XTEK LIMITED AND ITS CONTROLLED ENTITIES

ABN 90 103 629 107

HALF-YEAR FINANCIAL REPORT
APPENDIX 4D
31 DECEMBER 2005

CONTENTS

XTEK Limited Half Year Financial Report – 31 December 2005

Results for Announcement to the Market

Name of the Company: XTEK Limited
ABN 90 103 629 107

				December 2005 $
Revenue	up	26.1%	to	6,998,447
Loss from continuing operations before tax	down	N/A	to	(2,563,151)
Net loss attributable to members of parent	down	N/A	to	(1,895,808)

Dividends	Amount per security	Franked amount per security	Record date for determining entitlements to dividends
Current year – 2006:			
- Interim dividend	n/a	n/a	n/a
- Final dividend	n/a	n/a	n/a
Previous year – 2005:			
- Interim dividend	$0.01	100%	
- Final dividend	$0.02	100%	

Net tangible assets	December 2005	December 2004
Net tangible assets per security	$0.20	$0.22

For further explanation of the above figures please refer to the Directors' report and Management Discussion and Analysis. Other financial information required by the Appendix 4D is contained in the Financial Statements.

Management Discussion & Analysis

RESULTS REVIEW

	Half-Year ended 31 December 2005 $	Half-Year ended 31 December 2004 $
Revenue		
Agency operations - Australia	6,998,447	5,547,271
	6,998,447	5,547,271
Cost of Goods Sold	(5,353,694)	(3,532,276)
Gross Profit	1,644,753	2,014,995
Gross Profit %	24%	37%
Operating Costs		
Agency operations – Australia	(2,894,864)	(2,006,939)
Net foreign currency losses	(93,412)	-
Expenses incurred from operating as a listed entity	(360,000)	-
Expenses associated with listing	(555,188)	-
Research and Development Costs	(140,137)	-
United Kingdom Operations	(164,303)	-
	(4,207,904)	(2,006,939)
Net (loss) /profit before tax for the period	(2,563,151)	8,056
Income tax benefit	667,343	-
Net (loss) /profit for the period	(1,895,808)	8,056

RECENT DEVELOPMENTS

The Company has been active following its listing on 15 September 2005, through to 31 December 2005 and subsequent to balance date. The following are the key highlights;

Agency Sales

- XTEK has secured an exclusive distribution agreement with AeroVironment Inc. (www.aerovironment.com) against strong local competition. The Company will sell and technically support the leading brand of Small Unmanned Aerial Vehicles (SUAV) in the Pacific region. Sales will not be restricted to Homeland Security as there are significant prospects in other markets including Emergency Management.

- Upgrades of Explosive Ordnance Device (EOD) kits in excess of $1 million.

- Recent sales of specialist ammunition and weapons in the first half of 2006 with recurring sales forecast over the next three years.

- Appointed to the NSW Government Agency panel and the DFAT panel as a key Homeland Security supplier of risk management and consultancy services.

Management Discussion & Analysis (continued)

RECENT DEVELOPMENTS (continued)

Research & Development

- The purpose built XTEK Spectre Research Centre located in Adelaide became operational in early March 2006. The premise facilitates the commercialisation of innovative intellectual property acquired in September 2005.
- XTEK's leading new product, the Casualty Simulator ('CaSim'), is in the final stages of commercialisation and is expected to have a major impact on response planning for bomb incidents.
- A significant specialist weapon ancillary, generating immediate sales. The product has already attracted strong interest from a large international weapons manufacturer, including discussions involving its inclusion in a global weapons product catalogue.
- XTEK's Ballistic Plate Insert (BPI) is presently undergoing testing and certification procedures to comply with international standards. Initial discussions with Australian customers are encouraging.
- Armour piercing small arms ammunition is currently in the trial phase with the intention of selling the product under license to international ammunition manufacturers.

International Opportunities

- XTEK UK Limited has been developed into a fully operational sales and marketing organisation to market and distribute new products and services.

Investment Activities

- In February 2006, XTEK invested $1 million in QRSciences Limited ('QRS'). The investment enables direct access to QRS' current products, the ability to influence next generation products and establish a presence and sales outlet in the USA. The US office will be open for business within two months which will be essential for the sale of our own products. (XTEK, as distributor, has already interested potential customers and collaborators both in Australia and overseas).
- In March 2006, XTEK invested $250,000 in QeS Broadband Pty Ltd. The investment forms the cornerstone of a strategic commercial relationship with the small wireless internet service provider to provide mobile and deployable surveillance systems.

Management Discussion & Analysis (continued)

Divisional Commentary

Agency Sales

Overview

XTEK offers an extensive range of bomb search and render safe equipment including bomb disposal robots, exploders, detectors and disrupters and other specialist equipment.

The Company is the main provider of essential equipment used by the Australian and New Zealand police forensic markets and products supplied include digital imaging systems and gunshot residue kits.

XTEK's Technical Services Division specialised facility is equipped and staffed to cater for Defence and Homeland Security equipment manufacturing, repair and services needs.

Results

Revenue

- First half revenue performance highlights the Company's revenue seasonality.
- A large proportion of XTEK's sales are negotiated centrally with the Federal Government and subject to the normal distribution of government expenditure which is disproportionately skewed to the June quarter of each financial year.
- First tranche of tEODor large robots delivered on schedule in November 2005, sales of traditional EOD and general security equipment consistent with previous years.
- Two anticipated first half sales deferred. One tEODor large robot re-scheduled to June 2006 and the Cyclops small robot contract for approximately \$3.6 million delayed while Department of Defence reviews functional requirements in light of recent operational experiences in combat areas.

Cost of goods sold

- Lower gross margin compared to half-year ended 31 December 2004, due to the tEODor large robot \$14 million contract. A reduced margin was negotiated by Department of Defence due to the volume of robots purchased and work in progress directly related to product enhancements expensed.
- Offset by higher gross margins from enduring stream of support, maintenance and upgrades valued at over \$1 million per year over the ten year life of the robots.

Operational costs

- Payroll and related costs increased by \$1.351 million compared to the half-year ended 31 December 2004. The increase includes the following expenses specifically related to the half-year ended 31 December 2005.

Share based payment transactions	\$271,289
Shares issued to employees for no consideration	\$180,000
Employee leave provisions	\$103,899

Management Discussion & Analysis (continued)

Divisional Commentary (continued)

Agency Sales (continued)

- Staff levels increased by 30% compared to the half-year ended 31 December 2004, to support the significant growth in sales and new company reporting requirements and business processes required to support products supplied to Defence and Law Enforcement agencies.

- Expenses, including consulting and travel, specifically related to the Company's ASX listing and reporting requirements includes share registry, public relations, corporate advisory services and associated travel costs totaling $360,000.

- Foreign currency losses were incurred in relation to the holding of an Euro account for the purchase of tEODor large robots.

- Travel increase reflects costs to establish UK operations and acquire servicing expertise in relation to the tEODor large robot.

Research and Development (IP Commercialisation)

Overview

In September 2005, XTEK completed the purchase of intellectual property from Spectre Ballistic Solutions Pty Limited ('Spectre'). Spectre is owned by Dr Alex Krstic, a recognized expert in ballistics technology, who has entered into an employment contract with the Company to develop innovative products.

Results

Operating costs for the half-year ended 31 December 2005 comprised:

- Spectre Research Centre staff salaries and overheads.

Overview

XTEK UK continues to seek new agency agreements and prepare for the sales and distribution of commercialised IP.

Agency sales to date have been restricted by the UK Ministry of Defence (MOD) moratorium on defence expenditure until the end of the UK financial year.

Results

- Sales severely restricted by the UK Ministry of Defence (MOD) moratorium on expenditure until the end of the UK financial year 31 March 2006

Management Discussion & Analysis (continued)

Balance Sheet Commentary

Receivables / Payables

- The reduction in receivables and payables is due to the seasonality of revenue where traditionally second half sales and associated purchases and debtors are stronger as a consequence of XTEK's customer base.

Other assets

- Increase in other assets reflects deposits paid for the import tEODor large robots to be sold in the second half of the financial year.

Property, plant and equipment

- Principally, the fit out of the Adelaide R&D facility, $750,000.

Intangible assets

- Acquisition of intellectual property $2,100,000.
- Goodwill on acquisition of XTEK UK Limited $320,000.

Interest bearing liabilities

- Reflects financing of R&D equipment.

Provisions

- Reduction reflects 2004 – 2005 income tax and dividends paid in the first half of the financial year.

Directors' Report

Your directors submit their report for the half- year ended 31 December 2005.

Directors

The names of the company's directors in office during the half-year ended 31 December 2005 and until the date of this report are as below. Directors were in office for this entire period unless otherwise stated.

Brig. J. Wallace (Retd.) AM	Chairman and Director (appointed 28 July 2005)
N. French	Director and Chief Executive Officer
T. Vertes	Director (appointed 15 July 2005)
R. Dawson	Director (appointed 15 July 2005)
N. Weber	Director (resigned 21 July 2005)
R. Butcher	Director (resigned 21 July 2005)

Review and Results of Operations

A review of XTEK's operations and the results of those operations are contained in both the attached Management Discussion and Analysis and the Financial Statements which both form part of this Half-Year Financial Report.

Auditor's Independence Declaration

We have obtained an independence declaration from our auditors, Ernst & Young. The signed declaration is included on the following page.

Signed in accordance with a resolution of the directors.

Nigel French
Director
Canberra
10th March, 2006

ERNST & YOUNG

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Auditor's Independence Declaration to the Directors of XTEK Limited and its controlled entities

In relation to our review of the financial report of XTEK Limited for the half-year ended 31 December 2005, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the *Corporations Act 2001* or any applicable code of professional conduct.

Ernst & Young

James Palmer
Partner
Canberra
10 March 2006

Condensed Income Statement
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

	Notes	*CONSOLIDATED*	
		2005	*2004*
		$	*$*
Revenue	2	6,998,447	5,547,271
Cost of Sales		(5,353,694)	(3,532,276)
Gross profit		1,644,753	2,014,995
Other expenses	2	(4,207,904)	(2,006,939)
(Loss)/profit from continuing operations before tax		(2,563,151)	8,056
Income tax benefit / (expense)		667,343	-
(Loss)/profit after tax from continuing operations		(1,895,808)	8,056
Net (loss)/profit attributable to members of parent		(1,895,808)	8,056
Earnings per share (cents per share)			
- basic for the half-year		(0.06)	0.00
- diluted for the half-year		(0.06)	0.00
- dividends paid per share	3	-	0.01

Condensed Balance Sheet
AS AT 31 DECEMBER 2005

	Notes	CONSOLIDATED As at 31 December 2005 $	As at 30 June 2005 $
ASSETS			
Current Assets			
Cash and cash equivalents		1,547,276	576,430
Trade and other receivables		2,332,046	3,566,063
Inventories		3,663,087	3,268,335
Other		883,708	378,572
Total Current Assets		8,426,117	7,789,400
Non-current Assets			
Receivables		-	241,600
Property, plant and equipment		2,021,654	1,022,084
Deferred tax assets		1,460,498	208,808
Intangible assets		2,732,178	315,083
Total Non-current Assets		6,214,330	1,787,575
TOTAL ASSETS		14,640,447	9,576,975
LIABILITIES			
Current Liabilities			
Trade and other payables		1,335,132	3,366,205
Interest-bearing loans and borrowings		140,164	8,441
Accrued liabilities		360,780	83,157
Provisions		397,693	773,728
Total Current Liabilities		2,233,769	4,231,531
Non-current Liabilities			
Interest-bearing loans and borrowings		221,433	72,988
Other liabilities		-	33,348
Provisions		153,251	428,510
Total Non-current Liabilities		374,684	534,846
TOTAL LIABILITIES		2,608,453	4,766,377
NET ASSETS		12,031,994	4,810,598
EQUITY			
Issued capital	4	11,354,354	2,492,212
Retained earnings		422,577	2,318,386
Other reserves		255,063	-
TOTAL EQUITY		12,031,994	4,810,598

Condensed Cash Flow Statement

FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

	Notes	*CONSOLIDATED* 2005 $	2004 $
Cash flows used in operating activities			
Receipts from customers		8,974,133	8,311,083
Payments to suppliers and employees		(12,518,694)	(8,794,836)
Interest received		74,160	-
Borrowing costs		(24,552)	(22,620)
Income tax paid		(455,293)	(455,293)
Net cash flows used in operating activities		(3,950,246)	(961,666)
Cash flows used in investing activities			
Proceeds from sale of property, plant and equipment		5,965	-
Purchase of property, plant and equipment		(745,245)	(186,459)
Advances to related parties		-	(41,096)
Purchase of intellectual property		(2,096,771)	(212,077)
Acquisition of subsidiary, net of cash acquired		49,316	-
Net cash flows used in investing activities		(2,786,735)	(439,632)
Cash flows from financing activities			
Proceeds from issues of ordinary shares		12,147,794	2,362,079
Repayments of borrowings		(75,155)	(776,428)
Payment of dividends on ordinary shares		(300,000)	(200,000)
Buyback of equity holder shares		(3,800,000)	-
Transfer of founder shares to public		(250,000)	-
Net cash flows from financing activities		7,722,639	1,385,651
Net increase/(decrease) in cash and cash equivalents		985,658	(15,647)
Net foreign exchange difference		(14,812)	-
Cash and cash equivalents at beginning of period		576,430	828,225
Cash and cash equivalents at end of period	9	1,547,276	812,578

Condensed Statement of Changes in Equity
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

CONSOLIDATED	Attributable to equity holders of the parent				
	Issued Capital $	Equity-based payments reserve $	Foreign currency translation reserve $	Retained earnings $	Total equity $
At 1 July 2004	100	-	-	1,069,203	1,069,303
Profit for the half-year	-	-	-	8,056	8,056
Issues of ordinary shares during the half-year:					
Issue of share capital	3,000,000	-	-	-	3,000,000
Transaction costs associated with issue of share capital	(637,921)				(637,921)
Equity dividends	-	-	-	(500,000)	(500,000)
At 31 December 2004	2,362,179	-	-	577,259	2,939,438
At 1 July 2005	2,492,212	-	-	2,318,386	4,810,598
Currency translation differences	-	-	(16,227)	-	(16,227)
Loss for the half year	-	-	-	(1,895,808)	(1,895,808)
Issues of ordinary shares during the half-year:					
Issue of share capital	14,000,000	-	-	-	14,000,000
Transaction costs associated with issue of share capital	(1,852,206)				(1,852,206)
Recognition of deferred tax asset on IPO costs recognised in equity	584,348	-	-	-	584,348
Existing (founder) shares offered to public in prospectus	(250,000)	-	-	-	(250,000)
Share buy back	(3,800,000)	-	-	-	(3,800,000)
For no consideration:					
Shares to employees	180,000	-	-	-	180,000
Cost of share based-payments	-	271,289	-	-	271,289
At 31 December 2005	11,354,354	271,289	(16,227)	422,578	12,031,994

Notes to the Half-Year Financial Statements

FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT

This half-year financial report does not include all notes normally included within the annual financial report and therefore cannot be expected to provide as full an understanding of the financial performance, financial position and financing and investing activities of the consolidated entity as the full financial report. This half-year financial report should be read in conjunction with the annual Financial Report of XTEK Limited as at 30 June 2005, which was prepared based on Australian Accounting Standards applicable before 1 January 2005 ('AGAAP'), together with any public announcements made by XTEK Limited (XTEK) and its controlled entities during the half-year ended 31 December 2005 in accordance with the continuous disclosure obligations arising under the *Corporations Act 2001*.

(a) Basis of accounting

The half-year financial report is a general purpose financial report, which has been prepared in accordance with the requirements of the *Corporations Act 2001*, applicable Accounting Standards including AASB 134, "Interim Financial Reporting" and other mandatory professional reporting requirements.

The half-year financial report has been prepared on a historical cost basis, except employee share-based compensation transactions which have been measured at fair value.

For the purpose of preparing the half-year financial report, the half-year has been treated as a discrete reporting period.

(b) Statement of compliance

The half-year report complies with Australian Accounting Standards, which include Australian equivalents to International Financial Reporting Standards ('AIFRS'). Compliance with AIFRS ensures that the half-year financial report, comprising the financial statements and notes thereto, complies with International Financial Reporting Standards ('IFRS').

This is the first-half-year financial report prepared based on AIFRS and comparatives for the half-year ended 31 December 2004 and full-year ended 30 June 2005 have been restated accordingly. A summary of the significant accounting policies of the Group under AIFRS are disclosed in Note 1(c) below.

(c) Summary of significant account policies

(i) Basis of consolidation

The consolidated financial statements comprise the financial statements of XTEK Limited and its subsidiaries ('the Group'). The financial statements of subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies.

Adjustments are made to bring into line any dissimilar accounting policies that may exist.

All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full. Unrealised losses are eliminated unless costs cannot be recovered. XTEK UK Limited has been included in the consolidated financial statements using the purchase method of accounting, which measures the acquiree's assets and liabilities at fair value at acquisition date. Accordingly, the consolidated financial statements include the results of XTEK UK Limited for the three month period from its acquisition on 30 September 2005. The purchase consideration has been allocated to the assets and liabilities on the basis of fair value at the date of acquisition.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(c) Summary of significant account policies (continued)

(ii) Foreign currency translation

Both the functional and presentation currency of XTEK Limited and its Australian subsidiaries is Australian dollars (A$).

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date.

All differences in the consolidated financial report are taken to the income statement with the exception of differences on foreign currency borrowings that provide a hedge against a net investment in a foreign entity. These are taken directly to equity until the disposal of the net investment, at which time they are recognised in the income statement.

Tax charges and credits attributable to exchange differences on those borrowings are also recognised in equity. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The functional currency of the overseas subsidiary (XTEK UK Limited) is English Pounds Sterling.

As at the reporting date the assets and liabilities of the overseas subsidiary are translated into the presentation currency of XTEK Limited at the rate of exchange ruling at the balance sheet date and the income statements are translated at the weighted average rates for the period. The exchange differences arising on the retranslation are taken directly to a separate component of equity.

(iii) Property, plant and equipment

Cost and Valuation
Property, plant & equipment are stated at cost less accumulated depreciation and any impairment value.

Depreciation
Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

	2005	**2004**
Plant and equipment	3 to 15 years	3 to 15 years
Plant and equipment under lease	Over 3 to 4 years	Over 3 to 4 years

Impairment
The carrying values of plant and equipment are reviewed for impairment when events or changes in the circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable amount. The recoverable amount of plant and equipment is the greater of fair value less costs to sell and value in use.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(c) Summary of significant account policies (continued)

(iv) Borrowing Costs

Borrowing costs are recognised as an expense when incurred.

(v) Goodwill

Goodwill on acquisition is initially measured at cost being the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is not amortised. Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

As at the acquisition date, any goodwill acquired is allocated to each of the cash-generating units expected to benefit from the combination's synergies. Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit retained.

(vi) Intangibles

Intellectual Property
Intellectual property acquired separately is capitalised at cost and from a business combination is capitalised at fair value as at the date of acquisition. Following initial recognition, the cost model is applied. The useful lives of intellectual property are assessed to be either finite or infinite. Where amortisation is charged on assets with finite lives, the expense is taken to the income statement. Intangible assets, excluding development costs, created within the business are not capitalised and expenditure is charged against profits in the period in which the expenditure is incurred.

Intangible assets are tested for impairment where an indicator of impairment exists, and in the case of indefinite lived intangibles annually, either individually or at the cash generating unit level. Useful lives are also examined on an annual basis and adjustments, where applicable, are made on a prospective basis.

Research and development costs
Research costs are expensed as incurred.

Development expenditure incurred on an individual project is carried forward when its future recoverability can reasonably be regarded as assured. Following the initial recognition of the development expenditure, the cost model is applied requiring the asset to be carried at cost less any accumulated amortisation and accumulated impairment losses. Any expenditure carried forward is amortised over the period of expected future sales from the related project.

The carrying value of development costs is reviewed for impairment annually when the asset is not yet in use, or more frequently when an indicator of impairment arises during the reporting year indicating that the carrying value may not be recoverable. Where recognition criteria are not met development costs are recognised in the income statement as incurred.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(c) Summary of significant account policies (continued)

(vi) Intangibles (continued)

A summary of the policies applied to the Group's intangible assets is as follows;

	Intellectual Property	*Development Costs*
Useful lives	Finite	Finite
Method used	5 years – Straight line or revalued	5 years – Straight line
Internally generated / Acquired	Acquired	Internally generated
Impairment test / Recoverable amount testing	Annually and where an indicator of impairment exists	Amortisation method reviewed at each financial year-end; Reviewed annually for indicator of impairment

Gains or losses from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement when the asset is derecognised.

(vii) Recoverable amount of assets

At each reporting date, the Group assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, the Group makes a formal estimate of recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount the asset is considered impaired and is written down to its recoverable amount.

Recoverable amount is the greater of fair value less costs to sell and value in use. It is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs to sell and it does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

(viii) Inventories

Inventories are valued at the lower of cost and net realisable value. Costs incurred in bringing each product to its present location and condition are accounted for as follows:

Raw materials – purchase cost on a first-in, first-out basis; and
Finished goods and work-in-progress – cost of direct materials and labour and a proportion of manufacturing overheads based on normal operating capacity but excluding borrowing costs.

Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(c) Summary of significant account policies (continued)

(ix) Trade and other receivables

Trade receivables are recognised and carried at original invoice amount less a provision for any uncollectible amounts. Receivables are non-interest bearing and are generally on 30 day terms, unless otherwise agreed with the customer. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off as incurred.

Receivables from related parties are recognised and carried at amortised cost, with interest recognised using the effective interest rate method.

(x) Cash and cash equivalents

Cash and short-term deposits in the balance sheet comprise cash at bank and in hand and short-term deposits with an original maturity of three months or less. For the purposes of the Cash Flow Statement, cash and cash equivalents consist of cash and equivalents as defined above, net of outstanding bank overdrafts.

(xi) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Where the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement.

If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and , where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time, is recognised as a finance cost.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(c) Summary of significant account policies (continued)

(xii) Share-based payment transactions

The Group provides benefits to employees (including directors) of the Group in the form of share-based payment transactions, whereby employees render services in exchange for shares or rights over shares ('equity-settled transactions').

There are currently two plans in place to provide these benefits;

i. the Senior Executive Share Ownership Plan (SESOP), which provides benefits to senior executives; and
ii. the Employee Share Ownership Plan (ESOP), which provides benefits to all employees, excluding senior executives.

The cost of these equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. The fair value is determined by reference to the Black Scholes valuation model.

In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of XTEK Limited ('market conditions'). The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ('vesting date').

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflects:
(i) the extent to which the vesting period has expired; and
(ii) the number of awards that, in the opinion of the directors will ultimately vest.

This opinion is formed based on the best available information at balance date. No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition. Where the terms of an award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification as measured at the date of modification.

The dilutive effect, if any, of outstanding options is reflected as additional share dilution in the computation of earnings per share.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(c) Summary of significant account policies (continued)

(xiii) Leases

Leases are classified at their inception as either operating or finance leases based on the economic substance of the agreement so as to reflect the risks and benefits incidental to ownership.

Finance Leases
Leases which effectively transfer substantially all the risks and benefits incidental to ownership of the leased item to the Group are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments and disclosed as property, plant and equipment under lease. A lease liability of equal value is also recognised.

Capitalised lease assets are depreciated over the shorter of the estimated useful life of the assets and the lease term. Minimum lease payments are allocated between interest expense and reduction of the lease liability with the interest expense calculated using the interest rate implicit in the lease and charged directly to the Income Statement.

Operating Leases
The minimum lease payments of operating leases, where the lessor effectively retains substantially all of the risks and benefits of ownership of the leased item, are recognised as an expense on a straight-line basis over the lease term.

(xiv) Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the entity and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Sale of Goods
Control of the goods has passed to the buyer.

Rendering of Services
Revenue is recognised to the extent that costs have been incurred.

Interest
Control of a right to receive consideration for the provision of, or investment in, assets has been attained.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(c) Summary of significant account policies (continued)

(xv) Taxes

Deferred income tax is provided on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting processes.

Deferred income tax liabilities are recognised for all taxable differences:
- except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax assets and unused tax losses can be utilised:
- except where the deferred income tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each balance date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow or part of the deferred income tax asset to be utilised.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantially enacted at the balance sheet date.

Income taxes relating to items recognised directly in equity are recognised in equity and not in the income statement.

(xvi) Other taxes

Revenues, expenses and assets are recognised net of the amount of GST except:
- where the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the balance sheet.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(c) Summary of significant account policies (continued)

(xvi) Other taxes (continued)

Cash flows are included in the Cash Flow Statement on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority are classified as operating cash flows.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(xvii) Employee benefits

Provision is made for employee benefits accumulated as a result of employees rendering services up to the reporting date. These benefits include wages and salaries, annual leave, long service leave and sick leave.

Liabilities arising in respect of wages and salaries, annual leave, sick leave and any other employee benefits expected to be settled within twelve months of the reporting date are measured at their nominal amounts based on remuneration rates which are expected to be paid when the liability is settled. All other employee benefit liabilities are measured at the present value of the estimated future cash outflow to be made in respect of services provided by employees up to the reporting date. In determining the present value of future cash outflows, the market yield as at the reporting date on national government bonds, which have terms to maturity approximating the terms of the related liability, are used.

Employee benefit expenses and revenues arising in respect of the following categories:

- wages and salaries, non-monetary benefits, annual leave, long service leave and other leave entitlements; and
- other types of employee entitlements, are charged against surpluses on a net basis in their respective categories.

(xviii) Earnings per share (EPS)

Basic EPS is calculated as net profit attributable to members, adjusted to exclude costs of servicing equity (other then dividends) and preference share dividends, divided by the weighted average number of ordinary shares, adjusted for any bonus element.

Diluted EPS is calculated as net profit attributable to members, adjusted for:

- costs of servicing equity (other than dividends) and preference share dividends;
- the after tax effect of dividends and interest associated with dilutive potential ordinary shares that have been recognised as expenses; and
- other non-discretionary charges in revenues or expenses during the period that would result from the dilution of potential ordinary shares;

divided by the weighted average number of ordinary shares and dilutive potential ordinary shares, adjusted for any bonus element.

(xiv) Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at cost, being the fair value of the consideration received net of issue costs associated with the borrowing. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement. Gains and losses are recognised in the income statement when the liabilities are derecognised and as well as through the amortisation process.

Notes to the Half-Year Financial Statements

FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(d) AASB 1 Transitional exemptions

The Group has made its election in relation to the transitional exemptions allowed by *AASB 1:"First-time Adoption of Australian Equivalents to International Financial Reporting Standards"* as follows:

Business combinations
AASB 3 *Business Combinations"* was not applied retrospectively to past business combination (i.e. business combinations that occurred before the date of transition to AIFRS).

Designation of previously recognised financial instruments
Financial instruments were designated as financial assets or liabilities at fair value through profit or loss (held for trading) or as available-for-sale at the date of transition to AIFRS.

Share--based payment transactions
AASB 2 *"Share-Based Payments'* is applied only to equity instruments granted after 7 November 2002 that had not vested on or before 1 January 2005.

(e) Impact of adoption of AIFRS

The impacts of adopting AIFRS on the total equity and profit after tax as reported under Australian Accounting Standards applicable before 1 January 2005 ('AGAAP') are illustrated below.

(i) Reconciliation of total equity as presented under AGAAP to that under AIFRS

	CONSOLIDATED	
	30 June 05 $	01 July 04 $
Total equity under AGAAP	2,362,179	100
Adjustments to equity:		
Application of AASB 112 (A)	130,033	-
Total equity under AIFRS	2,492,212	100

(A) Application of AASB 112 to capitalised costs relating to equity raising giving rise to a deferred tax asset, not previously accounted for under AASB 1020 requirements.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

1. BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT (continued)

(e) Impact of adoption of AIFRS (continued)

(ii) Reconciliation of profit after tax under AGAAP to that under AIFRS

	CONSOLIDATED	
	Year ended 30 June 05 $	Half–Year ended 31 December 04 $
Profit after tax previously reported	1,749,183	8,056
AIFRS adjustments	-	-
Profit after tax under AIFRS	1,749,183	8,056

(iii) Explanation of material adjustments to the cash flow statements

There are no material differences between the cash flow statements presented under AIFRS and those presented under AGAAP.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

2. REVENUE AND EXPENSES

	CONSOLIDATED	
	2005	2004
	$	$
(a) Specific Items		
(Loss)/profit before income tax expense includes the following revenues and expenses whose disclosure is relevant in explaining the performance of the entity:		
(i) Revenue		
Sale of goods	6,626,899	5,030,077
Repairs	168,696	212,669
Services	95,204	216,786
Interest	74,160	-
Hire and rent of equipment	33,488	87,739
	6,998,447	5,547,271
(ii) Other expenses		
Depreciation and amortisation	151,169	41,680
Employee benefits and related costs	1,968,939	1,069,332
Borrowing costs expense	24,552	22,620
Accountancy fees	26,995	25,875
Advertising and conferences	74,829	69,358
Audit fees	42,750	18,917
Bank charges	22,635	9,375
Consultancy fees	208,337	71,635
Insurance	108,234	72,351
Lease charges	124,102	76,046
Net foreign currency losses	93,412	-
Office administrative costs	331,495	257,805
Share based payments	451,289	-
Travel and related costs	417,472	212,301
Other expenses	161,694	59,644
	4,207,904	2,006,939

(b) Seasonality of Operations

Due to the nature of contracts held with the Department of Defence, the majority of the revenue and profits for the financial year will be reflected in the results of the second half of the financial year.

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

3. DIVIDENDS PAID OR PROPOSED

	CONSOLIDATED	
	2005	2004
	$	$
Equity dividends on ordinary shares:		
(a) Dividends paid during the half-year		
Final franked dividend for financial year 30 June 2005: 2 cents (2004: nil)	300,000	200,000
(b) Dividends proposed and not recognised as a liability		
Interim franked dividends for financial year 30 June 2006: nil (2005: nil)	-	-
	300,000	200,000

4. ISSUED CAPITAL

	December 05	June 05
	$	$
Ordinary shares		
Issued and fully paid	11,354,354	2,492,212

	Number of shares	$
Movements in ordinary shares on issue		
Beginning of the financial year		
At 1 July 2005	15,237	2,492,212
Share split (i)	19,488,123	-
Issue of share capital	27,500,000	12,147,794
AASB 112 implications relating to IPO costs	-	584,348
Existing (founder) shares offered to public in prospectus	-	(250,000)
Share buy back (ii)	(6,831,360)	(3,800,000)
Shares to employees for no consideration	360,000	180,000
At 31 December 2005	40,532,000	11,354,354

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

4. ISSUED CAPITAL (continued)

(i) On 28 July 2005, the Company's issued capital of 15,237 ordinary shares was converted into 19,503,360 by means of a share split, the conversion being a split of each ordinary share on issue into 1,280 ordinary shares.

(ii) Ramico was the holder of 6,831,360 shares representing a 35% interest in the Company. Ramico decided not to participate in the proposed offer of shares pursuant to the prospectus and entered into a Share Buy-Back Agreement with the Company on 21 July 2005. Upon successful completion of the initial public offering the Company paid Ramico a fixed sum of $3,800,000 and the shares held by Ramico were cancelled.

5. GEOGRAPHICAL SEGMENTS

The following table presents the revenue and profit information regarding geographical segments for the half-year periods 31 December 2005 and 31 December 2004.

	Australia $	United Kingdom $	Total $
31 December 2005			
Segment revenue	6,998,447	-	6,998,447
Segment result	(2,399,217)	(163,934)	(2,563,151)
31 December 2004			
Segment revenue	5,547,271	-	5,547,271
Segment result	8,056	-	8,056

Notes to the Half-Year Financial Statements
FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

6. CHANGE IN COMPOSITION OF ENTITY

Acquisition of XTEK UK Limited

On 30 September 2005, XTEK Limited acquired 100% of the voting shares of XTEK UK Limited, an unlisted company based in the United Kingdom for nil consideration. The shares were previously held by Mr Nigel French who holds the position as Director and Chief Executive Officer of XTEK Limited. From the date of acquisition, XTEK UK Limited has contributed $163,934 to the net loss of the Group. If the combination had taken place at the beginning of the year, the loss for the Group would have been $242,270 with no change to revenue from continuing operations.

The fair value of the identifiable assets and liabilities of XTEK UK Limited as at the date of acquisition are:

	CONSOLIDATED	
	Recognised on acquisition	Carrying value
	$	$
Other debtors	5,013	5,013
Stock	5,958	5,958
Current account	13,499	13,499
Deposit account	35,817	35,817
	60,287	60,287
Trade creditors	(2,706)	(2,706)
Other tax & social security	(12,240)	(12,240)
Other creditors	(2,605)	(2,605)
Accruals & deferred income	(2,088)	(2,088)
Loan from XTEK Limited	(360,973)	(360,973)
	(380,611)	(380,611)
Fair value of net liabilities	(320,324)	(320,324)
Goodwill arising on acquisition	320,324	
	-	
Total consideration	-	
The cash outflow on acquisition is as follows:		
Net cash acquired with subsidiary	49,316	
Cash paid	-	
Net cash inflow	49,316	

Included in the $320,324 of goodwill recognised above are certain intangible assets that cannot be individually separated and reliably measured from the acquiree due to their nature. Assets included in this balance consist of key personnel and strategic alliances.

7. CONTINGENT ASSETS AND LIABILITIES

Since the last annual reporting date, there has been no material change of any contingent liabilities or contingent assets.

Notes to the Half-Year Financial Statements

FOR THE HALF-YEAR ENDED 31 DECEMBER 2005

8. EVENTS AFTER THE BALANCE SHEET DATE

(ii) Convertible Notes

On 21 February 2006, XTEK Limited announced the issuance of 3,636,364 Convertible Notes. The notes have a five year term and were issued at a face value of $0.55 per note, with total proceeds raised of $2,000,000. Interest is payable six monthly in arrears at a nominal interest rate of 10%. Each note is convertible at any time up to maturity into one ordinary share. XTEK has calculated the liability component of the issue to be $1,926,082 and the equity component to be $73,918.

The balance of the notes proposed to be issued to raise a further $3 million (a total of $5 million), will have an issue price per note which is a ten percent (10%) premium to the volume weighted average trading price of the Company's ordinary shares as recorded by the Australian Stock Exchange (ASX) on the ten trading days after the announcement of the Company's half year results to 31 December 2005, with a ceiling price of 55 cents. If the issue price so calculated is less than 55 cents, the notes previously issued shall be cancelled and replaced with the number of notes which would have been issued had the lower price applied. All notes will have a term with a common expiry date of 17 February 2011.

The Company will seek shareholder approval to issue notes where the issue would exceed fifteen percent (15%) of the Company's issued ordinary shares. The precise number of notes for which shareholder approval will be sought will be determined when the price of the notes calculated after the release of the Company's half year results to 31 December 2005.

The funds raised by the issue of the notes will be used to finance further expansion as foreshadowed at the time of listing last year, and further information about the expansion projects will be announced in the near future.

(iii) Investment in QRSciences Holdings Limited

On 10 February 2006, XTEK subscribed for 12,500,000 shares at 8 cents each for a total consideration of $1,000,000 in QRSciences Holdings Limited, a technology-based company involved in the commercial development of physical sciences research and development with a primary focus on Quadrupole Resonance (QR) technology.

9. ADDITIONAL INFORMATION

Reconciliation of Cash

For the purposes of the Condensed Cash Flow Statement, cash and cash equivalent comprise the following at 31 December:

	CONSOLIDATED	
	2005	2004
	$	$
Cash at bank and in hand	1,547,276	812,578

Directors' Declaration

In accordance with a resolution of the directors of XTEK Limited, I state that:

In the opinion of the directors:

(a) the financial statements and notes of the consolidated entity:

i. give a true and fair view of the financial position as at 31 December 2005 and the performance for the half-year ended on that date of the consolidated entity; and

ii. comply with Accounting Standard AASB 134 "Interim Financial Reporting" and the Corporations Regulations 2001; and

(b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

On behalf of the Board

Nigel French
Director
Canberra
10th March, 2006

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Independent Review Report

To the members of XTEK Limited

Scope

The financial report and directors' responsibility

The financial report comprises the balance sheet, income statement, cash flow statement, statement of changes in equity and accompanying notes to the financial statements for the consolidated entity comprising both XTEK Limited (the company) and the entities it controlled during the half-year, and the directors' declaration for the company, for the period ended 31 December 2005.

The directors of the company are responsible for preparing a financial report that gives a true and fair view of the financial position and performance of the consolidated entity, and that complies with Accounting Standard AASB 134 "Interim Financial Reporting", in accordance with the *Corporations Act 2001*. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

Review approach

We conducted an independent review of the financial report in order to make a statement about it to the members of the company, and in order for the company to lodge the financial report with the Australian Stock Exchange and the Australian Securities and Investments Commission.

Our review was conducted in accordance with Australian Auditing Standards applicable to review engagements, in order to state whether, on the basis of the procedures described, anything has come to our attention that would indicate that the financial report is not presented fairly in accordance with the *Corporations Act 2001*, Accounting Standard AASB 134 "Interim Financial Reporting" and other mandatory financial reporting requirements in Australia, so as to present a view which is consistent with our understanding of the consolidated entity's financial position, and of its performance as represented by the results of its operations and cash flows.

A review is limited primarily to inquiries of company personnel and analytical procedures applied to the financial data. These procedures do not provide all the evidence that would be required in an audit, thus the level of assurance is less than given in an audit. We have not performed an audit and, accordingly, we do not express an audit opinion.

Independence

We are independent of the company, and have met the independence requirements of Australian professional ethical pronouncements and the *Corporations Act 2001*. We have given to the directors of the company a written Auditor's Independence Declaration, a copy of which is included in the Directors' Report.

Statement
Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the financial report of the consolidated entity, comprising XTEK Limited and the entities it controlled during the half-year is not in accordance with:

(a) the *Corporations Act 2001*, including:

(i) giving a true and fair view of the financial position of the consolidated entity at 31 December 2005 and of its performance for the half-year ended on that date; and
(ii) complying with Accounting Standard AASB 134 "Interim Financial Reporting" and the Corporations Regulations 2001; and

(b) other mandatory financial reporting requirements in Australia.

Ernst & Young

Ernst & Young

James Palmer

James Palmer
Partner
Canberra
10 March 2006