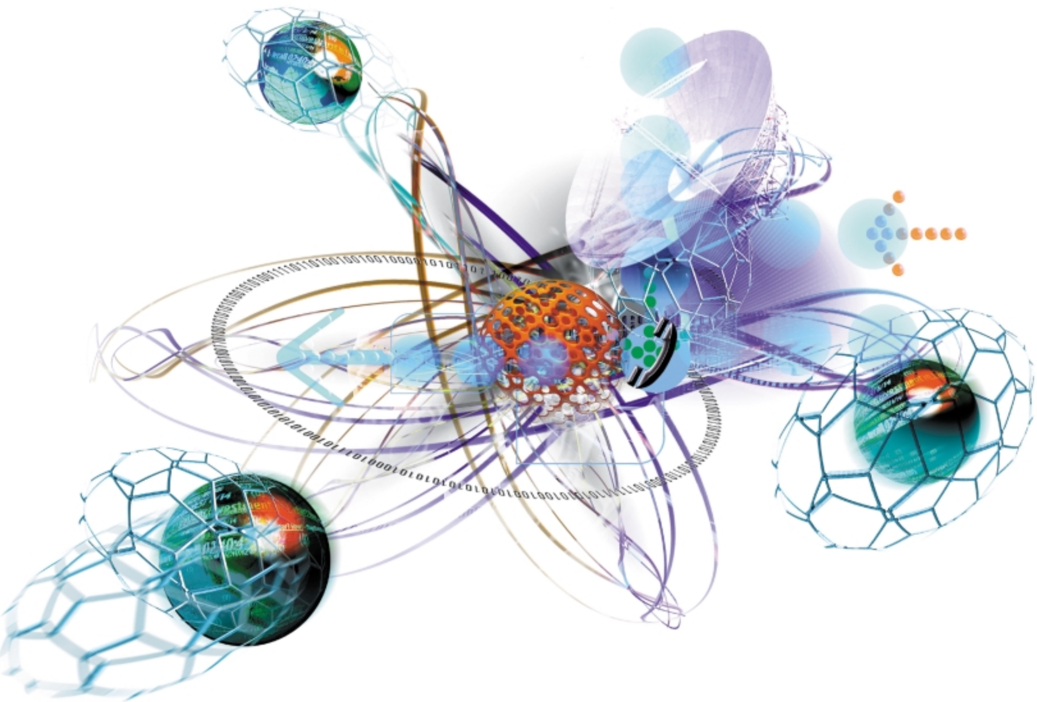
INTELEK

INTERIM REPORT 2005



Chairman's Statement

Introduction

I am particularly pleased to report that the half-year results to 30 September 2005 were very encouraging and demonstrated a continuing improvement in performance. The Group's profit before tax increased by 26% to £0.79 million (2004: £0.63 million) with earnings per share increasing by 41% to 0.62 pence per share.

Results

Sales for the first six months of this year were £16.8 million, an increase of 9% on the same period in 2004 (£15.4 million), after adjusting for the effect of the disposal of Pascall Electronics which was completed just before the end of our last financial year. On the same basis, headline profit before tax and restructuring costs improved by 5% to £0.80 million (2004: £0.76 million).

The improved performance has been achieved despite the expected reduction in a long-standing customer programme at Labtech and is after incorporating the benefits from restructuring parts of the business prior to the beginning of the financial year and from adding our new Labtech Microwave division, which was acquired in March 2005.

The order book on 30 September, deliverable within 12 months, amounted to £11.0 million compared with £8.8 million at September 2004 (excluding Pascall Electronics). Net borrowings increased by £1.1 million in the half year largely as a result of the Labtech Microwave acquisition from Filtronic Components. As a consequence of net borrowings being £2.8 million lower than September 2004, the net interest charge reduced by 27% and is now covered 7.6 (2004: 5.8) times by headline operating profit.

Due to these Interim accounts being prepared under International Financial Reporting Standards, the format of the profit and loss account has been changed and, indeed, renamed the consolidated income statement. The major effect of this change has been to bring the Group's pension deficit, the magnitude of which has been well known to shareholders for some considerable time, on to the balance sheet. (The Scheme was closed for future service accrual on 30 September 2002.) The income statement includes the substitution of the net finance cost of the Pension Scheme for the amortisation charge under the previous standard.

Note 11 to these interim accounts reconciles the reported balance sheet and income statement with that which would have been reported under UK Accounting Standards. On headline profit, the reported figure of £0.80 million for 2005 would have been £0.87 million under UK GAAP, while the 2004 comparative of £0.76 million was originally reported under UK GAAP as £0.81 million.

Dividend

The Board of Directors is maintaining the interim dividend at 0.12 pence per Ordinary share (2004: 0.12 pence). The payment date for this dividend will be on 25 January 2006 for shareholders on the register at 23 December 2005. The adoption of International Standards has led to the restatement of retained earnings at Group level to a negative £5.5 million as at 30 September 2005 whilst retained earnings at the parent company, although reduced, would remain comfortably positive. However, we consider the accounting treatment of distributable reserves is still far from being concluded and therefore, after consultation with our auditors, we have decided to continue to apply UK GAAP to the accounts of the parent company and subsidiaries.

Trading

Satellite communications — Paradise Datacom, based both in the UK and USA, closed the half year strongly. Amplifier order intake grew by 25% compared with the same period last year, driven by demand from the Government sector and by the breadth and quality of Paradise Datacom's product range. The new Evolution modem, which was launched at the Satellite Show in Washington in March 2005, has now been through an extensive demonstration and sampling programme and has been trialled successfully by a number of major names within the industry. The feedback has been extremely positive with considerable interest in a number of the innovative and unique features of the new modem. In addition to the IF modem, a new L Band version and a redundancy controller (this switches services to another modem should backup be required) were launched at the International Broadcasting Convention in Amsterdam in September. Overall modem sales were down in the six months but we are expecting sales to pick up as the new modem range begins to penetrate the market.

The successful move at the beginning of April into our US operations' new facility in State College, Pennsylvania, has been one of the contributing factors to the increased level of output and margins of the amplifier products. A further $0.8 million tranche of a significant government programme was placed with Paradise Datacom in September. This will be delivered in the second half of this year. In net terms, Paradise Datacom's sales were £0.4 million lower than last year, with operating profit at £0.83 million (2004: £1.00 million), 12.5% of sales.

Chairman's Statement

Microwave circuits and components — Labtech Circuits, as predicted in the 2004/05 Report and Accounts, experienced a drop in sales of some of their older technology programmes which are being phased out and replaced by more complex, lower volume products. **Labtech Microwave** performed well in the first six months with both sales and profit exceeding our expectations at the time of purchase. In overall terms, Labtech's operating profit reduced to £0.32 million (2004: £0.61 million).

Aerostructures — CML performed extremely well in the first half of the year by taking a break even position in the previous year up to a level of profit slightly over 10% of sales, which increased by 35% on the previous year. This improvement in CML's performance is not only due to the much improved aerospace market but also to the reshaping, restructuring and internal improvements made within CML over the past 12 months.

People

I was very pleased to accept the position of Chairman of your Company at the AGM in September. I would very much like to pay tribute to Nigel Mills, my predecessor, who stepped in at short notice in May 2004. I am delighted that Nigel is continuing as Deputy Chairman of the Group and will continue to provide the Board and the operating companies with his detailed knowledge of the communications market and, in particular, the satcom element of that market and its inherent technologies.

Prospects

The Group is midway through a major change programme which was started some time ago. New products have been added, we have sold a business which was non-core, added a new business and strengthened some aspects of the management and organisation structure. All this has been achieved whilst improving the performance of the continuing operations.

Quotations and order inflow are at healthy levels after the traditional European holiday season slowdown. This, combined with the strong order inflow at Paradise Datacom in the second quarter and the sustained performance at CML, leads me to reconfirm the view that 2005/06 will see an overall improvement in performance compared with the previous year.

Strategy

We will continue to change and improve the management and organisation structure to ensure that the Group is quick to respond to movements in the markets in which we operate. Product and market development are cornerstones of our strategy to ensure that the Group becomes a significant player in the global satellite and wireless communications industry. Although organic growth is central to our strategy we will consider acquisition opportunities as and when they arise.

David M. Bramwell
Chairman
22 November 2005

Please consult Intelek's web site **www.intelek.plc.uk** for press releases from Intelek and Intelek's subsidiaries. Alternatively, if you would like to receive copies of press releases by e-mail, please notify **info@intelek.plc.uk**

Consolidated Income Statement (unaudited)

for the six months ended 30 September 2005

	Note	Half year to 30 September 2005 £000	Half year to 30 September 2004 £000	Year to 31 March 2005 £000
Sales	2	**16,839**	15,449	31,523
Cost of goods sold		**(12,106)**	(10,924)	(22,376)
Selling and administrative expenses		**(2,573)**	(2,376)	(4,781)
Research and development expenses		**(893)**	(830)	(1,578)
Headline operating profit		**1,267**	1,319	2,788
Interest receivable		**80**	—	28
Interest payable		**(247)**	(228)	(475)
Pension: Expected return on assets	7	**383**	326	653
Pension: Interest on liabilities	7	**(688)**	(658)	(1,284)
Finance costs — net		**(472)**	(560)	(1,078)
Headline profit		**795**	759	1,710
Restructuring costs	3	**(6)**	(133)	(309)
Profit before tax		**789**	626	1,401
Taxation	4	**(278)**	(205)	(426)
Post-tax profit/(loss) of discontinued operation	10	**17**	(48)	1,725
Profit for the period	2	**528**	373	2,700
Earnings per share	5			
Basic		**0.62p**	0.44p	3.19p
Diluted		**0.62p**	0.44p	3.19p
Continuing				
Basic		**0.60p**	0.50p	1.15p
Diluted		**0.60p**	0.50p	1.15p
Discontinued				
Basic		**0.02p**	-0.06p	2.04p
Diluted		**0.02p**	-0.06p	2.04p

Consolidated Statement of Recognised Income and Expense (unaudited)

for the six months ended 30 September 2005

	Note	Half year to 30 September 2005 £000	Half year to 30 September 2004 £000	Year to 31 March 2005 £000
Foreign exchange translation differences		**5**	2	(15)
Net gain/(loss) on hedge of net investment in foreign subsidiary		**53**	27	(47)
Actuarial gain/(loss) on defined benefit pension plan		**575**	(494)	(1,329)
Income and expense recognised directly in equity		**633**	(465)	(1,391)
Profit for the period		**528**	373	2,700
Total recognised income and expense for the period		**1,161**	(92)	1,309
Equity at 1 April		**11,040**	10,138	10,138
Dividends paid	6	**(203)**	(102)	(407)
Equity at 30 September / 31 March		**11,998**	9,944	11,040

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Consolidated Balance Sheet (unaudited)

as at 30 September 2005

	Note	**30 September 2005 £000**	30 September 2004 £000	31 March 2005 £000
ASSETS				
Goodwill		**13,529**	13,505	13,416
Intangible assets		**318**	315	343
Property, plant and equipment		**6,091**	6,335	5,729
Deferred tax assets arising on pension obligation	7	**3,708**	4,041	3,875
Other deferred tax assets		**152**	57	152
Total non-current assets		**23,798**	24,253	23,515
Inventories		**3,278**	4,387	3,479
Trade and other receivables		**6,557**	7,842	6,000
Cash and cash equivalents		**803**	1,047	1,091
Total current assets		**10,638**	13,276	10,570
Total assets		**34,436**	37,529	34,085
LIABILITIES				
Defined benefit pension obligation	7	**(12,360)**	(13,470)	(12,918)
Borrowings		**(2,155)**	(2,292)	(2,100)
Deferred tax liabilities		**(572)**	(764)	(455)
Deferred government grants		**(108)**	(136)	(100)
Total other non-current liabilities		**(2,835)**	(3,192)	(2,655)
Borrowings		**(2,116)**	(5,027)	(1,335)
Trade and other payables		**(4,966)**	(5,752)	(5,292)
Current tax liabilities		**(84)**	(37)	(206)
Provisions and other liabilities		**(77)**	(107)	(639)
Total current liabilities		**(7,243)**	(10,923)	(7,472)
Total liabilities		**(22,438)**	(27,585)	(23,045)
Net assets		**11,998**	9,944	11,040
EQUITY				
Issued capital		**4,304**	4,304	4,304
Share premium		**9,104**	9,104	9,104
Investment in own shares		**(326)**	(326)	(326)
Merger reserve		**3,411**	3,411	3,411
Capital redemption reserve		**955**	955	955
Retained earnings		**(5,450)**	(7,504)	(6,408)
Total equity		**11,998**	9,944	11,040

Consolidated Cash Flow Statement (unaudited)

for the six months ended 30 September 2005

	Note	Half year to **30 September 2005 £000**	30 September 2004 £000	Year to 31 March 2005 £000
Cash flows from operating activities				
Cash generated from operations	8	**1,205**	1,452	1,883
Interest paid		**(247)**	(256)	(506)
Interest received		**80**	—	—
Tax paid		**(404)**	21	82
Net cash from operating activities		**634**	1,217	1,459
Cash flows from investing activities				
Proceeds from sale of property, plant and equipment		**—**	—	116
Purchases of property, plant, equipment and intangible assets		**(275)**	(441)	(1,004)
Proceeds from sale of businesses	10	**48**	—	4,587
Acquisition of businesses		**(474)**	—	—
Net cash used in investing activities		**(701)**	(441)	3,699
Cash flows from financing activities				
Increase/(decrease) in bank loans		**420**	(237)	(4,065)
Finance lease payments		**(292)**	(260)	(602)
Dividends paid	6	**(203)**	(102)	(407)
Net cash used in financing activities		**(75)**	(599)	(5,074)
Net increase in cash and cash equivalents		**(142)**	177	84
Cash and cash equivalents at 1 April		**1,091**	946	946
Effect of foreign exchange rates		**(144)**	(49)	61
Cash and cash equivalents at 30 September / 31 March	9	**805**	1,074	1,091

The financial information contained herein does not constitute statutory accounts within the meaning of Section 240 of the Companies Act 1985.

The statutory accounts for the year ended 31 March 2005, which have been delivered to the Registrar of Companies, carry an unqualified report by the auditors and do not contain a statement under Section 237(2) or Section 237(3) of the Companies Act 1985.

Copies of this Statement are being sent to Shareholders. Further copies are available from the Company Secretary, PO Box 25, South Marston Park, Swindon, SN3 4TR, and it is also available on our web site, http: //www.intelek.plc.uk.

Notes to the Interim Report (unaudited)

for the six months ended 30 September 2005

1 Significant accounting policies

(a) Basis of preparation

The next annual financial statements of the Group will be prepared in accordance with International Financial Reporting Standards (IFRS). Accordingly, this interim financial report has been prepared under IFRS that the Directors expect to be applicable for the financial year ended 31 March 2006 and specifically in accordance with IAS 34, Interim Financial Reporting. The comparative data for the year to 31 March 2005 and for the six months to 30 September 2004 have been restated and reconciliations are included in Note 11 to explain the changes.

(b) Basis of consolidation

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(c) Foreign currency

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of transaction. Monetary assets and liabilities in foreign currencies are translated at the exchange rates ruling at the balance sheet date. Foreign exchange differences arising are recognised in the income statement.

The results and cash flows of overseas subsidiaries are translated to sterling at average exchange rates. The assets and liabilities are translated at exchange rates ruling at the balance sheet date. Foreign exchange differences arising are taken to reserves.

(d) Financial instruments and hedging

The Group uses derivative financial instruments to hedge significant exposure on foreign exchange transactions. These instruments are measured at the balance sheet date at their fair value. Where the derivative qualifies as an effective hedge, the movement in fair value is deferred in equity and released to the income statement as the cash flows relating to the underlying transactions are incurred. Where this is not the case, the movement in fair value is taken directly to the income statement.

From time to time, the Group uses foreign currency borrowings to create a hedge against the net investment in foreign subsidiaries. Where this qualifies as an effective hedge, foreign exchange differences arising are taken to reserves.

(e) Intangible assets

(i) Goodwill

In respect of acquisitions since 1 April 2004, goodwill arising on consolidation represents the excess of cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of the acquired entity at the date of acquisition. For acquisitions prior to this date, goodwill is included on the basis of its deemed cost, which represents the amount recorded under previous GAAP. Goodwill is recognised as an asset and assessed for impairment at least annually. Impairment is assessed by comparing the goodwill with the discounted cash flows projected for the acquired entity, using a discount rate that management estimate to be the risk adjusted average cost of capital for that entity.

(ii) Research and development

Research expenditure is written off as incurred. Expenditure on a development project will be written off as incurred unless and until the project is identified as being:

(a) for a new or substantially improved product or process;

(b) technically feasible;

(c) commercially feasible, with a high probability that recovery will take place.

For a project meeting these criteria, subsequent costs will be capitalised and amortised from the date the product or process is available for use on a straight-line basis over the product's estimated life up to a maximum of 3 years.

(iii) Acquired intangible assets

Intangible assets that are acquired as a result of a business combination are recorded at fair value at acquisition date, provided they can be separately and reliably measured. The assets are amortised on a straight-line basis over their expected useful lives.

1 Significant accounting policies (continued)

(f) Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and any impairment loss. Cost comprises the purchase price and costs directly incurred in bringing the asset into use. Where assets are in the course of construction at the balance sheet date, they are classified separately and not depreciated.

Depreciation is charged so as to write off the cost of assets to their residual value over their expected useful lives using the straight-line method. The principal rates are as follows:

Freehold land	Nil
Leasehold properties	Over the lease period
Plant and equipment	7%-33%

(g) Leased assets

Leasing agreements that transfer substantially all the risks and rewards of ownership to the Group are classified as Finance Leases. Assets financed by a Finance Lease are accounted for as if they had been purchased outright, with the corresponding liability to the leasing company included as an obligation. The rentals payable are apportioned between interest, which is charged to the income statement, and capital, which reduces the outstanding obligation. All other leases are classified as Operating Leases and lease rentals are charged to the income statement on a straight-line basis over the term of the lease.

(h) Impairment of non-current assets

All non-current assets are assessed annually for indications of impairment. Where impairment is likely, the fair value is measured and any impairment loss is charged to the income statement.

(i) Inventories

Inventories are valued at the lower of cost and estimated net realisable value, due allowance being made for obsolete and slow-moving items. Cost includes the relevant proportion of production overhead assuming normal levels of activity. Net realisable value is the estimated selling price less the estimated costs of completion and selling expenses.

(j) Employee benefits

(i) Defined contribution plans

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

(ii) Defined benefit plan

The Group's net obligation in respect of its defined benefit pension plan is calculated by estimating the amount of future benefit payable to members, discounted to present value, and deducting the fair value of the plan assets. The calculation is performed by a qualified actuary using the projected unit credit method. Actuarial gains or losses are included in the Statement of Recognised Income and Expense. Current and past service costs, curtailments and settlements are recognised within operating profit. Returns on scheme assets and interest on obligations are recognised as a component of financing costs.

(iii) Share-based payment transactions

Share-based incentive arrangements are provided to employees under the Group's share option, incentive and other share award schemes. Share-based arrangements put in place since 7 November 2002 are valued at the date of grant or award and charged to operating profit over the performance or vesting period of the scheme. Options are valued using an appropriate pricing model. The annual charge is modified to take account of shares forfeited by employees who leave during the performance or vesting period and where it becomes unlikely that the option or shares will vest.

(k) Provisions

A provision is recognised in the balance sheet when the Group has a legal or constructive obligation as a result of a past event.

(i) Warranty

Provision for warranty is made only for those customer claims in respect of which the Group expects to incur liability.

(ii) Restructuring

A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating costs are not provided for.

Notes to the Interim Report (unaudited)

for the six months ended 30 September 2005

1 Significant accounting policies (continued)

(iii) Onerous contracts

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract.

(l) Sales and revenue recognition

(i) Sales

Sales represent the invoiced value, excluding value added tax, of goods and services, where the significant risks and rewards of ownership have been transferred to the buyer. No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due or the possible return of goods.

(ii) Government grants

Government grants are recognised in the balance sheet initially as deferred income. Grants in respect of assets are transferred to the income statement as other operating income over the estimated useful life of the asset concerned. Grants to compensate for expenses are transferred to the income statement in the same periods as the expenses are incurred.

(m) Taxation

The tax charge for the year includes the charge for tax currently payable and deferred taxation. The current tax charge represents the estimated amount due that arises from the operations of the Group in the financial year and after making adjustments in respect of prior years.

Deferred tax is recognised in respect of all differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, except where the temporary difference arises from goodwill or from the initial recognition of assets or liabilities that affect neither accounting nor taxable profit.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

Deferred tax is measured at the tax rates that are expected to apply in the periods in which the timing differences are expected to reverse.

2 Segment reporting

Geographical markets

	Half year ended 30 September 2005 £000	Half year ended 30 September 2004 £000	Year to 31 March 2005 £000
UK	**7,314**	5,685	12,168
Rest of Europe	**5,037**	5,242	11,235
North America	**2,271**	3,207	5,767
Rest of World	**2,217**	1,315	2,353
	16,839	15,449	31,523

Business segment

	Half year ended 30 September						Year to 31 March		
	2005			2004			2005		
	Sales £000	**Profit £000**	**Margin %**	Sales £000	Profit £000	Margin %	Sales £000	Profit £000	Margin %
Satellite communications	**6,642**	**830**	**12%**	7,046	999	14%	13,710	1,957	14%
Microwave circuits and components	**4,849**	**323**	**7%**	4,472	609	14%	9,086	1,149	13%
Aerostructures	**5,389**	**564**	**10%**	3,979	23	1%	8,817	360	4%
Eliminate intra-segment trading	**(41)**	**—**	**—**	(48)	—	—	(90)	—	—
Continuing operations	**16,839**	**1,717**	**10%**	15,449	1,631	11%	31,523	3,466	11%
Central costs		**(450)**			(312)			(678)	
Finance costs		**(472)**			(560)			(1,078)	
Restructuring costs:									
Satellite communications		**(6)**			—			(115)	
Aerostructures		**—**			(133)			(194)	
Taxation		**(278)**			(205)			(426)	
Discontinued operation		**17**			(48)			1,725	
Total for the period	**16,839**	**528**		15,449	373		31,523	2,700	

3 Restructuring costs

An additional £6,000 was incurred in the first half of 2005/06 completing the restructuring in Satellite Communications.

4 Taxation

Tax for the interim period is based on effective tax rates expected to be applicable to the full year.

	Half year ended 30 September 2005 £000	Half year ended 30 September 2004 £000	Year to 31 March 2005 £000
Current taxation	**(161)**	(126)	(287)
Deferred taxation	**(117)**	(79)	(139)
	(278)	(205)	(426)

Tax for the interim period is charged at 35% (2004: 32%), representing the best estimate of the tax rate expected for the full financial year.

Notes to the Interim Report (unaudited)

for the six months ended 30 September 2005

5 Earnings per Share

Basic earnings per share were calculated based on the profit for the period divided by the weighted average number of ordinary shares outstanding during the period, excluding those held by the Employees Share Trust (84,586,000 (2004: 84,586,000)). There was no dilution of EPS for the period (2004: Nil).

In order to provide a trend measure of underlying performance, the Board also monitors headline earnings per share, computed as follows:

	Earnings			EPS		
	Half year to September		Year to March	Half year to September		Year to March
	2005	2004	2005	**2005**	2004	2005
	£000	£000	£000	**p**	p	p
Profit for the period	**528**	373	2,700	**0.62**	0.44	3.19
Restructuring costs	**6**	133	309	**0.01**	0.16	0.37
Tax on restructuring costs	**(2)**	(40)	(93)	**—**	(0.05)	(0.11)
Post-tax (profit)/loss of discontinued operation	**(17)**	48	(1,725)	**(0.02)**	0.06	(2.04)
Headline	**515**	514	1,191	**0.61**	0.61	1.41

6 Dividends

The following dividend payments have been made:

Interim 2003/04	**—**	102	102
Final 2003/04	**—**	—	203
Interim 2004/05	**—**	—	102
Final 2004/05	**203**	—	—
	203	102	407

At 21 November 2005, the 2005 interim dividend had not been approved by the Board and as such was not included as a liability. The dividend is expected to be £102,000, to be paid in January 2006.

7 Defined benefit pension

	Half year ended		Year to
	30 September	30 September	31 March
	2005	2004	2005
	£000	£000	£000
Gross deficit 1 April	**(12,918)**	(12,435)	(12,435)
Contributions	**—**	—	2,180
Curtailment gain	**—**	—	51
Finance costs	**(305)**	(332)	(631)
Actuarial (loss)/gain	**863**	(703)	(2,083)
Gross deficit	**(12,360)**	(13,470)	(12,918)
Deferred tax asset	**3,708**	4,041	3,875
Net deficit	**(8,652)**	(9,429)	(9,043)

The defined benefit plan was reassessed by a qualified actuary as at 30 September 2005. The principal assumptions were:

Rate of increase in salaries	**3.30**	3.10	3.30
Rate of increase in pensions in payment	**2.80**	2.60	2.80
Discount rate	**5.50**	5.75	5.50
Inflation	**2.80**	2.60	2.80

8 Cash generated from operations

		Half year ended		Year to
		30 September	30 September	31 March
		2005	2004	2005
		£000	£000	£000
Headline operating profit		**1,267**	1,319	2,788
Operating loss of discontinued operation		**—**	(40)	(57)
Depreciation		**679**	781	1,520
Pension curtailment gain		**—**	—	(51)
Pension contribution		**—**	—	(1,371)
Deferred income		**8**	(16)	(31)
(Profit)/loss on disposal of tangible fixed assets		**1**	(24)	(11)
Working capital movements:	Stock	**263**	(135)	(278)
	Debtors	**(469)**	(132)	152
	Creditors	**(468)**	(278)	204
Net cash flow before restructuring		**1,281**	1,475	2,865
Restructuring		**(12)**	(23)	(182)
Special pension contribution in respect of Pascall disposal	(Note 10)	**(64)**	—	(800)
Cash generated from operations		**1,205**	1,452	1,883
Being: Continuing operations		**1,269**	1,586	3,167
Discontinued operations		**(64)**	(134)	(1,284)

Notes to the Interim Report (unaudited)

for the six months ended 30 September 2005

9 Reconciliation of net cash flow to movement in net debt

	Half year ended		Year to
	30 September	30 September	31 March
	2005	2004	2005
	£000	£000	£000
Increase in cash	**(142)**	177	84
Effect of foreign exchange rates	**(144)**	(49)	61
Repayment of finance leases	**292**	260	602
Cash (inflow)/outflow from debt	**(420)**	237	4,065
Changes in net debt resulting from cash flows	**(414)**	625	4,812
New finance leases	**(710)**	(267)	(526)
Net movement in debt	**(1,124)**	358	4,286
Opening debt	**(2,344)**	(6,630)	(6,630)
Closing debt	**(3,468)**	(6,272)	(2,344)
Analysis of net debt:			
Cash at bank	**805**	1,047	1,091
Debt	**(3,173)**	(6,556)	(2,754)
Finance leases	**(1,100)**	(763)	(681)
	(3,468)	(6,272)	(2,344)

10 Disposal of subsidiary in prior year

On 18 March 2005, the Group completed the disposal of Pascall Electronic (Holdings) Ltd and its trading subsidiary Pascall Electronics Ltd. The consideration included a contingent element estimated at the year-end March 2005 at £100,000. This element has been finalised and settled at £130,000 less expenses.

The revised summary of the transaction is as follows:

	Profit	**Cash**
Net assets of the disposed businesses	(2,806)	—
Cash included in net assets	—	41
Consideration	4,830	4,830
Expenses	(241)	(236)
Net proceeds	4,589	4,594
Profit/cash flow on disposal	1,783	4,635
Net operating loss in 2004/05 prior to disposal	(116)	
Taxation	75	
Profit after taxation	1,742	
Accounted for in the Annual Report to 31 March 2005	1,725	4,587
Accounted for in this Interim Report to 30 September 2005	**17**	**48**

The results of Pascall Electronics are shown separately in the Income Statement after deducting taxation.

In consideration for Pascall's withdrawal from the Group's defined benefit pension scheme, a special contribution was agreed at £864,000 plus any tax savings that may arise; £800,000 of this was paid in March 2005 and £64,000 in April 2005.

11 Explanation of transition to IFRS

An explanation of how the transition from UK GAAP to IFRS has affected the Group's financial position, financial performance and cash flows is set out in the following tables and accompanying notes.

Reconciliation of equity		1 April 2004					
		UK GAAP	Goodwill	Pension	Reclass.	Dividend	IFRS
	Note		(a)	(b)	(c)	(d)	
ASSETS							
Goodwill		13,473	—	—	—	—	**13,473**
Intangible assets		265	—	—	—	—	**265**
Property, plant and equipment		6,545	—	—	—	—	**6,545**
Deferred tax assets arising on pension obligation		—	—	3,731	—	—	**3,731**
Other deferred tax assets		57	—	—	—	—	**57**
Total non-current assets		20,340	—	3,731	—	—	**24,071**
Inventories		4,252	—	—	—	—	**4,252**
Trade and other receivables		9,206	—	(1,496)	—	—	**7,710**
Current tax receivable		60	—	—	28	—	**88**
Cash and cash equivalents		946	—	—	—	—	**946**
Total current assets		14,464	—	(1,496)	28	—	**12,996**
Total assets		34,804	—	2,235	28	—	**37,067**
LIABILITIES							
Defined benefit pension obligation		—	—	(12,435)	—	—	**(12,435)**
Borrowings		(2,637)	—	—	—	—	**(2,637)**
Deferred tax liabilities		(798)	(235)	449	—	—	**(584)**
Deferred government grants		(152)	—	—	—	—	**(152)**
Total other non-current liabilities		(3,587)	(235)	449	—	—	**(3,373)**
Borrowings		(4,939)	—	—	—	—	**(4,939)**
Trade and other payables		(6,393)	—	—	162	305	**(5,926)**
Current tax liabilities		—	—	—	—	—	**—**
Provisions and other liabilities		—	—	—	(256)	—	**(256)**
Total current liabilities		(11,332)	—	—	(94)	305	**(11,121)**
Total liabilities		(14,919)	(235)	(11,986)	(94)	305	**(26,929)**
Net assets		19,885	(235)	(9,751)	(66)	305	**10,138**
EQUITY							
Issued capital		4,304	—	—	—	—	**4,304**
Share premium		9,104	—	—	—	—	**9,104**
Reserves		4,040	—	—	—	—	**4,040**
Retained earnings		2,437	(235)	(9,751)	(66)	305	**(7,310)**
Total equity		19,885	(235)	(9,751)	(66)	305	**10,138**

Notes to the Interim Report (unaudited)

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11 Explanation of transition to IFRS (continued)

Reconciliation of equity		30 September 2004				
	UK GAAP	Goodwill	Pension	Reclass.	Dividend	IFRS
Note		(a)	(b)	(c)	(d)	
ASSETS						
Goodwill	13,103	402	—	—	—	**13,505**
Intangible assets	315	—	—	—	—	**315**
Property, plant and equipment	6,335	—	—	—	—	**6,335**
Deferred tax assets arising on pension obligation	—	—	4,041	—	—	**4,041**
Other deferred tax assets	57	—	—	—	—	**57**
Total non-current assets	19,810	402	4,041	—	—	**24,253**
Inventories	4,387	—	—	—	—	**4,387**
Trade and other receivables	9,147	—	(1,305)	—	—	**7,842**
Current tax receivable	—	—	—	—	—	**—**
Cash and cash equivalents	1,047	—	—	—	—	**1,047**
Total current assets	14,581	—	(1,305)	—	—	**13,276**
Total assets	34,391	402	2,736	—	—	**37,529**
LIABILITIES						
Defined benefit pension obligation	—	—	(13,470)	—	—	**(13,470)**
Borrowings	(2,292)	—	—	—	—	**(2,292)**
Deferred tax liabilities	(880)	(275)	392	—	—	**(764)**
Deferred government grants	(136)	—	—	—	—	**(136)**
Total other non-current liabilities	(3,308)	(275)	392	—	—	**(3,192)**
Borrowings	(5,027)	—	—	—	—	**(5,027)**
Trade and other payables	(6,090)	—	—	33	305	**(5,752)**
Current tax liabilities	(59)	—	—	22	—	**(37)**
Provisions and other liabilities	—	—	—	(107)	—	**(107)**
Total current liabilities	(11,176)	—	—	(52)	305	**(10,923)**
Total liabilities	(14,484)	(275)	(13,078)	(52)	305	**(27,585)**
Net assets	19,907	127	(10,342)	(52)	305	**9,944**
EQUITY						
Issued capital	4,304	—	—	—	—	**4,304**
Share premium	9,104	—	—	—	—	**9,104**
Reserves	4,040	—	—	—	—	**4,040**
Retained earnings	2,459	127	(10,342)	(52)	305	**(7,504)**
Total equity	19,907	127	(10,342)	(52)	305	**9,944**

11 Explanation of transition to IFRS (continued)

Reconciliation of equity

	Note	UK GAAP	Goodwill (a)	Pension (b)	Reclass. (c)	Dividend (d)	IFRS
		31 March 2005					
ASSETS							
Goodwill		12,627	789	—	—	—	**13,416**
Intangible assets		343	—	—	—	—	**343**
Property, plant and equipment		5,729	—	—	—	—	**5,729**
Deferred tax assets arising on pension obligation		—	—	3,875	—	—	**3,875**
Other deferred tax assets		152	—	—	—	—	**152**
Total non-current assets		18,851	789	3,875	—	—	**23,515**
Inventories		3,479	—	—	—	—	**3,479**
Trade and other receivables		9,108	—	(3,108)	—	—	**6,000**
Current tax receivable		—	—	—	—	—	**—**
Cash and cash equivalents		1,091	—	—	—	—	**1,091**
Total current assets		13,678	—	(3,108)	—	—	**10,570**
Total assets		32,529	789	767	—	—	**34,085**
LIABILITIES							
Defined benefit pension obligation		—	—	(12,918)	—	—	**(12,918)**
Borrowings		(2,100)	—	—	—	—	**(2,100)**
Deferred tax liabilities		(1,106)	(281)	932	—	—	**(455)**
Deferred government grants		(100)	—	—	—	—	**(100)**
Total other non-current liabilities		(3,306)	(281)	932	—	—	**(2,655)**
Borrowings		(1,335)	—	—	—	—	**(1,335)**
Trade and other payables		(6,038)	—	—	543	203	**(5,292)**
Current tax liabilities		(235)	—	—	29	—	**(206)**
Provisions and other liabilities		—	—	—	(639)	—	**(639)**
Total current liabilities		(7,608)	—	—	(67)	203	**(7,472)**
Total liabilities		(10,914)	(281)	(11,986)	(67)	203	**(23,045)**
Net assets		21,615	508	(11,219)	(67)	203	**11,040**
EQUITY							
Issued capital		4,304	—	—	—	—	**4,304**
Share premium		9,104	—	—	—	—	**9,104**
Reserves		4,040	—	—	—	—	**4,040**
Retained earnings		4,167	508	(11,219)	(67)	203	**(6,408)**
Total equity		21,615	508	(11,219)	(67)	203	**11,040**

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for the six months ended 30 September 2005

11 Explanation of transition to IFRS (continued)

Reconciliation of equity — 30 September 2005

	Note	UK GAAP	Goodwill (a)	Pension (b)	Reclass. (c)	Dividend (d)	IFRS
ASSETS							
Goodwill		12,334	1,195	—	—	—	**13,529**
Intangible assets		318	—	—	—	—	**318**
Property, plant and equipment		6,091	—	—	—	—	**6,091**
Deferred tax assets arising on pension obligation		—	—	3,708	—	—	**3,708**
Other deferred tax assets		152	—	—	—	—	**152**
Total non-current assets		18,895	1,195	3,708	—	—	**23,798**
Inventories		3,278	—	—	—	—	**3,278**
Trade and other receivables		9,515	—	(2,958)	—	—	**6,557**
Current tax receivable		—	—	—	—	—	**—**
Cash and cash equivalents		803	—	—	—	—	**803**
Total current assets		13,596	—	(2,958)	—	—	**10,638**
Total assets		32,491	1,195	750	—	—	**34,436**
LIABILITIES							
Defined benefit pension obligation		—	—	(12,360)	—	—	**(12,360)**
Borrowings		(2,155)	—	—	—	—	**(2,155)**
Deferred tax liabilities		(1,138)	(321)	887	—	—	**(572)**
Deferred government grants		(108)	—	—	—	—	**(108)**
Total other non-current liabilities		(3,401)	(321)	887	—	—	**(2,835)**
Borrowings		(2,116)	—	—	—	—	**(2,116)**
Trade and other payables		(5,091)	—	—	23	102	**(4,966)**
Current tax liabilities		(100)	—	—	16	—	**(84)**
Provisions and other liabilities		—	—	—	(77)	—	**(77)**
Total current liabilities		(7,307)	—	—	(38)	102	**(7,243)**
Total liabilities		(10,708)	(321)	(11,473)	(38)	102	**(22,438)**
Net assets		21,783	874	(10,723)	(38)	102	**11,998**
EQUITY							
Issued capital		4,304	—	—	—	—	**4,304**
Share premium		9,104	—	—	—	—	**9,104**
Reserves		4,040	—	—	—	—	**4,040**
Retained earnings		4,335	874	(10,723)	(38)	102	**(5,450)**
Total equity		21,783	874	(10,723)	(38)	102	**11,998**

11 Explanation of transition to IFRS (continued)

Reconciliation of profit	Note	Six months ended 30 September 2004					
		UK GAAP	Disc. Op.	Goodwill	Pension	Reclass.	IFRS
	Note		(f)	(a)	(b)	(c)	
Sales		18,295	(2,846)	—	—	—	**15,449**
Cost of goods sold		(17,227)	2,886	—	191	3,226	**(10,924)**
Selling and administrative expenses		—	—	—	—	(2,376)	**(2,376)**
Other operating income		—	—	—	—	—	**—**
Research and development expenses		—	—	—	—	(830)	**(830)**
Headline operating profit		1,068	40	—	191	20	**1,319**
Interest receivable		—	—	—	—	—	**—**
Interest payable		(256)	28	—	—	—	**(228)**
Expected return on pension assets		—	—	—	326	—	**326**
Interest on pension liabilities		—	—	—	(658)	—	**(658)**
Finance costs — net		(256)	28	—	(332)	—	**(560)**
Headline profit		812	68	—	(141)	20	**759**
Amortisation		(402)	—	402	—	—	**—**
Restructuring costs		(133)	—	—	—	—	**(133)**
Loss on disposal of discontinued operation		—	—	—	—	—	**—**
Profit before tax		277	68	402	(141)	20	**626**
Taxation		(181)	(20)	(40)	42	(6)	**(205)**
Post-tax loss of discontinued operation		—	(48)	—	—	—	**(48)**
Profit for the period		96	—	362	(99)	14	**373**
Earnings per share							
Basic		0.11	—	0.43	-0.12	0.02	**0.44**
Diluted		0.11	—	0.43	-0.12	0.02	**0.44**

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for the six months ended 30 September 2005

11 Explanation of transition to IFRS (continued)

Reconciliation of profit

		Year ended 31 March 2005					
		UK GAAP	Disc. Op.	Goodwill	Pension	Reclass.	IFRS
	Note		(f)	(a)	(b)	(c)	
Sales		37,292	(5,769)	—	—	—	**31,523**
Cost of goods sold		(28,834)	4,882	—	—	1,576	**(22,376)**
Selling and administrative expenses		(6,289)	944	—	432	132	**(4,781)**
Other operating income		132	—	—	—	(132)	**—**
Research and development expenses		—	—	—	—	(1,578)	**(1,578)**
Headline operating profit		2,301	57	—	432	(2)	**2,788**
Interest receivable		—	—	—	—	28	**28**
Interest payable		(506)	59	—	—	(28)	**(475)**
Expected return on pension assets		—	—	—	653	—	**653**
Interest on pension liabilities		—	—	—	(1,284)	—	**(1,284)**
Finance costs — net		(506)	59	—	(631)	—	**(1,078)**
Headline profit		1,795	116	—	(199)	(2)	**1,710**
Amortisation		(789)	—	789	—	—	**—**
Restructuring costs		(309)	—	—	—	—	**(309)**
Loss on disposal of discontinued operation		(1,876)	1,876	—	—	—	**—**
Profit before tax		(1,179)	1,992	789	(199)	(2)	**1,401**
Taxation		(359)	(82)	(46)	60	1	**(426)**
Post-tax profit of discontinued operation		—	1,725	—	—	—	**1,725**
Profit for the period		(1,538)	3,635	743	(139)	(1)	**2,700**
Earnings per share							
Basic		-1.82	4.30	0.88	-0.16	—	**3.19**
Diluted		-1.82	4.30	0.88	-0.16	—	**3.19**

11 Explanation of transition to IFRS (continued)

Reconciliation of profit — Six months ended 30 September 2005

	Note	UK GAAP	Disc. Op. (f)	Goodwill (a)	Pension (b)	Reclass. (c)	IFRS
Sales		16,839	—	—	—	—	**16,839**
Cost of goods sold		(15,804)	—	—	190	3,508	**(12,106)**
Selling and administrative expenses		—	—	—	—	(2,573)	**(2,573)**
Other operating income		—	—	—	—	—	**—**
Research and development expenses		—	—	—	—	(893)	**(893)**
Headline operating profit		1,035	—	—	190	42	**1,267**
Interest receivable		—	—	—	—	80	**80**
Interest payable		(167)	—	—	—	(80)	**(247)**
Expected return on pension assets		—	—	—	383	—	**383**
Interest on pension liabilities		—	—	—	(688)	—	**(688)**
Finance costs — net		(167)	—	—	(305)	—	**(472)**
Headline profit		868	—	—	(115)	42	**795**
Amortisation		(406)	—	406	—	—	**—**
Restructuring costs		(6)	—	—	—	—	**(6)**
Loss on disposal of discontinued operation		24	(24)	—	—	—	**—**
Profit before tax		480	(24)	406	(115)	42	**789**
Taxation		(267)	7	(40)	35	(13)	**(278)**
Post-tax loss of discontinued operation		—	17	—	—	—	**17**
Profit for the period		213	—	366	(80)	29	**528**
Earnings per share							
Basic		0.25	—	0.43	-0.09	0.03	**0.62**
Diluted		0.25	—	0.43	-0.09	0.03	**0.62**

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11 Explanation of transition to IFRS (continued)

Notes to the reconciliation of equity and of profit

(a) Under UK GAAP, Goodwill was being amortised over 20 years. Under IFRS, there is no amortisation and this is made retrospective to the date of transition, 1 April 2004. The effect is to increase goodwill in the balance sheet, with consequent reductions in the amortisation charge in the income statement.

Under IFRS, Goodwill must be reviewed annually for impairment. The goodwill relates entirely to Paradise Datacom. The cash flow forecasts of Paradise Datacom have been projected for five years and discounted at 12%, being the management's estimate of the risk adjusted average cost of capital for that entity. This assessment confirmed that no adjustment for impairment is required.

Also, under UK GAAP, provision for deferred tax on certain timing differences is subject to an assessment on the likelihood of crystallisation. Under IFRS, full provision is required. This has the effect of increasing the deferred tax liability associated with goodwill by £235,000 on 1 April 2004, with small adjustments thereafter.

(b) Under UK GAAP, contributions towards the defined benefit pension scheme were classified as prepayments, reduced by annual charges to profit for the amortisation of the pension deficit as computed under SSAP 24. Under IFRS, the deficit is computed on a more conservative basis, approximating to the values used for FRS 17, as disclosed in the notes to the 2005 Annual Report. The deficit gross of tax is recorded as an obligation of the Group, with the potential tax recovery shown as a separate deferred tax asset.

The amortisation of the pension deficit in the income statement is reversed and the following entries are added to the income statement:
- (i) Curtailment gain/(loss) (part of operating profit)
- (ii) Expected return on pension assets
- (iii) Interest on pension liabilities

Actuarial gains and losses are charged directly to equity.

(c) There are several reclassifications required in both the Income Statement and the Balance Sheet. Most of these have no net effect. The one adjusting item shown for net assets is the requirement under IFRS to accrue for holidays earned but not yet taken. Accrual had only been taken previously where there was a contractual employee right to payment in lieu.

(d) Dividend under IFRS is recorded only upon payment being made, whereas under UK GAAP it was accrued for in the period to which it related.

(e) The above changes increased/(decreased) the tax current and deferred liabilities as shown in the tables.

(f) Under IFRS, the results and associated gain/(loss) on disposal of discontinued operations (Pascall) are required to be separated from continuing businesses and disclosed after taxation in the Income Statement. In addition, under UK GAAP, goodwill associated with the disposed business previously written off to reserves had to be reinstated and written off against profit for the year. For Pascall, this amounted to £3,635,000. Under IFRS, this adjustment is not required.

(g) Under UK GAAP, all research and development expenditure had been expensed except for development projects subcontracted to third parties where those projects were separately identifiable and for each of which the outcome could be assessed with reasonable certainty. Under IFRS, the development expenditure has been reassessed in accordance with IAS 38 and management has concluded that no alteration in capitalisation is required as:

- (i) Many of the development projects, especially for RF products, result in incremental improvements to existing products or processes and significant capitalisation is considered unlikely;
- (ii) Large projects, such as for the Evolution Modem, can only be capitalised once the development is both technically and commercially feasible: the uncertainties in the technology and the marketplace make this difficult to substantiate, and a prudent view has therefore been taken;
- (iii) For intangible assets (in this case, R&D) acquired from third parties, there is a presumption in the new standards that the commercial feasibility has been proven, and hence capitalisation is more likely to be appropriate.

Explanation of material adjustments to the cash flow statement

The cash flow statement has changed significantly only to reflect the accounting treatment of goodwill and pension amortisation.

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