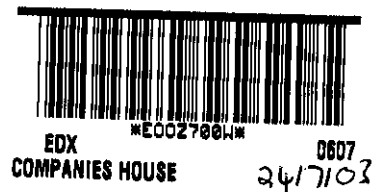


XAAR

Report and Accounts

2002

Company Number 3320972



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Xaar is a market focused technology leader driving the expansion of digital inkjet printing into targeted profitable sectors of the printing industry.

Xaar's primary business is the manufacture and sale of high performance specialised printheads and inks to original equipment manufacturers (OEMs) in the speciality graphics, industrial printing and packaging printing markets.

Our focus is on applications where our technology can offer the end-user distinct and quantifiable benefits.

Xaar's vision is to have its technology become a core digital printing technology adopted over a broad range of applications.

Xaar's digital inkjet technology enables drop on demand printing on a wide range of different substrates including vinyl, plastics, cardboard, ceramics, metal, textiles, glass and paper.

The technology is protected by a substantial portfolio of patents.

Xaar offers licenses to its technology where appropriate.

Our aim is to license leaders in markets that complement our business strategy.

We remain focussed on producing further growth in sales of Xaar products and, more importantly, growth in margins and profitability

Introduction

I am pleased to report further significant growth in sales of Xaar products during the second half of the year and solid progress in positioning the group within the digital printing industry as a developer, manufacturer and vendor of high performance inkjet printheads. This change of strategy, set out in the interim report last September, also offers us more control over our future development and growth.

The total value of Xaar's product sales increased by 46% during the year with growth during the second half of the year ahead of that for the first half. Within this, the volume of XJ500 heads shipped in the year more than doubled, with over half going to our new markets in Asia, and China in particular.

Although no new licence was signed in the year, we received a further small stage payment under an existing licence agreement. Whilst Xaar continues to maintain and develop its extensive portfolio of patents, currently standing at over 700, R&D emphasis has now been swung behind the development and refinement of Xaar's product portfolio.

As previously stated, efforts to secure licence revenue continue but, given the difficulty in predicting both quantum and timing, we are planning our business without relying on new licence revenues. In future, we intend to comment on new licences only as and when they arise. Royalty revenues received during the second

half-year were little changed from the level reported for the first half of the year, reflecting continued difficult market conditions for many of our licensees.

Overall, we are pleased with the growth seen in what we now regard as our mainstream business, during what was another challenging year of change. The company ends the year with a healthy cash balance and no borrowings.

Results and Finance

Group revenues for the year to 31 December 2002 grew to £30.9m (2001: £24.0m). Sales of Xaar products (printheads, inks and peripherals) increased by 46% to £28.5m (2001: £19.5m). Development fees received for contract R&D projects were £1.2m (2001: £1.5m). Licence fees and royalties were £1.2m (2001: £3.0m) reflecting the fact that no new licence was signed in the year. Within that, royalty income for the year was £0.9m (2001: £1.3m). Profit before tax and exceptional items was £0.9m (2001: £1.6m). There were no exceptional items in 2002 (2001: £1.0m). Earnings per share were 1.7p (2001 as restated: loss of 0.6p).

As reported in the end-of-year trading update issued early in January, the immediate benefit of the increase in sales was diluted by somewhat higher than expected warranty returns for the XJ500 product during the latter part of the year. The product has now been modified, with all claims settled or provided for in the results for 2002.

An imbalance between manufacturing profits in Sweden and the costs of R&D activities in the UK, together with full utilisation of acquired tax losses in Sweden, gave rise to a disproportionate tax charge in the interim results for 2002. Xaar's tax structure has now been reorganised so that a more normal tax charge will be incurred going forward. Further details are provided in the Finance review.

Printheads and related products

In the interim statement, we set out clearly our strategy for 'cherry picking' digital printing market segments where Xaar's technology is best suited and where it can become a market leader. Xaar's current strength lies in the graphic arts market, particularly in wide-format printing machines for banner and poster advertising where it is already a market leader in non-water based printing. We have now chosen to enter new markets within the packaging and industrial printing sectors in order to provide greater long-term growth potential. The digital printing marketplace as a whole is huge and capable of successfully supporting a number of different technologies and suppliers; each of the market segments being chosen for a concentration of our marketing effort is substantial in its own right and offers tremendous scope for our products. More details of these initiatives are set out in the Chief Executive's review.

In geographic markets, Asia and Europe increased sales by 48% and 45% respectively, whilst sales into the US market declined by 28%. We intend to arrest this decline in the US market over the coming year.

The route to market within both packaging and industrial markets is more complex than our current markets and will take time to generate volume sales. We will therefore be working closely with existing and new partners in both these markets. In addition, we have recognised that many customers, especially in the important US market, often require assistance in integrating digital printing technology into their business before they can become significant users of Xaar products.

To that end, I am pleased to report that Xaar has reached agreement in principle to acquire for a nominal sum Vivid Print Innovations Inc. (VPI), a San Antonio, Texas, based start-up business. VPI comprises an established

engineering team with considerable experience in designing and integrating digital printing systems, mostly utilising Xaar products. Further details are provided in the Finance review.

New technology and product development

A revised version of the XJ500 product was introduced at the beginning of 2003. This update includes performance enhancing modifications, as well as resolving the problems that gave rise to the recent warranty claims. Sales of the XJ500 are expected to show another year of growth. We continue to develop the new printhead referred to in the interim statement and plan to start previewing the product with customers during the second half of 2003.

Technology revenues

Royalty income is expected to remain at around current levels for the foreseeable future. Longer term, the company continues to look for new licensing opportunities and to develop new patentable technology.

Outlook

We remain focussed on producing further growth in sales of Xaar products and, more importantly, growth in margins and profitability. Management continues to maintain tight control over costs and has recently instituted further headcount savings as part of a constant review of the cost base of the business. Demand in key Asian and European markets remains firm at the current time and the proposed increase in systems integration resources is expected to lead to an improved performance in the US, even though it is not clear whether economic conditions will improve in that region in the short term.



Arie Rosenfeld
CHAIRMAN 18 February 2003

The strength of what we now regard as our mainstream business is shown in the 46% organic growth in revenue and record shipments of printheads and inks to a worldwide market

During 2002 Xaar's resources were focussed on our rapidly growing business of designing, manufacturing and selling printheads and inks, rather than our former strategy which placed an equal reliance on the generation of revenues from intellectual property rights.

The strength of what we regard as our mainstream business is shown in the 46% organic growth in revenue and record shipments of printheads and inks to a worldwide market. The decision to move production of the XJ500 to Sweden resulted in improved efficiencies in line with expectations, although this did not result in immediately improved margins due to the level of warranty returns referred to in the Chairman's statement. As a result, margins on product sales were little changed for the second half of the year. Nevertheless, the company was profitable and cash generative without new licence fees during the year, representing an important milestone.

Market focus

Historically, the majority of our products have sold into the graphic arts market for incorporation into wide format and specialised digital printers of billboards, banners and other advertising materials. This market is expected to continue growing steadily over the coming years. In addition, analysis of other potential market opportunities for Xaar's products has shown that while Xaar printheads can be used successfully in a very wide range of applications, there are particular segments in which Xaar has a clear opportunity to become a market leader and resources are being focussed progressively on these segments.

The Chairman's statement refers to the two new markets initially identified to provide future growth; industrial printing and packaging printing. Both contain substantial segments where Xaar's technology brings clear and quantifiable advantages to the customer when compared with existing technologies and processes.

Xaar has already successfully sold products into industrial printing applications which include the printing of ceramic tiles, and the marking of legends onto printed circuit boards. The Leopard printhead, launched during 2002 and manufactured by our licensee, Toshiba TEC, enables us to target further applications in this market where near-photographic quality is needed such as plastic cards (for example; credit cards, identity cards and telephone cards), CD and DVD printing.

Within packaging printing we also supply to a number of existing customers building printers for coding and marking applications (including bar coding, sell-by dates and logo printing). We will now be expanding into additional sectors including flexible packaging, folding cartons and labels. Development within this area will be accelerated by the acquisition of Vivid Print Innovations Inc. (VPI).

Sales

Sales of printheads and inks have grown rapidly during the year with the highest growth coming from Asia where turnover increased by 48% and accounted for 55% of the group total. We also saw growth in Europe of 45% contributing 31% to overall turnover. There was a decrease in US sales (accounting for 14% of total turnover) due largely to economic conditions in the US market. We have recently strengthened our operation in China with a small office in Shanghai in addition to our existing operation in Hong Kong. We expect China to continue to be a key market for Xaar.

The proposed acquisition of Vivid Print Innovations Inc. is expected to materially improve Xaar's performance in the US market. VPI specialises in integrating printheads into customer applications and building bespoke printers on a customer demand basis. As an integral part of our sales organisation, VPI will

offer a complete printing machine design service to customers that wish to use Xaar's products in packaging and industrial applications, but who do not have skills within the digital inkjet printing field. All of VPI's team of experienced engineers have a long history of working with Xaar's printheads and already have a number of projects under way with new customers. The focus of this service will initially be US led but it will also become available to customers on a global basis.

In 2002, ink sales grew in line with printhead sales and eight new inks were approved either for direct sales or customer evaluation.

Development activities and product portfolio

Development activities within Xaar's Cambridge facility have been refocussed onto projects that will have a short or medium-term impact on revenues. Investment in R&D in 2002 was £4.4m (2001: £4.1m), we do not expect this spend to increase over the coming year.

Enhancements to the XJ500 product have been a key area of activity during 2002 and by the end of the year resulted in significantly improved performance. This work will continue in 2003 with the emphasis placed on reducing the cost of manufacturing the product.

Work on preparing the new Leopard head for launch as a Xaar product was also completed during the year. The Leopard head is the result of our collaboration with Toshiba TEC, a Xaar licensee. Toshiba TEC manufactures the printheads in Japan where it will sell a version direct to major Japanese users. Xaar sells the head under its own brand name into markets outside Japan, and to customers requiring the sales and service back-up offered by Xaar through its network of regional sales offices. The Leopard has concluded field testing with customers in the industrial printing field and is now being made

generally available. The Leopard head is unique in its greyscale capability – allowing it to vary dynamically the drop size on a pixel-by-pixel basis giving near-photographic quality at high speeds.

The XJ500 and Leopard printheads complement the well established smaller XJ128 currently used extensively in wide-format printers throughout the world, and the XJ126 which is now in full scale production.

Development of our next generation of printheads referred to in the interim statement has also been progressed during the year. This development has generated a modular printhead design that can be more rapidly adapted to different formats than is currently the case with existing product designs. The performance shown in prototypes has given us optimism about the future for products based on this platform.

Manufacturing

In October 2001 we announced our decision to transfer all manufacturing operations into our Swedish plant with R&D activities being undertaken at our Cambridge facility. The move to Sweden was completed during the first half of 2002 and as a result we were able to almost triple output of the XJ500 printhead last year compared to 2001. The higher warranty returns of our XJ500 product during the last four months of the year should be taken in the context of this significant increase in production and sales, in particular to our new markets in China. Once the particular issues giving rise to the problems were identified, changes to the XJ500 were made quickly and we are confident that these problems

have now been eliminated. A revised version of the XJ500 is now being offered to the market, providing improved performance, greater reliability and increased manufacturing margin.

Although strong demand for the XJ500 has made this the fastest growing product in our portfolio, we also sold record numbers of our XJ128 product which in 2002 still contributed the larger part of our revenue. This is particularly encouraging given the fact that it is now a mature product.

Licensing

We continue to work towards securing new licensees but we are no longer relying on new licence income as a fundamental part of our business plan. Royalty income has been steady during the year, albeit at a reduced level. We believe this to be a result of the tough market environment facing our licensees, resulting in lower than expected sales of their products. At the current time royalties for 2003 appear likely to continue at a level similar to 2002.

Priorities for 2003

Xaar starts 2003 with continuing demand for its printheads and inks, an expanding product portfolio and increased systems integration resources with which to drive our sales and marketing efforts in established and new markets.

The key focus for 2003 is to convert higher sales into significantly improved profitability. Emphasis is being placed on reducing the cost of manufacturing of all our products, with ongoing programmes designed to cut

material costs, increase yields and control overhead expenditure in order to improve the contribution from our manufacturing operation. A reduction in the group's headcount was implemented in February 2003 at both the Cambridge and Swedish facilities.

People

As the company is focussing more on its manufacturing business with a target to become a world class manufacturing operation, our staff worldwide have had to respond to rapid change during the year. I would like to acknowledge the contribution everyone in the group has made to this process.



Jan Fineman
CHIEF EXECUTIVE 18 February 2003

2002 was a year of change for the group. We have focussed the business on its manufacturing activities, and intend to grow those significantly within existing and new markets. Whilst it is pleasing to report strong growth within this context, there are important issues facing the group which must be addressed during 2003 and which are being given priority.

Results for 2002

Turnover for the year was £30.9m (2001: £24.0m) which resulted in a profit before taxation and exceptional items of £0.9m (2001: £1.6m). There were no exceptional items in the year (2001: £1.0m). Net assets at the end of the year were £17.3m (2001 as restated: £15.4m), of which £9.9m was represented by cash and liquid resources (2001: £9.8m). The gross profit margin for the group was 46%, down from 53% in 2001 reflecting reduced technology revenues of £1.2m (2001: £3.0m). Margins on printheads and related products were 42% for the full year, largely in line with the first half, with underlying second-half improvements in yield offset by additional warranty claims of £0.3m.

The group taxation charge for the year is a credit of £0.1m (2001 as restated: charge of £0.9m). This is lower than the charge made in the interim results for the reasons set out below. Earnings per share for the year were 1.7p (2001 as restated: loss of 0.6p).

We have amended the way we report segmental information for the year to improve understanding of the business. Development fees, which were previously included with technology revenue, have been separately identified. Technology revenue now only includes licence and royalty income.

In addition, we have adjusted our reporting of geographic turnover to cover Xaar's three main markets; Asia, Europe and the Americas. Results by class of business are now detailed at both the revenue and gross margin level. Going forward we will also include details of turnover by industry segment, matching the target markets discussed in the Chairman's and Chief Executive's reports; graphic arts, packaging printing and industrial printing. As a guide, for 2002 the majority of sales remain in the company's existing graphic arts market, which accounted for 85% of sales, but newer markets such as packaging, at 12% and industrial markets at 3% made growing contributions in the year.

Taxation

The strategy changes implemented during the year, including the concentration of manufacturing activities in Sweden, have provided greater clarity with regard to the revenue streams originating within the group and the costs that should properly be associated with those different activities.

The result of more closely matching relevant costs and revenues is an underlying group tax charge of 48% for the full year 2002, with a more normalised charge expected from 2003 onwards. In addition, an adjustment of £0.3m was made in the year in order to recognise a deferred tax asset which should have been included in the results for 2001. After taking account of this and other adjustments there was a net credit for the year of £0.1m.

A new 100% owned group company, Xaar Group AB, was established in Sweden during the second half of the year. This company now holds the group's investment in XaarJet AB.

Costs

Total operating costs (including cost of sales) for the group were £30.1m (2001: £22.6m). The increase is a result of three main factors; the higher level of product sales made by the group during the year; the higher proportion of sales of the XJ500, on which yields and margins do not yet match those of our more established XJ128 product (including the cost of warranty returns); and higher operating expenses.

The higher expenses arise from a full year of the Hong Kong office, established in the second half of 2001, higher patent costs, marketing costs and external project-related R&D costs.

The group is taking steps to reduce its total costs as follows;

- The XJ500 product was re-engineered during 2002 which has reduced unit costs and improved ease of manufacture. The revised product was introduced early in 2003 and will generate improved yields and margins. Further improvements are planned during 2003.

- A reduction in group headcount of 10% was made early in February 2003, although savings made in Sweden will only come through during the second-half year due to local employment legislation.
- The problems resulting in the higher cost of warranty claims have been resolved.
- The group has implemented an ongoing process of continuous efficiency improvement across the organisation and of refocussing group resources to areas where they can generate maximum returns.

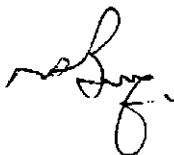
Vivid Print Innovations Inc.

The group has reached agreement in principle to acquire Vivid Print Innovations Inc. (VPI). Under the agreement Xaar will acquire all the outstanding share capital of VPI for a nominal sum of \$1,500. VPI has negligible net assets. The five principals of the business will have remuneration packages commensurate with similar employees within the Xaar group, including an annual bonus scheme related to the results of the VPI business. VPI had (unaudited) turnover of \$0.4m in 2002 and the acquisition is expected to be earnings neutral for the full year 2003.

Cash and capital expenditure

Cash and liquid resources closed the year at £9.9m (2001: £9.8m). This was after capital expenditure, before lease financing, of £1.1m (2001: £1.2m). Total capital expenditure for the year was £1.9m (2001: £1.8m), which was lower than previously indicated due to late delivery of an additional laser costing £0.8m. This will now be commissioned in the first quarter of 2003. The group used additional working capital of £1.0m to support the increase in sales during the year.

The group considers its level of cash holding to be prudent in the current economic climate.



Nigel Berry
FINANCE DIRECTOR 18 February 2003

Executive directors

Jan Fineman, Chief Executive

Aged 43 - joined Xaar in April 1999 when Xaar acquired MIT (now renamed XaarJet AB), where he had been Managing Director for two years. He was appointed to the Xaar board in August 1999, taking responsibility for all Xaar manufacturing and development operations in Sweden and Cambridge. Before joining MIT, he was Vice President of Technical Operations at Biacore AB, formerly a division of Pharmacia.

Nigel Berry, Group Finance Director

Aged 43 - joined Xaar in May 2002 from Cambridge Display Technology Ltd where he was Chief Financial Officer. Previously with Wassall plc and Rexam Printing Ltd., he has a wide range of experience in global manufacturing businesses, including time based in the US and Asia.

Stephen Temple, Technical Director

Aged 55 - is one of the original inventors of the Xaar technology. His inventions and joint inventions have led to more than 90 patents covering the technology. His primary role, aside from leading the technical team, is to focus on future development. He has been a director since 1991.

Hugh Baker-Smith, Group Sales Director

Aged 38 - joined the board in November 1998 to develop Xaar sales internationally. He previously worked for Hitachi and has considerable hi-tech industry experience gained in a variety of sales, marketing and management roles.

Ian Dinwoodie, Group Operations Director

Aged 42 - joined Xaar in September 2001. With over 20 years experience in hi-tech operations, he has held a variety of roles in engineering, quality assurance and manufacturing within the semiconductor, electronics, and electronic imaging industries. He most recently worked as Director of Manufacturing for Fujifilm Electronic Imaging Ltd.

Non-executive directors¹**Arie Rosenfeld*⁺, Chairman**

Aged 59 - was until 1995 President of Scitex, which he joined shortly after its formation in 1968. Scitex is a world leader in graphic arts, digital printing and digital video products. He joined the Xaar board in February 1997 and was appointed Chairman in June 1997.

Richard King CBE*⁺, Deputy Chairman

Aged 73 - is Chairman of Aveva Group plc, Sentec Ltd and is a director of a number of other Cambridge hi-tech companies. An Emeritus Fellow of Darwin College, he was a founding member of Xaar and has been a director of Xaar since 1990. He was appointed Deputy Chairman of the company in September 1997.

Michael Geary*⁺

Aged 52 - is a director of Euroventures, a pan-European venture capital group, based in Holland. An engineer, he worked for 3i and Charterhouse, before becoming Managing Director of Munford & White plc in 1982 on its flotation. He was later founder of Prudential Venture Managers. He joined the Xaar board in 1996.

John Scott*⁺, Senior Independent Director

Aged 50 - until 2001 an executive director of Lazard Brothers & Co. Limited and currently a director of a range of quoted and private companies, including Dunedin Income Growth Investment Trust plc., The Scottish Mortgage and Trust Plc, Miller Holdings Ltd and Albany Venture Managers Ltd. He joined the Xaar board in April 2001 and was appointed the senior independent director in February 2002.

⁺ Member of audit committee

* Member of remuneration committee

¹ All non-executive directors are considered to be independent by the Board

The directors present their annual report on the affairs of the group together with the financial statements and auditors' report for the year ended 31 December 2002.

Principal activity and business review

The principal activity of the group continues to be the development and commercial exploitation of its patented inkjet printing technology. A detailed review of the group's operations during the year and of its plans for the future is given in the Chairman's statement and the Chief Executive's review.

The subsidiary undertakings of the group are listed in Note 27 to the financial statements.

Research and development

£4.4m (2001: £4.1m) was spent on research and development in the year.

Results and dividends

Turnover for the year was £30.9m (2001: £24.0m) and comprised sale of printheads and related products, development fees and licence fees and royalties.

The profit/(loss) after tax for the year was £1,011,000 (2001 as restated: £(363,000)). The directors do not recommend the payment of a dividend (2001: £nil).

Directors and their interests

The directors who served during the year were as follows: -

- J Fineman
- N Berry (appointed 20 May 2002)
- G MacLeod (resigned 20 May 2002)
- S Temple
- H Baker-Smith
- I Dinwoodie
- A Rosenfeld
- R King
- M Geary
- J Scott

Brief biographical descriptions of the directors and their membership of certain board committees are set out on page 10.

The interests in the shares of the company and its subsidiaries (all of which are beneficial) as at 31 December 2002 of the directors are as follows:

Shareholdings in the company

	Number of ordinary shares of 10p each 31 December 2002	Number of ordinary shares of 10p each 31 December 2001
J Fineman	10,000	10,000
N Berry	200,000	-
S Temple	485,499	485,499
H Baker-Smith	25,375	25,375
I Dinwoodie	-	-
A Rosenfeld	300,000	300,000
R King	163,580	123,580
M Geary	63,000	28,000
J Scott	21,500	21,500

There have been no changes in the directors' interests in shares of the company between 31 December 2002 and 18 February 2003.

In accordance with the company's articles of association, at the Annual General Meeting referred to in more detail on page 40, Mr H Baker-Smith and Mr J Fineman will retire from the board by rotation and offer themselves for re-election. Additionally, Mr N Berry who was appointed to the board during the year, offers himself for re-appointment.

Share capital

As at 13 February 2003 the company had been notified in accordance with sections 198 to 208 of the Companies Act 1985, of the following material interests in its share capital:

	Number of ordinary shares held	Percentage of issued share capital
Framlington Investment Management Limited	7,521,056	12.6%
Artemis Investment Management Limited	5,009,750	8.4%
The Throgmorton Trust Plc	4,189,756	7.0%

Annual General Meeting

The notice convening the Annual General Meeting is set out on page 40. Resolutions 1 to 6 set out in the notice of the meeting deal with the ordinary business to be transacted at the meeting. The special business at the meeting (Resolutions 7 to 9) is explained on page 15 (in relation to Resolution 7) and on page 12 (in relation to Resolutions 8 and 9).

Power to issue securities

Resolution 8

Under the Companies Act 1985 the directors of the company may only allot shares (whether for cash or otherwise) with the authority of shareholders given at a general meeting of the company. Under Resolution 7 authority is sought to allot shares up to an aggregate nominal amount of £1,029,161, which is equal to the whole of the unissued share capital as at 18 February 2003 and which represented 17% of the company's ordinary share capital in issue as at 18 February 2003 and is an amount within the maximum amount permitted under institutional guidelines. The directors do not currently have an intention to exercise the authority, other than the allotment of 120,000 ordinary shares in the company to be issued in exchange for ordinary shares of Xaar Technology Limited acquired by the company pursuant to a put and call mechanism in the articles of association of Xaar Technology Limited (such Xaar Technology Limited shares will be issued on the exercise of options over Xaar Technology Limited shares).

Resolution 9

This special resolution will give the directors power to allot shares for cash on a non-pre-emptive basis in the following circumstances:

- (a) in connection with a rights issue, open offer or otherwise to holders of ordinary shares but allowing the directors to make adjustments to deal with practical problems such as those arising from fractional entitlements or compliance with overseas legislation; and
- (b) other than as described in (a) above, up to a maximum aggregate nominal value of £298,542, representing 5% of the issued ordinary share capital of the company as at 18 February 2003.

The directors do not currently have an intention to exercise any power given to them by shareholders to allot shares for cash on a non-pre-emptive basis, and in any event, the directors will not allot any shares for cash on a non-pre-emptive basis if such allotment would exceed the limits established by the guidance published by the investment committees of the ABI and the NAPF.

The authorities contained in Resolutions 7 and 8 will expire no later than 15 months after the passing of those resolutions.

Charitable contributions

The group made charitable contributions during the year totalling £420 (2001: £270). No political donations were made (2001: £nil).

Supplier payment policy

The group's and the company's policy is to settle terms of payment with suppliers when agreeing the terms of each transaction, ensure that suppliers are made aware of the terms of payment and abide by the terms of payment.

Average payment days to suppliers of the company during the year was nil days (2001: 29 days).

Auditors

On 24 June 2002, Arthur Andersen resigned as auditors of the Company. Deloitte & Touche were appointed as auditors for the current year by the Board to fill the vacancy. Deloitte & Touche have expressed their willingness to continue in office as auditors and a resolution to reappoint them will be proposed at the forthcoming Annual General Meeting.

Science Park
Cambridge
CB4 0XR

By order of the Board

18 February 2003
Registered no. 3320972

N Berry
Secretary

Compliance with the Code of Best Practice

The company has complied throughout the year with the Provisions of the Code of Best Practice set out in section 1 of the Combined Code, published by the Hampel Committee and the London Stock Exchange.

Statement about applying the Principles of Good Governance

The company has applied the Principles of Good Governance set out in section 1 of the Combined Code by complying with the Code of Best Practice as described above. Further explanation of how the Principles have been applied is set out below and, in connection with directors' remuneration, in the Directors' remuneration report.

Board of directors

The executive directors of the company are fully involved with the management of the group at all levels, and the direction and control of the group remains firmly in their hands. The Board is fully involved in the nomination, selection and appointment of non-executive and executive directors, although there is no formal written procedure in place.

The Board comprises the non-executive Chairman, five executive and three further non-executive directors, including the senior independent director, and met twelve times during the year. It is responsible for the business and commercial strategy, monitoring progress, the approval of major transactions and the approval of financial statements and operating and capital expenditure budgets. Comprehensive board papers, dealing with all aspects of the business, are distributed by the Company Secretary one week in advance of each board meeting. A nomination committee for Board appointments has not been established because the full Board is actively involved in all appointments. There is no intention to form a nomination committee given the Board's current size.

On 12 February 2002 Richard King stepped down from the positions of senior independent director and Chairman of the audit committee, to be replaced in both roles by John Scott. Richard King continues to serve as a non-executive director and Chairman of the remuneration committee.

Audit committee

The audit committee comprises the four non-executive directors, Arie Rosenfeld, Richard King, Michael Geary and John Scott, and is chaired by the senior independent director, John Scott. It examines and reviews, on behalf of the Board, internal financial controls, financial and accounting policies and practices, the form and content of financial reports and statements, and the work of the external auditors. The Chief Executive and the Group Finance Director attend meetings of the audit committee by invitation.

Remuneration committee

The remuneration committee comprises the four non-executive directors, Arie Rosenfeld, Richard King, Michael Geary and John Scott and is chaired by Richard King. It makes recommendations to the Board on the group's policy for executive remuneration and determines the individual remuneration packages on behalf of the Board for the executive directors of the group. The Chief Executive attends meetings by invitation. The committee has access to professional advice, both inside and outside the company, in the furtherance of its duties.

Constructive use of the AGM

The Board used the AGM held on 26 March 2002 as an opportunity to present to shareholders an overview of Xaar's business. Further presentations are expected to be made at future AGMs.

Dialogue with institutional shareholders

The directors seek to build on a mutual understanding of objectives between the company and its institutional shareholders by meeting at least twice per year, following interim and annual results, to provide an update on trading and obtain feedback.

Internal control

The Board has applied *Principle D.2 of the Combined Code* by establishing a continuous process for identifying, evaluating and managing the significant risks the group faces. The Board regularly reviews the process, which has been in place from the start of the year to the date of approval of this report and which is in accordance with *Internal Control: Guidance for Directors on the Combined Code (The Turnbull Report)* published in September 1999 and reports in accordance with that guidance. The Board is responsible for the group's system of internal control and for reviewing its

effectiveness. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance with respect to the preparation of financial information and the safeguarding of assets and against material misstatement or loss.

In compliance with *Provision D.2.1* of the *Combined Code*, the Board continuously reviews the effectiveness of the group's system of internal control. The Board's monitoring covers all controls, including financial, operational and compliance controls and risk

management. It is based principally on reviewing reports from management to consider whether significant risks are identified, evaluated, managed and controlled and whether any significant weaknesses are promptly remedied and indicate a need for more extensive monitoring. The Board has also performed a specific assessment for the purpose of this annual report. This assessment considers all significant aspects of internal control arising during the period covered by the report. The audit committee assists the Board in discharging its review responsibilities.

Statement of directors' responsibilities

Directors' responsibilities

United Kingdom company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the group, and of the profit or loss of the group for the period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent; and
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and group and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Going concern

After making enquiries, the directors have a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

This report has been prepared in accordance with the Directors' Remuneration Report Regulations 2002 which introduced new statutory requirements for the disclosure of directors' remuneration in respect of periods ending on or after 31 December 2002. The report also meets the relevant requirements of the Listing Rules of the Financial Services Authority and describes how the Board has applied the Principles of Good Governance relating to directors' remuneration. As required by the Regulations, Resolution 7 to approve the report will be proposed at the Annual General Meeting of the company at which the financial statements of the company will be approved.

The Regulations require the auditors to report to the company's members on the 'auditable part' of the Directors' remuneration report and to state whether in their opinion that part of the report has been properly prepared in accordance with the Companies Act 1985 (as amended by the Regulations). The report has therefore been divided into separate sections for audited and unaudited information.

Unaudited information

Remuneration committee

The principal function of the remuneration committee (comprising A Rosenfeld, R King, M Geary and J Scott) is to determine, on behalf of the Board, the specific remuneration and other benefits of all executive directors, including pension contributions, bonus payments, share options and service contracts. In determining the directors' remuneration for the year, the committee consulted Mr J Fineman (Chief Executive) and Mrs W Hepburn (Group HR Manager) about its proposals. The fees paid to the non-executive directors are determined by the Board. Additionally, the remuneration committee makes recommendations to the Board on the framework of executive remuneration.

Total level of remuneration

The remuneration committee is aware that it must both attract and retain individuals of the highest calibre by offering remuneration competitive with comparable publicly listed companies, and fairly and responsibly reward individuals for their contribution to the success of the company.

Basic salaries

The basic salary of each executive director is determined by taking into account the individual's performance and responsibilities and the achievement of personal objectives.

Bonus payments

Bonuses are non-pensionable and based on a percentage of basic salary. Bonuses are paid each six months, following the interim and annual results, in recognition of each executive director's contribution to the success of the company and upon achievement of certain corporate and personal targets. The maximum potential bonus payment as a percentage of

basic salary for directors depends on the director's role and responsibility; in 2002 this maximum bonus percentage ranged from 50% to 80% depending on director. Non-executive directors do not receive a bonus.

Share options

All executive directors are entitled to participate in the company's share option schemes. Any options granted thereunder are approved by the remuneration committee.

Certain options granted to directors are subject to vesting criteria as summarised below.

J Fineman – 150,000 options with an exercise price of 120p where, as long as the share price remains above the relevant threshold for at least 20 consecutive days after the earliest date of exercise, 33% vest at a share price of 200p, 66% vest at 225p and 100% vest at 250p. 100,000 options with an exercise price of 120p where 33% vest at a share price of 250p, 66% vest at 300p and 100% vest at 350p.

N Berry – 250,000 options with an exercise price of 71.5p where, as long as the share price remains above the relevant threshold for at least 20 consecutive days after the earliest date of exercise, 33% vest at a share price of 110p, 66% vest at 125p and 100% vest at 140p.

S Temple – 100,000 options with an exercise price of 74p where, as long as the share price remains above the relevant threshold for at least 20 consecutive days after the earliest date of exercise, 33% vest at a share price of 110p, 66% vest at 125p and 100% vest at 140p.

H Baker-Smith – 133,500 options with an exercise price of 131p where, as long as the share price remains above the relevant threshold for at least 20 consecutive days after the earliest date of exercise, 33% vest at a share price of 200p, 66% vest at 225p and 100% vest at 250p. 16,500 options with an exercise price of 131p where, as long as the share price remains above the relevant threshold for at least 20 consecutive days after the earliest date of exercise, 33% vest at a share price of 250p, 66% vest at 300p and 100% vest at 350p.

I Dinwoodie - 150,000 options with an exercise price of 88p where, as long as the share price remains above the relevant threshold for at least 20 consecutive days after the earliest date of exercise, 33% vest at a share price of 130p, 66% vest at 145p and 100% vest at 160p. 100,000 options with an exercise price of 68.5p where, as long as the share price remains above the relevant threshold for at least 20 consecutive days after the earliest date of exercise, 33% vest at a share price of 110p, 66% vest at 125p and 100% vest at 140p.

All options detailed above additionally require EPS growth over the 3 year vesting period to be more than RPI + 5% per annum compound.

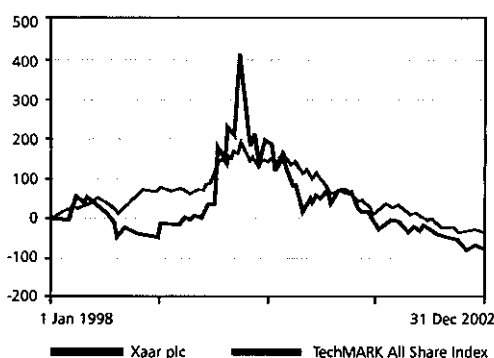
Non-executive directors do not participate in the company's share option schemes. It is the policy of the company to grant share options to employees and executive directors as a means of encouraging ownership and providing incentives for performance.

Pension scheme

The company operates a self-administered, defined contribution, Inland Revenue approved pension scheme. All current executive directors participate in this scheme. Non-executive directors do not receive pension contributions.

Performance graph

The following graph shows the company's performance, measured by total shareholder return, compared with the performance of the TechMARK All Share Index.



The TechMARK All Share Index has been selected for this comparison because it is the index used by the company to partly determine payments under the bonus scheme for executive directors. For the purposes of this comparison the TechMARK All Share Index is based on the constituent companies in the index at a point in time.

Terms of appointment

Executive directors' appointments are terminable by 12 months' written notice. Non-executive directors' have specific terms of engagement and their appointments are terminable by 6 months written notice.

The details of directors' contracts are summarised below:

	Date of contract
J Fineman	16.09.99
N Berry	20.05.02
S Temple	08.10.97
H Baker-Smith	19.01.99
I Dinwoodie	13.11.01

Audited information

Directors' remuneration

The remuneration of directors who served during the year was as follows (total remuneration for all directors who served during 2001 was £648,000):

Director	Basic salary £'000	Fees £'000	Benefits in kind £'000	Bonus payments £'000	Money purchase pension contributions £'000	Total 2002 £'000	Total (including pension contributions) 2001 £'000	Money purchase pension contributions 2001 £'000
Executive								
J Fineman	105	-	13	5	12	135	150	10
N Berry ¹	62	-	8	1	7	78	-	-
S Temple	95	-	15	10	10	130	127	10
H Baker-Smith	95	-	15	40	10	160	136	9
I Dinwoodie ²	90	-	13	21	10	134	22	1
G MacLeod ³	35	-	5	-	4	44	88	6
Non-executive								
A Rosenfeld	-	36	-	-	-	36	36	-
R King	-	24	-	-	-	24	24	-
M Geary	-	21	-	-	-	21	20	-
J Scott ⁴	-	21	-	-	-	21	16	-
	482	102	69	77	53	783	619	36

1 N Berry was appointed to the Board on 20 May 2002. All amounts represent remuneration from this date.

2 I Dinwoodie was appointed to the Board on 13 November 2001. All amounts represent remuneration from this date.

3 G MacLeod was appointed to the Board on 27 March 2001 and resigned from the Board on 20 May 2002. All amounts represent remuneration between these dates.

4 J Scott was appointed to the Board on 10 April 2001. All amounts represent remuneration from this date.

Directors' share options

Directors' emoluments disclosed above do not include any amounts for the value of options to acquire ordinary shares in the company granted or held by the directors. Details of the options are as follows:

Name	As at 1 January 2002	Granted	Exercised/ lapsed	As at 31 December 2002	Gain on exercise 2002 £	Exercise price	Earliest date of exercise	Expiry date
J Fineman	100,000	-	-	100,000	-	85.5p	20.04.02	20.04.06
	150,000	-	-	150,000	-	95p	16.08.02	16.08.06
	150,000	-	-	150,000 ²	-	120p	01.12.03	01.12.07
	100,000	-	-	100,000 ³	-	120p	01.12.05	01.12.07
	-	12,757 ¹	-	12,757	-	56p	01.04.04	01.10.04
	500,000			512,757				
N Berry	-	250,000	-	250,000 ²	-	71.5p	21.05.05	21.05.12
S Temple	-	100,000	-	100,000 ²	-	74p	27.02.05	22.02.12
H Baker-Smith	201,620	-	-	201,620	-	62p	20.10.01	20.10.05
	48,380	-	-	48,380	-	62p	20.10.01	20.10.08
	133,500	-	-	133,500 ²	-	131p	23.07.04	23.07.11
	16,500	-	-	16,500 ²	-	131p	23.07.06	23.07.11
	-	12,757 ¹	-	12,757	-	56p	01.04.04	01.10.04
	400,000			412,757				
I Dinwoodie	150,000	-	-	150,000 ²	-	88p	22.11.04	22.11.11
	-	100,000	-	100,000 ²	-	68.5p	12.06.05	12.06.12
	150,000			250,000				
G MacLeod (resigned 20 May 2002)	48,380	-	-	48,380 ²	-	62p	20.10.01	20.10.08
	1,620	-	-	1,620 ²	-	62p	20.10.01	20.10.05
	11,625 ¹	-	-	11,625 ³	-	52p	01.12.01	31.05.02
	4,211 ¹	-	-	4,211 ³	-	92p	01.12.02	31.05.03
	200,000	-	-	200,000 ³	-	160p	16.02.04	16.02.08
	265,836			265,836				

1. These options were granted under the Xaar plc 1998, 1999, 2001 and 2002 Share Save Schemes.
2. These options carry certain specific performance criteria which must be achieved prior to vesting, relating to share price performance and index-linked earnings per share growth. Further details of vesting criteria are shown on page 15.
3. These amounts represent options outstanding as at the date of resignation from the Board. All options have fully vested, except for the Share Save Schemes and the grant of 200,000 options, which lapsed on resignation. The 50,000 options with an earliest exercise date at 20.10.01 lapsed three months from resignation.

Directors' share options (continued)

The following gains on the exercise of share options were made by directors in 2001. A Rosenfeld £550,000, H Baker-Smith £8,622, S Temple £6,758.

The market value of the ordinary shares of the company as at 31 December 2002 was 24p per share. The closing mid range price ranged from 21p to 94.5p per share during the year.

Approval

This report was approved by the Board of directors on 18 February 2003 and signed on its behalf by:


Ian Dinwoodie
Director

18 February 2003

We have audited the financial statements of Xaar plc for the year ended 31 December 2002 which comprise the profit and loss account, the balance sheets, the cash flow statement, the statement of total recognised gains and losses and the related notes 1 to 28. We have also audited the company balance sheet and related notes numbered 1 to 4. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the part of the directors' remuneration report that is described as having been audited.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As described in the statement of directors' responsibilities, the company's directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards. They are also responsible for the preparation of the other information contained in the annual report including the directors' remuneration report. Our responsibility is to audit the financial statements and the part of the directors' remuneration report described as having been audited in accordance with relevant United Kingdom legal and regulatory requirements and auditing standards.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the company and other members of the group is not disclosed.

We review whether the corporate governance statement reflects the company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules of the Financial Services

Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the group's corporate governance procedures or its risk and control procedures.

We read the directors' report and the other information contained in the annual report for the above year as described in the contents section including the unaudited part of the directors' remuneration report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the directors' remuneration report described as having been audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements and of whether the accounting policies are appropriate to the circumstances of the company and the group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the directors' remuneration report described as having been audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the directors' remuneration report described as having been audited.

Opinion

In our opinion:

- the financial statements give a true and fair view of the state of affairs of the company and the group as at 31 December 2002 and of the profit of the group for the year then ended; and
- the financial statements and part of the directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985.

Debitte + Tancin

Deloitte & Touche

Chartered Accountants and Registered Auditors
Cambridge

18 February 2003

	Notes	2002 £'000	2001 £'000 (restated)
Turnover	2	30,870	23,982
Cost of sales		(16,770)	(11,374)
Gross profit		14,100	12,608
Other operating expenses (net)	3	(13,315)	(11,231)
Operating profit		785	1,377
Exceptional item	7	-	(1,049)
Profit on ordinary activities before interest		785	328
Interest receivable	4	275	315
Interest payable	5	(135)	(67)
Profit on ordinary activities before taxation	6	925	576
Tax on profit on ordinary activities	9	86	(939)
Retained profit/(loss) for the financial year	21	1,011	(363)
Earnings/(loss) per share – basic	11	1.7p	(0.6)p
Earnings/(loss) per share – diluted	11	1.7p	(0.6)p

The accompanying notes are an integral part of this consolidated profit and loss account.

All activities during the financial year relate to continuing operations.

The restatement of the results for 2001 is described further in note 12.

Consolidated statement of total recognised gains and losses for the year ended 31 December 2002

	Notes	2002 £'000	2001 £'000 (restated)
Retained profit/(loss) for the financial year		1,011	(363)
Gain/(loss) on foreign currency translation	21	718	(489)
Total recognised gains and losses relating to the financial year		1,729	(852)
Prior year adjustment	12	(332)	-
Total recognised gains and losses since last annual report		1,397	(852)

The accompanying notes are an integral part of this consolidated statement of total recognised gains and losses.

Consolidated balance sheet as at 31 December 2002

Xaar plc

	Notes	2002 £'000	2001 £'000 (restated)
Fixed assets			
Intangible assets	13	1,260	1,456
Tangible assets	14a	4,733	4,336
Investments	14b	20	20
		6,013	5,812
Current assets			
Stocks	15	1,967	1,125
Debtors	16	6,801	5,517
Short term investments	25	-	2,875
Cash at bank and in hand	25	9,852	6,885
		18,620	16,402
Creditors: amounts falling due within one year	17	(6,388)	(5,271)
Net current assets		12,232	11,131
Total assets less current liabilities			
Creditors: amounts falling due after more than one year	18	(906)	(470)
Provisions for liabilities and charges	19	-	(1,024)
Net assets		17,339	15,449
Capital and reserves			
Called-up share capital	20	5,971	5,934
Share premium account	21	11,129	11,009
Other reserves	21	1,099	1,095
Accumulated deficit	21	(860)	(2,589)
Shareholders' funds - all equity	22	17,339	15,449

Signed on behalf of the Board
18 February 2003


I Dinwoodie
Director

N Berry
Director

The accompanying notes are an integral part of this consolidated balance sheet.
The restatement of the results for 2001 is described further in note 12.

Consolidated cash flow statement for the year ended 31 December 2002

Xaar plc

	Notes	2002 £'000	2001 £'000
Net cash inflow from operating activities	23	540	2,769
Returns on investments and servicing of finance	24	149	248
Capital expenditure and financial investment	24	(1,090)	(1,192)
Cash (outflow)/inflow before management of liquid resources and financing		(401)	1,825
Management of liquid resources	24	2,875	1,925
Financing	24	(141)	238
Increase in cash in the year	25	2,333	3,988

The accompanying notes are an integral part of this consolidated cash flow statement.

1. Accounting policies

The principal accounting policies, all of which have been applied consistently throughout the year and the prior year, with the exception of the policy for deferred tax discussed in note 12, are set out below:

a) Basis of accounting

The financial statements are prepared under the historical cost convention and in accordance with applicable accounting standards. Cash and liquid resources shown on the balance sheet in the 2001 financial statements have been shown separately as cash at bank and in hand and short term investments within these financial statements in order to clarify the presentation.

b) Basis of consolidation

The group financial statements consolidate the financial statements of Xaar plc and its subsidiary undertakings drawn up to 31 December each year. The results of subsidiaries acquired or sold are consolidated for the periods from or to the date on which control passed. Acquisitions are accounted for under the acquisition method, except the company has accounted for Xaar Technology Limited under merger accounting principles.

c) Intangible assets - goodwill and licence rights

Goodwill arising on the acquisition of subsidiary undertakings and businesses, representing any excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired, is capitalised and written off on a straight-line basis over its useful economic life, which is considered to be ten years in the case of XaarJet AB. Provision is made for any impairment.

Payments in respect of licence rights acquired are capitalised at cost and amortised on a straight-line basis over their estimated useful lives.

d) Tangible fixed assets

All fixed assets are shown at original historical cost net of depreciation and any provision for impairment.

Depreciation is provided at rates calculated to write off the cost, less estimated residual value, of each asset on a straight-line basis over its estimated useful life, as follows:

Improvements to leasehold property	10 years
Plant and machinery	3 - 5 years
Furniture, fittings and equipment	3 - 5 years
Motor vehicles	3 years

e) Investments

Fixed asset investments are shown at cost less any provision for impairment.

f) Stocks

Stocks are stated at the lower of cost and net realisable value. Cost includes materials, direct labour and an attributable proportion of manufacturing overheads based on normal levels of activity. Net realisable value is based on estimated selling price, less further costs expected to be incurred to completion and disposal. Provision is made for obsolete, slow-moving or defective items where applicable.

g) Foreign currency

Transactions denominated in foreign currencies are recorded in the local currency at actual exchange rates as of the date of the transaction or, if hedged, at the forward contract rate. Monetary assets and liabilities denominated in foreign currencies at the year end are reported at the rates of exchange prevailing at the year end or, if appropriate, at the forward contract rate. Gains or losses arising from a change in exchange rates subsequent to the date of the transactions are included as exchange gains or losses in the profit and loss account.

The results of overseas operations are translated at the average rates of exchange during the period and their balance sheets at the rates ruling at the balance sheet date. Exchange differences arising on translation of the opening net assets and results of overseas operations are dealt with through reserves. All other exchange differences are included in the profit and loss account.

h) Research and development

Research and development costs including the costs associated with the acquisition, registration and development of patents and know-how, are written off to the profit and loss account as incurred. Third party research and development costs for specific identifiable projects may be capitalised in accordance with SSAP13 if considered appropriate.

i) Pension costs

Amounts charged in the profit and loss account comprise employer's contributions payable to the company's defined contribution group personal pension scheme in respect of pensionable payroll costs for the accounting year.

j) Turnover

Turnover, all of which arises from continuing activities, comprises printheads and related products net of trade discounts, VAT and other sales-related taxes, development fees receivable under agreements (gross of any tax withheld), licences and royalties receivable.

k) Leases

Assets held under finance leases are initially capitalised at the fair value of the asset with an equivalent liability categorised as appropriate under creditors due within or after one year. The asset is depreciated over the shorter of the lease term and its useful economic life. Finance charges are allocated to accounting periods over the period of the lease to produce a constant rate of charge on the outstanding balance. Rentals are apportioned between finance charges and reduction of the liability. Hire purchase assets are dealt with similarly except that assets are depreciated over their useful economic lives.

Rentals under operating leases are charged on a straight-line basis over the lease term, even if the payments are not made on such a basis.

l) Taxation

Current tax, including UK corporation tax and foreign tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantially enacted by the balance sheet date.

Deferred taxation is provided in full on timing differences that result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when the timing differences crystallize based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

2. Segmental information

Turnover by class of business:

	2002 £'000	2001 £'000
Printheads and related products	28,477	19,488
Development fees	1,227	1,463
Licence fees and royalties	1,166	3,031
	30,870	23,982

Turnover by geographical segment:

	2002 £'000	2001 £'000
Europe & Middle East	9,641	6,652
Asia	17,071	11,553
Americas	4,158	5,777
	30,870	23,982

2. Segmental information (continued)

Gross margin by class of business:

	2002 £'000	2001 £'000
Printheads and related products	11,859	8,278
Development fees	1,227	1,463
Licence fees and royalties	1,014	2,867
	14,100	12,608

No additional segmental information is provided on the basis that it would be seriously prejudicial to the interests of the group.

3. Other operating expenses (net)

	2002 £'000	2001 £'000
Distribution costs	3,172	2,520
Administrative expenses	10,143	8,711
	13,315	11,231

Administrative expenses consist of:

Research and development	4,425	4,137
Other	5,718	4,574
	10,143	8,711

Research and development:

Research and development costs for year	4,425	4,137
Less: third party development fees received ¹	(1,227)	(1,463)
Net research and development costs	3,198	2,674

¹ Third party development fees received in respect of specific research and development projects are accounted for within turnover as development fees (see Note 2). They are shown here for informational purposes.

4. Interest receivable

	2002 £'000	2001 £'000
Interest receivable on short term deposits	275	315

5. Interest payable

	2002 £'000	2001 £'000
Bank loans and overdrafts	22	9
Finance leases and hire purchase contracts	113	58
	135	67

6. Profit on ordinary activities before taxation

The profit on ordinary activities before taxation is stated after charging/(crediting):

	2002 £'000	2001 £'000
Auditors' remuneration		
- audit (Andersen)	-	48
- non audit (Andersen)	31	152 ¹
- audit (Deloitte & Touche)	45	-
- non audit (Deloitte & Touche)	95	-
Depreciation of tangible fixed assets		
- on assets owned	1,242	1,216
- on assets held under finance leases and hire purchase contracts	264	336
Amortisation of goodwill	138	138
Amortisation of licences	58	48
Exceptional warranty costs	333 ²	-
Staff costs (see note 8)	9,671	8,631
Operating lease rentals in respect of:		
- Hire of plant and machinery	25	40
- Land and buildings	723	731
(Profit)/loss on disposal of tangible fixed assets	(19)	(13)

¹ Includes £50,000 in respect of the group restructuring and is included in the exceptional item

² Exceptional warranty costs represent the additional costs incurred in meeting XJ500 warranty claims in the year

The audit fee for Xaar plc in 2002 was £10,000 (2001: £10,000).

7. Exceptional item reported after operating profit

The costs of a fundamental restructuring of continuing operations arose in 2001 in respect of the transfer of all volume production to the XaarJet AB facility, which has had a material effect on the nature and focus of the group's operations. The effect of the exceptional item reported after operating profit on the amounts charged to the profit and loss account for taxation were:

	2002 £'000	2001 £'000
Costs of a fundamental restructuring of continuing operations	-	(81)
Decrease in charge to profit and loss account	-	(81)

8. Staff costs

Particulars of employees (including executive directors) are shown below:

	2002 £'000	2001 £'000
Employee costs during the year amounted to:		
Wages and salaries	7,609	6,890
Social security costs	1,505	1,235
Other pension costs	557	506
	9,671	8,631

The average monthly number of persons employed by the group was as follows:

	2002 Number	2001 Number
Research and development	48	49
Sales and marketing	31	22
Manufacturing and engineering	155	138
Administration	22	16
	256	225

Remuneration of directors

The remuneration report on pages 15 to 17 includes details of directors' emoluments, which form part of these financial statements.

9. Tax on profit on ordinary activities

	Year to 31 December 2002 £'000	Year to 31 December 2001 £'000 (restated)
Foreign tax	680	607
Deferred tax – origination and reversal of timing differences	(232)	332
	448	939
Adjustments in respect of prior years		
Foreign tax	(41)	-
Deferred tax	(493)	-
Tax on profit on ordinary activities	(86)	939

9. Tax on profit on ordinary activities (continued)

The standard rate of tax for the year, based on the UK standard rate of corporation tax is 30%. The actual tax charge for the current and the previous year varies from the standard rate for the reasons set out in the following reconciliation:

	2002 £'000	2001 £'000
Profit on ordinary activities before tax	925	576
Tax on ordinary activities at standard rate	277	173
Effect of:		
Expenses not deductible for tax purposes	14	56
Capital allowances in excess of depreciation	(29)	(20)
Utilisation of tax losses	-	(590)
Movement in short term timing differences	(78)	147
Unrelieved current year UK losses	415	695
Other unrecognised deferred tax movements	-	493
Effect of foreign tax rates	(76)	(90)
Unrelieved foreign tax suffered	56	207
Enhanced tax deduction for R&D expenditure	(131)	(132)
Total actual amount of current tax	448	939

Factors that may affect the future tax charge:

A deferred tax asset has not been recognised in respect of timing differences relating to UK revenue losses as the directors consider there is insufficient evidence that the assets will be recovered. The amount of the asset not recognised is £3,653,000 (2001: £3,238,000). These assets will be utilised if the UK companies make future taxable income.

Included in the unrecognised deferred tax asset are enhanced tax allowances in respect of R&D expenditure. These allowances either have been or will be surrendered for a cash payment from the Inland Revenue which will be recognised when approval is received.

10. Loss attributable to Xaar plc

The loss for the financial year dealt with in the accounts of Xaar plc was £699,000 (2001: £688,000). As provided by section 230 of the Companies Act 1985, no profit and loss account is presented in respect of Xaar plc.

11. Earnings/(loss) per ordinary share - basic and diluted

The calculation of earnings/(loss) per share is based upon the profit/(loss) for the period after taxation and on the weighted average number of ordinary shares in issue during the period. For basic earnings/(loss) per share, this is 59,603,709 (2001: 58,890,234) and for diluted earnings/(loss) per share, this is 59,842,670 (2001: 58,890,234), the only difference being in relation to movements in share options.

12. Prior year adjustment

The group's policy for accounting for deferred tax has changed to take into account the new accounting standard FRS19 "Deferred tax". Previously deferred tax was only provided to the extent that timing differences were expected to reverse in the future without being replaced. Deferred tax is now provided in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more or less tax in the future have occurred at the balance sheet date. This change was also referred to in the interim report and the notes thereto.

12. Prior year adjustment (continued)

As a result the comparative figure for the tax on profit on ordinary activities and the deferred tax provision have been restated. The effects of the change in policy are summarised below:

	2002 £'000	2001 £'000
Profit and loss account		
Decrease in profit for the financial year	-	(332)
Balance sheet		
Decrease in net assets	-	(332)
	-	-

13. Intangible fixed assets

	Licences acquired £'000	Goodwill £'000	Total £'000
Cost			
At 1 January 2002 and at 31 December 2002	533	1,375	1,908
Amortisation			
At 1 January 2002	73	379	452
Charge for the year	58	138	196
At 31 December 2002	131	517	648
Net book value			
At 31 December 2002	402	858	1,260
At 31 December 2001	460	996	1,456

14a. Tangible fixed assets

	Leasehold property £'000	Plant & machinery £'000	Furniture, fittings & equipment £'000	Assets in the course of construction £'000	Motor vehicles £'000	Total £'000
Cost						
At 1 January 2002	1,276	6,885	1,030	210	285	9,686
Additions	64	1,117	116	549	46	1,892
Transfers	218	238	-	(456)	-	-
Exchange movements	22	230	14	57	-	323
Disposals	-	(39)	-	-	(317)	(356)
At 31 December 2002	1,580	8,431	1,160	360	14	11,545
Depreciation						
At 1 January 2002	470	4,247	523	-	110	5,350
Charge for the year	174	1,061	197	-	74	1,506
Exchange movements	20	128	7	-	-	155
Disposals	-	(22)	-	-	(177)	(199)
At 31 December 2002	664	5,414	727	-	7	6,812
Net book value						
At 31 December 2002	916	3,017	433	360	7	4,733
At 31 December 2001	806	2,638	507	210	175	4,336
Leased assets included in the above:						
Net book value						
At 31 December 2002	-	1,270	57	-	7	1,334
At 31 December 2001	-	1,053	67	-	145	1,265

14b. Investment in own shares

An Employee Benefit Trust was established in 1995 to hold shares for the benefit of the employees of the company and the group. Xaar Trustee Limited was formed during 1995 to act as trustee to the Trust. At 31 December 2002 and 2001 there were 91,250 ordinary shares in Xaar plc held in trust by Xaar Trustee Limited at a cost of £20,000.

15. Stocks

	2002 £'000	2001 £'000
Raw materials and consumables	1,086	824
Work in progress	122	130
Finished goods	759	171
	1,967	1,125

There is no material difference between the balance sheet value of stocks and their replacement cost.

16. Debtors: amounts receivable within one year

	2002 £'000	2001 £'000
Trade debtors	4,850	4,595
VAT	529	339
Other debtors	73	13
Prepayments and accrued income	931	570
Deferred tax (see note 19)	418	-
	6,801	5,517

17. Creditors: amounts falling due within one year

	2002 £'000	2001 £'000
Obligations under finance leases and hire purchase contracts	356	236
Trade creditors	2,789	2,496
Corporation tax	1,066	476
Other taxation and social security	449	292
Amount due to pension scheme	30	30
Other creditors	904	462
Accruals	794	1,279
	6,388	5,271

18. Creditors: amounts falling due after more than one year

	2002 £'000	2001 £'000
Obligations under finance leases and hire purchase contracts, due between 2 to 5 years	906	470

19. Provisions for liabilities and charges

	Deferred tax £'000	Restructuring £'000	Total £'000
At 31 December 2001, as previously stated	-	692	692
Prior year adjustment	332	-	332
At 1 January 2002, as restated	332	692	1,024
Utilised	-	(692)	(692)
Credited to profit and loss account	(725)	-	(725)
Foreign exchange movements	(25)	-	(25)
At 31 December 2002	(418)	-	(418)

The restructuring provision created in 2001 relates to amounts payable in respect of the relocation of volume manufacturing from the UK to Sweden.

An analysis of the deferred tax asset is shown below:

	2002 £'000	2001 £'000
Capital allowances in excess of depreciation	-	8
Other timing differences	(418)	332
Losses	-	(8)
	(418)	332

The deferred tax asset has been recognised as the directors consider it recoverable based on the expected availability of future taxable profits, and has been classified within debtors in accordance with FRS19.

20. Called-up share capital

	2002 £'000	2001 £'000
Authorised		
70,000,000 ordinary shares of 10p each	7,000	7,000
Allotted, called-up and fully paid		
59,708,386 (2001: 59,340,416) ordinary shares of 10p each	5,971	5,934

The movement during the year on the company's allotted, called-up and fully paid shares was as follows:

	2002 Number	2002 £'000	2001 £'000
At beginning of year	59,340,416	5,934	5,742
Consideration for Xaar Technology Limited ¹	70,000	7	80
Exercise of share options	297,970	30	112
At end of year	59,708,386	5,971	5,934

¹ Relates to the exercise of Xaar Technology Limited share options which are subject to a put and call mechanism, whereby each £1 ordinary Xaar Technology Limited share option exercised and allotted is exchanged for ten 10p ordinary shares in Xaar plc.

20. Called-up share capital (continued)

Options have been granted under separate share option schemes to subscribe for ordinary shares of the company as follows:

Scheme	Date of grant	Number of shares under option	Subscription price per share - pence
Xaar Technology Limited 1992 Unapproved Scheme ¹	09.05.96	120,000	15p
		120,000	
Xaar Technology Limited 1997 Unapproved Scheme ²	11.02.97	161,530	48p
	26.06.97	85,000	48p
		246,530	
Xaar plc 1997 Share Option Scheme	24.10.97	37,500	110p
	20.10.98	300,000	62p
	18.03.99	37,500	52.5p
	20.04.99	100,000	85.5p
	17.05.99	75,000	90p
	16.08.99	150,000	95p
	20.10.99	155,000	115p
	06.04.00	15,000	319p
	18.04.00	50,000	279p
	01.12.00	250,000	120p
	18.12.00	30,000	142p
	16.02.01	70,000	160p
	23.07.01	225,000	131p
	22.11.01	200,000	88p
	22.02.02	100,000	74p
	21.05.02	250,000	71.5p
	12.06.02	100,000	68.5p
	19.11.02	507,500	25p
		2,652,500	
Xaar plc Share Save Scheme	17.11.99	52,635	92p
	01.04.01	27,846	128p
	01.04.02	302,693	56p
		383,174	
Total share options outstanding at 31 December 2002		3,402,204	

1. Options under this scheme are in fact options over Xaar Technology Limited shares. However, as a put and call mechanism provides for immediate conversion to Xaar plc shares upon exercise, the figures included in the above table assume such conversion.

2. Holders of the options under this scheme have exchanged their options for options in Xaar plc.

20. Called-up share capital (continued)

Options under the Xaar Technology Limited 1992 Unapproved Scheme, the Xaar Technology Limited 1997 Unapproved Scheme and the Xaar plc 1997 Share Option Scheme are exercisable within three to seven years after the date of the grant, except that approved options, and unapproved options granted after 27 March 2001, granted under the Xaar plc 1997 Share Option Scheme are exercisable within three to ten years after the date of the grant. The maximum value of approved options, under the Xaar plc 1997 Share Scheme, which may be granted to individual employees is £30,000.

Options under the Xaar plc Share Save Scheme are exercisable between 36 and 42 months after the date of the grant.

21. Capital and reserves

The movement on reserves for the year is as follows:

	Called-up share capital £'000	Share premium account £'000	Accumulated deficit £'000	Other reserves £'000	Total £'000
At 31 December 2001, as previously stated	5,934	11,009	(2,257)	1,095	15,781
Prior year adjustment	-	-	(332)	-	(332)
At 1 January 2002, as restated	5,934	11,009	(2,589)	1,095	15,449
Retained profit for the financial year	-	-	1,011	-	1,011
Shares issued during the year	37	120	-	4	161
Exchange differences	-	-	718	-	718
At 31 December 2002	5,971	11,129	(860)	1,099	17,339

The share premium account and other reserves are not distributable. Other reserves represent the share premium account in Xaar Technology Limited.

22. Reconciliation of movements in group shareholders' funds

	2002 £'000	2001 £'000 (restated)
Profit/(loss) for the financial year	1,011	(363)
New shares issued	161	757
Gain/(loss) on foreign currency translation	718	(489)
Net increase/(decrease) in shareholders' funds	1,890	(95)
Opening shareholders' funds, as previously stated	15,781	15,544
Prior year adjustment	(332)	-
Opening shareholders' funds, as restated	15,449	15,544
Closing shareholders' funds	17,339	15,449

23. Reconciliation of operating profit to net cash inflow from operating activities

	2002 £'000	2001 £'000
Operating profit	785	1,377
Cash outflow from exceptional item	(979)	(75)
Depreciation charge	1,506	1,552
Amortisation of intangibles	196	186
(Profit) on disposal of tangible fixed assets	(19)	(13)
(Increase) in stock	(748)	(255)
(Increase) in debtors	(701)	(970)
Increase in creditors	500	967
Net cash inflow from operating activities	540	2,769

24. Analysis of cash flows

	2002 £'000	2001 £'000
Returns on investments and servicing of finance		
Interest received	284	315
Interest paid	(22)	(9)
Interest element of finance lease rentals	(113)	(58)
Net cash inflow	149	248
Capital expenditure and financial investment		
Purchase of tangible fixed assets	(1,129)	(1,225)
Sale of tangible fixed assets	39	33
Net cash outflow	(1,090)	(1,192)
Management of liquid resources		
Decrease in treasury deposits	2,875	1,925
Net cash inflow	2,875	1,925
Financing		
Issue of ordinary share capital	161	757
Capital element of finance lease rental payments	(302)	(519)
Net cash (outflow)/inflow	(141)	238

25. Analysis and reconciliation of net funds

	1 January 2002 £'000	Cash flow £'000	Exchange differences £'000	Other non- cash changes £'000	31 December 2002 £'000
Cash at bank and in hand	6,885	2,333	634	-	9,852
Finance leases	(706)	302	(40)	(818)	(1,262)
Treasury deposits	2,875	(2,875)	-	-	-
Net funds	9,054	(240)	594	(818)	8,590

	2002 £'000	2001 £'000
Increase in cash in the year	2,333	3,988
Cash outflow from decrease in lease financing	302	519
Cash (inflow) from (decrease) in liquid resources	(2,875)	(1,925)
Change in net funds resulting from cash flows	(240)	2,582
Exchange differences	594	(311)
New finance leases	(818)	(612)
Movement in net funds in year	(464)	1,659
Net funds at beginning of year	9,054	7,395
Net funds at end of year	8,590	9,054

Other non-cash changes relate to new finance leases in the year.

26. Guarantees and other financial commitments

a) Capital commitments

At the end of the year, capital commitments were:

	2002 £'000	2001 £'000
Contracted for but not provided for	1,814	1,525

b) Lease commitments

The group has entered into non-cancellable leases in respect of fixtures, fittings and equipment, the payments for which extend over a period of up to 3 years. The total rental for the year was £25,000 (2001: £40,000). In addition, the group leases land and buildings. The rental for the year was £723,000 (2001: £731,000). The minimum annual rentals under non-cancellable operating leases are as follows:

	Land and buildings		Fixtures, fittings and equipment	
	2002 £'000	2001 £'000	2002 £'000	2001 £'000
Operating leases which expire:				
- within 1 year	-	-	2	3
- between 2 and 5 years	468	423	91	7
- after 5 years	371	375	-	-

The company has no operating lease commitments or capital commitments at the balance sheet date (2001: £nil).

27. Subsidiary undertakings

The following entities are wholly-owned subsidiary undertakings of the company:

Name & country of incorporation	Registered office	Issued & fully paid up share capital	Proportion of ordinary share capital held by the company
Xaar Technology Limited England and Wales	Science Park Cambridge, CB4 0XR	4,426,322 ordinary £1 shares	100%
XaarJet Limited England and Wales	Science Park Cambridge, CB4 0XR	2 ordinary £1 shares	100%
Xaar Trustee Limited ¹ England and Wales	Science Park Cambridge, CB4 0XR	2 ordinary £1 shares	100%
Xaar Digital Limited ² England and Wales	Science Park Cambridge, CB4 0XR	1 ordinary £1 share	100%
Xaar Group AB Sweden	Box 516, SE-17526 Järfälla, Sweden	1,000 ordinary shares of SEK 100 each	100%
XaarJet AB ³ Sweden	Box 516, SE-17526 Järfälla, Sweden	1,000 ordinary shares of SEK 100 each	100%

¹ Xaar Trustee Limited shares are held by Xaar Technology Limited.

² Dormant.

³ XaarJet AB shares are held by Xaar Group AB.

The principal activity of Xaar Technology Limited is the development and commercial exploitation of patented inkjet printing technologies. The principal activity of XaarJet Limited and XaarJet AB is the manufacture and marketing of specialist Xaar printheads and inks. The principal activity of Xaar Group AB is to act as a holding company. No subsidiary undertakings have been excluded from the consolidation.

28. Financial instruments

There were no significant changes during the year to the financial risks to which the group was exposed.

The group's financial instruments comprise finance lease and hire purchase commitments, cash and liquid resources, and various items, such as trade debtors and trade creditors, that arise directly from its operations. The group undertakes foreign currency transactions in the course of operations. Where such transactions are individually material, the group has a policy of entering into foreign currency contracts to manage currency risk arising. Otherwise, group entities undertake natural hedging of revenue and expense streams in foreign currencies to the extent possible.

It is, and has been throughout the year, the group's policy that no active trading in financial instruments shall be undertaken.

The main risks arising from the group's financial instruments are interest rate risk, currency risk and liquidity risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below.

Interest rate risk

The group is currently funded by equity and invests its funds in short-term bank deposits, typically with maturity periods less than three months. Limits have been set by the board in relation to maximum deposits with any one institution.

28. Financial instruments (continued)**Currency risk**

The group's objective in managing the currency exposures arising from its net investment overseas is to maintain a broadly equivalent revenue and expense stream in the local currency of the subsidiary. The residual structural risk which results from movements in overseas subsidiary net assets may be hedged where considered appropriate.

Liquidity risk

With regard to liquidity, the group's policy throughout the year has been to fund significant fixed asset purchases by finance leases repayable over a period of three to five years depending on the asset being financed. Finance lease and hire purchase commitments are the only borrowings of the group.

The numerical disclosures in this note deal with financial assets and financial liabilities as defined in Financial Reporting Standard 13 "Derivatives and other financial instruments: Disclosures" ("FRS13"). Certain financial assets such as investments in subsidiaries are excluded from the scope of these disclosures. As permitted by FRS13, short term debtors and creditors have been excluded from the disclosures.

Interest rate profile

The group has no financial assets, other than cash and fixed rate deposits. Fixed rate deposits amount to £nil (2001: £2,875,000), and are part of the financing arrangements of the group. The weighted average rate of interest in respect of the sterling deposits was nil% (2001: 3.7%). The weighted average period to maturity for which these rates were fixed was nil days (2001: 1 day). No individual deposits exceeded three months in duration. The interest rate on floating rate financial assets is linked to base rate.

	Floating rate 2002 £'000	2001 £'000
Sterling	1,257	1,506
United States Dollar	1,579	2,298
Euro	30	46
Swedish Kroner	6,986	3,035
Total	9,852	6,885

The group's financial liabilities, totalling £1,262,000 at 31 December 2002 (2001: £706,000), solely comprise finance leases and hire purchase commitments. These are further analysed below.

	Fixed rate finance lease and hire purchase commitments		Weighted average interest rate		Weighted average period for which rate is fixed		Floating rate	
	2002 £'000	2001 £'000	2002 %	2001 %	2002 Months	2001 Months	2002 £'000	2001 £'000
Sterling	356	564	5.7%	5.4%	37	41	-	-
Swedish Kroner	-	-	-	-	-	-	906	142

The interest rate on floating rate financial liabilities is linked to base rate.

28. Financial instruments (continued)**Maturity of financial liabilities**

The maturity profile of the group's financial liabilities at 31 December 2001 was as follows:

	Borrowings (notes 16 and 17)	
	2002 £'000	2001 £'000
In one year or less	356	236
In more than one year but not more than two years	305	218
In more than two years but not more than five years	601	252
Total	1,262	706

Borrowing facilities

The group had no borrowing facilities at 31 December 2002 (2001: none).

Fair values

There was no material difference between the book value and fair value of the group's financial instruments in either financial year.

Gains and losses on hedges

No unrecognised gains or losses existed at 31 December 2002 (2001: nil) in respect of the group's financial instruments.

Interest rate risk

Group funds are invested in deposit accounts with the objective of maintaining a balance between accessibility of funds and competitive rates of return. In practice, this has meant that no deposits were made with a maturity date greater than three months during the year (2001: three months).

Currency exposures

As explained above, the group's objective in managing the currency exposures arising from its net investment overseas (in other words, its structural currency exposures) is to maintain a broadly equivalent revenue and expense stream in local currency. Any gains and losses arising from these structural currency exposures are recognised in the statement of total recognised gains and losses.

The table below shows the group's currency exposures; in other words, those transactional (or non-structural) exposures that give rise to the net currency gains and losses recognised in the profit and loss account. Such exposures comprise the monetary assets and monetary liabilities of the group that are not denominated in the operating (or "functional") currency of the operating unit involved. These exposures were as follows:

Net foreign currency monetary assets/(liabilities)

Functional currency of group operation	Sterling £'000	Swedish Kroner £'000	US Dollar £'000	Yen £'000	Swiss Francs £'000	Euro £'000	Total £'000
Sterling	-	-	657	(10)	(12)	571	1,206
Swedish Kroner	21,653	-	293	(4)	56	95	22,093
At 31 December 2002	21,653	-	950	(14)	44	666	23,299

28. Financial instruments (continued)

Net foreign currency monetary assets/(liabilities)

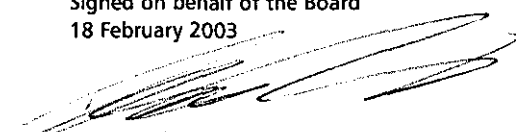
Functional currency of group operation	Sterling £'000	Swedish Kroner £'000	US Dollar £'000	Yen £'000	Swiss Francs £'000	Euro £'000	Total £'000
Sterling	-	(2)	527	(2)	(3)	(25)	495
Swedish Kroner	1,173	-	(42)	(2)	36	47	1,212
At 31 December 2001	1,173	(2)	485	(4)	33	22	1,707

The amounts shown in the above tables take into account the effect of any currency swaps, forward contracts and other derivatives entered into to manage these currency exposures.

Company balance sheet as at 31 December 2002

	Notes	2002 £'000	2001 £'000
Fixed asset investments	1	12,433	7,578
Current assets			
Debtors	2	26,072	3,562
Short term investments		-	2,875
Cash at bank and in hand		419	647
		26,491	7,084
Creditors: amounts falling due within one year	3	(268)	(312)
Net current assets		26,223	6,772
Net assets		38,656	14,350
Capital and reserves			
Called-up share capital	4	5,971	5,934
Share premium account	4	11,129	11,009
Other reserves	4	24,848	-
Accumulated deficit	4	(3,292)	(2,593)
Shareholders' funds - all equity		38,656	14,350

Signed on behalf of the Board
18 February 2003



I Dinwoodie
Director



N Berry
Director

The accompanying notes are an integral part of this balance sheet

1. Fixed asset investments

Subsidiary undertakings

	2002 £'000	2001 £'000
At beginning of year	7,578	7,498
Investment in Xaar Technology Limited ¹	7	80
Disposal of XaarJet AB	(3,152)	-
Investment in Xaar Group AB	8,000	-
At end of year	12,433	7,578

1. The company, pursuant to the put and call provisions in the articles of association of Xaar Technology Limited, acquired the shares issued as a result of the exercise of Xaar Technology Limited options during the year and, in consideration for their acquisition, issued ten ordinary 10p shares in the company for each £1 ordinary share so acquired.

During the year, the company sold its investment in XaarJet AB to Xaar Group AB for £28.0m, which comprised £8.0m of equity in Xaar Group AB and £20.0m in a loan note. The company made an unrealised profit on this sale of £24.8m which has been taken to reserves. There is no impact on the group results as this profit is eliminated upon consolidation.

2. Debtors: amounts receivable within one year

	2002 £'000	2001 £'000
Amounts owed by group undertakings	26,072	3,554
Prepayments and accrued income	-	8
	26,072	3,562

Amounts owed by group undertakings include £20.0m (2001:£nil) in respect of a five-year loan note granted to Xaar Group AB, which can be repaid early at the option of Xaar Group AB.

3. Creditors: amounts falling due within one year

	2002 £'000	2001 £'000
Trade creditors	6	37
Other taxation and social security	-	12
Accruals	262	263
	268	312

4. Capital and reserves

	Called-up share capital £'000	Share premium account £'000	Other reserves £'000	Accumulated deficit £'000	Total £'000
At 1 January 2002	5,934	11,009	-	(2,593)	14,350
New shares issued	37	120	-	-	157
Loss for the financial year	-	-	-	(699)	(699)
Profit on sale of subsidiary	-	-	24,848	-	24,848
At 31 December 2002	5,971	11,129	24,848	(3,292)	38,656

Full details of movements in share capital are given in note 19 to the consolidated financial statements. The share premium account and other reserves are non-distributable.

NOTICE IS HEREBY GIVEN that the SIXTH ANNUAL GENERAL MEETING of the company will be held at The Q-ton Forum, Science Park, Milton Road, Cambridge on 15 April 2003 at 10.30am for the following purposes:

Ordinary business

1. TO receive the company's annual financial statements for the financial year ended 31 December 2002, together with the directors' report and the auditors' report on those financial statements.
2. TO re-appoint Deloitte & Touche as auditors to hold office from the conclusion of this meeting until the conclusion of the next general meeting of the company at which accounts are laid and to authorise the directors to fix their remuneration.
3. TO re-appoint Jan Fineman as a director in accordance with the company's articles of association.
4. TO re-appoint Hugh Baker-Smith as a director in accordance with the company's articles of association.
5. TO re-appoint Nigel Berry as a director in accordance with the company's articles of association.
6. TO re-appoint Richard King as a director in accordance with current corporate governance guidelines on directors over 70 years old.

Special business

To consider and, if thought fit, pass the following resolutions which will be proposed in the case of Resolutions 7 and 8 as ordinary resolutions and in the case of Resolution 9 as a special resolution:

7. TO approve the directors' remuneration report in accordance with section 241A of the Companies Act 1985.
8. THAT in substitution for all existing authorities the authority conferred on the directors by article 4(B) of the company's articles of association be renewed for the period expiring 15 months after the date of the passing of this resolution and for that period the "section 80 amount" is £1,029,161.
9. THAT subject to the passing of Resolution 7, the power conferred on the directors by article 4(C) of the company's articles of association be renewed for the period expiring 15 months after the date of the passing of this resolution and for that period the "section 89 amount" is £298,542.

BY ORDER OF THE BOARD

N Berry
SECRETARY

18 February 2003

NOTES

1. A member entitled to attend and vote at the meeting is also entitled to appoint one or more proxies to attend and, on a poll, vote instead of him. The proxy need not be a member of the company.
2. To be effective, the instrument appointing a proxy and any authority under which it is executed (or a notorially certified copy of such authority) must be deposited at the office of the company's registrars not less than 48 hours before the time for holding the meeting. A form of proxy is enclosed with this notice. Completion and return of the form of proxy will not preclude ordinary shareholders from attending and voting in person.
3. In accordance with Regulation 41 of the Uncertified Securities Regulations 2001, the company specifies that only those members entered on the register of members of the company as at 10.30am on 13 April 2003 (or in the event the meeting is adjourned, on the register of members 48 hours before the time of any adjourned meeting) shall be entitled to attend or vote at the meeting in respect of the number of shares registered in their name at that time. Changes to entries on the register of members after 10.30am on 13 April 2003 (or in the event the meeting is adjourned, on the register of members less than 48 hours before the time of any adjourned meeting) shall be disregarded in determining the rights of any person to attend or vote at the meeting.
4. Copies of director's service agreements and the register of directors' interests kept by the company under section 325 of the Companies Act 1985 will be produced at the commencement of the meeting and remain open and accessible during the continuance of the meeting to any person attending the meeting.
5. Biographical details of all directors offering themselves for re-election are set out on page 10.

Company information and advisers

Registered Office

Science Park
Cambridge CB4 0XR

Secretary

Nigel Berry

Financial advisor and lead broker

WestLB Panmure Ltd
Woolgate Exchange
25 Basinghall Street
London
EC2V 5HA

Registered auditors

Deloitte & Touche
Cambridge

Solicitors

Clifford Chance
200 Aldersgate Street
London EC1A 4JJ

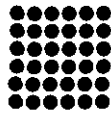
Bankers

Barclays Bank
15 Bene't Street
Cambridge CB2 3PZ

Registrars

Capita Registrars
Balfour House
390/398 High Road
Ilford
Essex IG1 1NQ

Registration Number: 3320972



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