

responding to change



delivering growth

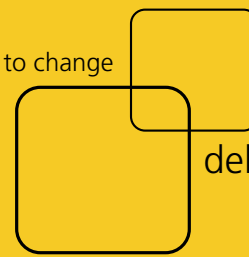
Ultra

Ultra Electronics Holdings plc Annual Report and Accounts 2005

ELECTRO



responding to change



delivering growth

ULTRA ELECTRONICS IS A GROUP OF SPECIALIST BUSINESSES OFFERING A THROUGH-LIFE PRODUCT AND SERVICE PORTFOLIO THAT INCLUDES SYSTEMS, SUB-SYSTEMS, PRODUCTS AND COMPONENTS FOR DEFENCE, SECURITY, AEROSPACE AND TRANSPORT APPLICATIONS WORLDWIDE.

ULTRA, WHICH EMPLOYS 3,000 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 COMPETITIVE ADVANTAGE THROUGH TECHNOLOGICAL EDGE AND BY HAVING A LEADING POSITION IN NICHE MARKETS.

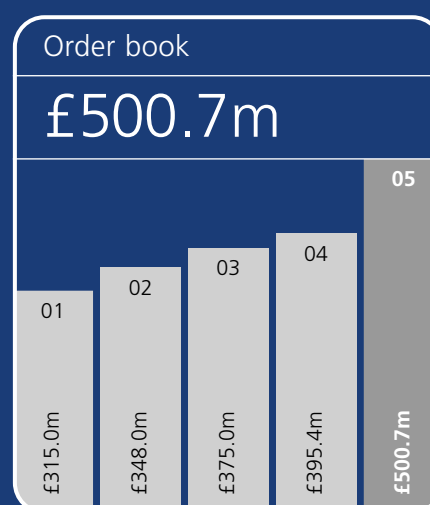
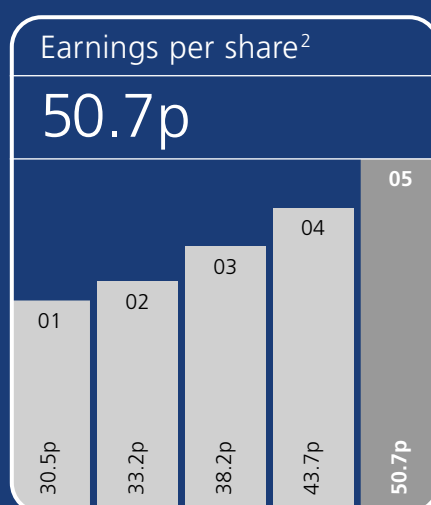
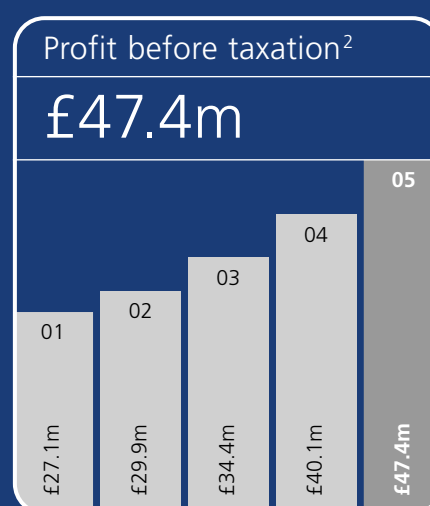
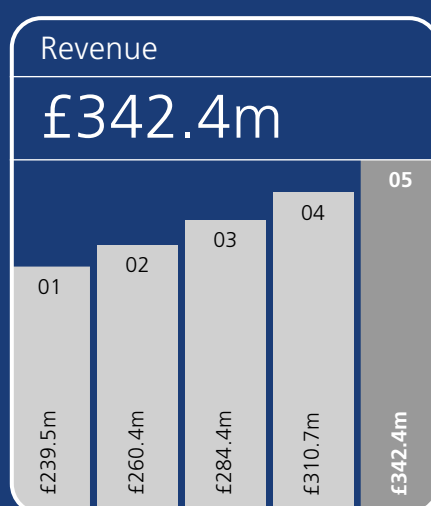
ULTRA'S PRODUCTS AND SERVICES ARE USED IN AIRCRAFT, SHIPS, SUBMARINES, ARMoured VEHICLES, SURVEILLANCE AND COMMUNICATION SYSTEMS, AIRPORTS AND TRANSPORT SYSTEMS AROUND THE WORLD. INCREASINGLY, ULTRA UNDERTAKES SPECIALIST SYSTEM AND SUB-SYSTEM INTEGRATION USING THE COMBINED EXPERTISE OF THE GROUP BUSINESSES AND BY TEAMING WITH WORLD-CLASS INTERNATIONAL PARTNERS.

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THE QUEEN'S AWARD
FOR ENTERPRISE 2003
FOR
HIPAG
AT PRECISION
AIR SYSTEMS

	2005	2004	Growth
Revenue (£m)	342.4	310.7	+10%
Operating profit (£m) ¹	51.1	43.3	+18%
Profit before taxation (£m) ²	47.4	40.1	+18%
Earnings per share ²	50.7p	43.7p	+16%
Operating profit margin ¹	14.9%	13.9%	
Employees (average number)	2,880	2,678	



¹Before amortisation of intangibles arising on acquisition. IFRS profit from operations £47.8m (2004: £43.3m).

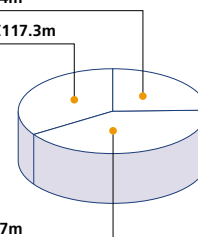
²Before amortisation of intangibles arising on acquisition and loss on derivative financial instruments. IFRS profit before tax £40.7m (2004: £40.1m). Basic EPS 43.9p (2004: 43.7p).

Divisional sales

Aircraft & Vehicle Systems **£84.4m**

Information & Power Systems **£117.3m**

Tactical & Sonar Systems **£140.7m**



ULTRA ELECTRONICS SPECIALISES IN THE DESIGN, MANUFACTURE AND SUPPORT OF ELECTRONIC AND ELECTROMECHANICAL SYSTEMS, SUB-SYSTEMS, PRODUCTS AND SERVICES 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.**

<p>Aircraft & Vehicle Systems</p> <p>Revenue £84.4m</p> <p>(2004: £76.6m)</p>	<p>Information & Power Systems</p> <p>£117.3m</p> <p>(2004: £113.7m)</p>	<p>Tactical & Sonar Systems</p> <p>£140.7m</p> <p>(2004: £120.4m)</p>
<p>Profit¹ £15.9m</p> <p>(2004: £14.9m)</p>	<p>£18.1m</p> <p>(2004: £15.0m)</p>	<p>£17.1m</p> <p>(2004: £13.4m)</p>
<p>CONTROLS[■] Airframe de-icing and crack detection systems. Civil and military aircraft cabin quietening systems using active noise and vibration control technology. Landing gear control and proximity sensing systems. Propeller balancing systems.</p> <p>DATTEL[■] High integrity systems including safety critical software. Internet-based secure collaborative working environments and resilient, secure communication networks. Health monitoring and asset availability solutions for military vehicles.</p> <p>ELECTRICS[■] Data management and vision control systems for armoured vehicles. Specialised control handles, high integrity switches and indicators. Lighting systems. Ruggedised cable harnesses.</p> <p>MEASUREMENT SYSTEMS INC[▲] Haptic devices: displacement and force joysticks, hand grip controls, trackballs, encoders and simulation equipment. Cockpit equipment.</p> <p>PRECISION AIR SYSTEMS[■] High Pressure Pure Air Generators (HIPAG) for cooling thermal imagers and infra-red sensors, and for pneumatic ejection of aircraft munitions.</p> <p>■ Businesses in the United Kingdom ▲ Businesses in North America</p>	<p>ADVANCED TACTICAL SYSTEMS[▲] Battlespace IT solutions. Software based data fusion and display systems for applications in military command, control, communications, computers, intelligence, surveillance and reconnaissance (C4ISR) systems.</p> <p>AIRPORT SYSTEMS[■] IT applications, managed services and systems integration for airlines and airports: common use check-in and boarding (UltraCUSE), local departure control (UltraSEATS), aircraft weight and balance management systems; passenger-bag matching (UltraTrak); airport operational database (UltraDB), integration message broker (UltraIB), flight information display (UltraFIDS), airport resource management (UltraResource); plant and utilities remote control and monitoring (UltraControl).</p> <p>COMMAND & CONTROL SYSTEMS[■] Optical and infra-red surveillance and tracking systems. Battlespace IT solutions. Geographical information management systems. Combat management systems. Multifunction command and control console systems. Naval data processing and distribution systems. Weapon interface electronics. High integrity electronic control systems for nuclear reactors.</p> <p>EMS[▲] Specialised power supplies and demagnetising systems for the electromagnetic silencing of naval vessels. Transformer rectifier units.</p> <p>MANUFACTURING & CARD SYSTEMS[■] High integrity contract electronic manufacturing services. The Magicard range of identity card printers.</p> <p>PMES[■] Power control, conversion and distribution equipment for naval and other demanding environments. Transit system DC power sub-stations and rectification equipment. Multi-influence measurement and control systems for the management of complex signatures of naval vessels. Magnetic and electric field sensors.</p> <p>SML TECHNOLOGIES[■] Radar surveillance, navigation and safety systems for offshore platforms and maritime vessels, coastal and border surveillance and protection systems.</p>	<p>AUDIOPACK[▲] Rugged voice communications equipment for personnel wearing protective clothing, masks and breathing apparatus in harsh and hazardous environments.</p> <p>DNE TECHNOLOGIES[▲] Military network communications equipment for voice, data and video information. High-speed protocol converters and modems.</p> <p>FLIGHTLINE SYSTEMS[▲] Sonobuoy telemetry receivers for maritime patrol aircraft and helicopters. Aircraft cockpit indicators. Mechanical gyroscopes. Specialist military test equipment.</p> <p>MARITIME SYSTEMS[▲] Active source and passive sonobuoys, bathythermal buoys and expendable submarine communication buoys. Towed array sonars. High power sonar transducers.</p> <p>OCEAN SYSTEMS[▲] Underwater acoustic countermeasures and systems. Torpedo defence systems. Torpedo sonar. Active and passive transducer technologies. Submarine communication systems.</p> <p>SONAR & COMMUNICATION SYSTEMS[■] 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. Airborne targeting pods. Cryptographic equipment.</p> <p>TACTICAL COMMUNICATION SYSTEMS[▲] High capacity line-of-sight radios, electronic counter-countermeasure radios, multiplexers, and turn-key tactical communication systems.</p> <p>UNDERSEA SENSOR SYSTEMS INC[▲] Active and passive sonobuoys. Multi-static acoustic systems. Advanced autonomous sensor systems for coastal surveillance.</p>

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IMPORTANT CONTRACTS WERE SECURED DURING 2005, INCLUDING POSITIONS ON NEW PROGRAMMES, THAT WILL SUPPORT FURTHER GROWTH OF THE GROUP.

Ultra made excellent progress in 2005, achieving high growth in revenue and profits. The Group's performance was helped by its battlespace IT, airport IT systems and torpedo countermeasures activities. Contributions were made by the acquisitions completed in 2004 and the two further acquisitions made during 2005, which strengthened Ultra's position in the civil aerospace and homeland security markets. Important contracts were secured during 2005, including positions on new programmes, that will support further growth of the Group.

Sales at £342.4m grew 10% with the Tactical & Sonar Systems division showing the strongest growth. Operating profit¹ at £51.1m increased by 18% over the previous year. This was despite the £5.2m negative impact of weaker hedged exchange rates for US\$ sales made by Ultra's businesses in the UK and Canada. Earnings per share² at 50.7p increased by 16% reflecting a slightly higher effective tax rate for 2005 than in the prior year. The Board will be recommending a final dividend of 10.7p per share, making a total for the year of 15.9p, a 15% increase over 2004.

Ultra has achieved its track record of success through its strategy of achieving organic growth by securing niche positions on long-term platforms and programmes. Growth has also been aided by acquisitions that either augmented Ultra's existing niches or added new related niches. The key to achieving this growth is Ultra's investment strategy. In 2005 the Group invested a total of £61.2m in acquisitions, research and development, capital expenditure and new business development. The investment contributed directly to the winning of new contracts that drove the year-end order book to the record level of £500.7m.

The company's net debt⁵ increased through the year by just £10.2m to £34.3m after funding the significant level of investment in 2005. Cash conversion continued to be strong in 2005 through management's continuing focus on cash generation. The

conversion of operating profit¹ to operating cash flow³ in the year was 105%. Over the last five years the Group's average cash conversion⁴ has been 114%, reflecting the high quality of Ultra's earnings.

The acquisitions of Horizon Aerospace and Audiopack Technologies Inc. were completed in the year. Horizon, now fully integrated into Ultra's Flightline Systems business, supplies a broad range of cockpit instruments for military and civil aircraft. Audiopack strengthens Ultra's communications capability within the military and homeland security markets and is also part of the Group's Tactical & Sonar Systems division.

In Ultra's main defence markets worldwide, budgets continue to rise. Within these budgets, expenditure is increasing on battlespace IT systems and equipment to provide better situational awareness, quicker command and control and the synchronisation of military effects with much improved accuracy. Funds are being spent on equipping modern armed forces to allow the rapid deployment of light, mobile troops and to enable the exploitation of superior intelligence of the military situation through the use of battlespace IT. Ultra has pursued a strategy that has positioned the Group to benefit from these trends and constantly seeks opportunities to offer new products and services to meet such customer requirements.

In civil markets, aerospace remains buoyant and healthy demand continues, both for sales of original equipment and for aftermarket support equipment. Development programmes for new aircraft types provide Ultra with opportunities to win positions for its innovative solutions. The growth in passenger air travel is strong, increasing demand for new infrastructure including airport IT systems.

The planned Board changes that were discussed in Ultra's 2004 Annual Report came into effect at the Group's AGM last April. I succeeded Peter Macfarlane as Chairman, upon his retirement, relinquishing

the Chief Executive's role to Douglas Caster who has been an Executive Director of Ultra since 1993 and who was appointed Chief Operating Officer in 2004. Peter served as Chairman for ten years; on behalf of the Board I thank Peter for his leadership and wish him a long and happy retirement.

Ultra's performance in 2005 built on its long track record of continuous progress and the Group enters 2006 with a strong balance sheet and a record order book. Ultra has the headroom to make further acquisitions that will enhance and complement the Group's range of niche activities, and to invest to respond to market demands. The order book has increased significantly in the year and provides Ultra with its customary level of visibility for 2006 earnings. It reflects the Group's strong positions on existing platforms as well as its success in winning positions on new programmes. Gaining positions on new platforms and programmes has driven the growth of Ultra. It is still true, however, that no single programme contributes more than 5% of sales in a year, thereby underpinning the resilience of the Group's performance.

Current market conditions, coupled with Ultra's proven ability to win new business and to execute contracts effectively, give the Board confidence in the continuing progress of the Group in 2006.

Finally I would like to thank all Ultra employees for their hard work and continuing commitment, which have made such important contributions to the success of the Group.

Julian Blogh Chairman

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a long-term strategy

+10%

Revenue

Reflecting increased sales of battlespace IT, airport IT and torpedo countermeasure systems

+18%

Operating profit¹

Margin improvement driven by increased volume, effective execution of development programmes and a continuing focus on cost control

IN ULTRA'S MAIN DEFENCE MARKETS WORLDWIDE, BUDGETS CONTINUE TO RISE. WITHIN THESE BUDGETS, EXPENDITURE IS INCREASING ON BATTLESPACE IT SYSTEMS AND EQUIPMENT TO PROVIDE BETTER SITUATIONAL AWARENESS, QUICKER COMMAND AND CONTROL AND THE SYNCHRONISATION OF MILITARY EFFECTS WITH MUCH IMPROVED ACCURACY.

ULTRA AND ITS MARKET ENVIRONMENT

Ultra Electronics is a group of specialist businesses offering a through-life product and service portfolio that includes systems, sub-systems, products and components for defence, security, aerospace and transport applications worldwide. Ultra's products and services are used on aircraft, ships, submarines, armoured vehicles, surveillance and communication systems, airports and transport systems around the world.

In Ultra's main defence markets worldwide, budgets continue to rise. Within these budgets, expenditure is increasing on battlespace IT systems and equipment to provide better situational awareness, quicker command and control and the synchronisation of military effects with much improved accuracy. Funds are being spent on equipping modern armed forces to allow the rapid deployment of light, mobile troops and to enable the exploitation of superior intelligence of the military situation through the use of battlespace IT. Ultra has pursued a strategy that has positioned the Group to benefit from these trends and constantly seeks opportunities to offer new products and services to meet such customer requirements.

The recent UK Government Defence Industrial Strategy document confirmed that a future priority for the MoD will be to upgrade existing platforms with smarter capabilities through the integration of enhanced electronic solutions. The report also confirmed the MoD's reliance on the private sector for innovative solutions and through-life support. The MoD is open to solutions from overseas suppliers but will require technology transfer to the UK in order to maintain operational sovereignty for its armed forces. Consequently, Ultra's market position, together with its expertise in international teaming, positions the Group to continue to play a significant role in fulfilling the MoD's objectives.

In the US, the recently published Quadrennial Defense Review ("QDR") emphasises the need to combat the asymmetric terrorist threat. Additionally, the QDR supports the simultaneous maintenance of a US, worldwide capability to wage a major conflict against a near-peer opponent. As a consequence, there will be a continuing focus of expenditure on battlespace IT solutions, especially advanced surveillance and command and control systems. The US will pursue dominance in the air, land and maritime domains through the continued development of smart capability.

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.

In civil markets, aerospace remains buoyant with Airbus and Boeing increasing build rates driving healthy demand for both sales of original equipment and equipment for aftermarket support. Development programmes for new aircraft types provide Ultra with opportunities to win positions for its innovative solutions. The growth in passenger air travel is strong, increasing demand for new infrastructure including airport IT systems.

This Operating and Financial Review contains certain forward-looking information and statements in relation to Ultra's operations, economic performance and financial conditions which cannot be objectively verified and should be treated with caution. These statements are made by Ultra in good faith, based on the information available to it at the time of the approval of this report and, although Ultra believes that the expectations reflected in such forward-looking statements are reasonable, they should not be relied upon and no assurance can be given by Ultra that such expectations will prove to be correct. Accordingly, results could differ materially from those set out in the forward-looking statements as a result of, among other factors, changes in the economic, market and competitive conditions underlying such forward-looking information.

¹before amortisation of intangibles arising on acquisition. ²before amortisation of intangibles arising on acquisition and loss on derivative financial instruments. ³Cash generated by operations, less net capital expenditure, R&D and LTIP share purchases. ⁴Cash generated by operations, less net capital expenditure, R&D and LTIP share purchases as % of profit from operations before amortisation of intangibles arising on acquisition. ⁵Bank overdrafts and loans less cash and cash equivalents.

PERFORMANCE WAS BOOSTED BY RECENT INVESTMENTS TO ENHANCE THE GROUP'S BATTLESPACE IT, AIRPORT IT SYSTEMS AND TORPEDO COUNTERMEASURES CAPABILITIES.



ULTRA'S OBJECTIVE AND STRATEGIES FOR ACHIEVING THE OBJECTIVE

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, and by communicating effectively with shareholders and the financial community generally.

Ultra's strategies to achieve this objective are summarised in the following eight-point statement. Ultra's core strategies are:

1. To concentrate on aerospace and defence
2. To be a niche player where the Group has competitive advantage through technology or market position
3. To offer a through-life product and service portfolio that includes systems, sub-systems, products and components
4. To grow both organically and by acquisition
5. To have an efficient organisation with committed and competent people
6. To be an excellent and strategic supplier to our customers
7. To gain competitive advantage by internal and external teaming
8. To meet our commitments

Ultra believes that sustainable success is derived from a focus on positioning its products and services on a broad range of major international platforms and programmes. Such successful positioning is achieved by ensuring that Ultra's offerings are differentiated from those of the competition in a manner that the customer values. Focus is sustained on creating and maintaining this differentiation in the future and on continuing to provide innovative solutions to satisfy customer requirements.

Underpinning Ultra's continuing success is its investment strategy. Ultra has a demonstrated 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 services. During 2005, Ultra invested a total of £61.2m (2004: £43.5m) on acquisitions, research and development, capital expenditure and new business development. This investment contributed directly to the new contracts won in the year and also supports the Group's long-term positioning for future business.

To ensure that this investment strategy remains affordable, Ultra focuses on delivering a high quality of earnings from its operations. Evidence of this quality is the consistently strong cash generation that the Group has achieved. The cash generated from operations is then available to fund acquisitions – Ultra seeks to maintain a broad balance between organic and acquisition growth. Since formation, all of Ultra's acquisitions have been funded by free cash flow and so the level of net debt has remained relatively constant.

The Group's acquisition strategy is summarised as being the pursuit of bolt-on acquisitions that:

- are defence or aerospace based
- are in a growth market sector
- augment a current niche or
- add a new, related niche or
- widen Ultra's geographic reach

The ideal size of acquisitions is currently about £25m to £50m and so "organisation transforming" acquisitions are unlikely. The Group will seek to maintain a robust portfolio of niche activities. In short, the acquisition strategy that has served Ultra well to date will be continued.

ULTRA'S 2005 RESULTS

Ultra made excellent progress in 2005, achieving high growth in revenue and operating profit¹. The Group's performance was helped by its battlespace IT, airport IT systems and torpedo countermeasures activities. Contributions were made by the acquisitions completed in 2004 and the further two acquisitions made during 2005, which strengthened Ultra's position in the civil aerospace and homeland security markets. Important contracts were secured during 2005 including positions on new programmes that will support further growth of the Group.

Group results

Revenue increased to £342.4m, a rise of 10% over the prior year, of which 6% was organic growth. In addition to the investments noted above, strong sales of tactical data link systems to the US armed forces, increased deliveries of battlespace IT equipment for military vehicles, airport IT systems and torpedo countermeasures contributed to the Group's performance.

There was a further increase in the Group's operating margin¹ from 13.9% in 2004 to 14.9%, driven mainly by a combination of a rise in volume, effective execution of development programmes and a continuing focus on cost control. Operating profit¹ rose by 18% to £51.1m (2004: £43.3m), while profit before tax² increased by 18% to £47.4m (2004: £40.1m). This was despite a £5.2m negative impact of weaker hedged exchange rates for US dollar sales made by Ultra's businesses in the UK and Canada.

The effective tax rate for the Group increased to 27.7% (2004: 27.2%), due mainly to a higher proportion of Ultra's profits being generated in North America, where marginal tax rates are higher. This resulted in earnings per share² growth of 16% to 50.7p (2004: 43.7p).

continued on page 7

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19 times

Interest cover

Bank interest cost was covered 19 times by operating profit¹

105%

Cash conversion⁴

Demonstrating Ultra's consistently high quality of earnings

18%

Total annual shareholder return

Ultra has delivered an average annual total shareholder return of 18% since flotation in 1996

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, AND BY COMMUNICATING EFFECTIVELY WITH SHAREHOLDERS AND THE FINANCIAL COMMUNITY GENERALLY.

Key performance indicators

	Performance indicator	Definition	2005 result
1	Revenue growth	Growth in total Group revenue compared to prior year.	10%
2	Profit growth	Growth in Group profit before tax ² , compared to prior year.	18%
3	Order book visibility	Order cover for next financial year as percentage of market consensus sales forecast for the year.	62% cover for 2006 on consensus sales of £379m
4	Growth in earnings per share over a three year period	Growth in earnings per share ² , calculated over a rolling three year period.	45%
5	Cash conversion	Cash generated by operations, less net purchases of property, plant, equipment and LTIP shares, less expenditure on product development, expressed as percentage of operating profit ¹ .	105%
6	Interest cover	The ratio of operating profit ¹ to financing costs associated with bank borrowings.	19 times
7	Relative total shareholder return	Total shareholder return (capital growth plus dividends paid, assuming dividends reinvested) over a rolling three year period compared to the FTSE 250 index.	+2% per annum

Key performance indicators

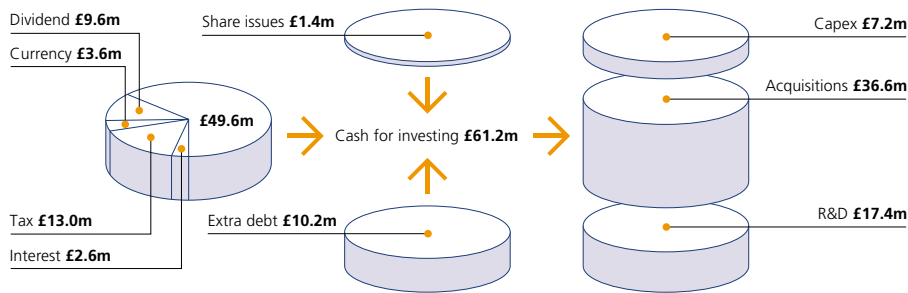
The indicators shown above have been identified by the Directors as giving the best overall indication of the Group's long-term success. **Revenue growth** gives a quantified indication of the rate at which the Group's business activity is expanding. A satisfactory **profit growth** trend confirms that additional revenue is being gained without profit margins being compromised. It also indicates that the additional contribution to profits from new acquisitions is greater than the financing costs incurred as a result of taking on additional debt to fund those acquisitions. **Order book visibility**, based upon expected sales during the year to come, gives the Board

confidence as to the achievement of future growth forecasts. A key objective of the Board is to increase **earnings per share²** at a faster rate than other similar quoted companies in the UK. If successful this should ensure that investors will continue to hold Ultra's shares, rather than those of its peers. Achievement of this objective is the key measure that is used for determining awards under the Executive Directors' Long Term Incentive Plan scheme. The Directors aim to manage the business so that it continues to generate high levels of cash, which can then be reinvested in the business in the form of acquisitions. The Board uses **operating cash conversion** as a simple yet reliable measure of cash generation, which

represents the major element of the Group's short-term incentive bonus scheme. Whilst free cash will continue to fund Ultra's expansion by acquisition, it is important to ensure that the balance sheet remains sufficiently strong and that the cost of carrying additional debt does not become too high. **Interest cover** is a reliable indicator of balance sheet strength. Finally it remains the overriding objective of the Board to provide shareholders with a long-term return on their investment in Ultra that exceeds that which would be achieved by other potential equity investments that present a similar risk profile. **Total shareholder return** is a suitable measure, as compared to the overall population of FTSE 250 companies.

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Investing for growth



£61.2m

Investment

Ultra invested £61.2m in 2005 in acquisitions, research and development, capital expenditure and on new business development

AT THE END OF 2005 THE GROUP'S ORDER BOOK WAS VALUED AT THE RECORD LEVEL OF £500.7 MILLION, AN INCREASE OF 27% OVER THE POSITION AT THE SAME TIME LAST YEAR.

Group results (continued from page 5)

Operating cash flow³ was again excellent at £53.8m (2004: £46.9m). The conversion of operating profit¹ to operating cash flow³ was 105%, emphasising Ultra's high quality of earnings. This brings the Group's average cash conversion over the last five years to 114%. Net debt⁵ at the year-end increased by just £10.2m to £34.3m (2004: £24.1m), after funding an investment of £61.2m in the year. Of this, a total of £36.6m after expenses was spent on acquisitions, with £24.6m (2004: £20.7m) spent on research and development, capital expenditure and new business development. This £24.6m investment of Ultra's funds was supplemented by customer-funded product development activity. In 2005, this amounted to £60.6m (2004: £54.9m) and so, in total, over 20% of Ultra's activity is new product development.

At the end of 2005 the Group's order book was valued at the record level of £500.7m, an increase of 27% over the position at the same time last year. This impressive order book achievement maintains historic levels of firm order cover for the coming year and reflects Ultra's success in winning substantial positions on new programmes.

2005 ACQUISITIONS

In 2005, the Group made two acquisitions, Horizon Aerospace in March and Audiopack Technologies in July. The total cash consideration for acquisitions was £36.6m including expenses, financed using Ultra's banking facilities.

Horizon, now fully integrated into Ultra's Flightline Systems business in Rochester, New York, USA, supplies and supports a broad range of cockpit instruments for military and civil aircraft. The range includes mechanical, electro-mechanical, digital and analogue-digital instruments. These products are used on many aircraft including Boeing's 737 and 777 and complement Flightline's existing range of specialist sonobuoy receivers

and electro-mechanical gyroscopes. Flightline Systems is part of Ultra's Tactical & Sonar Systems division.

Audiopack strengthens Ultra's communications capability within the military and homeland security markets and is now also part of the Tactical & Sonar Systems division. Based in Cleveland, Ohio, USA, Audiopack's main activity is developing and manufacturing rugged voice communications equipment for personnel wearing protective clothing, gas masks and breathing apparatus. The products are supplied mainly to the military and homeland security sectors together with 'first responders' such as the fire, medical and police services. These customers demand robust products of the highest quality to provide reliable communications between team members operating in harsh and hazardous environments. Ultra will be able to offer elements of its battlespace IT product range to this market sector for command and control purposes.

DIVISIONAL REVIEW

AIRCRAFT & VEHICLE SYSTEMS

AIRCRAFT & VEHICLE SYSTEMS COMPRISES FIVE BUSINESSES IN THE UK AND US THAT SUPPLY ADVANCED TECHNOLOGY PRODUCTS AND SOFTWARE FOR MILITARY AIRCRAFT, LAND VEHICLES AND FOR CIVIL AEROSPACE MARKETS.

Revenue in the division increased by 10% to £84.4m (2004: £76.6m). Operating profit¹ grew by 7% to £15.9m (2004: £14.9m), giving an operating margin¹ of 18.9% (2004: 19.4%).

The continued buoyancy of the civil aerospace market drove sales growth of Ultra's cabin quietening equipment for the Bombardier Q Series of turboprop aircraft and landing gear control computers for Airbus aircraft. The development activity on the door and landing gear proximity sensing and wing ice protection systems for the Boeing 787 aircraft progressed to plan, with

the increased investment funded by Ultra impacting margins slightly in the division. Sales of these systems should commence in 2007 ahead of the 787 entering service in 2008.

An important achievement in the year was the selection of Ultra to supply equipment for the Airbus A400M military transport aircraft. Ultra secured the contract to supply a noise cancellation system for the aircraft's main cargo bay to reduce the propeller-induced noise to an acceptable level within the latest health and safety requirements. Ultra's scope of supply on the aircraft also includes proximity sensors and associated electronics, which sense the position of the landing gear and the landing gear doors to ensure correct operation, together with the provision of ruggedised wiring harnesses for the landing gear. This major new programme for Ultra contributed significantly to the order book growth in 2005. At the end of the year, Airbus had orders for 192 aircraft, which is due to enter service in 2009.

Sales of Ultra's HiPPAG missile cooling compressor for the US Navy's F/A-18 E/F Super Hornet aircraft rose in 2005 but the rate of production for the Eurofighter Typhoon aircraft was reduced in order to realign HiPPAG deliveries to the aircraft programme. Following a number of successful trials in the US of Boeing's Small Diameter Bomb system, Ultra was awarded the first low-rate initial production contracts for this munitions ejection variant of HiPPAG. The lead aircraft for this programme is the F-15 Eagle to which the Small Diameter Bomb system will be retrofitted. The development of HiPPAG for its munitions ejection role on the F-35 Joint Strike Fighter aircraft also proceeded satisfactorily.

In the UK, deliveries of cockpit controls, indicators and landing gear control equipment for the first tranche of the Eurofighter Typhoon continued on schedule during 2005 and additional orders for this equipment were secured for the second tranche of 236 aircraft, for which the delivery period extends out to 2012.

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>500

Air Defense Systems Integrator
Ultra has over 500 ADSIs in operational use

30%

Battlespace IT
Sales of battlespace IT equipment represented more than 30% of Group revenue for the first time

42%

North America
42% of Ultra's revenue came from the North American market in 2005

ULTRA'S DOMINANCE OF AIRLINE BAGGAGE RECONCILIATION SYSTEMS, TO ENSURE THAT UNACCOMPANIED BAGS ARE NOT INADVERTENTLY LOADED ONTO AIRCRAFT, CONTINUED WITH THE ON-TIME COMMISSIONING OF THE SYSTEM THAT SERVES ALL OF THE INTERNATIONAL AIRPORTS IN NEW ZEALAND.

Production deliveries commenced to BAE Systems of the indirect vision and vetronics systems for the British Army's Engineer Tank System and crew controls equipment for the Terrier combat engineering vehicle, making a significant contribution to the division's growth. A future priority for the UK's armed forces will be the enhancement of military capability through technology insertion to existing platforms as outlined in the MoD's recent Defence Industrial Strategy. In anticipation of this, Ultra teamed with CTAI, a joint venture between BAE Systems and GIAT, to position for a competition to upgrade the turret of the British Army's Warrior armoured fighting vehicle.

INFORMATION & POWER SYSTEMS

INFORMATION & POWER SYSTEMS CONSISTS OF SEVEN BUSINESSES THAT SUPPLY INFORMATION MANAGEMENT AND POWER PRODUCTS FOR DEFENCE, COMMERCIAL AND AIRPORT APPLICATIONS WORLDWIDE.

Revenue in the division increased by 3% to £117.3m (2004: £113.7m). Operating profit¹ increased by 20% to £18.1m (2004: £15.0m). The operating margin¹ was 15.4% an increase from 13.2% in the prior year.

Revenue growth in the division was impacted by the decline of the trackside rail power supply activity for the UK's Network Rail that peaked in 2004. However, this reduction was more than compensated for by the growth in battlespace IT equipment and the continued success of Ultra's ADSI data link processor and situational awareness system in the US. Development contracts were secured to adapt the ADSI to be part of a monitoring and control element of tactical data link networks for the US Air Force and to provide a common data link processor for all four services of the US armed forces. These are multi-year programmes at the heart of US battlespace IT capabilities and they contributed considerably to the growth of the division. The continuing peace-keeping operations in Iraq have also driven strong demand for ADSI systems to provide

situational awareness and airspace management capabilities vital to the US Army units deployed in the theatre of operations.

Ultra's airport IT systems business achieved an excellent performance which also contributed to the growth of the division. There was increased activity on the IT infrastructure of BAA's new Terminal 5 at London Heathrow airport as the project transitioned from design to implementation. In September, Ultra secured the contract to supply IT integration services to Shanghai Pudong international airport. This built on Ultra's success at Terminal 5 and capitalised on Ultra's market position in China gained through the acquisition of Videcom in 2004. Shanghai will be a world class reference site for Ultra in the rapidly-growing Asia-Pacific airport market.

Ultra's dominance of airline baggage reconciliation systems, to ensure that unaccompanied bags are not inadvertently loaded onto aircraft, continued with the on-time commissioning of the system that serves all of the international airports in New Zealand. Ultra's managed baggage reconciliation services, provided at Heathrow, in Australia and in the US, continued to operate successfully and are providing the expected revenue growth and return on investment.

The highest priority planned procurement programme for the British Army is the Future Rapid Effects System (FRES) comprising a family of medium-weight armoured vehicles to cover a wide range of combat and support roles. FRES will incorporate a significant amount of battlespace IT so that it is able to connect to and cooperate with other military systems. By teaming with Lockheed Martin, one of the two competing lead contractors, Ultra has secured a sub-contract relating to the electronic architecture technology demonstrator programme. This work will define and prototype the team's proposed battlespace IT infrastructure for FRES. It is strategically important early positioning for the eventual development and production phases. The in-service date for FRES is

expected to be early in the next decade with production continuing into the late 2020s.

Development activity for the replacement control system for the nuclear reactors powering the Royal Navy's submarines progressed satisfactorily to plan and the complex central control consoles for the Astute submarine were also delivered. A contract was secured to upgrade and support the equipment that enables the control and firing of weapons from the torpedo tubes of the Royal Navy's Trafalgar and Vanguard Class submarines. The installation of this equipment, which was originally developed for the Astute Class submarine, will achieve a common fit across the fleet and much reduced through-life support costs for the UK MoD.

TACTICAL & SONAR SYSTEMS

TACTICAL & SONAR SYSTEMS, WITH THE ADDITION OF AUDIOPACK AND THE INTEGRATION OF HORIZON INTO FLIGHTLINE SYSTEMS, COMPRISES EIGHT BUSINESSES IN THE UK AND NORTH AMERICA THAT SUPPLY COMMUNICATIONS AND UNDERWATER EQUIPMENT TO HOMELAND SECURITY AND MILITARY USERS WORLDWIDE.

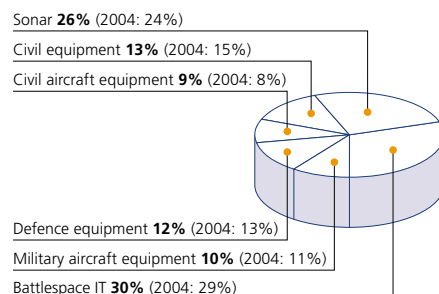
Revenue in the division increased to £140.7m from £120.4m in 2004, a rise of 17% of which 7% was organic. Operating profit¹ increased 28% to £17.1m (2004: £13.4m) giving an operating margin¹ of 12.2%, an increase from 11.1% in the prior year.

The new variant of the US Navy's passive sonobuoy was successfully introduced in the second half of 2005, providing improved performance at reduced cost. Overall, however, the level of sonobuoy sales was broadly unchanged for the third year in a row. In both the US and UK, funded development proceeded on the next generation of sonobuoy systems that will improve the ability to detect small, extremely quiet, diesel-electric submarines able to operate in shallow, coastal waters. Ultra's dominance of the sonobuoy export market continued with sales to France, Australia, Canada, Taiwan and Korea.

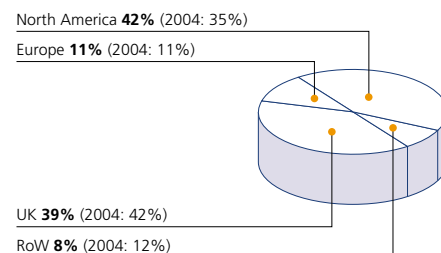
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A KEY FEATURE OF ULTRA'S STRONG NORTH AMERICAN RESULTS WAS AN EXCELLENT PERFORMANCE BY ADVANCED TACTICAL SYSTEMS, WHERE SHIPMENTS OF ADSI SYSTEMS TO THE US ARMED FORCES REACHED RECORD LEVELS.

Sales by sector



Sales by destination



Significant orders for Ultra's specialist sonobuoy telemetry receivers were won during the year, securing long-term positions on a number of new anti-submarine warfare aircraft programmes. For fixed wing aircraft these included the Boeing P-8A aircraft being developed to replace the US Navy's ageing P-3 Orions, which has a potential for up to 150 aircraft, and the Turkish Navy's ATR-72 ASW programme. In addition, the latest helicopter versions of Ultra's sonobuoy receiver were selected for the Cyclone maritime helicopter programme in Canada and the MH-60R Seahawk in the US.

Sales in the division were boosted by the on-time delivery of a further six ship-sets of the Group's Surface Ship Torpedo Defence system to the Royal Navy, with three of these systems installed on ships and at sea by the year-end. In the US, the torpedo defence technology demonstrator programme secured in 2004 made excellent progress and successful trials have now been conducted against real weapons. The Group also benefited from increased sales of submarine-launched torpedo countermeasures, both for the US Navy and international customers. During the year, development of the bow sonar for the Royal Navy's Type 45 destroyer made satisfactory progress and the first system was nearing completion by the year-end.

The Group was awarded a contract for the Royal Navy's mine disposal programme, teamed with Atlas Elektronik in Germany. The system is an adaptation of an existing design that Ultra will supply and then support from within the UK.

Sales of battlespace IT equipment once again contributed to the growth of this division, with particular success achieved in international markets. Ultra made further deliveries of high capacity radios to the US Army's communications infrastructure programme and for its Patriot missile defence system. A new jam-resistant radio with improved data transmission capacity was developed for the South Korean armed

forces and initial production deliveries were made in the second half of the year. Radios were supplied to the Canadian armed forces for use during their deployment in Afghanistan for peace-keeping duties.

Following several years of investment and market positioning, during which Ultra designed what is planned to be the NATO standard for radio control links for unmanned air vehicles (UAVs), Ultra won a contract to supply such equipment for the British Army's Watchkeeper UAV programme. This is another new niche for Ultra which, with its associated encryption equipment, is anticipated to contribute to the growth of the Group.

SECTORAL ANALYSIS OF ULTRA'S RESULTS

Market sector analysis

The Group has seen its battlespace IT activities grow in importance during the past few years and sales of this equipment represented more than 30% of total revenue for the first time. While the products of both Audiopack and DNE are in this sector, strong growth in sales of ADSI systems to the US armed forces was the main reason for this excellent performance. Ultra's dependence upon its sonobuoy products continues to decline and it was encouraging to see new product niches driving a strong increase in sales of sonar equipment, up by 17% in the year. Notable growth was achieved by Sonar & Communication Systems, where shipments of surface ship torpedo defence systems ramped up during the year. In addition Ocean Systems received more funding under its torpedo defence demonstrator contract with the US Navy. While the value of sales of equipment for military aircraft increased slightly, it reduced in 2005 from 11% to 10% of Group revenue. Lower shipments of equipment for the Eurofighter Typhoon programme, in response to the customer's demands, inhibited the growth in this sector. Ultra's focus on the defence sector strengthened during the year, driven by the acquisitions, and this area represented 78% of

the Group's activities, 2% higher than in 2004. Sales to civil markets accounted for the 22% balance of Ultra's business (2004: 23%). Here the main feature was strong demand for civil aircraft equipment, both for Airbus new build and also in the after-market. Sales in this area increased by 16% in absolute terms and were 9% of total revenue, up by 1% from 2004. Other civil sales declined from a 15% to a 13% share, with the reduced demand for transit power equipment being the key reason.

Geographic analysis

Ultra continues to increase its presence in North America and 2005 was the first year for which this market was the Group's most significant, accounting for 42% of total revenue (2004: 35%). This change was caused partly by acquisitions, with DNE contributing for the entire year and the additional benefit of two further US acquisitions during the year, Horizon Aerospace and Audiopack. However the key feature of Ultra's strong North American results was record sales of ADSI systems. The significance of the UK market for Ultra declined in the year and domestic sales represented 39% of Group revenue in the year, down from 42% in 2004. Lower sales of railway transit power equipment was the main reason, although it was encouraging to see above-average growth coming from Electrics, driven by strong sales of equipment for armoured fighting vehicles, and Airport Systems, where activity increased at London Heathrow's new Terminal 5. Ultra's largest business, Sonar & Communication Systems also reported sales growth of more than 10%. Exports to continental Europe accounted for 11% of Group revenue, in line with the previous year. The most marked reduction was seen in sales to the rest of the world, which declined from 12% to 8% of revenue. This was due mainly to lower sales of sonobuoys and torpedo countermeasures to Australia, where two large orders were fulfilled during 2004, and to the timing of shipments of military radios to South Korea.

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>100

The US Navy has committed to procuring more than 100 new Anti-Submarine Warfare aircraft, each of which will be fitted with Ultra equipment

ONE OF ULTRA'S STRENGTHS IS THE GROUP'S POSITION ON MANY MAJOR INTERNATIONAL PROGRAMMES AND PLATFORMS. AS A RESULT OF THIS BROAD SPREAD OF ACTIVITY, NO SINGLE PROGRAMME GENERATES MORE THAN 5% OF ULTRA'S REVENUE IN ANY SINGLE YEAR, UNDERPINNING THE RESILIENCE OF THE GROUP'S PERFORMANCE.

ULTRA'S FUTURE OUTLOOK

Market trends

Whilst budgets have risen over recent years in Ultra's main defence markets, in both the US and UK the continuing costs of peace-keeping operations is putting strain on these defence budgets. The recently published US Department of Defense Quadrennial Defense Review generally maintained support for the current US defence equipment programmes. However the affordability of the implied procurement plans was not addressed by the review. As a consequence it is possible that some US equipment programmes will be deferred, curtailed or cut altogether at some future date. In the UK, the Defence Industrial Strategy, published in December 2005, also indicated the degree of strain in the present budgets.

One of Ultra's strengths, however, is the Group's position on many major international programmes and platforms. As a result of this broad spread of activity, no single programme generates more than 5% of Ultra's revenue in any single year underpinning the resilience of the Group's performance. It is considered unlikely that sufficient programmes would be cut severely or curtailed simultaneously to cause a major reduction in Ultra's level of business.

Within the US and UK defence budgets, expenditure continues to be focused on improving the use of intelligence, on enhancing the ability rapidly to deploy forces and in providing increased protection for personnel. Ultra has pursued a strategy that has positioned the Group to benefit from these trends and constantly seeks opportunities to offer new products and services to meet such customer requirements.

There is some evidence that the decline in one of Ultra's traditional market sectors, that of Anti-Submarine Warfare (ASW), has bottomed out. The US has committed to buying over 100 P-8A ASW fixed wing aircraft and is also procuring over 240 ASW

helicopters. The Canadian government is procuring 28 ASW helicopters. In Europe, the NH-90 ASW helicopter will shortly enter service as will the long-delayed Nimrod MRA4 aircraft. In the short-term, Ultra is supplying equipment for each of these programmes. In the longer-term, the entry into service of these platforms might be expected to increase the annual consumption and therefore demand for sonobuoys, the acoustic sensors that are used to detect submarines and for which Ultra is the world-leading supplier.

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. This is a market sector in which Ultra provides innovative and cost-effective solutions.

Worldwide, there is a move to increase the unmanned element of fighting forces. By so doing the cost per platform is reduced, as is the risk to personnel from enemy action. For Ultra, this will reduce demand for specialist Human-Machine Interface (HMI) equipment used in cockpits, for example. Anticipating this, Ultra has positioned its HMI equipment for use on the base stations that are used to control the unmanned vehicles.

Ultra's customers aspire to stable or reducing prices for the goods and services that they procure. This inevitably leads to cost pressures to which the Group must respond. Ultra has a long track record of product innovation to reduce costs whilst delivering improved performance and achieving operational efficiencies by working more intelligently. More recently Ultra has made significant progress in sourcing production in low cost economies where this is appropriate, given the nature of the products that the Group provides. The anticipated cost reductions have been achieved, thereby helping to protect and improve the Group's operating margins.

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30

International success

Ultra sells its products and services in more than 30 countries worldwide

15%

Increased dividend

The Directors are recommending a total dividend increase of 15% to 15.9p

62%

High visibility of earnings

Ultra started 2006 with firm order cover for 62% of projected revenue

Management of risks and uncertainties

ULTRA'S CONFIDENCE IN ITS ABILITY TO CONTINUE TO DELIVER GROWTH IS UNDERPINNED BY A NUMBER OF KEY FACTORS. THE GROUP HAS A TRACK RECORD OF YEAR-ON-YEAR SUCCESS DESPITE SIGNIFICANT VOLATILITY 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.

Approximately 80% of Ultra's revenue is from the defence sector. A risk would therefore be a significant worldwide reduction in defence expenditure. The overall size of the defence budgets relative to Ultra's annual revenue provides sufficient headroom for the Group's growth to continue. Ultra's constant focus has been on ensuring that its businesses operate in a large number of growing niche markets where the Group can create and maintain sustainable competitive advantage. This specialisation and diversity give some protection from budget variations and so provide robustness to Ultra's performance.

Ultra's financial performance has not been significantly affected by the current allied operations in Afghanistan and Iraq. It is possible that these operations might be scaled back in the next few years. Since Ultra did not benefit materially from the start of these operations, it is anticipated that a withdrawal would not harm the Group's trading position. Indeed, it might well be an overall benefit to the Group as it may alleviate some of the current pressures on defence budgets.

The international spread of Ultra's activities provides resilience to its performance. The Group now sells its products and services in over 30 countries worldwide and this has broadened the customer base. Ultra also

has a transatlantic capability, with 10 of its 20 businesses located in North America. As such, it operates as a domestic agent in both markets and can exploit its innovative solutions on both sides of the Atlantic.

Ultra is represented on a significant range of major international programmes and platforms. As a result, no single programme represents more than 5% of Ultra's revenue in any single year. The cancellation or curtailment of any single programme is unlikely therefore to have a material adverse impact on the Group.

Ultra supplies to all elements of the armed forces, i.e. the army, navy, air force and marines, together with first responders such as medical staff and firefighters. This customer spread provides an element of risk mitigation. In addition, Ultra operates in a number of different and distinct market sectors, including battlespace IT, sonar and equipment for military air, land and sea platforms. Again, this mitigates the risk of decline in any one market sector materially affecting Ultra's overall performance.

Ultra has significant business in the civil sector and this provides useful diversification, often providing an alternative market in which to exploit complementary skills and technologies. Within the civil market, Ultra operates in the aerospace, transport and commercial security sectors. This spread gives further resilience to Ultra's performance.

The Group's largest exposure to the adverse effects of exchange rate volatility is to the UK£:US\$ impact. Whilst Ultra has a natural hedge from its geographic split of businesses, the Group has also responded by sourcing a higher proportion of the cost of dollar-denominated products in dollar zones. This is in addition to the Group's usual currency hedging arrangements described later.

The industries in which the Group operates continue to experience restructuring, which sometimes results in Ultra's customers

themselves becoming more vertically integrated. This may increase the incidence of the Group's customers having capabilities that overlap with Ultra's. The threat that this otherwise might pose is offset by Ultra's strategy of operating in specific market niches where it has some sustainable differentiation.

Outlook for Ultra

The record order book of £501m represents a significant increase in the year and provides Ultra with its customary level of visibility of earnings. It reflects the Group's strong positions on existing platforms as well as its success in winning positions on new programmes. Importantly, the Group started 2006 with firm order cover for 62% of projected revenue, a similar level of visibility to previous years.

In Ultra's main defence markets worldwide, budgets continue to rise and the recent emphasis on security and surveillance activities continues. The continuing buoyancy of the civil aerospace market not only drives increasing levels of production equipment but also benefits important aftermarket spares and repairs revenues. The strong growth in air passenger travel will drive demand for new infrastructure including airport IT.

Ultra enters 2006 with a strong balance sheet and the headroom, not only to make further acquisitions that will enhance and complement the Group's range of niche activities, but also to continue to invest in new product development to meet market demands. Current market conditions, coupled with Ultra's proven ability to win new business and to execute contracts effectively, give the Board confidence in the continuing progress of the Group in 2006.

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114%

Five year cash conversion⁴

The Group has achieved an average operating cash conversion of 114% over the last five years

£38.1m

Free cash flow

Ultra generated £38.1m of free cash in 2005

THE DIRECTORS ARE PROPOSING A FINAL DIVIDEND OF 10.7P, BRINGING THE TOTAL DIVIDEND TO 15.9P (2004: 13.8P), AN INCREASE OF 15%. DIVIDEND COVER WILL THEREFORE BE MAINTAINED AT ABOUT THREE TIMES.

FINANCIAL POSITION

Operating cash flow³

Ultra maintained its record of strong cash generation during the year, with operating cash flow, after capital expenditure and LTIP share purchases, of £53.8m (2004: £46.9m), equivalent to an operating profit¹ to cash conversion ratio of 105%. Ultra continues to focus upon maintaining working capital at a low level without jeopardising the viability of the business. At the end of 2005, Ultra had net current liabilities, excluding cash and bank borrowings, of £18.8m (2004: £10.4m). The main driver for this position was an increase of £7.1m in payables, excluding the effect of acquisitions. Creditor days outstanding at year-end were 51, a similar level to 2004. Inventories rose by £1.6m and receivables by £1.3m, reflecting the overall growth in revenue. There was a £7.3m net cash investment in property, plant and equipment during the year compared to a depreciation charge of £6.1m. Within this total the only significant capital investment was in New Zealand. Here new baggage reconciliation systems have been installed at the country's six international airports, with expenditure during the year of £1.6m. In addition £0.6m was spent on buying Ultra shares for the Long-Term Incentive Plan. This was lower than the previous year's £1.1m because shares not awarded during 2004 were used during 2005.

Acquisitions and intangible assets

Ultra made two acquisitions during the year. Horizon Aerospace was acquired in March for a total cost including expenses of £2.4m, of which £1.3m has been treated as goodwill. Audiopack Technologies Inc was acquired in July through a share purchase transaction for £33.9m, including expenses. Of the total consideration £4.1m has been treated as goodwill and a further £27.7m as intangible assets. In both cases the goodwill has been capitalised and, under International Financial Reporting Standards, will remain on the balance sheet at the acquired value,

assuming no future impairment charge. Intangible assets of Audiopack will be amortised over a ten-year period. Following a review during the year of the fair value of assets acquired with Videcom International Ltd in July 2004, a reduction of £0.2m was made to the goodwill associated with that business. Capitalised investments of £2.9m were made in new product development and other intangible assets with long-term commercial value during the year.

Interest and profit before taxation

Financing costs, excluding losses on financial instruments, grew by £0.9m to £4.3m for the year. One reason was a £0.5m rise in interest charges resulting from an increase in bank borrowings to fund acquisitions. This increase was partly offset by a reduction in the effective cost of debt following the maturity in April 2005 of the fixed interest rate hedging contract to which Ultra committed in 2000. Interest costs on bank debts, including amortised fees, amounted to £3.3m overall, compared to £2.8m in 2004. The 2005 cost was covered 18.6 times by operating profit¹. In addition, financing costs included a notional charge of £0.9m (2004: £0.5m) representing the amortisation of the UK defined benefit pension fund deficit.

The growth in financing costs meant that the headline profit before tax² improved by 18% to £47.4m (2004: £40.1m). Amortisation of intangibles arising on acquisition amounted to £3.3m in the year. A loss of £3.4m was reported on financial instruments and this was caused by a 12% strengthening in the US dollar against sterling during the year. The Group's UK and Canadian businesses hedge forward their US dollar denominated sales revenues, typically over an eighteen-month period, and the stronger dollar had the effect of reducing the nominal value of these financial instruments at the year-end closing exchange rates. It should be emphasised that this notional reported "loss" will never be realised; it is simply a timing effect. The real worth of the hedging

contracts to the Group is to fix the value in local currency of foreign currency sales receipts in the future, thus reducing the uncertainty that would otherwise exist as to their realisable value. Under the transitional arrangements for the implementation of International Financial Reporting Standards this item was not separately reported in the previous year. Statutory profit before tax was £40.7m (2004: £40.1m).

Earnings per share² and dividends

The effective Group tax rate rose slightly to 27.7% (2004: 27.2%) due to a higher proportion of Ultra's profits being generated in the US, where marginal tax rates are higher. Earnings per share², rose by 16% to 50.7p (2004: 43.7p). The Directors are proposing a final dividend of 10.7p, bringing the total dividend to 15.9p (2004: 13.8p), an increase of 15%. This continues to reflect the Group's policy of maintaining a dividend that is covered about three times by earnings per share².

Financing

Ultra generated £38.1m of free cash flow before dividends and acquisitions during 2005 (2004: £36.0m). After dividend payments of £9.6m, this left £28.5m available to help fund the acquisition expenditure of £36.6m. The balance came from the Group's banking facilities and, as a result of this and certain currency effects, net debt⁵ increased by £10.2m during the year to close at £34.3m (2004: £24.1m). The balance sheet remains very strong and Ultra has substantial headroom on its banking facilities to make further acquisitions.

Ultra's existing operations and new acquisitions are funded by a combination of retained cash and medium-term bank borrowings. During November 2005 the Group renewed the banking facility that is provided by a small syndicate led by The Royal Bank of Scotland. The new facility, which provides up to £120m of revolving credit over a five-year period, is denominated in sterling, US dollars and Canadian dollars

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£120m

Funding

Ultra's new banking facility provides up to £120m of revolving credit

+16%

Earnings per share²

Ultra's earnings per share² increased by 16% to 50.7p

ULTRA MAINTAINED ITS RECORD OF STRONG CASH GENERATION DURING THE YEAR, WITH OPERATING CASH FLOW, AFTER CAPITAL EXPENDITURE AND LTIP SHARE PURCHASES, OF £53.8M (2004: £46.9M).

and is used for balance sheet and operational needs. Both the sterling and US dollar elements fund day-to-day working capital requirements and the US and Canadian dollar borrowings also represent natural hedges against assets denominated in those currencies. A further overdraft of £10m is also available for funding short-term working capital requirements.

Financial risk management

Interest rates

An interest rate hedge, denominated in sterling, which had been in place for five years, matured during 2005. A significant portion of the Group's current borrowings has been incurred to fund recent acquisitions in North America and is therefore denominated in US and Canadian dollars. With the objective of reducing the risk that is associated with debt at floating interest rates, new three-year interest rate hedging contracts were entered into in December. These cover \$40m of US dollar borrowings, reducing to \$20m over two years, and \$30m of Canadian dollar debt. These amounts compare to gross debts of US \$58.5m and Canadian \$42.4m that were in place at the end of 2005. The remaining £36.4m of gross debt was at floating interest rates. The effective overall annual interest rate for the total gross debt of £74.7m at year-end was 4.8%.

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 sensitivities are to the US and Canadian dollars.

The average dollar exchange rates used in the year to translate the sales and operating profits of Ultra's US and Canadian subsidiaries into sterling strengthened by 3% and 9% respectively compared to 2004. For the Group as a whole, currency translation effects increased sales by £5.7m or 2% and operating profit¹ 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 operating profit¹ is subject to 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 to 24 months. Exposure to other currencies is hedged as it arises on specific contracts. Based upon the combined net exposure of about US \$80m last year, operating profit¹ in 2005 would have been £5.2m or 10% higher had the overall hedged rate remained unchanged from the previous year. Ultra's effective US\$:UK£ rate for 2006, based upon the forward contracts currently in place, is expected to be approximately \$1.77, compared to \$1.73 in 2005.

Pensions

Ultra offers company-funded retirement benefits to all its employees. In the UK most staff still participate in the Ultra Electronics Limited defined benefit scheme, which was closed to new entrants in 2003. There was a net IAS 19 deficit after tax of £31.3m on the scheme at the end of 2005, compared to £27.1m in 2004. Although the value of the scheme assets increased by £22.4m during the year, this was less than the increase of £28.4m in the liabilities. The main reason for this growth was a lower discount rate for future liabilities, due to the current low yield on gilts. Its investment strategy is focused upon equities, which represent 87% of the scheme assets. This reflects the fact that the scheme is relatively immature, with just 17% of the members already retired, and remains strongly cash positive.

The scheme has a statement of investment principles. This includes a statement on socially responsible investment which is delegated to the investment managers.

Pension management and governance is undertaken by pension trustees on behalf of the members. 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.

Employees at Tactical Communication Systems in Canada also participate in a defined benefit scheme. There was an IAS 19 deficit of £1.3m on this scheme at the end of 2005 compared to £1.0m in 2004. This will be eliminated over the following ten years by increasing company contributions by an amount that has been agreed with the scheme actuaries and the Canadian regulatory agencies.

All staff that have joined Ultra in the UK since the defined benefit scheme was closed in 2003 have been invited to become members of the Ultra Electronics Group Personal Pension Plan. Under the terms of this defined contribution scheme, company contributions are supplemented by contributions from the employees.

In the US, Ultra offers a defined contribution 401(k) retirement benefit plan to full-time employees. Under this plan, Ultra provides participating and contributing employees with matching contributions, subject to plan and US Internal Revenue Service rules. DNE transferred its assets into the Ultra plan in 2005. Audiopack, which became part of Ultra during 2005, will also consolidate its current plan into the Ultra scheme during 2006. Wells Fargo provides administration and is also a directed trustee of the plan.

¹before amortisation of intangibles arising on acquisition. ²before amortisation of intangibles arising on acquisition and loss on derivative financial instruments.
³cash generated by operations, less net capital expenditure, R&D and LTIP share purchases. ⁴cash generated by operations, less net capital expenditure, R&D and LTIP share purchases as % of profit from operations before amortisation of intangibles arising on acquisition. ⁵bank overdrafts and loans less cash and cash equivalents.



Ultra supplies high-capacity tactical radio systems



Ultra's ADSI systems drive the displays at air operations centres

battlespace IT for military advantage

30%

Battlespace IT equipment

Sales of battlespace IT equipment and systems accounted for over 30% of Ultra's 2005 revenue





Ultra's ADSI systems provide a deployable air defence capability



Ultra is providing the secure data links for the UK Watchkeeper UAV programme



The Polish Navy is achieving NATO compatibility by using Ultra equipment

ULTRA IS DEVELOPING EQUIPMENT TO MANAGE REAL-TIME INFORMATION FLOWS EFFECTIVELY AND TO DELIVER MILITARY ADVANTAGE THROUGH HAVING INFORMATION SUPERIORITY.

In conflicts, the side that manages real-time battlespace intelligence most effectively to achieve information superiority has a decisive edge. Ultra is constantly investing in the development of new battlespace IT products that will help deliver that military advantage. Ultra's Air Defense Systems Integrator (ADSI) product provides a world-leading capability for processing information from tactical data links, intelligence feeds and radar data in many different formats. This information is translated into an unambiguous, coherent picture of the tactical situation that is used by the combatants around the battlespace. The latest version of ADSI contains significant additional features and functionality. Many existing users – and Ultra has over 500 ADSIs in operational use – have opted to upgrade to the new version. The flexibility of the ADSI product helped position Ultra to be Northrop Grumman's partner in the development of two new integrated battlespace IT solutions. Ultra's work on these programmes will continue for some time to come. The US Army is also procuring ADSIs to be the heart of new deployable airspace management

cells for air defence. The compact nature of ADSI helps fit the complete capability into wheeled armoured vehicles, thereby maximising mobility.

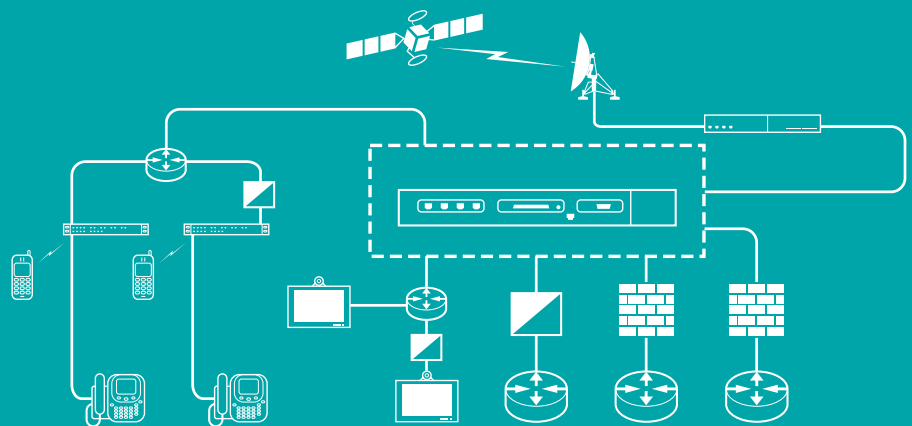
A key element of military tactical communication systems is the wide area network for voice and data transmission between various command levels in land forces. Ultra's advanced microwave trunk radios serve as the backbone of modern tactical line-of-sight networks. They provide high-capacity telecommunication services to interlink battlefield command posts and combat forces. These networks must be able to handle ever-increasing volumes of information, including voice, data, email and real-time video transmissions. Ultra is upgrading the high capacity radio systems for both the US Patriot air-defence missile systems and those used for the US Army's battlefield backbone communications infrastructure. In a parallel move, Ultra has also developed a higher-capacity version of the secure, frequency-hopping radio used by the army of South Korea.

To be tactically useful, communications must be secure. Ultra has a world-leading cryptographic capability and has achieved export sales of such equipment to the US, Canada, Sweden and Germany. Secure data links are also vital in controlling unmanned aerial vehicles and for transferring time-critical information to ground stations. Ultra is developing this equipment for the UK Watchkeeper programme.

Data must be shared across multiple battlespace IT networks, including legacy systems. Ultra provides voice and data multiplexers, multi-service access concentrators and communication switches, and protocol converters used by all branches of the US armed forces. Ultra has recently demonstrated the ability to provide bandwidth efficient communications within an Internet Protocol network while maintaining the high quality of service demanded by military commanders.



Ultra is upgrading the high-capacity radios for the Patriot air defence missile system



Solving IP convergence congestion



Ultra is equipping modern command and control centres



Ultra provides advanced communication equipment for firefighters and other first responders



Six

Torpedo defence systems

In 2005, Ultra sold six torpedo defence systems to the Royal Navy and three were at sea by the year-end

Twenty

Long-term support

Ultra's new weapons interfacing electronics for the Royal Navy will be supported for 20 years



Ultra supplied new power equipment for the US Navy's submarine Dolphin



Modern battlespace IT equipment must survive in harsh environments



Ultra has developed weapon interfacing equipment for the new Astute submarines

expertise in depth

Digitisation of the battlespace is a dominant theme in defence expenditure. Modern command and control systems must meet the need for interoperability, not only with other services but also with allies and coalition partners. Modern designs must also provide integrated solutions – the link between the command and the weapons' fire control functions must be seamless. Ultra's high-integrity, low-latency naval data distribution systems help make this so. Integrated combat systems must be highly cost effective if they are to penetrate the growing market for minor warships and offshore patrol vessels that are required by the world's navies. Ultra has demonstrated its ability to provide very competitive combat systems for this market sector. These integrate radar and electro-optic surveillance, command and control and weapon fire control functions together with navigation, communication and platform management in one cohesive, modular design of integrated bridge. Much use is made of commercial computing equipment and the system design contains industry-standard interfaces to ensure that the system can easily be upgraded and maintained for the life of the platform.

Ultra has won a contract to supply and support new weapon interfacing electronics for the Royal Navy's existing submarines. This system, originally developed for the new Astute class submarines, manages the weapons – the Spearfish heavyweight torpedo and the Tomahawk land attack cruise missile – while they are still in the submarine launch tubes, providing power and monitoring their condition. The equipment manages the upload of target data prior to weapon launch and controls and monitors the launch sequence. The Ultra solution will maximise the commonality of equipment across all Royal Navy submarines. It uses off-the-shelf technology to facilitate the management of obsolescence issues for the next 20 years.

With the acquisition of Audiopack in July 2005, Ultra provides a broad range of rugged voice communications equipment for personnel wearing protective clothing, masks and breathing apparatus in harsh and hazardous environments. This equipment is used in the military and homeland security sectors and by 'first responders' such as the fire, medical and police services. Reliable communications between team members is

vital when operating in dangerous environments. The Ultra equipment can also provide the user with visual information about the condition of the breathing apparatus, including the amount of air left in the tanks, to maximise the safety of operations. Synergistically, Ultra can also offer solutions to provide enhanced command and control information, including the location of users at an incident, using proven technology already developed within the Group.

ULTRA IS SUPPLYING AND SUPPORTING THE EQUIPMENT THAT CONTROLS THE WEAPONS LAUNCH FROM ALL OF THE ROYAL NAVY'S SUBMARINES, INCLUDING THE NEW ASTUTE CLASS.



Ultra supplies advanced electronic control systems for armoured vehicles



Ultra is providing the indirect vision system and the vetronics system for the Engineer Tank System

battlespace IT in armoured vehicles

The British Army's highest priority planned procurement programme is the Future Rapid Effects System ("FRES") family of armoured vehicles. FRES will provide the UK land forces with the capability to conduct rapid intervention, war fighting and a diverse range of other roles. It will comprise a range of network-enabled, medium-weight armoured vehicles designed for rapid deployment by air worldwide. Ultra is part of the team led by Lockheed Martin UK which is one of two teams selected to undertake work on the initial design, assessment and integration of a potential electronic architecture for the vehicles. Ultra positioned itself for selection to the team by successfully demonstrating an ability to provide significant sub-systems for modern armoured vehicles.

For the British Army's Engineer Tank System programme, Ultra has developed two major sub-systems: the indirect vision system and the vetronics system. These are to be fitted to the 33 Trojan obstacle-clearing vehicles and the 33 Titan bridge-layers being supplied by BAE Systems. The vision system comprises cameras, video management electronics and

displays and provides situational awareness to all crew members when operating under armour. The vetronics system provides smart management of electrical power usage and constant power health monitoring. Ultra also provides a range of cameras and crew controls for the British Army's Terrier armoured vehicles. In modern conflicts, the crews must be provided with sufficient all round vision to allow the vehicle to complete its full range of tasks while the hatches are closed to give protection against enemy action. Ultra's success in developing these systems has positioned it to supply similar sub-systems for the potential upgrade of the British Army Warrior armoured vehicle. The UK MoD is planning to extend the life and upgrade the capability of up to 450 Warriors including a new turret to enhance lethality. In preparation for the turret competition, Ultra has teamed with CTAI, a joint venture between BAE Systems and GIAT, the French manufacturer of armoured vehicles. CTAI has developed an innovative gun and associated ammunition and Ultra is supplying a number of different crew controls and electronic units as part of the overall system.

In addition to making a significant contribution to the operational capability of new armoured vehicles, Ultra is also innovating to improve the availability of the current fleet of vehicles. Ultra has demonstrated its ability not only to collect health and usage data from vehicles but also to turn this into useful fleet management information and to present it to the appropriate decision makers. This includes the use of Ultra's 'Syntaxis' collaborative working environment to provide secure data exchange and transmission and also to host third party software tools used for data analysis and decision-making.

33 Trojan obstacle-clearing vehicles are being supplied to the British Army by BAE Systems

FRES

Ultra is undertaking the initial design and integration of a potential electronic architecture for the advanced FRES network-enabled armoured vehicles



Ultra is developing vision equipment and crew controls for Terrier



Armoured vehicle electronics must survive in harsh environments



The British Army's Warrior vehicles will require upgraded electronics

78%

Strong defence

The defence sector is responsible for 78% of the Group's revenue

ULTRA HAS DEVELOPED TWO MAJOR BATTLESPACE IT SUB-SYSTEMS FOR THE BRITISH ARMY'S NEW ENGINEER TANK SYSTEM VEHICLES.





Development of the bow sonar for the Type 45 destroyer made satisfactory progress

ULTRA LEADS INTERNATIONAL TEAMS PROVIDING THE ROYAL NAVY WITH LOW-RISK UNDERWATER BATTLESPACE DEFENCE CAPABILITIES. NEW SYSTEMS ARE AT SEA WITH THE ROYAL NAVY.



Ultra won its UK mine disposal system contract after an extensive set of competitive trials

17%

Increasing sales

Ultra's sales of sonar equipment rose by 17% in 2005, driven by successes in new product niches





Ultra supplied six torpedo defence systems to the Royal Navy in 2005



Ultra specialises in underwater battlespace equipment



Ultra is developing a stealthy communication system for submarines

defending the fleet

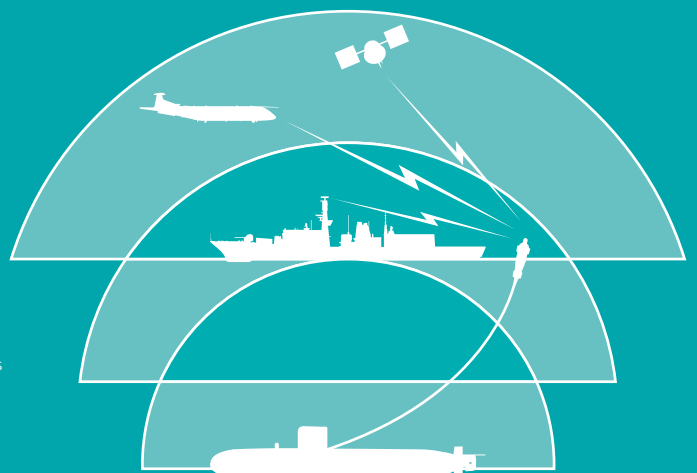
Ultra has a particular expertise in teaming with partners to provide its customers with the 'best of breed' solutions for their requirements at low risk. Typically, this teaming is with international partners and Ultra will manage the transfer of technology into the customer's country to provide and support a sovereign operational capability for that nation. In 2005, Ultra was awarded a contract to supply the Royal Navy with an advanced capability for the destruction of sea mines using a UK variant of the proven SEAFOX system designed by Atlas Elektronik of Germany. The system comprises expendable, remotely-operated underwater vehicles with on-board guidance and navigation equipment. This links to the control station on the host ship and the vehicle is manoeuvred to the sea mine which is then neutralised using an explosive warhead. Ultra will modify the existing SEAFOX design to meet the UK requirement and will manufacture the systems in the UK and then provide a ten-year support and upgrade capability. Ultra's contract from the MoD was won after an extensive series of competitive trials culminating in live explosive trials against a variety of sea mines.

During 2005 Ultra made excellent progress on its US Navy technology demonstrator contract for an advanced torpedo defence system to protect its surface fleet. Successful trials have now been conducted against real weapons. The development work for the US Navy is able to take full advantage of Ultra's work on the Royal Navy surface ship torpedo defence contract. Ultra has specialist underwater battlespace businesses in both the UK and US and so is able to exploit its innovative technologies in both markets. For the Royal Navy torpedo defence programme, Ultra delivered on time a further six ship-sets of equipment and three systems were on ships and at sea by the end of the year.

During 2005, development of the bow sonar for the Royal Navy's new Type 45 destroyer made satisfactory progress. For this programme, Ultra is teamed with the US sonar and combat system specialist EDO Corporation. By the year-end, the first system was nearing completion.

One of the great advantages of a submarine is its stealth – by staying submerged for extended periods, a submarine can avoid detection and so pose a considerable threat

to hostile forces. In order to use a submarine as a tactical asset, however, it must be able to share information about the wider battlespace. A way must therefore be found to allow a submarine to communicate above surface whilst operating freely at depth. Ultra, with its partners Strachan & Henshaw and QinetiQ, is developing a system incorporating a recoverable buoy that provides a satellite communication capability. Ultra, as system integrator, will undertake systems engineering, design and integration. The team will manufacture the equipment, which includes outboard equipment to deploy, retrieve, capture and stow the buoy, together with satellite communications and other antennas. Within the Ultra team each company contributes its specialist skills and experience to optimise the final solution for the customer.



Ultra is developing a stealthy communication system for submarines incorporating a recoverable buoy that provides a satellite interface capability



Ultra's active noise and vibration control system will be fitted to the A400M aircraft



Each Eurofighter aircraft has many Ultra systems and products fitted

leading edge technology

16%

Buoyant civil aerospace

Ultra's sales of equipment for civil aircraft rose by 16% in 2005

THE DESIGN OF THE WING ICE PROTECTION SYSTEM, FOR WHICH ULTRA IS THE SYSTEM INTEGRATOR, IS CRITICAL TO THE OPTIMISATION OF THE OPERATING EFFICIENCY OF THE BOEING 787 AIRCRAFT.



Ultra is supplying the wing ice protection system and proximity sensor interface electronics for the Boeing 787 aircraft



Ultra's HiPPAG is fitted to the F-35 JSF aircraft



Ultra quieters Bombardier's Q-series aircraft



Ultra constantly upgrades the electronic systems of the Tornado aircraft

Ultra maintains a constant focus on positioning its innovative solutions on long-term programmes and platforms. In the aerospace sector, typical project lifecycles can exceed fifty years. Ultra has been successful in positioning its unique products, services and systems on a number of key new programmes.

Ultra is developing the wing ice protection system and, with Goodrich of the US, the door and landing gear proximity sensing system for the new Boeing 787 "Dreamliner" aircraft. In 2005, these programmes made good progress. Ultra is the system integrator for the wing ice protection system which provides electro-thermal heating to the leading edge slats of the 787 wing. The design of the system is critical to the optimisation of the operating efficiency of the aircraft as it avoids the use of bleed air from the engines, which adversely impacts fuel efficiency. The 787 aircraft is scheduled to enter service in 2008.

An important achievement in 2005 was Ultra's selection to supply its active noise cancellation system for the main cargo bay of the new Airbus A400M turboprop military transport

aircraft. Ultra's innovative system will substantially reduce noise inside the aircraft and will protect troops from the noise of the powerful propellers. The system is based on active noise cancellation technology which Ultra has developed over more than 20 years and which is in operational service on more than 800 turboprop aircraft.

Ultra is also supplying the landing gear control system proximity sensors, harnesses and associated interface electronics for the A400M aircraft. These components are used mainly in the landing gear extension and retraction system to sense the position of the landing gear and landing gear doors. Ultra is partnered with Goodrich for the supply of this equipment. Airbus has an order book of 192 A400M aircraft with first deliveries planned for 2009.

Ultra is providing its innovative and highly reliable HiPPAG airborne compressor for the US Small Diameter Bomb (SDB) programme in the US. The SDB system, for which the prime contractor is Boeing, is the latest low cost precision-strike weapon for deployment on fighters, bombers and unmanned combat air

vehicles, for which it is estimated that the USAF will procure at least 2,000 carriages. HiPPAG provides the pneumatic energy source which enables the controlled ejection of the smart, individually targeted bombs, four of which are suspended from each carriage.

Successful firing trials have demonstrated the exceptional precision of the SDB system. A bomb flew more than 55 miles from an altitude of 30,000 feet, hitting within 34 inches of its planned impact point. SDB is initially to be deployed on USAF F-15E aircraft in 2006. To support this, Ultra was awarded in 2005 a contract to cover the Low Rate Initial Production (LRIP) phase of the programme.





Ultra's integrated IT solutions support busy airports worldwide



Ultra provides baggage management at all of New Zealand's international airports

25 million

Ultra's baggage reconciliation and matching system at London Heathrow airport processed over 25 million bags in 2005

Customers worldwide rely on Ultra's advanced, integrated IT solutions to support the efficient and safe operation of complex modern airports. With rising passenger numbers, many airports are investing in new or upgraded facilities to cater for the increased throughput. In 2005, Ultra's airport IT business continued its recent record of strong growth.

The prestigious new Terminal 5 at London Heathrow airport is taking shape. As IT system integrator for the whole project, Ultra's activity levels are rising as the project transitions from design to implementation. As integrator, Ultra is demonstrating its broad spread of domain knowledge in airport IT systems by integrating the many diverse functions that will contribute to the successful operation of Terminal 5. Ultra's success at Heathrow helped secure the contract to supply IT integration services for the expansion at Shanghai's Pudong international airport. This is a rapidly growing airport – a second terminal is being constructed, a second runway already having been opened in 2005. Shanghai Pudong will act as a world class reference site to support Ultra's continuing penetration of the Asia-Pacific region, the world's fastest growing airport market.

Ultra is the world's leading provider of airline baggage reconciliation systems. These ensure that unaccompanied bags are not inadvertently loaded onto aircraft and also enhance the efficiency of the departure process. The Group has invested in the infrastructure to provide a baggage reconciliation and tracking service to airports, airlines and ground handling agents. Ultra is now providing this service at Heathrow and in New Zealand and the US. These installed systems consistently meet the required availability and reliability levels and process millions of items of baggage each year.

At facilities such as airports, schools and similarly sensitive areas, access control is vital to minimise any risk to security. Ultra's Magicard range of ID card printers is used extensively as part of access control systems. In 2005, the Magicard range of printers was extended to offer additional features while continuing to offer as standard Ultra's unique holographic anti-counterfeiting technology. The new printers allow smaller organisations to afford an access control solution using customised ID badges for all authorised personnel.

ULTRA'S ADVANCED, INTEGRATED IT SOLUTIONS SUPPORT THE EFFICIENT AND SAFE OPERATION OF THE MOST PRESTIGIOUS MODERN AIRPORTS WORLDWIDE.

International Departures			16:02
14:05	Seattle	BA049	
14:05	Basle	AA8710	
14:05	Hamburg	AA8611	Go to Departures
14:05	Copenhagen	BD3794	
14:05	Los Angeles	LH8374	
	via San Francisco		
14:10	Rome	AA8455	Go to Departures
14:15	Chicago	AY8781	
14:15	Accra	AA6415	
14:15	Shanghai	BA169	
14:15	Copenhagen	AA8547	
14:15	Stuttgart	BA920	Go to Departures
14:20	Madrid	IB7445	Go to Departures

Ultra is selling advanced airport IT solutions all round the world



Ultra is the IT systems integrator for the new fifth terminal at London's Heathrow airport

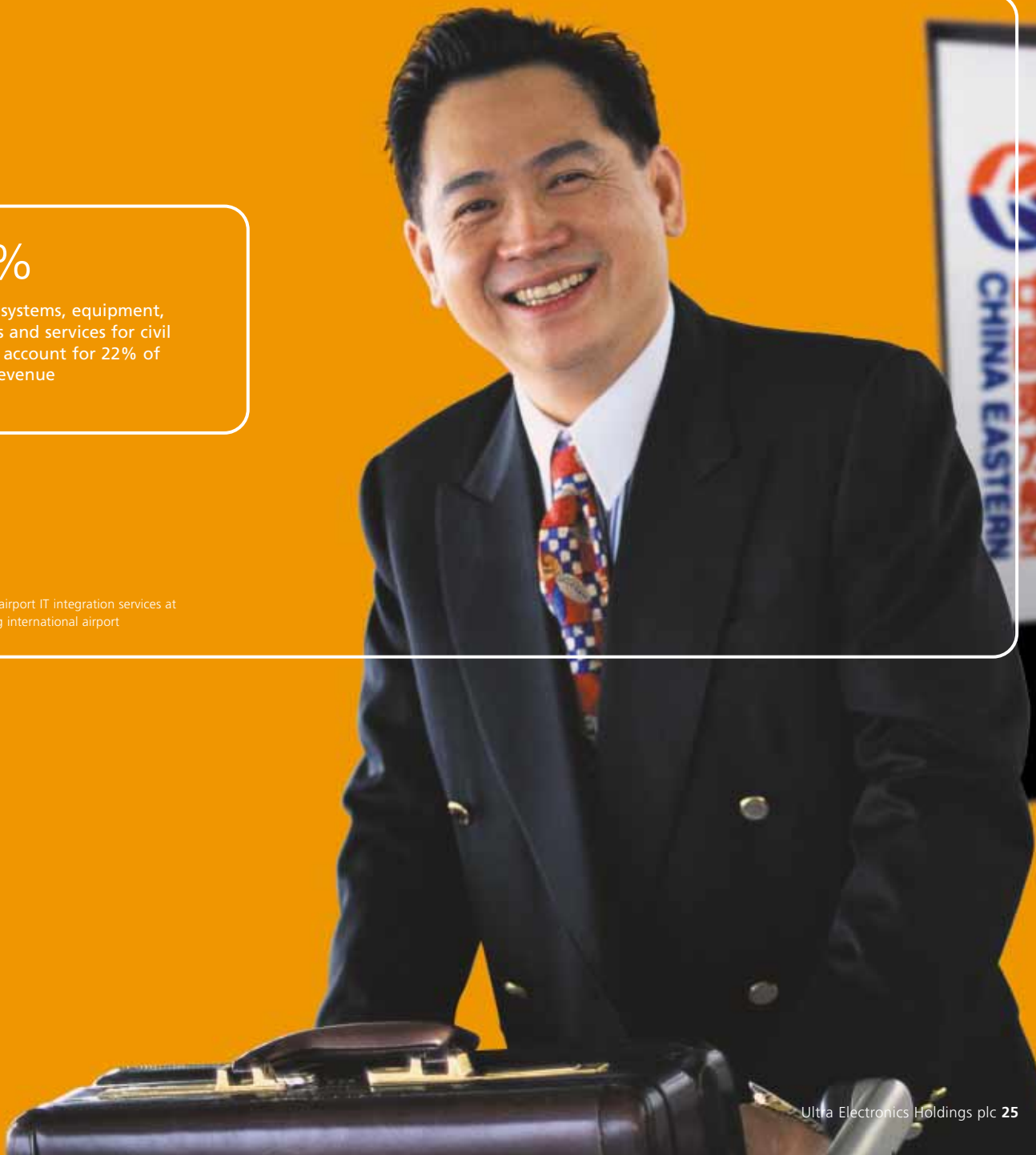


integrated airport IT worldwide

22%

Sales of systems, equipment, products and services for civil markets account for 22% of Ultra's revenue

Ultra will supply airport IT integration services at Shanghai Pudong international airport



Ultra is a responsible citizen

8%

The number of Ultra people increased by 8% during 2005

2 years

Each Ultra business is independently audited every 2 years for Health, Safety and Environmental compliance

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.

CUSTOMERS

Business ethics

Ultra requires that the Group's employees comply with the spirit and principles of 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 and are bound by strict rules on insider dealing and insider information.

IN ADDITION, ALL BUSINESSES ARE STRICTLY REQUIRED TO COMPLY FULLY WITH THE RELEVANT NATIONAL EXPORT CONTROL REGULATIONS. THEY ARE ALSO REQUIRED TO CONDUCT THEIR BUSINESS IN STRICT ACCORDANCE WITH COMPETITION AND ANTI-TRUST LAWS.

Ultra supports and respects the protection of internationally proclaimed human rights in the countries in which it operates. Ultra does not make any political donations.

Customer relationships

Ultra promotes good working relationships with all its customers with a special emphasis on meeting 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 the UK MoD Supplier Relations Group. Across the range of Ultra businesses, other customer relationships are also regularly recognised through feedback and award processes.

For example, in 2005 ATS received two awards from Lockheed Martin for achieving a supplier total performance rating of 99%. Also during 2005, DNE again received "Best Value Gold Medallist" recognition from the Defense Supply Center Richmond, Virginia; Flightline Systems received a letter of appreciation from Lockheed Martin for outstanding support while Sonar & Communication Systems received a letter of commendation from the UK DPA for the RTOF programme.

EMPLOYEES

THE PERFORMANCE OF ULTRA IS FUNDAMENTALLY DRIVEN BY THE CONTRIBUTIONS MADE BY THE GROUP'S EMPLOYEES. ULTRA'S SUCCESS IN INNOVATING TO MEET CUSTOMER NEEDS IS FOUNDED IN THE BROAD RANGE OF SKILLS AND CAPABILITIES OF THE STAFF EMPLOYED BY ULTRA. ALL MANAGERS IN ULTRA, SUPPORTED BY HR PROFESSIONALS, WORK TOWARDS THE AIM OF DELIVERING AN EFFICIENT ORGANISATION WITH COMPETENT AND COMMITTED PEOPLE TO MEET THE GROUP'S BUSINESS COMMITMENTS.

In order to ensure that Group businesses can recruit, retain, motivate and develop the right staff, Ultra pursues a range of initiatives, which are described below.

Employment practices

Ultra believes that superior business performance can only be achieved through having committed and efficient people. Achieving this high quality 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,

100%

Contribution

All Ultra employees contribute to the continuing success of the Group



THE PERFORMANCE OF ULTRA IS FUNDAMENTALLY DRIVEN BY THE CONTRIBUTIONS MADE BY THE GROUP'S EMPLOYEES.

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.

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.

Most UK businesses are accredited to the Investors In People (IIP) standard and are regularly audited. During 2005 Datel was re-assessed against the updated version of the IIP standard and was one of the first businesses in the UK to be successfully recognised against all the new indicators.

IN COMPLYING WITH THE PUBLIC INTEREST DISCLOSURE ACT 1998 IN THE UK, THE GROUP HAS ESTABLISHED A PROCEDURE ENABLING EMPLOYEES TO BRING MATTERS TO THE ATTENTION OF AN APPROPRIATE MANAGER OUTSIDE THEIR OWN BUSINESS IN THE EVENT THAT THEY DO NOT FEEL ABLE TO APPROACH THEIR LOCAL LINE MANAGEMENT. THIS PROCEDURE WAS REVIEWED DURING 2005. A SIMILAR SYSTEM OF THIRD PARTY HOTLINES HAS ALSO BEEN ESTABLISHED AT US AND CANADIAN BUSINESSES.

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 and strategic selling processes.

Most Ultra businesses offer scholarship and tuition reimbursement programmes. Ultra has also sponsored undergraduate students and supported other development activities including work placement and work shadowing during 2005. Within the US and Canada many businesses support formal co-op programmes with respected universities; during 2005 Audiopack was recognised by Case Western University for 3 years of outstanding co-op sponsorship and has expanded its programme to two additional universities. Some UK businesses run apprenticeship programmes. Links with local universities and other academic institutions are encouraged. For example, TCS in Montreal sponsors a chair at a local university. Also during 2005, Ultra provided sponsorship of undergraduate students, work experience placements as well as direct graduate recruitment.

Benefits

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

All US and Canadian employees are offered medical plans and many offer specific wellness programmes such as smoking cessation.

IN THE UK EMPLOYEES CAN PARTICIPATE IN THE "ULTRASELECT" FLEXIBLE BENEFITS PLAN. THIS WAS FIRST LAUNCHED IN 2000 AND IN 2005 APPROXIMATELY TWO-THIRDS OF ELIGIBLE UK EMPLOYEES PARTICIPATED. AS PART OF THE SCHEME UK EMPLOYEES ARE ELIGIBLE TO PARTICIPATE IN THE GOVERNMENT'S HOME COMPUTING INITIATIVE. ULTRA OFFERS A TAX-EXEMPT HIRE 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 OFFERED AGAIN DURING 2005. A COMPUTER PURCHASE PLAN IS ALSO OFFERED AT ONE BUSINESS IN NORTH AMERICA.

6 months

UltraNews is published every 6 months and provides valuable news and information for all employees

BI-ANNUAL AUDITS BY INDEPENDENT, EXTERNAL, QUALIFIED ASSESSORS COVERING HEALTH AND SAFETY MATTERS ARE CONDUCTED, MOST RECENTLY IN 2005. ALL UK AND US BUSINESSES IMPROVED THEIR HEALTH AND SAFETY PERFORMANCE ON A LIKE-FOR-LIKE BASIS IN COMPARISON WITH THE 2003 AUDIT.

Retirement benefits

Ultra offers retirement benefits to employees in the UK, US and Canada. Further details are provided elsewhere in this document.

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 "UltraNews", 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 2005 the survey took place in 11 businesses and showed high levels of employee satisfaction and engagement.

In the United Kingdom more formal information and consultation practices were introduced during 2005, following successful pilot testing in 2004.

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

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 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 THE IMPLEMENTATION OF THE POLICY.

Bi-annual audits by independent, external, qualified assessors covering health and safety matters are conducted, most recently in 2005. All UK and US businesses improved their health and safety performance on a like-for-like basis in comparison with the 2003 audit. Overall results, which take into account the newer businesses that were audited for the first time in the US, also improved. Both TCS and Maritime Systems were audited in 2005 to a new Canadian-specific audit framework; both businesses had very good overall results and met the required standard. Previous audits and the resulting follow-up process have proved effective in reaching and maintaining high standards across all sites.

Each business is required to submit a separate annual report on health and safety issues. The results of the audits and annual reports from each business are reviewed by the Board annually.

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 2005 when PMES received a RoSPA Silver Occupational Health & Safety Award in recognition of a very high standard of health and safety at work over three years.

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. Such relationships engender a



top: Ultra helped fund the degree studies of George Graham from Ocean Systems

bottom: The team at PMES received a health and safety award in 2005



Health, Safety and Environmental management is taken seriously at Ultra



UltraNews is published twice a year for all employees



Customer relationships are extremely important and are actively managed

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. Conflicts of interest are avoided at all times. During 2005, Airport Systems received the 'Innovative Solutions Award' from supplier lonix for the most innovative use of its SCADA product in the building systems integration of the new fifth terminal at London Heathrow airport.

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 2005 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 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 the implementation of the policy.

Bi-annual external audits covering environmental matters are conducted by independent, external, qualified auditors; the last audit was performed in 2005 in the UK, US and Canada. All UK and US businesses improved their environmental performance on a like-for-like basis in comparison with the 2003 audit. Overall results, which take into account the newer US businesses that were audited for the first time, also improved. Both TCS and Maritime Systems were audited in 2005 to a new Canadian-specific audit framework; both businesses had very good overall results and met the required standard. 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 from each business are reviewed by the Board annually.

Shareholders have been encouraged to receive an electronic version of this Annual Report and Accounts in order to reduce the consumption of paper and the environmental impact of the delivery process. The weight of packaging used by UK businesses is assessed and reported annually to ensure compliance with the current packaging regulations.

Charitable and community activities

In addition to the charitable donations made by the Group, disclosed elsewhere in this document, Ultra employees are actively

supported in their charitable fund-raising endeavours. A large number of local and national charities is supported.

FOR EXAMPLE, A NUMBER OF BUSINESSES SUPPORTED EMERGENCY HURRICANE RELIEF PROJECTS WITH CLOTHING AND FOOD DRIVES. EMPLOYEES AT MANY NORTH AMERICAN BUSINESSES SUPPORT THE UNITED WAY CHARITY. IN THE UK THOUSANDS OF POUNDS HAVE BEEN RAISED THROUGH A VARIETY OF EVENTS ACTIVELY SUPPORTED BY EMPLOYEES; EIGHT EMPLOYEES FROM PMES, FOR EXAMPLE, RAISED OVER £2,000 FOR THREE LOCAL CHARITIES BY TAKING PART IN A 40-MILE WALK.

As well as charitable work there is also a wide variety of community-orientated activities. DNE has again been nominated for the Governor's Prevention Partnership Corporate Honor Roll in Connecticut through its participation in a mentoring programme at a local school. Elsewhere, Audiopack sponsored an annual river clean-up day. Fifteen employees from USS1 supported a project called "Exchange City" where 5th and 6th grade school children took part in an interactive simulation that will hopefully spur their interest to pursue a career in engineering. In addition, many businesses hold annual family days.

Community

Many Ultra businesses support local charities and provide training opportunities.

THE BOARD OF ULTRA COMPRISES INDIVIDUALS WITH THE BREADTH AND DEPTH OF EXPERIENCE NECESSARY TO STEER THE CONTINUED PROGRESS OF THE GROUP.



- 01 **Julian Blogh** CBE PhD CEng MIEE
- 02 **Douglas Caster** BSc MIEE
- 03 **Chris Bailey*** FCA MCT
- 04 **Ian Griffiths*** BSc
- 05 **Andrew Hamment** BA FRAeS
- 06 **Frank Hope** PhD CPhys MInstP
- 07 **David Jeffcoat** BA FCMA
- 08 **Andrew Walker*** MA CEng



responding to change

delivering growth

01 Julian Blogh CBE PhD CEng MIEE

Chairman, age 62, 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 led the management buy-out of seven Dowty defence and aerospace electronics businesses from the TI Group to form Ultra Electronics and became Chief Executive when it began trading in October 1993. Dr Blogh was also appointed Deputy Chairman in April 2004 and became Chairman in April 2005.

02 Douglas Caster BSc MIEE

Chief Executive, age 52, 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 business and joined the Board of Ultra when it began trading in October 1993. In 1999 he became Managing Director of Command & Control Systems with responsibility for Manufacturing & Card Systems, PMES, and ATS. In April 2000, he was promoted to the position of Managing Director of the Information & Power Systems division. In April 2004 he was appointed Chief Operating Officer and became Chief Executive in April 2005.

03 Chris Bailey* FCA MCT

Non-Executive Director, age 59, was appointed to the Board in January 2005. Mr Bailey retired from his role of Group Finance Director of Aggregate Industries plc in 2004. He was the Finance Director of the precursor companies of Aggregate Industries from 1984 until its formation in 1997. He is a Fellow of the Institute of Chartered Accountants of England & Wales and is also a Member of the Association of Corporate Treasurers. Mr Bailey is also a Non-Executive Director of Rok property solutions plc.

04 Ian Griffiths* BSc

Non-Executive Director, age 55, was appointed to the Board in April 2003. Until February 2006, he was a main board executive director of GKN plc, where he was Group Managing Director GKN Automotive. Mr Griffiths was responsible for all of GKN's automotive activities world wide. Prior to this he was Chief Executive of GKN Driveline and had been a member of the GKN Driveline senior management team since 1990. In February 2006, Mr Griffiths became Managing Director, Royal Mail Letters.

05 Andy Hamment BA FRAeS

Group Marketing Director, age 51, 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.

06 Frank Hope PhD CPhys MInstP

Managing Director, Information & Power Systems, age 51, 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 business. 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.

07 David Jeffcoat BA FCMA

Finance Director and Company Secretary, age 55, 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.

08 Andrew Walker* MA CEng

Senior Non-Executive Director, age 54, 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, Delta plc, Fountains plc and is Chairman of Bioganax Ltd.

*Audit and Remuneration Committee members

Executives and Advisors

Executive Team members

Douglas Caster,
Chief Executive

David Jeffcoat,
Group Finance Director
& Company Secretary

Andy Hamment,
Group Marketing Director

Frank Hope,
Managing Director,
Information & Power Systems

Alan Jan-Janin,
Managing Director,
Aircraft & Vehicle Systems

Rakesh Sharma,
Managing Director,
Tactical & Sonar Systems

Keith Thomson,
Group Human Resources Director

Colin Ross,
Managing Director,
Controls

Business MDs & Presidents

Jon Adams,
President, Audiopack

Bill Gill,
President, DNE Technologies

Carlos Santiago,
President, Flightline Systems

Doug Burd,
President, Maritime Systems

Rick Kielmeyer,
President, Ocean Systems

Phil Evans,
Managing Director, Sonar &
Communication Systems

Alan Barker,
President, Tactical Communication Systems

Roland Fritts,
President, UnderSea Sensor Systems Inc.

Colin Ross,
Managing Director, Controls

Ross Parsell,
Managing Director, Datel

Mark Doyle,
Managing Director, Electrics

Ken Tasch,
President, Measurement Systems Inc.

Paul Benson,
Managing Director, Precision Air Systems
(Andy Yates, Managing Director from
May 2006)

Graeme Stacey,
Managing Director, Airport Systems

John McAlonan,
President, Advanced Tactical Systems

Paul Summers,
Managing Director, Command
& Control Systems

Jim Rowland,
President, EMS

Ray Coles,
Managing Director, Manufacturing
& Card Systems

Andy Freer,
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Dave Cheadle,
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(Mike Clayton, Managing Director
from January 2006)

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