacity, multi-channel line-of-sight radios and multiplexers. Electronic counter-counter measure radio systems. <b>UNDERSEA SENSOR SYSTEMS INC</b> • Active and passive sonobuoys. Advanced autonomous sensor systems for coastal surveillance.

• Businesses in the UNITED KINGDOM  
 • Businesses in NORTH AMERICA

2004 was a very positive year for Ultra; once again the Group achieved record sales and profit and the acquisitions made in the last few years made an important contribution to this success. Ultra again made good progress on its major development contracts and won several others which will materially broaden its technological base.

Sales at £320m grew 12.4%, with the Information & Power Systems division showing the strongest growth. Profit before tax and goodwill amortisation at £39.7m increased by 15.5% over the previous year despite the adverse impact on the translation of US profits of the weak dollar, which declined 10% against sterling. Earnings per share before goodwill amortisation, at 44.1p, increased at a similar rate to profit. The Board will be recommending a final dividend of 9.2p per share, making a total for the year of 13.8p, a 12.2% increase over 2003.

At the heart of Ultra's success is its investment strategy. The management has a real expertise in identifying investment opportunities that deliver growth, either within existing businesses or by acquiring businesses which complement and broaden the Group's portfolio of products and capabilities. During 2004, Ultra invested a total of £44m in acquisitions, research and development, capital expenditure and new business development. This investment contributed directly to the new contracts won in the year and underpins the Group's long-term positioning for future business.

After the significant investment in 2004, the company's net debt still decreased by £7m over the course of the year. Cash generation

continued to be strong in 2004, with a conversion percentage from operating profit\* of 111%. Over the last five years, the Group's average cash conversion is an impressive 106%.

The acquisitions made in 2003 have been fully integrated into the Group and the new acquisitions of DNE and Videcom in the year have met expectations and have also provided synergies to support other closely related businesses.

The order book stood at £395m at the year end, a record level. Importantly, the Group started 2005 with firm order cover for 60% of projected sales, a similar level of visibility to previous years.

Defence markets continue to hold up, particularly in Ultra's chosen niche areas, and the recent emphasis on security and surveillance activities continues. An encouraging sign for Ultra is the continuing recovery of the civil aerospace market which not only drives increased levels of production but also benefits the important aftermarket for sales of spares and repairs.

It is planned that Board changes will take place at the company's AGM in April; these were foreshadowed in announcements last year. I have been Chairman since December 1994 and intend to retire and to hand over to Dr Julian Blogh – he is currently Chief Executive and Deputy Chairman, but will become Chairman as from the AGM, relinquishing the Chief Executive's role. I believe shareholders share my and the Board's view that his record as Chief Executive has been outstanding and the

company will benefit significantly from his continued guidance in strategic matters.

It is also planned that Douglas Caster, currently Chief Operating Officer, will succeed Dr Blogh as Chief Executive. The Board has been strengthened since the year end by the appointment of a new non-executive director, Chris Bailey, who has recently retired as Finance Director of Aggregate Industries plc.

Looking ahead to 2005 and thereafter, the Board is confident that, despite a further impact of the continuing weakness of the US dollar, the outlook for the Group remains encouraging. Current market conditions, coupled with Ultra's ability to win new business and to execute contracts effectively, should enable the Group to continue its long-term record of profit and sales growth.

Finally, it remains for me to thank Ultra employees for their hard work, commitment and support. I have enjoyed my time with the Group immensely and it has been an exciting and rewarding ten years. I am confident the Group will continue to enjoy much success.

Peter Macfarlane, Chairman

\* before goodwill amortisation

\* operating profit after goodwill amortisation of £5.9m (2003: £4.9m). Operating cash flow after capital expenditure and Long-Term Incentive Plan share purchase



# achieving high quality growth



DURING 2004, ULTRA INVESTED A TOTAL OF £44 MILLION IN ACQUISITIONS, RESEARCH AND DEVELOPMENT, CAPITAL EXPENDITURE AND NEW BUSINESS DEVELOPMENT.

## Investment strategy

Ultra invests to broaden its portfolio of products and capabilities

Ultra made excellent progress in 2004, achieving high growth in sales and profits. The three acquisitions made in the second half of 2003 performed well and the Group's investment in two further acquisitions during 2004 strengthens Ultra's position in the growth sectors of battlespace IT and airport systems. In 2004 the Group underpinned its position in its key sonobuoy and civil aerospace activities with the signing of ten year sole source agreements. Ultra also won a broad range of new

contracts in 2004 that will support the continued progress of the Group.

### GROUP RESULTS

Sales increased to £320m, a rise of 12.4% over the prior year, and this was achieved despite the significant weakening of the US dollar. At constant currencies, sales growth reached 17%, of which 9% was organic. The main drivers of the organic increase were higher battlespace and airport IT activity and deliveries of equipment for military vehicles.

There was a further increase in the Group's operating margin\* to 13.3% (2003: 13.2%), driven mainly by a combination of increased volume, effective execution of development contracts and a continuing focus on cost control. Operating profit\* rose by 13.1% to £42.5m (2003: £37.5m), while profit before tax and goodwill amortisation increased by 15.5% to £39.7m (2003: £34.4m). A slightly lower effective tax rate\* for the Group of 26.0%, due partly to additional UK R&D tax credits, helped the Group achieve a 15.4%

\* before goodwill amortisation of £5.9m (2003: £4.9m)

## +12.4%

### Sales

Reflecting increased battlespace and airport IT activity and deliveries of equipment for military vehicles

increase in earnings per share\* to 44.1p (2003: 38.2p).

Operating cash flow\*\* was again excellent at £46.9m (2003: £48.3m). Conversion of operating profit\* to operating cash flow\*\* was 111%, giving an average conversion over the last five years of 106%. Net debt at the year end reduced to £23.2m (2003: £30.3m) despite investing £23.3m after expenses on two acquisitions during the year. In addition, the Group invested £20.7m (2003: £19.5m) in research & development, capital expenditure and new business development. Interest paid was covered 15 times by operating profit\*.

Ultra had net current liabilities at the year end of £33.9m compared with net current assets of £12.7m at the end of 2003. The Group's banking facility matures in December 2005, with £48.1m (2003: £nil) of the loan therefore falling due within one year. In preliminary discussions, all of the banks providing Ultra's existing facility have expressed a desire to participate in a future arrangement. The Board is confident that new funding arrangements will be secured in a timely manner.

There was a 5.4% increase in the Group's order book in the year, with a closing value of £395.4m, maintaining historic levels of firm order cover for the coming year and providing in total equivalent cover of approximately 14 months of future sales.

### INVESTING IN GROWING MARKETS

Ultra's continuing success is driven by its investment strategy. Ultra invests in order to deliver growth, either within existing businesses or through the acquisition of businesses that complement and broaden the Group's portfolio of products and capabilities. During 2004, Ultra invested

\* before goodwill amortisation

\*\* after capital expenditure and Long-Term Incentive Plan share purchase

## +15.5%

### Profits

Profits before tax and goodwill amortisation increased by 15.5% to £39.7m (2003: £34.4m)

£44.0m (2003: £37.8m) in acquisitions, research and development, capital expenditure and new business development. The benefits of such investments include a direct effect on the winning of new contracts in the year and also a contribution to the Group's long-term positioning for future business.

In Ultra's largest markets, the UK and US defence sector, there is a growing emphasis on electronic systems for military platforms, battlespace IT and homeland security. The businesses acquired by Ultra in recent years operate mainly in these growth sectors. Ultra is well placed to benefit from this market growth by continuing successfully to develop innovative solutions to meet customer needs.

In the civil air transport sector the recovery of the aftermarket and the increase in orders and production schedules for civil aircraft continues as passenger numbers rise. Demand for airport IT systems is seeing strong growth, driven by investment in new airport facilities both in the UK and overseas. In the UK rail sector, following recent rapid growth, activity is expected to reduce in 2005. Worldwide, however, investment in mass transit system infrastructure is increasing as a solution to urban congestion.

Ultra's confidence in its ability to deliver growth is underpinned by a number of key factors. The Group has achieved year-on-year success despite significant changes in foreign exchange rates and whilst experiencing full market cycles in both the civil aerospace and defence sectors. These risks will continue to be mitigated through robust business strategies. Further, Ultra has access to adequate financial and human

resources to implement its strategy for the foreseeable future.

### 2004 ACQUISITIONS

The Group made two acquisitions in 2004, DNE Systems Inc. ("DNE") and Videcom for a total cash cost of £23.3m, financed using Ultra's existing banking facilities.

DNE strengthens Ultra's tactical communications capability within the battlespace IT sector and is now part of the Tactical & Sonar Systems division of Ultra. Based in Wallingford, Connecticut, USA, DNE provides specialist equipment to facilitate the transmission of data over satellite and terrestrial radio links and to achieve interoperability between commercial and military communication interfaces for modern and legacy systems.

Videcom, now co-located at our facility in Loudwater, Buckinghamshire, UK, has a strong capability in airport IT systems and complements Ultra's product portfolio with flight check-in, aircraft passenger seat allocation, baggage reconciliation and departure control systems. The products are used in a wide variety of airports around the world and Videcom has a presence in the rapidly growing Chinese market. Ultra will benefit by offering the combined range of products to its airline and airport customers.

### AIRCRAFT & VEHICLE SYSTEMS

Aircraft & Vehicle Systems comprises five businesses in the UK and US that supply advanced technology products and software for military aircraft and land vehicles and also for civil aerospace markets.

Sales in the division increased by 2.6% to £81.9m (2003: £79.9m). Operating profit\*

# £395m

## Order book

Maintaining historic levels of firm order cover for the coming year

# 111%

## Cash performance

Operating cash flow\*\* was again excellent at £46.9m (2003: £48.3m). Conversion of operating profit\* to operating cash flow\*\* was 111%

# Success

Ultra's proven strategy underpins further progress for the Group

# +15.4%

## Earnings per share\*

Earnings per share\* was 15.4% higher at 44.1p (2003: 38.2p)

## THE GROUP'S INVESTMENT IN TWO FURTHER ACQUISITIONS DURING 2004 STRENGTHENS ULTRA'S POSITION IN THE GROWTH SECTORS OF BATTLESPACE IT AND AIRPORT SYSTEMS.

was £14.7m (2003: £13.9m) giving an operating margin\* of 17.9% (2003: 17.4%).

The continuing recovery in air travel since the terrorist attacks of September 2001 drove the launch of new aircraft development programmes, an increase in build rates on existing programmes and a rise in aftermarket support activity during 2004. An important achievement in the year was the selection of Ultra to supply two sub-systems on the Boeing 787 "Dreamliner" aeroplane. Ultra will be the integrator and supply the electronic controls for the system that provides electro-thermal ice protection for the wings of the 787. In addition, Ultra teamed with Goodrich to provide the proximity sensing equipment for the 787 passenger cabin, cargo and landing gear doors. Sales of these systems should commence in 2008, ahead of the 787 entering service in 2009.

Sales of Ultra's HiPPAG for the US Navy's F/A-18 E/F Super Hornet aircraft achieved record levels. The development of HiPPAG variants for use in the munitions ejection systems of both the US Small Diameter Bomb programme and the F-35 Joint Strike Fighter aircraft proceeded to plan.

In the US, Ultra is supplying its joysticks and related 'cockpit' equipment for a large number of different types of unmanned aerial vehicles and for many variants of vehicle within the Future Combat System programme. In the UK, deliveries to BAE Systems of the indirect vision equipment for the Engineer Tank System and development activity on the crew controls for the British Army's Terrier combat engineering vehicle progressed to plan.

### INFORMATION & POWER SYSTEMS

Information & Power Systems, with the integration of Videcom into the Airport Systems business, consists of seven businesses that supply information management and power products for defence, commercial and airport applications worldwide.

Sales increased in the division by 21.1% to £115.6m (2003: £95.5m) of which 12.7% was organic. Operating profit\* increased 34.6% to £14.8m (2003: £11.0m). The operating margin\* was 12.8%, an increase from 11.5% in the prior year.

The airport IT systems business achieved an excellent performance which contributed significantly to the growth of the division. Development work on the IT infrastructure for BAA's Terminal 5 at Heathrow Airport proceeded well and Ultra's flight information display system was selected by BAA to be used throughout all its operations. In the US, the airport IT system at Kansas City, for which Ultra is the integrator, neared completion and the installation of an integrated suite of airport IT at Oakland, California, provides another showcase for Ultra's systems integration capabilities. UltraTrak, the world-leading passenger baggage reconciliation system, was selected for all the international airports in New Zealand, building on the managed service provision now operating successfully at Heathrow and in Australia, as well as in the US.

The division benefited from a rise in government expenditure on battlespace IT which resulted in new sales and upgrades of the latest version of the ADSI data link processor and situational awareness system. Radar coastal surveillance system

contracts were secured in the UAE and for commercial ports in the US to improve homeland security. There was a high level of contract manufacturing activity where deliveries of battlespace IT equipment for the British Army Bowman programme also increased.

Rolls-Royce placed an important order for the development of a replacement control system for the nuclear reactors that power the Royal Navy's submarines. In the medium-term, this is expected to lead to further orders for production and long-term support.

### TACTICAL & SONAR SYSTEMS

Tactical & Sonar Systems, with the addition of DNE, comprises seven businesses in the UK and North America that supply tactical communications and underwater warfare equipment to military users worldwide.

Sales in the division increased to £122.1m from £109.0m in 2003, a rise of 12.0%. Operating profit\* increased 2.7% to £13.0m (2003: £12.7m) giving an operating margin\* of 10.7%. At constant currencies the sales growth was 19.9% and the operating profit\* growth was 19.2%.

As anticipated, the level of sales of sonobuoys in the year was broadly unchanged from 2003. Sales of anti-submarine warfare mission system equipment were also flat as deliveries to the RAF Nimrod programme ended. One of the highlights of the year was securing a long-term, sole source partnering contract with the UK Ministry of Defence for the supply and support of all the UK's sonobuoys. Ultra's dominance of the sonobuoy export market continued with exports to France, Canada, Australia and Korea.

The Group's Surface Ship Torpedo Defence system entered service with the Royal Navy on schedule during the year and a contract for a torpedo defence technology demonstrator programme for the US Navy was also secured. Both Lockheed Martin and General Dynamics have selected Ultra's torpedo defence system for the US Navy's Littoral Combat Ship.

Sales of battlespace IT equipment contributed to the growth of this division, with deliveries of high capacity radios to the US Army for its Patriot missile defence systems and network access equipment for all the US armed services. The award to Ultra in the UK of a contract from the US Navy for the development of specialist cryptographic equipment is expected to contribute to future growth as contracts for production items are secured. This is the first time the US government has contracted offshore for the development of such equipment.

### MANAGEMENT CHANGES

As noted in the Chairman's Statement, it is planned that the management changes described last year will come into full effect after the Annual General Meeting on 22 April 2005. Peter Macfarlane will retire from the Board at that time, having been Chairman since 1994, and I will take over the role. On behalf of the Board I thank Peter for his excellent contribution to the development of Ultra, and we wish him well in his retirement. Douglas Caster, currently Chief Operating Officer will succeed me as Chief Executive.

### PROSPECTS

In Ultra's main defence markets, expenditure is increasing on battlespace IT to enable better

situational awareness, quicker command and control, and the synchronisation of military effects with much improved accuracy. Modern armed forces must be equipped to allow the rapid deployment of light, mobile troops and to be able to exploit superior intelligence of the military situation through the use of battlespace IT.

The perceived terrorist threat to individuals and to economically important assets together with the need to protect borders and coastlines from illegal immigrants and smugglers are driving an increase in global demand for surveillance and enforcement systems.

With its range of niche businesses, Ultra is well placed to benefit from these market forces.

In civil markets, aerospace is continuing to recover with both Airbus and Boeing forecasting increased build rates, leading to further growth in original equipment sales and after-market support. The growth in air traffic is strong, driving new airport construction and refurbishment with increasing demand for airport IT systems. Investment in rail transport and mass transit systems that require specialist power equipment continues, although in the UK this will be at a lower level than experienced in recent years.

Following its successful 2004, Ultra enters 2005 with a strong balance sheet and a record order book. Its proven strategy of providing niche products, being a responsive and competent supplier and achieving growth, both organically and through acquisition, underpins further progress for the Group. Ultra's investment in new

products and in the acquisition of complementary businesses is expected to be funded from internal cash generation, unless a truly compelling acquisition opportunity demanding additional finance arises. The Board's prime objective is to outperform the market in terms of annual increases in shareholder value by delivering above average annual increases in earnings.

The outlook for the Group remains encouraging although in 2005 there will be some impact on sales and profit due to the weakness of the US dollar. However, current market conditions together with recent acquisitions and contract awards provide the foundations for future growth. The Board has confidence in the continued progress of the Group in 2005.

Julian Blogh, Chief Executive

# Outlook

Current market conditions coupled with recent acquisitions and contract awards provide the foundations for future growth

\* before goodwill amortisation

\*\* after capital expenditure and Long-Term Incentive Plan share purchase

\* before goodwill amortisation of £5.9m (2003: £4.9m)



# achieving success on major programmes



Ultra will supply equipment worth about \$100,000 on each Boeing 787 aircraft



Image courtesy of Boeing

## ULTRA WILL PROVIDE A NEW APPROACH TO WING ICE PROTECTION THAT INCREASES THE EFFICIENCY OF THE BOEING 787 "DREAMLINER" AIRCRAFT.

Ultra derives a long-term benefit from its single source position on programmes and platforms. Typical project lifecycles can exceed fifty years. In 2004, Ultra was successful in positioning its unique products, services and systems on a number of key new programmes.

Ultra was selected by Boeing to supply key elements of the Wing Ice Protection System (WIPS) on its new 787 "Dreamliner" aircraft, for which over 140 orders were booked by the end of 2004. Ultra will be the system integrator for WIPS which provides a new approach to wing ice protection that increases the operating efficiency of the aircraft. Ultra leads a team including GKN Aerospace and Thermion Systems that has been working with Boeing for over two years to demonstrate that Ultra's innovative solution meets Boeing's demanding requirements.

Ultra's success with WIPS on the 787 aircraft adds to Boeing's earlier selection of a team of Goodrich and Ultra to supply the proximity sensor system for the same aircraft. This system monitors the position of the aircraft's doors, thrust reversers and landing gear. Combined with WIPS, the value to Ultra for each 787 aircraft is about \$100,000.

The successful reputation of Ultra's innovative HiPPAG airborne compressor continues to be enhanced. The Lockheed Martin programme director for a missile development programme said "We selected Ultra to provide critical cooling for the seeker because HiPPAG has a proven track record and offers a low-risk, affordable solution". In this application, HiPPAG will generate a constant supply of pure air to cool the infra-red seeker in the

nose of the missile. This track record of success comes from HiPPAG's position on aircraft such as the US Navy's F/A-18E/F Super Hornet where the in-service performance of HiPPAG in recent and continuing operations has been exemplary. Ultra continued through the year to develop a variant of HiPPAG for Boeing's Small Diameter Bomb programme for which it will provide the permanently available energy source for launching smart or individually targeted munitions.

In modern warfare, there is an increasing focus on the use of unmanned vehicles for air, land and sea operations. However, these vehicles still need to be controlled. Throughout 2004 Ultra has continued to upgrade its advanced ground based cockpit control system for the Predator B unmanned air vehicle. This 'virtual cockpit' incorporates a number of Ultra's new and innovative technologies that improve the human-computer interface and make piloting the Predator easier. Many similar products have also been adopted for use on the various armoured vehicles within the US Army's Future Combat System programme.

Ultra has been selected to develop advanced electronic control systems for new armoured vehicle turrets being designed by CTAI, a joint venture company owned by BAE Systems and by GIAT in France. Ultra's success was aided by the excellent reputation that the Group has achieved in delivering a range of equipment for the UK Bowman communications programme.



Ultra provides the Predator B 'virtual cockpit'



Ultra equipment is fitted to modern armoured vehicles



Ultra's HiPPAG is fitted to F/A-18 aircraft

Image courtesy of US DoD

## Highlights

Within Ultra's aircraft and vehicle systems activities, successes in 2004 included the following

- Long-term agreement with Airbus extended to secure Ultra's position on single-aisle and long-range aircraft for at least 10 years
- Ultra's Internet-based collaborative working environment endorsed by a contract from the UK Government Communications Head Quarters
- Ultra's innovative 'virtual cockpit' for the Predator B unmanned aerial vehicle provides realistic responses to 'pilot' inputs
- General Dynamics, Boeing and United Defense all selected Ultra equipment for the US Army's Future Combat System programme
- Ultra supplies equipment worth over £200,000 on every Eurofighter 'Typhoon' aircraft

# achieving success through effective solutions

Ultra has a presence in the vibrant Chinese market for airport IT systems



Ultra provides oilfield surveillance systems



Ultra's enhanced Magicard ID printers



Ultra's coastal surveillance systems

## CONTRACTS WON BY ULTRA IN 2004 DEMONSTRATE CUSTOMER CONFIDENCE IN THE GROUP'S ABILITY TO DELIVER EFFECTIVE SOLUTIONS AROUND THE WORLD.

Ultra's advanced integrated Information Technology systems support the efficient and safe operation of modern airports worldwide. With passenger numbers rising, many airports are upgrading their systems to cater for the increase in traffic. In 2004, Ultra's airport IT business continued the strong growth that was evident in 2003.

Ultra successfully operated its UltraTrak passenger baggage reconciliation and matching system at London's Heathrow airport throughout 2004, meeting the required availability and reliability levels whilst handling over 25 million items of baggage. Building on this success, Ultra delivered an UltraTrak solution for a number of different airports in Australia and was then selected later in the year to supply a similar service for several international airports in New Zealand. These wins demonstrate customer confidence in Ultra's ability to deliver effective solutions around the world.

In 2004, Ultra acquired the airline and airport IT systems business of Videcom. This broadened Ultra's range of products and applications in the sector and widened the geographic spread of the customer base. Videcom brought to Ultra a successful operation in the vibrant Chinese market. With the enhanced range of offerings, Ultra is better able to address the growing need for flexible airport IT check-in and support systems that can be shared between a number of different airlines, including start-up, low cost operations. Demonstrating the successful integration of the enlarged business, the first contract utilising the combined capability was won for Montgomery Airport in the US only three months after the acquisition.

Airports are complex operations and a continuing focus on safety and security is required. In addition to the security derived from the positive matching of passengers and baggage, achieved through the use of UltraTrak, vigilance must also be exercised on access control and surveillance systems. Ultra was selected in 2004 to supply a combined radar and electro optical surveillance system for a major US airport. Ultra is able to provide either a local solution such as this or a much larger integrated coastal and border system, as demonstrated by the Group also winning a contract to supply a system linking over 20 radar sites in a Middle Eastern country.

Ultra has a world leading ability to provide highly cost effective surveillance systems able to detect very small targets using commercial radar sensors. Global demand for such solutions is increasing, driven by the need for military security or by the desire to protect, and to maintain the safe operation of, economically important assets such as oilfields and fishing areas.

Ultra's Magicard range of ID card printers are used extensively as part of access control systems. Controlling access to sites is a key contributor to personal safety. In 2004, Ultra's range of Magicard printers was augmented and new models introduced that provide additional features whilst continuing to offer as standard Ultra's unique holographic anti-counterfeiting technology. The new printers allow ever-smaller organisations to afford an access control and security solution using customised ID badges for all authorised personnel.



## Highlights

Within Ultra's information systems activities, successes in 2004 included the following

- Rolls-Royce awarded Ultra a contract to develop a new high-integrity control system for nuclear reactors for Royal Navy submarines
- The latest software upgrade for Ultra's ADSI® product was successfully certified, triggering an increase in sales of upgrades
- Ultra's world-class tactical data fusion product, ADSI®, is being developed for airborne applications, thereby increasing its potential market
- BP selected Ultra to supply a radar surveillance system to enhance safety at its operations in the North Sea
- Ultra has invested in quadrupling the capacity of its contract electronics manufacturing activity in the last two years



# achieving success through exploiting technologies



Ultra's modelling capability optimised the design of a ship's de-magnetising system



## THE USE OF ULTRA'S MODELLING CAPABILITY RESULTS IN A SYSTEM THAT IS LIGHTER AND MORE COST-EFFECTIVE THAN PREVIOUSLY POSSIBLE.

Ultra successfully shares technologies between the US and the UK. In its naval electrical power businesses, for example, the ability accurately and quickly to model a ship's magnetic signature during the design phase has been transferred from the UK to the US. Consequently, whether a new ship is being designed in the US or the UK, Ultra personnel can work alongside the ship's design team concurrently to optimise the vessel's signature and the associated control system. Uniquely, Ultra is able to take responsibility from the outset of the project for achieving the predicted signature levels.

Ultra's modelling capability and the resulting installed system maximise the protection of the ship from magnetically triggered mines. This is especially important as modern conflicts are increasingly likely to require naval operations in shallow, cluttered coastal waters where the mine threat is at its highest. The use of this modelling capability also results in a system installed on board that is lighter and more cost effective than previously was possible.

Ultra's ability to provide its customers with the maximum 'stealth' for its ships has helped successfully to position the Group on a number of key programmes. In the US, Ultra is working both on the Deepwater coastguard vessel programme and on the Littoral Combat Ship, a design specifically intended to support shallow water operations. This success extends internationally with a position on a new Spanish naval vessel, the BPE amphibious assault ship.

Ultra's technologies transfer both ways across the Atlantic. Key elements of the signature management equipment supplied in the year for the Royal Navy's new Type 45 destroyer were designed and built by Ultra in the US. Conversely the Group achieved a breakthrough in 2004 with its UK submarine electrical power management technology being purchased for the US Navy's USS Dolphin submarine.

In the UK, Ultra is developing an innovative electric start system for ships' gas turbines. This is being developed to meet the similar needs of both the Royal Navy and the US Navy.

In 2004, Ultra delivered the fourth boat set of specialised power equipment for the Virginia class of submarine, the first of which entered service with the US Navy in the year. Reflecting Ultra's success on the programme, a multi-year contract was negotiated, covering the equipment for an additional five boats. This arrangement improves the visibility of business for Ultra on the Virginia class submarines, for which further boats are planned.

## Highlights

Within Ultra's power systems activities, successes in 2004 included the following

- As London's Docklands Light Railway is extended, Ultra provides more of its specialist transit system power supplies
- Ultra will supply the de-magnetising system for the UK's new aircraft carriers and will work with the ship designers to optimise the system
- Investment in Network Rail's Southern Region power supplies is now a continuing process of "asset renewal"
- In 2004, Ultra delivered its specialist naval power supplies for the fourth US Navy Virginia and for the third Royal Navy Astute submarines
- Ultra's new electric starting system for naval gas turbines successfully completed initial testing during the year



Image courtesy of US DoD

Ultra is developing equipment for the US Navy LCS programme



Image of USS Dolphin courtesy of US DoD

Ultra supplies power equipment for submarines



Image courtesy of BAE Systems

Ultra's equipment de-magnetises the Type 45 destroyer



# achieving successful network solutions



Ultra supplies equipment to improve the efficiency of military satellite data links



Image courtesy of US DoD

## ULTRA PROVIDES A WORLD CLASS CAPABILITY TO FUSE TOGETHER INPUTS FROM MANY DIFFERENT MILITARY SENSORS AND DATA LINKS.

In modern day conflicts, the side that most successfully manages the timely flow of high-quality battlespace information is likely to have a decisive edge. Ultra is constantly investing to create new battlespace IT products that help deliver that advantage.

Ultra's integrated microwave trunk radio systems are an essential component of the battlespace network. They provide secure telephone and high capacity data communication services to battlefield commanders. Ultra is continually developing its range of radios to increase the capacity and security of the network. Just as in the commercial IT world, the capabilities of the tactical communication system must constantly be increased to provide the bandwidth for a broader range of data including email and near-real time video. Unlike commercial systems, however, military communication systems must move quickly as the front line moves and the battle develops. The speed with which a radio relay terminal can be set up is vitally important and special operator features on Ultra radios allow the rapid and reliable creation of a dependable link.

Ultra's 2004 acquisition, DNE, based in Wallingford, Connecticut, USA, designs, manufactures and supports battlespace IT products that control access to military tactical communication networks. DNE's products allow information to be shared across multiple battlespace IT networks, including legacy systems. Whilst the most advanced military communication networks provide an ever-broader range of capabilities, these must still interoperate with older

systems that may use different data formats, including those used by allied and coalition partners. DNE's protocol converters, voice and data multiplexers and multi-service access concentrators allow this to happen.

DNE's products are another key link in the communication chain that includes Ultra's tactical radio systems. Key information carried on the network includes the tactical battlespace picture. Ultra's ADSI® product provides a world class capability to fuse together the inputs from many different military sensors and data links in order to display a real-time view of the tactical battlespace.

Much of the real-time information is gathered by sensors mounted on unmanned aerial vehicles. Ultra specialises in data links both to allow the simultaneous control of multiple remotely piloted vehicles and also to transmit securely and robustly battlespace information from aircraft to ground based receiving equipment. DNE provides a broad range of data switches which are used extensively at such ground stations.

To be tactically useful, communication must be secure. Ultra has a world class cryptographic capability and in 2004 received a development contract for a new system from the US Navy, a significant win in that it was awarded offshore and one that has substantial potential. This award emphasises the Group's ability to offer tactical communication solutions to satisfy current and future NATO interoperability and battlespace IT requirements.

## Highlights

Within Ultra's tactical systems activities, successes in 2004 included the following

- Ultra's innovative data link management and encryption system will be used on Canada's new maritime helicopter
- Ultra is developing faster versions of its tactical military line-of-sight radios to provide users with a higher capacity system
- Ultra's tactical communication network access equipment has been used extensively in recent and continuing military operations
- Ultra is developing an innovative system to allow submerged submarines to communicate above water without compromising stealth
- The US and South Korean armies are upgrading their communications infrastructure with Ultra radios and placed contracts in the year



Image courtesy of US DoD

Ultra supplies high-capacity tactical radio systems



Ultra's ADSI® in operational use



Ultra's data links control unmanned vehicles



# achieving success by delivering on schedule



Ultra's torpedo defence system entered service with the Royal Navy in 2004



## ULTRA HAS DEMONSTRATED ITS ABILITY TO WIN AND SUCCESSFULLY EXECUTE CONTRACTS FOR SYSTEMS OF EVER-INCREASING SIZE.

In 2004, Ultra's Surface Ship Torpedo Defence (SSTD) system entered service with the Royal Navy, on schedule. Ultra successfully developed this complex system in less than three years. Utilising a suite of advanced sensors towed behind the vessel, SSTD detects and locates incoming torpedoes, gives tactical advice on ship manoeuvres and provides capabilities to decoy or defeat the torpedo threat. A key feature of the SSTD design is its stand-alone nature which makes it easy to transfer from ship to ship in a fleet. This also enhances the system's export potential including the possibility of being retrofitted to existing ships.

Ultra's SSTD solution is simple to deploy and to operate – important attributes for a key element of a ship's defensive suite. In sea trials, the in-water elements of SSTD proved to be easy to handle when being launched and brought back on board in heavy sea states, greatly enhancing its utility as a protective system for use in all weathers.

Ultra's success in entering service on schedule with SSTD reflects the Group's ability to win and successfully to execute contracts for systems of ever-increasing size. Ultra managed a team involving a number of international defence equipment subcontractors.

Also in 2004, Ultra was selected by the US Navy for a development contract relating to an advanced torpedo defence system to protect its surface fleet. This contract was won by Ultra's Ocean Systems business that was acquired in 2003. This award demonstrates the success of Ultra's acquisition strategy as Ocean Systems is able to take full advantage

of the work to date on the UK SSTD programme and so can now deliver a solution optimised for the particular needs of the US Navy. Ultra is a world market leader in specialist areas of underwater battlespace equipment, supplying towed and expendable torpedo countermeasures to the UK, US, Canadian and Australian navies.

In Ultra's traditional market for airborne Anti-Submarine Warfare (ASW) systems, some key milestones were reached. In the UK, the Nimrod MRA4 aircraft flew for the first time. This ASW aircraft is to be fitted with a broad range of Ultra equipment as part of its mission equipment and deliveries of these systems continued in 2004. At the platform level, both the US, with its Boeing MMA fixed wing programme, and Canada, with its selection of Sikorsky to supply its MHP helicopter solution, committed to procuring new ASW assets. In the US and Canada, Ultra worked throughout 2004 positioning its ASW mission equipment for these new platforms.

Ultra's manufacture of sonobuoys, the expendable acoustic sensors used in ASW systems, was marked by consistently excellent quality levels in both the US and the UK. Reflecting Ultra's continuing record of success in the UK market, the MoD awarded the Group in 2004 a long-term partnering contract for the supply and support of sonobuoys. This is a sole-source agreement under which Ultra will satisfy all of the MOD's requirements for an initial period of ten years.

## Highlights

Within Ultra's sonar systems activities, successes in 2004 included the following

- Ultra successfully completed a series of trials of a remotely operated mine destruction system for the Royal Navy
- In 2004, Ultra delivered advanced development models of a distributed autonomous underwater sensing system
- Ultra delivered a new sonar-based system to deter fish from congesting water inlets of hydro-electric power stations
- In the UK, Ultra demonstrated the feasibility of an enhanced anti-submarine warfare capability for maritime patrol aircraft
- Ultra sold its range of active and passive sonobuoys in 2004 to the US, UK, Australia, Canada, France, and Korea



Image courtesy of Boeing

Ultra provides equipment for modern ASW aircraft



Image courtesy of US DoD

Ultra provides equipment for modern ASW helicopters



Image courtesy of BAE Systems

Ultra's equipment is fitted to the new MRA4 ASW aircraft



# sales rose by 12.4% to £319.7m, with strong cash generation



ULTRA CONTINUED TO ACHIEVE STRONG GROWTH IN 2004. ORGANIC SALES INCREASED AT CONSTANT EXCHANGE RATES BY 8.7%, WITH AN ADDITIONAL 8.3% COMING FROM ACQUISITIONS.

## Organic growth

Ultra's acquisitions have all been funded by internally generated cash and so may be considered organic

### TRADING RESULTS

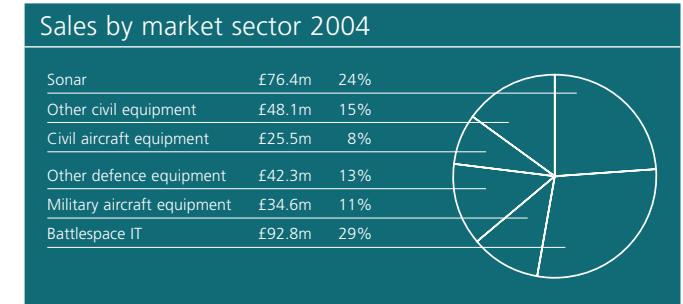
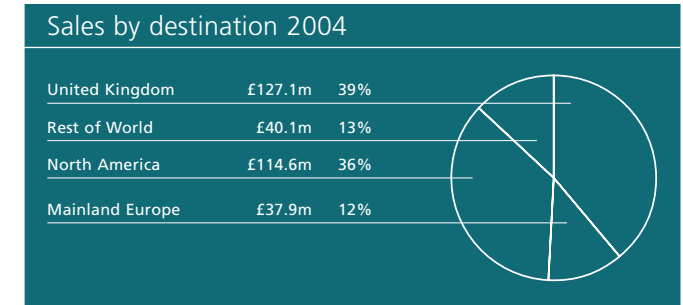
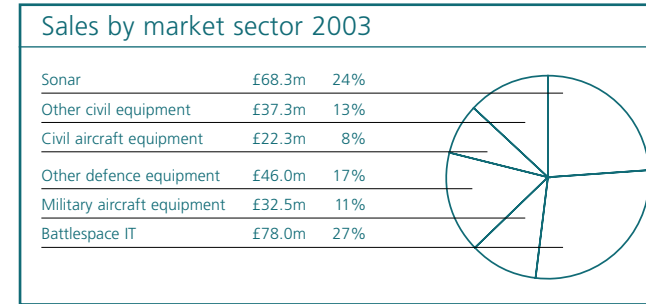
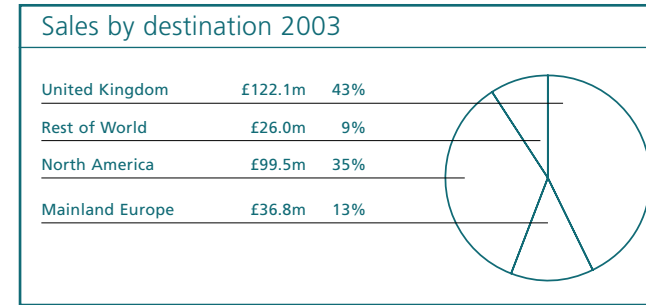
Ultra continued to achieve strong growth in 2004. Organic sales increased at constant exchange rates by 8.7%, with an additional 8.3% coming from acquisitions. However, since all of the Group's acquisitions have been funded by internally generated cash, they may also be regarded as organic. This excellent underlying performance was partly offset by the translation and transaction effects of the weaker US dollar, which reduced sales growth by 4.6% altogether, equivalent to £13.0m.

Hence, in sterling, the actual growth in Group sales was 12.4%. Group turnover was £319.7m, compared to £284.4m in 2003.

Operating profit\* rose by 13.1% to £42.5m (2003: £37.5m), equivalent to an operating margin\* of 13.3%, up from the 2003 result of 13.2% and maintaining the upward trend. This excellent level of profitability was achieved despite negative currency effects and continuing downward market pressures on selling prices. Foreign currency factors

reduced operating profit\* by £3.3m; at constant exchange rates growth would have been 8.8% higher.

Sales to North America continued to grow and represented 36% of annual turnover (2003: 35%), despite the weakening in the US dollar. Recent acquisitions Ocean Systems and DNE were partly responsible for this growth, but it was encouraging to see existing businesses such as Advanced Programming Concepts and UnderSea Sensor



Systems Inc. growing strongly. The latter business saw domestic sonobuoy sales recover from a low level in 2003, although total sonobuoy sales reduced slightly.

The proportion of Ultra's sales in the UK reduced from 43% to 39% in the year, but we still recorded a 4% increase in domestic revenues. Amongst the fastest growing UK businesses was Airport Systems with higher activity at London's Heathrow airport. Manufacturing & Card Systems saw a strong performance in its UK contract manufacturing business unit, especially on equipment for the British Army's Bowman communication system.

The biggest increase occurred in sales to the rest of the world, representing 13% of turnover, notably to the Middle East and the Pacific Rim countries. 2003 acquisitions were important contributors, with sales by SML Technologies of radar surveillance systems to the Middle East and deliveries by Ocean Systems of underwater countermeasures to Australia. Sonobuoy sales to Australia increased, as did revenues from Africa and the Far East for Airport Systems.

Ultra's exports to Continental Europe rose but this market reduced in significance from 13% to 12% of sales.

Sales of battlespace IT equipment grew from 27% to 29% of Group turnover in the year. This was despite the impact of the weaker US

dollar; the majority of sales in this area come from Ultra's North American businesses. DNE, acquired during the year, contributed to the increase. Sales of sonar and underwater defence systems increased to £76.4m, 24% of the total, driven by Ocean Systems' acoustic countermeasures and torpedo defence equipment. These compensated for the small overall reduction in sonobuoy sales. Military aircraft equipment sales, primarily for Eurofighter and F/A-18 E/F, increased so as to maintain an 11% share of revenues. As other areas increased in value, sales of other defence equipment dropped to 13% of turnover. Defence activities represented 77% of overall sales, a shift from 79% the previous year owing to the higher rate of growth in the Group's civil activities.

In the civil sector, aircraft equipment sales increased to £25.5m to maintain their 8% share of Group turnover, but other civil sales increased to 15% (2003: 13%). This was due to strong sales of IT systems for airports and high contract manufacturing activity for electronics equipment producers in the UK. Civil activities were 23% of total sales in the year.

### INTEREST AND PROFIT BEFORE TAXATION

Interest costs reduced by £0.4m to £2.8m, due to lower interest rates and the unwinding of the fixed interest rate hedging contract to which the Group committed in 2000. The amount of debt on which Ultra

has been paying a high 7.5% interest rate reduced by £12m to just £15m from April 2004 onwards. The hedging contract will mature in April 2005. The reduction in borrowing costs, together with the 13.1% improvement in operating profit\*, combined to give an excellent 15.5% growth in profit before tax and goodwill amortisation, to £39.7m (2003: £34.4m). The interest charge was covered 15.2 times by operating profit\*. Amortisation of goodwill rose by £1.0m to £5.9m, which reflected a full year's charge for the 2003 acquisitions and a partial charge for those acquisitions that took place in 2004. Profit before tax was therefore £33.8m (2003: £29.5m), an increase of 14.6%.

### ACQUISITIONS

Ultra made two acquisitions in July 2004. DNE was acquired for \$40.4m (£22.3m) and Videcom for £1.5m, both including expenses. The cash payments made during the year were £23.3m, lower than the total costs shown above, because of deferred expenditure. Both of these businesses are trading in line with expectations and made a positive contribution to Group profits after goodwill amortisation. The goodwill arising from these acquisitions was £21.1m. It was capitalised at the time that the transactions took place and amortised during the last five months of the year at a rate consistent with a twenty-year life.

\* before goodwill amortisation of £5.9m (2003: £4.9m)

\* before goodwill amortisation of £5.9m (2003: £4.9m)

## ONCE AGAIN CASH GENERATION WAS EXCELLENT DURING THE PAST YEAR AND THIS IS A DIRECT CONSEQUENCE OF THE EMPHASIS THAT ULTRA GIVES TO CASH MANAGEMENT.

### Headroom

Ultra's strong balance sheet gives headroom for further investments and acquisitions

### £36.0m

Free cash flow\*\*  
In 2004, Ultra's free cash flow\*\* was £36.0m, a new record level

#### EARNINGS PER SHARE AND DIVIDENDS

The effective tax rate on profit before goodwill amortisation decreased slightly to 26.0% (2003: 26.4%) and earnings per share\* rose by 15.4% to 44.1p (2003: 38.2p). The directors are proposing a final dividend of 9.2p, bringing the total dividend to 13.8p (2003: 12.3p), an increase of 12.2%. The full year dividend is covered 3.2 times by earnings per share\*, which reflects the Group's policy of strong dividend cover.

#### CASH FLOW AND BORROWINGS

Once again cash generation was excellent during the past year and this is a direct consequence of the emphasis that Ultra gives to cash management. Operating cash flow after capital expenditure and LTIP share purchases was £46.9m, which represents an operating profit\* to cash conversion ratio of 111%, bringing the average rate over the past five years to 106%. Effective management of working capital is the main reason for this achievement; overall there was a reduction of £4.8m. Although we saw stocks and debtors increasing by £2.2m and £1.7m respectively, due to growth in trading activities, creditors and provisions for liabilities and charges rose by £8.6m in total. Average creditor days rose to 51 days (2003: 43 days), slightly above the 47 day average over the last five years. There was a £5.2m investment in fixed assets during the year, virtually in line with the £5.1m depreciation charge. There were no major capital projects during the year and the bulk of this expenditure went on upgrading the IT infrastructure. In addition £1.1m was spent on buying Ultra shares for the directors' Long-Term Incentive Plan. Free cash flow\*\* was £36.0m (2003: £35.7m), a new record level. After spending of £23.3m

\* before goodwill amortisation of £5.9m (2003: £4.9m)

on acquisitions, together with £8.5m of dividends, net debt was reduced by £7.1m to close the year at £23.2m (2003: £30.3m). The balance sheet was very strong with a net debt:equity ratio of 29%, which leaves Ultra with substantial headroom on its banking facilities to make further acquisitions.

#### FINANCIAL RISK MANAGEMENT

Ultra's financial instruments, other than derivatives, comprise borrowings, cash and trade funding consisting of debtors, creditors and customer advances. Group policy prohibits speculative transactions and no trading in financial instruments is undertaken. Treasury policies are determined by the Group Finance Director and agreed by the Board. They are reviewed regularly to ensure that they remain appropriate.

#### FINANCING

Ultra's existing operations and new acquisitions are financed through a mix of retained cash and bank borrowings. The Group took out an £80m three-year revolving credit facility in 2002 with a small syndicate of banks, led by The Royal Bank of Scotland plc. The facility is denominated in sterling together with US and Canadian dollars and is used for balance sheet hedging and operational needs. Both the sterling and US dollar elements are used to fund day-to-day working capital requirements. The US and Canadian dollar borrowings provide hedges for assets denominated in those currencies. A further £10m overdraft is also available for short-term working capital funding. The facility is due for renewal in December 2005 and preliminary discussions have taken place with the syndicate members regarding new financing arrangements, to take effect at that

\*\* after purchase of LTIP shares but before dividends, acquisitions and financing

time. All of the existing banks have expressed a preliminary interest in participating in a future facility, although formal negotiations have yet to take place. The Board is confident that new funding arrangements can be secured well before the end of 2005. At 31 December 2004, 69% of total debt was at floating rates after taking account of the interest rate hedge, which applied to the first £15m of debt.

#### FOREIGN CURRENCY

Ultra's reported financial results are influenced by movements in exchange rates and the overall impact is a combination of currency translation and currency transaction effects. The biggest sensitivity is to the US and Canadian dollars.

The average rates used in the year to translate the sales and operating profits of Ultra's American and Canadian subsidiaries into sterling weakened by 10% for the US dollar, and 4% for the Canadian dollar, compared to 2003. For the Group as a whole, currency translation effects reduced sales by £9.2m or 3% and operating profit\* by £1.0m or 2%.

Some of Ultra's businesses in the UK and Canada also make sales in foreign currencies, mainly US dollars. When the US dollar weakens against local currencies this means that turnover suffers from a negative currency transaction effect. This is partly relieved by sourcing materials in US dollars, thus reducing the overall net exposure to currency fluctuations. The Group policy is to hedge the net exposure on orders in hand using forward foreign exchange contracts, typically extending 18-24 months. Exposure to other currencies is hedged as it arises on specific contracts. Based upon the combined

\* before goodwill amortisation of £5.9m (2003: £4.9m)

## +12.2%

#### Dividend

A total dividend increase of 12.2%, covered 3.2 times by earnings per share\*

## Growing markets

Ultra's sales to North America continued to grow in 2004 as did the Group's battlespace IT activity

net exposure of about US \$70m last year, Group sales in 2004 would have been approximately £3.8m or 1% higher had the overall hedged rate remained unchanged from the previous year. Operating profit\* on the same basis would have been £2.3m or 5% higher. Ultra's effective US dollar:sterling rate for 2005, based upon the forward contracts currently in place, is expected to be approximately \$1.70.

#### PENSIONS

In the UK, Ultra offers company-funded retirement benefits to all its employees. These benefits comprise a combination of defined benefit and defined contribution schemes, with most staff still participating in the Ultra Electronics Limited defined benefit scheme. This scheme was closed to new entrants in 2003 and all new joiners are invited to become members of the Ultra Electronics money purchase scheme. The defined benefit scheme was actuarially assessed in April 2004, when its funding level was 97% of the Minimum Funding Requirement. The UK Financial Reporting Standard 17 valuation of the scheme at the end of 2004 showed a deterioration compared to December 2003, with a net deficit of £27.1m (2003: £19.3m), after deducting the associated deferred tax asset. This deterioration occurred despite the Stock Market recovery during the year, and was due to using more conservative valuation assumptions, notably longer life expectancy. The scheme is relatively immature, with just 14% of the members already retired, and remains strongly cash positive. In order to maintain the scheme's financial strength, Ultra has committed to increase its contributions from 15% of pensionable pay to 18% by 2007, a total increase of

approximately £0.7m per annum. Ultra's US subsidiaries and Maritime Systems in Canada operate defined contribution schemes and employees at Tactical Communication Systems participate in a limited defined benefit scheme. There was an FRS17 £1.0m deficit on the Tactical Communication Systems scheme at the end of 2004. This will be eliminated over the next ten years by increasing the company contributions by an amount that has been agreed with the scheme actuaries.

#### INTERNATIONAL ACCOUNTING STANDARDS

As a company listed on the London Stock Exchange, Ultra is required to report its statutory results from 2005 onwards under International Accounting Standards. The first report to be affected will be the interim results, due to be published in August 2005. The Group is well advanced in preparing for the changeover to the new standards and has compiled its 2005 budget on the new basis. It is planned to reissue the 2004 results, restated for International Accounting Standards, during the second quarter of this year. This will provide a set of comparative numbers against which the 2005 results can be compared.

David Jeffcoat, Finance Director and Company Secretary



# Ultra is a responsible citizen

ULTRA BELIEVES THAT IT SHOULD AT ALL TIMES BE A RESPONSIBLE CORPORATE CITIZEN AND THAT THIS CONTRIBUTES TO ULTRA'S LONG-TERM SUPERIOR BUSINESS PERFORMANCE. ULTRA'S POLICIES RELATING TO ITS CORPORATE RESPONSIBILITY ARE ESTABLISHED BY THE BOARD WITH INDIVIDUAL BUSINESSES TAKING RESPONSIBILITY FOR THEIR IMPLEMENTATION.



Ultra believes that it should at all times be a responsible corporate citizen. As such the Group complies with all applicable legislation in the areas of trading, employment, health and safety and the environment. Ultra further believes that, in order to achieve superior business performance, the Group must, in certain areas, exceed the minimum standards required by law. Ultra's policies relating to its corporate responsibility are generally established by the Board with individual businesses taking a major role in their implementation. The policies are discussed below.

## CUSTOMERS

### Business ethics

Ultra requires that the Group's employees comply with the laws and standards of conduct of the countries in which it does business as well as behaving ethically and with fairness. Directors and employees are required to avoid personal conflicts of interest regarding company business.

In addition, all businesses are strictly required to comply fully with the relevant national export control regulations.

### Customer relationships

Ultra promotes good working relationships with all our customers with a special emphasis on "meeting our commitments". The Group receives direct feedback on relationships from customers such as BAE Systems where Ultra is a member of the Major Equipment Supply Programme (MESP) and from UK MoD Supplier Relations Group. These relationships are also regularly recognised by other customers across the range of Ultra businesses through feedback and award processes.

For example, in 2004 Controls received a prestigious award from Airbus in recognition of being rated by airline operators as one of the top ten suppliers of equipment on Airbus aircraft. Also during 2004, recently acquired DNE received "Best Value Gold Medallist" recognition from the Defense Supply Center Richmond, Virginia, while Measurement Systems Inc. received a Raytheon STARS Outstanding Vendor Award in recognition of exemplary performance, high quality standards, and the ability to meet demanding schedules.

## EMPLOYEES

### Employment practices

Ultra believes that superior business performance can only be achieved through having a committed and efficient workforce. Achieving this high quality of workforce requires Ultra to recruit widely and with no bias or discrimination. It is therefore the policy of Ultra to be an equal opportunities employer and to oppose all forms of unlawful or unfair discrimination on the grounds of sex, race, nationality, disability, sexual orientation, age, marital status, religion or political belief. In addition, the Group is a responsible employer, seeking to achieve a culture of fairness to employees and of being a good place both to work and develop a career. Employees and applicants are treated equally and fairly in respect of recruitment, remuneration, training, promotion and career development.

Many UK businesses are accredited to the Investors In People standard and are regularly audited.

In complying with the Public Interest Disclosure Act 1998 in the United Kingdom, the Group



has established a procedure enabling employees to bring matters to the attention of an appropriate manager outside of their own business in the event that they do not feel able to approach their local line management. This procedure was independently reviewed and updated during 2004.

### Development and training

The Group actively supports and invests in training and development linked to business needs. Each business is responsible for identifying the training needs of its employees and managing its own training budget. This typically takes place through individual employee performance and development reviews, which are held at least annually.

Specific training programmes are provided for individuals as necessary. Additionally, training programmes on management processes and techniques are run at Group level along with workshops on Ultra's successful competitive strategy process.

Some UK businesses run apprenticeship programmes and a number of businesses offer scholarship and tuition reimbursement programmes. Ultra has also sponsored

## Benefits

Ultra offers competitive benefits to all employees, which are regularly reviewed. The Group believes in rewarding its employees well for good performance

## Commitment

Ultra believes in having an efficient and committed workforce

undergraduate students and supported other development activities such as work placement and work shadowing during 2004.

Within the UK employees are eligible to participate in the Government's Home Computing Initiative. Under the programme, Ultra offers a tax-exempt loan scheme for computer equipment for employees to use at home. The programme was launched in 2004 as part of the "UltraSelect" flexible benefits package and there was a high take up rate with 10% of employees participating. A computer purchase plan is also operated at one business in North America.

### Benefits

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There is a very high satisfaction rate among employees based on the results of the employee surveys conducted during 2004 (see Employee consultation below). All US and Canadian employees are offered health plans. In the UK employees can participate in the "UltraSelect" flexible benefits plan. This was

first launched in 2000 and in 2004 approximately two-thirds of eligible UK employees participated in the scheme.

### Pensions

Ultra's pension arrangements are discussed in the Finance Review.

Pension management and governance is undertaken by pension trustees on behalf of members. The UK defined benefit pension scheme has a statement of investment principles. This includes a statement on socially responsible investment which is delegated to the investment managers. The pension trustees include company nominated and employee elected representatives. Ultra supports the trustees in a number of ways including training to the "Trustee Certificate of Essential Pensions Knowledge" standard which is independently assessed by the Pensions Management Institute.

### Succession planning

An annual organisation and succession plan is produced by the Managing Director or President of each business and is used to identify the development actions for employees with high potential. It also reviews

## ULTRA PROMOTES GOOD WORKING RELATIONSHIPS WITH ALL ITS CUSTOMERS WITH A SPECIAL EMPHASIS ON MEETING COMMITMENTS.

the performance of the business management teams, defines the local annual training plan and any planned organisation changes.

### Employee consultation

Gaining the commitment of the workforce is facilitated by effective communication and consultation. This takes a number of forms such as the bi-annual Group magazine "Ultra News", company-wide strategy and performance presentations, birthday and communication lunches, all-hands meetings and "YOURviews" employee surveys.

The "YOURviews" employee survey provides local management teams with feedback and an opportunity to benchmark across the Group. The process is typically conducted every one to two years; during 2004 the survey took place in eleven businesses and showed high levels of employee satisfaction.

In the United Kingdom more formal Information and Consultation practices were pilot tested during 2004 and will be formally introduced in 2005.

### Health and safety

A healthy and committed workforce is necessary to achieve better business results. Accordingly Ultra places great emphasis on maintaining high standards of health and safety. All Ultra businesses are required to have a written local policy, to have the necessary resources to implement the policy, to provide adequate information, instruction and training for employees and to implement monitoring of health and safety standards.

The Chief Operating Officer, who will become Chief Executive, has been appointed as the main Board member with overall health and

safety responsibility. The Managing Directors and Presidents of the operating businesses are responsible for implementation of the policy.

Bi-annual audits by independent, external, qualified assessors covering health and safety matters are conducted, the last of which took place in 2003. These were performed by EEF South in the UK and NATLSCO (now Broadspire) in North America. Planning started in 2004 on the 2005 cycle which will cover all Ultra businesses. Previous audits and the resulting follow-up process have proved effective in reaching and maintaining high standards across all sites. In addition, each business is required to submit a separate annual report on health and safety issues. The results of the audits and annual reports are reviewed by the divisional Managing Directors and Chief Operating Officer before a summary is submitted to the Board for review.

Health and safety of employees, visitors and the local community alike is taken very seriously by the Group and the individual businesses. Ultra's commitment to health and safety was exemplified during 2004 by the recognition by RoSPA of PMES through an occupational health and safety award. Other related achievements within Ultra include the establishment of an emergency medical response team and a wellness committee to increase awareness of critical health issues.

### SUPPLIERS

**Supplier and other partner relationships**  
Contracts with suppliers are placed following a fair, competitive tendering process on an arms length basis or through formal teaming agreements. Conflicts of interest are avoided

at all times. Such relationships engender a cooperative culture which helps with problem solving and helps to accommodate changes to requirements where these occur. Gain-share arrangements are also entered into where appropriate and provide benefits for both Ultra and its suppliers and partners.

### Supplier payment policy

Operating businesses are responsible for agreeing the terms and conditions under which they conduct business transactions with their suppliers. It is Group policy that payments to suppliers are made in accordance with those terms, provided that the supplier is also complying with all relevant terms and conditions. The Group's actual payment performance at the end of 2004 is described in the Directors' Report.

### COMMUNITY

Ultra recognises the importance of being a responsible partner in the communities in which it operates and in which its employees live. The Group has a positive attitude to environmental issues and is pleased to support selected charities and maintain links with the local communities.

### Environment

Ultra recognises it is important, both for its employees and the communities in which it operates, that effective measures are in place to ensure that the Group minimises the environmental impact of its activities.

Ultra has a formal environmental policy that addresses compliance with environmental legislation, conformity with standards for air, waste disposal and noise, the economical use of materials and the establishment of appropriate environmental performance



standards. Progress is monitored through annual reporting and a bi-annual audit process.

The Chief Operating Officer, who will become Chief Executive, has been appointed as the main Board member with overall environmental responsibility. The Managing Directors and Presidents of the operating businesses are responsible for implementation of the policy.

Bi-annual external audits covering environmental matters are conducted by independent, external, qualified auditors; the last audit was performed in 2003 by EEF South in the UK and NATLSCO (now Broadspire) in North America. In the year planning started on the 2005 cycle, which will cover all Ultra businesses. As with health and safety the audits and the resulting follow-up process have proved effective in reaching and maintaining high standards of compliance across all sites. In addition each business is required to submit an annual report on environmental issues. The results of the audits and annual reports are reviewed by the divisional Managing Directors and Chief Operating Officer before a summary is submitted to the Board for review.

The trend of improvement in recycling and waste reduction was maintained in 2004 in most Ultra businesses. Investment in new plant has also helped reduce the environmental impact of the Group's operations. For example, a new paint spray gun washing machine has helped reduce solvent usage and produces less hazardous waste while a new conformal coating machine also reduces solvent usage and significantly reduces operator risk. In

addition a new high technology surface mount production line will use lead-free solder thereby eliminating the risk of lead contamination when the circuit boards reach the end of their life.

The weight of packaging used by UK businesses is assessed and reported annually to ensure compliance with the current packaging regulations.

### Charitable activities

In addition to the charitable donations made by the Group, disclosed in the Directors' Report, Ultra employees are actively supported in their charitable fund-raising endeavours. A large number of local and national charities are supported. For example, employees at a number of businesses in the US raised over \$13,000 for the United Way charity. Charitable support led Ocean Systems to receive an "Outstanding Leadership Award" in 2004. Several businesses also collect food and clothing which is distributed to their local communities.

At Airport Systems, employees made voluntary donations in exchange for dressing casually on Fridays while at DNE, employees volunteered to spend time each week mentoring and helping children in a local school. Other activities included, in the UK, the Manchester 10km run, "cancer walks" and local "fun days".

### Local links

Links with local universities and other academic institutions are encouraged. During 2004 this has included sponsorship of undergraduate students, work experience placements, work shadowing as well as direct graduate recruitment. For example,

Measurement Systems Inc. provided internships for students from the University of New Haven and Fairfield University while Sonar & Communication Systems hosted an "insight" day with Brunel University for young women students considering a career in science and engineering.



## Board of Directors



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**01 Peter Macfarlane\*** FCA FCT, Non Executive Chairman, age 66, qualified as a Chartered Accountant with Touche Ross and, after three years with Coopers & Lybrand joined Kimberley Clark, managing their financial affairs in Europe, Africa and the Middle East. He joined Rolls Royce in 1979 as Group Treasurer and, after a period as Director of Corporate Development, was appointed Finance Director in 1989. Mr Macfarlane retired from the board of Allied Domecq plc in 1998 where he had been initially Finance Director and subsequently Chairman of two divisions. He was appointed to the board of Ultra in December 1994.

**02 Julian Blogh** CBE PhD CEng MIEE, Chief Executive, age 61, has spent most of his working life in the electronics industry working with Ferranti Radar, Plessey Radar and Dowty Electronic Systems. He was Managing Director of Sonar & Communication Systems from 1987 to 1992, when he was appointed Managing Director of Dowty Avionics. He became Chief Executive of Ultra Electronics when it began trading in October 1993 and was also appointed Deputy Chairman in April 2004.

**03 Douglas Caster** BSc MIEE, Chief Operating Officer, age 51, started as a Design Engineer with Racal in 1975, before moving to Schlumberger and then to Dowty as Engineering Director of Sonar & Communication Systems in 1988. In 1992, he became Managing Director of that division and joined the board of Ultra in October 1993. In 1999 he became Managing Director of Command & Control Systems with responsibility for Manufacturing & Card Systems, PMES, and APC. In April 2000, he was promoted to the position of Managing Director of the Information & Power Systems division and in April 2004 he was appointed to his current position.

**04 Chris Bailey\*** FCA MCT, Non-Executive Director, aged 58, was appointed to the board in January 2005. Mr Bailey joined English China Clays plc in 1969 becoming Finance Director of ECC Construction Materials Ltd in 1985. In 1994 he became Group Finance Director of CAMAS plc and in 1997, following that company's merger with Bardon Group plc to form Aggregate Industries plc, he became Group Finance Director, a position he held until his retirement in 2004. Mr Bailey is also a Non-Executive Director of Rok property solutions plc with effect from 1 March 2005.

**05 Ian Griffiths\*** BSc, Non-Executive Director, age 54, was appointed to the board in April 2003. He is a main board executive director of GKN plc, where he is Group Managing Director GKN Automotive. In this role, to which he was appointed in October 2004, Mr Griffiths is responsible for all of GKN's Automotive activities world wide. Prior to this he was Chief Executive of GKN Driveline, a major division of GKN with facilities in 30 countries designing and manufacturing driveline components and systems. He has been a member of the GKN Driveline senior management team since 1990 during which time he has been responsible for operations in the UK, USA, and global Marketing and Engineering based in Germany. He was appointed Chief Executive of GKN Driveline in November 2000 and to GKN plc main board in January 2001.

**06 Andy Hamment** BA FRAeS, Group Marketing Director, age 50, started his career with Hawker Siddeley before moving to Schlumberger in 1980, working in procurement and then marketing at Weston Aerospace before transferring to Solartron as Aerospace Business Manager. He joined Dowty in 1988 as Managing Director of the Controls business. He was appointed to his current position in July 2000 and joined the board at that time.

**07 Frank Hope** PhD CPhys MInstP, Managing Director, Information & Power Systems, age 50, started his career with Tecalemit as a design engineer working on robotics. He spent 13 years with Avimo Limited latterly as Managing Director, having previously held the positions of Technical Director and Operations Director. He joined Ultra in 1994 as Managing Director of the Electrics division. Dr Hope was appointed to the board of Ultra in January 1999 and in April 2000 became Managing Director of Aircraft & Vehicle Systems. He was appointed to his current position in April 2004.

**08 David Jeffcoat** BA FCMA, Finance Director and Company Secretary, age 54, started his career as a production engineer in the car industry. Since qualifying as an accountant he has held senior financial positions in several large corporations including GlaxoWellcome plc, where he was Finance Director of two subsidiaries. Before joining Ultra he was Group Financial Controller of Smiths Industries plc for three years. He was appointed to the board in July 2000.

**09 Andrew Walker\*** MA CEng, Senior Non-Executive Director, age 53, was appointed to the board in June 1996. He is Chairman of both the Audit and Remuneration Committees. Joining the Dowty Group plc in 1978, he became an operating board member in 1991. Following TI Group's acquisition of Dowty, he became Managing Director of John Crane Polymer Engineering. He was Chief Executive of South Wales Electricity plc (SWALEC) from 1993 to 1996, and was Chief Executive of McKechnie plc from 1997 to 2001. Mr Walker is also a Non-Executive Director of Halma plc, API Group plc, Manganese Bronze Holdings plc, Porvair plc and is Chairman of Bioganix Ltd.

## Business addresses

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