

Filtronic plc
Annual Report
2011



Inspired Wireless Solutions



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| | Continuing operations | |
|--|-----------------------|---------|
| | 2011 | 2010 |
| Revenue | £15.5m | £15.6m |
| Operating loss before amortisation and exceptional items | £(5.3)m | £(0.3)m |
| Operating loss | £(7.1)m | £(1.1)m |
| Loss before taxation | £(7.0)m | £(1.0)m |
| Basic and diluted loss per share | (7.19)p | (1.37)p |
| | Group | |
| | 2011 | 2010 |
| Loss for the period from continuing operations | £(6.7)m | £(1.0)m |
| Loss for the period from discontinued operations | £(0.3)m | – |
| Loss for the period | £(7.0)m | £(1.0)m |
| Basic and diluted loss per share | (7.48)p | (1.37)p |
| Final dividend per share | – | 1.00p |
| Cash | £4.1m | £16.2m |
| Total equity | £18.8m | £19.9m |



The year ended 31 May 2011 produced revenue of £15.5m and an operating loss before exceptional items and the amortisation of intangibles of £5.3m, compared with the prior year revenue of £15.6m and a £0.3m operating loss before exceptional items from continuing operations. Cash at the end of the year of £4.1m was down from last year's £16.2m following the November 2010 acquisition of the Isotek group. A full breakdown of the year is shown in the financial statements, notes and narrative which follow.

An annual dividend for 2009/10 of 1.00p (£0.7m) was paid to shareholders on 5 November 2010. In light of the higher operational losses, the Board has decided to recommend no annual dividend in respect of the financial year just ended.

In furtherance of our strategy to create a differentiated, high growth and higher margin wireless telecoms business, Isotek (Holdings) limited was acquired on 15 November 2010 for £4.2m cash plus £6.8m in Filtronic shares (18.55 million shares). The deal has delivered entry into the rapidly developing 3G/4G base station market sector by acquiring innovative intellectual property and a position on significant 3G/4G network upgrade programmes.

The Group operations now include two separately reported trading business segments; Broadband which has been transitioned from the traditional Point to Point backhaul (PTP) business segment and the acquired Isotek wireless Basestation business.

Broadband Business

Broadband saw a 22% decline in its revenues to £12.1m (2010 £15.6m), slightly better than projected in the latest communication to shareholders in April 2011. The segment loss before exceptional items was £2.5m (2010 £0.7m profit)

The second half performance was significantly impacted by a sharper than expected decline in sales of traditional products. The acquisition of a key customer (NERA) in January 2011 by Ceragon Networks resulted in a large reduction in its purchases of our short-haul radio products. There were, however, positive developments in Broadband strategy to broaden its addressable market with a new customer and product base, though the growth in sales revenue from these new activities did not fully compensate for the rapid reduction in Ceragon (NERA) sales. Cost reduction actions taken following the NERA acquisition at the start of 2011 with an annualised impact of £1.4m were delivering benefits by the financial year end.

Basestation Business

In the 28 week period since its acquisition in mid-November 2010, Isotek achieved sales revenues of £3.4m and incurred a loss of £2.0m. The revenue was short of the revised projection made to shareholders in April 2011 of revenue for the period of around £4m, though this still represented a significant step increase in revenue from the previous 24 week period of £1.2m. With the business still reliant on a very small number of early stage programmes, a couple of deferrals by end-customers in the US on significant LTE/4G programmes have had a considerable short-term impact on results.

Whilst the trading performance is disappointing, the group has continued to invest in engineering resource at Isotek to support these major programmes and to improve product margins on certain products for the forthcoming LTE/4G network rollouts, as well as expanding sales activity to address additional manifold opportunities for 3G and 4G mobile network upgrades.



Outlook

Action has been taken to reduce costs in the Broadband business where an appropriate headcount reduction has been implemented. Meanwhile the integration of the Isotek and Broadband businesses is being accelerated across the group, and specialist Broadband resources are being redeployed to maximise mobile base station product opportunities. In parallel, the company is expanding its business development activity on new opportunities for its innovative filtering products as operational capacity is scaled up.

The group has significantly increased its addressable market to circa \$600m estimated for 2012, with channels into Broadband, aerospace manufacturing and the larger base station market. The addressable base station market for Isotek filtering products comprises both major network equipment OEMs and a wide range of operators.

Explosive growth in mobile data is leading to a growing market for both new OEM 4G base station filters and operator network upgrade products to rapidly overlay new capacity onto existing infrastructure.

This growth is particularly evidenced in the US market by a series of network upgrade programs launched by leading operators.

The group is exploiting these opportunities with unique IP offering cost effective customised solutions with market leading spectrum efficiency and rapid time to market, enabling operators to maximise valuable assets.

The outlook is expanded upon in further detail in the Operating review.

Finally, I should like to thank all staff in the business for their contribution over the past year.

Howard Ford
Chairman
2 August 2011



Summary

Following the acquisition of Isotek in November 2010 the business comprised two trading segments during the second half of the financial year; Broadband and the new Basestation business. The group continues to execute its strategy to expand its addressable market through new product developments and customers. Actions have been taken to stabilise the Broadband business and Basestation sales growth is backed by significant opportunities in the rapidly developing 3G/4G base station market.

Operations

The Broadband business designs and manufactures customised microwave electronic sub assembly components that are integrated by OEM's into radios. These radios provide the backhaul links for telecom networks, particularly the mobile base station market. Filtronic is a leading merchant supplier of transceivers and duplex filters to this market.

The Basestation business develops and markets innovative filters and combiners, which enable operators to use their existing 2G infrastructure to also deliver 3G and 4G services simultaneously. Our products can bring significant cost savings as well as improving the use of available spectrum.

Broadband first half revenue (£7.1m) was up on the second half of the prior year (£6.0m) but following the January 2011 Ceragon acquisition of Nera there was a significant weakening of demand in the second half (revenue £5.0m). Whilst actions have been taken to reduce costs the benefits will not be derived until the next financial year, and an operating loss of £2.5m for the Broadband segment was reported for the year.

Basestation sales grew from £1.2m in the pre-acquisition 24 weeks to £3.4m in the post acquisition 28 weeks. However margins were tight prior to the delivery of production cost improvements possible on volume products, and a loss of £2.0m was reported for the period.

The group continues to invest in future product development, investing £3.5m in R&D during the year. This included continuing work supported by a research grant awarded by Yorkshire Forward with support from the European Regional Development Fund to assist in the development of a new product to target the emerging market for 4G mobile broadband services. This and other major programs are scheduled for completion by the end of 2011, leading to reduced costs in the second half of the coming financial year.

Operational cash outflows of £4.4m (primarily in the second half), were added to by acquisition related cash outflows of £5.8m, capex of £0.9m and dividends of £0.7m to explain the cash outflow of £12.1m in the year.

Overall revenue for the year of £15.5m, was similar to last years £15.6m, with an operating loss before exceptional items and intangible amortisation of £5.3m compared with a £0.3m loss in 2010.

Exceptional costs of £0.6m (2010 £0.8m) included acquisition related costs of £0.5m and redundancy costs incurred in the Broadband costs reduction program.

Broadband Business

There are more encouraging signs for the Broadband business at the start of FY2012. Though first half on first half comparisons will continue to be impacted by the Ceragon reductions and mature product phase-outs, there is now better forward visibility in both these areas, and activity has stabilised. The second half will start to benefit progressively from sales to the new customers of higher margin products as detailed below. The overall expectation is for FY2012 Broadband sales of just above £10m with broadly balanced halves.

As outlined in the statement to shareholders in April 2011, the growth in new programmes to a broader customer base will have an increasingly positive impact through FY2012. The business has secured initial production orders on Selex Galileo electronic radar programmes; production of the Multi-Chip Package semiconductor solutions for an OEM backhaul customer is ramping successfully; and initial customer orders for gigabit radio modules are being executed.



Meanwhile, the business has established a constructive working relationship with Ceragon that gives greater clarity about recovering levels of long-haul product demand over coming months. Actions to reduce costs earlier in 2011, combined with ongoing fixed cost reductions should result in an annualised benefit of some £2m by the second half of FY2012.

Basestation Business

There are indications that volume shipments should resume later this calendar year for the projects delayed in the final quarter, as these programmes are required to enable the relevant US carriers to address well documented capacity constraints.

There are encouraging signs deriving from the expansion of business development activity, particularly in the USA, where our US subsidiary Isotek Inc is now participating in a number of OEM programmes involving network operators AT&T, Verizon and most recently Sprint, who are engaged in adding LTE/4G overlay to meet the ever increasing demand for mobile data capacity. Although these programmes are as yet in early stage regional roll-out, OEM funding of our production for a number of these programmes underpins our volume production expectations for the next 6-12 months. Additionally, the sales initiative to address the US operator market has also begun to bear fruit, with demonstrations of filter or combiner products being planned with a total of five operators to address immediate capacity constraints.

As expected, the development of the LTE/4G market in Europe remains behind that of the USA due to regulatory licence timing. However, volume shipments of filter products to a major operator commenced in May, and will form the backbone of Isotek's European revenues in the first half of FY2012.

The challenge for Isotek during FY2012 is to convert the sharply increased level of customer enquiries for product sampling into a number of volume programmes. The business continues to budget for a significant step up in Isotek revenues to circa £15m for the year based on the increased customer activity together with current program insertions, though as previously stressed the revenues will be weighted towards the second half.

Employees

At 31 May 2011, the group employed 159 people (2010 139) including 51 in the Basestation business.

Hemant Mardia
Chief Executive Officer
2 August 2011



Results

The year ended 31 May 2011 generated revenue of £15.5m (2010 £15.6m), resulting in an operating loss before intangible amortisation, and exceptional items of £5.3m (2010 £0.3m loss from continuing operations). The group loss for the period from continuing operations was £6.7m (2010 £1.0m loss), reflecting a £1.2m amortisation of acquisition related intangibles as well as exceptional costs relating significantly to the acquisition. Revenue and operating results by segment (note 4) are the main key performance indicators used by the group. The operating results are discussed in the Chief Executive's Operating Review, along with a review of the business.

Exceptional Costs

In addition to £0.5m of costs related to the Isotek acquisition and subsequent integration, redundancy costs of £0.1m were also incurred in order to reduce the Broadband cost base.

Net finance income

The group ended the year with net cash of £4.1m (2010 £16.2m) and generated net finance income of £0.1m (2010 £0.1m), reflecting low interest rates on reduced cash deposits post the acquisition.

Taxation

No current tax is due on continuing operations, reflecting available losses. The £0.3m credit reported is a deferred tax liability release related to the intangible amortisation. It will not result in any tax refund.

Capital expenditure

Capital expenditure of £0.9m (2010 £0.6m) included £0.3m for the Isotek business.

Research and development costs

Research and development costs of £3.5m (2010 £2.3m), which represented 22.7% (2010 14.8%) of revenue were expensed. Offsetting these costs, Yorkshire Forward grant income of £0.3 (2010 £0.5m), was reported under other operating income. No research and development costs were capitalised in the balance sheet.

Working capital

At 31 May 2011 net working capital was £2.1m (2010 £2.5m). Net working capital comprised inventories of £1.7m (2010 £2.0m), receivables of £5.9m (2010 £3.4m) and payables of £5.5m (2010 £2.9m).

Cash flow

Cash outflow from operating activities was £4.4m (2010 £1.9m inflow), cash outflow from investing activities (including the acquisition) was £7.0m (2010 £1.2m outflow) and net cash outflow from financing activities was £0.7m (2010 £0.7m outflow). The closing cash balance as at 31 May 2011 was £4.1m (2010 £16.2m).

Dividend

An annual dividend of 1.00p per share in respect of 2009/10 was paid on 5 November 2010.

The Board does not recommend an annual dividend in respect of 2010/11.

Michael Brennan
Chief Financial Officer
2 August 2011



Introduction

Filtronic supplies microwave and base station filter products for the wireless telecommunications market. The business is in a fast-changing sector with a small number of sophisticated customers, demanding performance standards and international competition, all of which pose risks to the business.

Market

We supply a niche range of products to a small number of large OEM customers for both the Broadband and Basestation filter businesses as well as an as yet small number of network operators in the Basestation business. The loss of any of these customers, including Ceragon Networks, or any material reduction in orders from any such customers may have a material adverse effect upon Filtronic's financial condition. With the rapid evolution of product technology and other corporate decisions the size of our addressable market may be affected. We may also fail to forecast market movements correctly so missing opportunities or wrongly predicting product longevity.

Manufacturing

In most of the products, production is demand led and customers may vary their requirements from the business at short notice, which also impacts inventory management. Customers in these businesses expect consistent high quality product and reducing prices, hence we depend on control of our operating environment, including management of security of supply in our supply chain, and the provision of correctly designed technological solutions including the achievement of target cost reduction plans. Non-performance in these areas risks a diminished market position.

All our products are provided to customers after detailed qualification testing. However, this may not test all aspects of the product's design and manufacturing process or may not ensure that the product is viewed as fit for purpose in its intended use. Identification of these types of problem after release of product to customers creates the risk of being required to rectify such product defects. Historically such work has not had a substantial impact on the financial performance of the business, although a major defect, leading to a field recall, could do so in future.

The Broadband business operates a leased manufacturing location, located within the facility of our major semiconductor supplier. The Basestation business relies for the manufacture of its products on a large Chinese turnkey manufacturer that provides favourable supply and financing terms. The loss of this supplier or a material change to supply terms could have a material adverse effect on the Group.

Technology

Our product competitiveness is strongly influenced by technology choices at product concept stage and throughout execution of design to product launch. For products in the production cycle, technology insertion is often required as a means of achieving price reductions, which underpin sales. The market is time sensitive and opportunities may be lost if the technology we develop is not appropriate or ready for exploitation to match market demand, so having an adverse effect on business performance.

Our ability to remain competitive in terms of technology and product design is also underpinned by retaining key staff, the loss of whom could seriously impact the rate of introduction of new products and technologies.



Financial management

A large proportion of sales is denominated in US dollars with the cost base substantially in sterling, which may therefore create margin risks that may not be recoverable through price changes. This risk is mitigated to some extent by purchasing some input materials in US dollars.

We have sold four divisions of the group in the past seven years. We have provided warranties in support of these transactions, covering areas including product liability for an initial period and usually environment risks on freehold property and tax risks for longer specified periods. We have received claims on the sale of the Wireless Infrastructure and Defence Electronics business, some of which have been settled or rejected, and may receive claims in future related to these current and future commitments.

Goodwill and Going Concern

With the acquisition of the Basestation business, goodwill and intangibles have arisen. If the Basestation business does not develop as anticipated then this may have an adverse impact upon business performance which may result in a write down of the goodwill and/or the intangibles.

The directors have considered going concern matters and whilst they have a reasonable expectation that the group has adequate resources to continue in operational existence for the foreseeable future, it remains possible that sufficient events with material adverse impacts on the business could occur such as to change this expectation.



Executive directors

Hemant Mardia (aged 49) has been an executive director since 2007 and Chief Executive Officer since 2008. Since 1996 he has been Managing Director of the Broadband (PTP) business. He joined Filtronic in 1984 having gained a doctorate in electronics from Leeds University. He is a Fellow of the Institute of Electronics and Technology, a Fellow of the Society of Cable Telecommunications Engineers and a Senior Member of the Institute of Electrical and Electronic Engineers.

Michael Brennan (aged 51) was appointed as an executive director and Chief Financial Officer on 18 September 2009. Prior to joining Filtronic he was Finance Director of GTL Resources plc. Previously he held finance positions with Petroplus Refining Teesside Limited and various ICI businesses.

Alan Needle (aged 56) was appointed as an executive director on 16 November 2010. Prior to the acquisition of Isotek he was Head of Wireless Infrastructure of Isotek Electronics Limited, had been an Executive Director until January 2006, and Chief Executive of the Wireless Infrastructure Division of Filtronic plc.

Non-executive directors

Howard Ford (aged 60) has been a non-executive director since 2008. He was appointed non-executive Chairman on 18 September 2009. He has many years of operational experience in the IT and telecoms sector with IBM Europe, BT/Cellnet and Equant Network Services where as Managing Director the company was listed on the New York Stock Exchange and the Paris Bourse until its takeover by France Telecom in 2005. He has also served on the Boards of a UK Charity and a number of privately held companies in the UK and France.

Graham Meek (aged 64) has been a non-executive director since 1999. Since 2006 he has been the senior non-executive director and is chairman of the audit committee. He was Chairman of ICM Computer Group plc until its takeover in 2007 and was Chairman of SPI Lasers plc until its takeover in 2008. He is a non-executive director of Capital Gearing Trust plc.

Reginald Gott (aged 54) has been a non-executive director since 2006. He was appointed as chairman of the remuneration committee on 6 June 2008. He is Chief Executive of the Nuaire Group. From 2002 to 2008 he was an executive director of FKI plc, an international diversified engineering group. He has an extensive background in the machinery, automation and controls segments of the capital goods markets across Europe and North America.



The directors present their report and the audited financial statements for the year ended 31 May 2011.

Principal activities

The principal activities of the group are the design and manufacture of broadband microwave and base station filter products for wireless telecommunications systems.

Business review

The business review on pages 4 to 8 inclusive contains a review of the group's business performance and outlook. The business review includes the statutory requirements of the enhanced business review.

Financial results and dividend

The results for the year are set out in the income statement on page 26. The position at the end of the year is shown in the balance sheet on page 28.

The directors are not recommending payment of an annual dividend (2010 1.00p).

Research and development

Research and development costs were £3.5m (2010 £2.3m) for continuing operations and £nil (2010 £nil) for discontinued operations. Grant income of £0.3m was received to assist with part of these costs.

Directors and their interests

The directors of the company during the year were as follows:

Hemant Mardia

Michael Brennan

Howard Ford

Graham Meek

Reginald Gott

Alan Needle (appointed 16 November 2010)

Details of directors' interests in the share capital of the company are set out in the remuneration report on pages 18 to 22.

Alan Needle retires and, having been appointed by the Board on 16 November 2010, offers himself for election at the Annual General Meeting.

Hemant Mardia retires and offers himself for re-election at the Annual General Meeting.

Graham Meek, having served on the Board for more than nine years, retires and being eligible, offers himself for re-election at the Annual General Meeting.

Directors' indemnity

The company has in place directors' and officers' liability insurance on behalf of its directors and officers in accordance with the provisions of the Companies Act. In addition, certain directors benefit from an indemnity from the company, to the extent not prohibited by law, in respect of losses incurred as a result of the discharge of their duties in the management or supervision of any company in the group. The indemnity does not automatically terminate when the indemnified person ceases to be a director.



Directors' conflicts of interest

Alan Needle has provided general notice under Article 182 of The Companies Act 2006 of his interest in the Isotek working capital adjustment, until the adjustment is agreed and finalised with the Filtronic Board.

There are no other declarations to be made under Article 182 of The Companies Act 2006.

Share capital

The company's share capital consists of 10p ordinary shares. The rights and obligations attached to each share are equal. There are no limitations on holding or transfer of the shares. The Board has no powers to issue or buy back the company's shares, other than those approved by the shareholders at the Annual General Meeting held on 18 September 2010.

Substantial shareholdings

The following shareholders have indicated a holding of 3% or more of the issued share capital of 92,873,093 10p ordinary shares as at 28 July 2011.

| | Number of 10p ordinary shares | % of issued share capital |
|---|----------------------------------|------------------------------|
| Aberforth Partners LLP | 15,743,090 | 17.0% |
| Prudential plc | 10,872,820 | 11.7% |
| Gartmore Investment Limited | 8,590,967 | 9.3% |
| Aviva plc | 5,542,228 | 6.0% |
| Legal & General Investment Management Limited | 5,575,421 | 6.0% |
| John David Rhodes | 3,794,769 | 4.1% |
| | <u>50,119,295</u> | <u>54.1%</u> |

Employees

The group is committed to a policy of equal opportunities in employment by which the group ensures that all aspects of selection and retention are based on merit and suitability for the job regardless of sex, age, marital status, colour, race, ethnicity, sexual orientation or disability.

The group is conscious of its obligations towards disabled persons and tries to ensure that they receive equal opportunities. So far as particular disabilities permit, the group will continue to provide employment for any existing employee who becomes disabled. The group will also provide relevant training, career development and promotion for disabled employees where this is appropriate.

The Chief Executive Officer is the Board member responsible for human resources.



Corporate & social responsibility

(i) Health and safety

The Board is committed to ensuring the health and safety of the group's employees and applies high standards throughout the group in the control and management of its operations. The group analyses its practices and processes using systematic health and safety management techniques and auditing regimes. As part of the group's continued implementation of an occupational health, safety and management system, the group has put preventative measures in place that aim to continue to reduce major injuries and lost time accidents. In addition, the major manufacturing site has achieved OHSAS 18001 (health and safety management systems).

(ii) Employee development

Employee development has been established as one of the group's key objectives. The group has an education and training policy in place to implement continuous improvement where beneficial to the group and employee, thus underlying the group's commitment to ongoing employee development and training.

(iii) Employee communications

The group believes in keeping employees fully informed on matters which affect them through communication procedures including staff meetings and a culture which encourages openness and interaction between all members of staff. The group operates a UK-wide staff forum for information and consultation ('ICON forum'). The ICON forum is designed to be a gathering at which employee representatives can review group progress and raise, share and discuss specific issues and concerns that affect employees with senior management.

(iv) The environment

Care for the environment is an integral part of the group's business activities. It is the group's policy to ensure that its facilities are safe and the group is committed to ensuring that its impact on the environment is minimised. The group supports and trains its personnel to act responsibly in matters relating to the environment. The group takes account of relevant legislation and regulations and analyses its practices, processes and products to reduce their environmental impact, and works with its customers and suppliers to achieve a high standard of product stewardship. The group's in-house manufacturing sites have established environmental management systems and have achieved ISO 14001 certification.

Wherever possible, components and materials are reused or recycled. The reuse, utilisation and recycling of packaging is subject to monitoring. The group continues to work with its customers to implement programmes to design products for disassembly and recycling, and in particular so as to ensure compliance with the European Union directive on waste electrical and electronic equipment and the European Union initiatives in relation to the restriction of certain hazardous substances in electrical and electronic equipment. The group has introduced focused management teams throughout its business to ensure that compliance with these requirements is achieved within the required implementation timescales. The group continues to work with major suppliers, contractors and customers to assist them in improving their environmental, health and safety performance.

Political and charitable contributions

No contributions were made for political purposes. The group donated £450 (2010 £nil) to various charities.



Supplier payment policy

It is the group's policy to abide by the terms of payment agreed with suppliers in respect of the goods and services properly invoiced to the group. At 31 May 2011 trade payables of £5.5m represented 103 days' purchases, calculated in accordance with the requirements of the Companies Act.

Disclosure of information to the auditors

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the company's auditors are unaware; and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

Responsibility statement of the directors

The directors whose names appear on page 9 confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and
- the Chairman's Statement and Business Review which form part of the Report of the Directors, includes a fair review of the development and performance of the business and the position of the company and the undertakings included in the consolidation taken as a whole, together with the description of the principal risks and uncertainties that they face.

Auditors

A resolution to re-appoint KPMG Audit Plc as auditors will be proposed at the Annual General Meeting.

By order of the Board
M Moynihan
Company Secretary
2 August 2011



The Combined Code on Corporate Governance

The Board of Directors of Filtronic plc is committed to maintaining high standards of corporate governance. The Board has prepared this report with reference to the Combined Code on Corporate Governance issued by the Financial Reporting Council as revised in 2008 ("the Code"). For the year ended 31 May 2011 the directors confirm that the company has complied with the provisions of the Code.

The Board is currently comprised of six directors, the Chairman, two non-executives and three executive directors. For the current reporting period, the Company is deemed to be a "smaller company" as defined in provision A.3.2 of the Combined Code 2008. One of the non-executive directors, Reginald Gott, meets all of the specific criteria for independence set out in the Combined Code. The other non-executive director, Graham Meek, does not meet all of the requirements for independence set out in the Code since he has been a director for more than nine years. However Mr Meek is considered to be independent in character and judgement. He is the senior independent director and provides valuable advice to the company as well as continuity in the context of the recent corporate activity and Board changes.

Internal control

The Board has overall responsibility for establishing, maintaining and monitoring the company's system of internal control. Internal control systems are designed to be relevant to the company and the risks to which it is exposed and, by their nature, can provide reasonable but not absolute assurance against material misstatement or loss. The key procedures established by the directors with a view to providing effective internal control are as follows:

The Board's approach to risk management is aimed at early identification of key risks to the group's business and strategy, followed by an evaluation of those risks and the probable impact of those risks and the steps required to mitigate the likely effects. The executive directors report formally on key risks for each business unit at each meeting.

(a) Control environment and monitoring systems

The Board usually meets each month and has adopted a schedule of matters which are required to be brought to it for decision, thus ensuring that it maintains full and effective control over appropriate strategic, financial, operational and compliance issues. The Board has put in place an organisational structure with clearly defined lines of responsibility and delegation of authority. Additionally, the Board has established an Executive Management Committee that is responsible for operational matters within the company.

The division of responsibilities between the Chairman and the Chief Executive Officer has been set out in writing and agreed by the Board.

The audit committee, which comprises all of the non-executive directors including the Chairman reviews the effectiveness of the system of internal control. The external auditors are engaged to express an opinion on the company's annual financial statements. They test the system of internal financial control and the information contained within the annual report and financial statements to the extent necessary for expressing their opinion.

(b) Major information systems

The directors have delegated to executive management implementation of the system of internal control throughout the company. This includes financial controls that enable the Board to meet its responsibilities for the integrity and accuracy of the company's accounting records and a formal risk management reporting system for non-financial risk management

The Board approves, in aggregate, budgets and other performance targets, the components of which form the financial objectives for individual operating units. Performance against these targets is reported monthly and concentrates upon key performance indicators identified and updated as part of this budgetary control process. Financial forecasts are updated and reviewed monthly and include cash flow forecasts.



(c) Main control procedures

In addition to matters reserved for Board decisions, the company has established a system whereby authority to take decisions is distributed throughout the company. This distribution of authority defines procedures for authorisation and approval and sets appropriate levels of responsibility.

(d) Identification and evaluation of business risks

The company has clear principles and procedures that are appropriate to an electronics business of its size. These principles are designed to provide an environment of central leadership but with devolved operating responsibility as the framework for the exercise of accountability and control by the Board, its committees and executive management.

The Board directs activities in and allocates resources to the key areas of business development, product strategy, research and development, manufacture and financial practice.

Through these ongoing procedures, the Board is able to identify, evaluate and manage the significant risks that the group faces from time to time.

The Board has reviewed its approach to the identification and evaluation of business risks and has put in place a programme to review the main areas of risk identified for the company on an annual basis at the Board.

The Board confirms that it has carried out a review of the effectiveness of the system of internal control as it operated during the year. The Board undertakes, on an ongoing basis, a review of all aspects of the company's internal control procedures. The review is undertaken by the Board through the receipt and consideration of regular monthly and other reports prepared by management on operational, strategic, organisational and financial issues. All areas of operations are audited periodically either by external agencies or through peer review to ensure compliance with group policies.

Constitution of the Board

The Board comprises the Chairman, three executive and two independent, non-executive directors. Short biographies of all of the directors are set out on page 9. The Board considers that its constitution brings both independence and an appropriate balance of experience in judging matters of strategy, performance, resources, investor relations, internal control and corporate governance. Graham Meek is the senior non-executive director. Each of the directors is proposed for re-election at the Annual General Meeting at least every three years. Non-executive directors who have served longer than nine years on the Board are subject to annual re-election.

Graham Meek joined the company in 1999 and the Board has carefully considered his independence. He contributes significantly through his financial expertise and considerable knowledge of the company. He has provided continuity as well as contributing to the overall balance of the Board. The Board has decided that Graham Meek is an independent non-executive director.

A formal performance review of the Board, its committees and the directors was undertaken during the year. This has been implemented in the year by way of a written questionnaire completed by all Board members.

Board committees

The Board has a nominations committee, a remuneration committee and an audit committee. The remuneration and audit committees comprise all of the independent non-executive directors. Each of these committees operates under terms of reference which have been established by the Board.



The nominations committee

The nominations committee is chaired by Howard Ford, and the other member is the independent non-executive directors: Graham Meek and Reginald Gott. The nominations committee's duties are confined to the nomination of appointments, re-appointments and termination of employment or engagement of directors and the company secretary.

The nominations committee met three times during the year to consider Board composition and balance of skills.

The remuneration committee

The remuneration committee is chaired by Reginald Gott. Graham Meek, the other independent non-executive director, and Howard Ford, the Chairman of the Board, are members. The remuneration committee's responsibilities include ensuring that the remuneration and service contract terms of the executive directors and senior management are appropriate. The committee approves the grant of all share options and bonus arrangements. During the year the business discussed and considered at the Remuneration Committee included: approval of bonus payments or none made in respect of the previous financial year FY2009/10, review of compensation structure of employees across the group particularly following the Isotek acquisition, agreement of the terms of the ESOP plan and reviewing and agreeing on the terms and the documentation in respect of the issue of a further invitation to all UK employees under the Filtronic Share Save plan.

The remuneration committee met three times during the year.

The audit committee

The audit committee is chaired by Graham Meek, the senior non-executive director. The other members are Reginald Gott and Howard Ford, the Chairman of the Board (who was independent on appointment in accordance with the provisions of the Combined Code 2008). Graham Meek has sufficient, recent and relevant financial experience. The audit committee meets at least twice a year. The committee's terms of reference are consistent with the current best practice for the size of the company and are available on request from the company secretary or on the company's website.

The committee met twice during the financial year with management and external auditors. It also met twice with the external auditors in private. The chairman of the committee also met privately with the auditors regularly during the year. The committee reviewed the following matters and reported its conclusions to the Board:

- the financial statements contained in the company's annual and half-yearly reports to shareholders;
- various accounting matters, including the company's accounting policies, raised by management and the external auditors in the context of the financial statements;
- the effectiveness of internal controls and the group's internal controls manual;
- authorisation of the amount and purposes of non-audit fees;
- reviewing the external auditors' independence and objectivity;
- the external auditors' year end report and the findings of their work and confirmation that all significant matters had been satisfactorily treated;
- a full and careful consideration of the performance of the external auditors, as a result of which the committee resolved to recommend the re-appointment of KPMG Audit Plc as auditors to the company.



The Board has reviewed the composition of the audit committee and is satisfied that it has members who have sufficient, recent and relevant financial experience.

Attendance at Board meetings and committee meetings during the year ended 31 May 2011 was as follows:

Directors Attendance Table - FY2011

| | Board | Audit | Remuneration | Nominations |
|--|-------|-------|--------------|-------------|
| Director attendance | 19 | 2 | 3 | 3 |
| Executives | | | | |
| Hemant Mardia | 18 | n/a | n/a | n/a |
| Mike Brennan | 19 | n/a | n/a | n/a |
| Alan Needle (appointed 15 November 2010) | 5 | n/a | n/a | n/a |
| Non-executives | | | | |
| Howard Ford (Chairman) | 18 | 2 | 3 | 3 |
| Reginald Gott | 17 | 2 | 3 | 3 |
| Graham Meek | 17 | 2 | 3 | 3 |

Relations with investors

Communications with investors are given high priority. There is regular dialogue with institutional investors including presentations after the company's preliminary announcement of the year-end results and at the half year, which are attended by non-executive directors. Analyst reports and feedback from shareholders are discussed at Board meetings.

The Board uses the Annual General Meeting to communicate with private and institutional investors and welcomes their participation. The Chairman aims to ensure that the chairmen of the audit and remuneration committees are available at the Annual General Meeting to answer questions. Information is also available to all investors by way of the company's website at www.filtronic.co.uk.

Going concern

The group's business, together with the factors likely to affect its future development, performance and position are set out in the Business Review on pages 4 to 8. The financial position of the group, its cash flows, and its liquidity position are described in the Financial Review on page 6. Note 38 to the financial statements describes and quantifies exposures to liquidity, credit, interest rate and foreign currency risk and how they are managed. Also in note 38 capital management is described.

At 31 May 2011 the group had a cash balance of £4.1m.

The directors have reviewed the budgeted cash flow and other relevant information and have a reasonable expectation that the group has adequate resources to continue in operational existence for the foreseeable future. For this reason, the directors continue to adopt the going concern basis in preparing the financial statements.



Remuneration Report

for the year ended 31 May 2011

Composition of the remuneration committee

During the period 1 June 2010 to 31 May 2011 the remuneration committee consisted of the following non-executive directors:

Reginald Gott (Chairman)
Graham Meek
Howard Ford

The committee receives advice in its deliberations concerning the remuneration of the executive directors from the Chief Executive Officer, Hemant Mardia. The committee's recommendations have been accepted by the Board without amendment.

Compliance

The company has complied with the provisions in the Code of Best Practice relating to Directors' Remuneration. In preparing this report, the provisions in Schedule B to the Combined Code have been followed.

Policy on remuneration of executive directors and senior executives

(a) Total level of remuneration

The committee aims to ensure that remuneration packages offered are competitive and designed to attract, retain and motivate executive directors and senior executives.

(b) The main components

The company's policy is to structure remuneration packages to align the interests of employees with those of shareholders.

The main components of remuneration are:

(i) Salary

Salary for each executive is determined by the remuneration committee taking into account the performance and responsibilities of the individual. Electronic and electrical engineering is an international industry within which there is a clear market in executive talent. The overriding factor in determining executive remuneration is market forces. Salaries are normally reviewed on 1 July each year.

(ii) Executive directors bonuses

The executive directors were participants in an annual bonus scheme during the year under which a maximum of 30% of salary was payable to Hemant Mardia, Michael Brennan and Alan Needle subject to profit and cash targets and personal targets, the achievements of which have been assessed by the remuneration committee.

No bonuses were awarded in the year to Hemant Mardia (2010 £27,038 being 15%), Michael Brennan (2010 £15,000 being 15%) and Alan Needle (2010 £nil).

No non-recurring bonus arrangements were put in place in the year ended 31 May 2011.

(iii) Bonus scheme

The remuneration committee has agreed an approach for management incentives for the year ending 31 May 2012 of an annual bonus for performance in the year, based on profit and cash targets. The level of up to 30% of annual salary for executive directors and up to 25% of annual salary for senior managers has been agreed for each of these bonuses. The annual bonus will be assessed against the achievement of profit and cash targets in the year ended 31 May 2012.

Remuneration Report

for the year ended 31 May 2011



(iv) Performance share plan

A performance share plan was approved by shareholders at the Annual General Meeting in September 2008. During the year, under the plan, Hemant Mardia was awarded 257,500 shares being 50% of his salary and Michael Brennan was awarded 114,286 shares being 40% of his salary. In addition, a further four persons discharging managerial responsibilities participated in the plan including Hemant Mardia's wife, who is employed by the group, and was awarded 47,626 shares being 20% of her salary.

The vesting of the 29 November 2010 share awards is subject to performance targets based on growth in earnings per share (EPS) over a three year period. If EPS grows such that for the year to 31 May 2013 it exceeds a figure corresponding to £5.5m of earnings before intangible amortisation, exceptionals, interest and tax, then 25% of the awarded shares will vest. If EPS grows such that for the year to 31 May 2013 it exceeds a figure corresponding to £7.0m of earnings before intangible amortisation, exceptionals, interest and tax, then 100% of the awarded shares will vest. If EPS grows to be between these two targets then the awarded shares will vest on a sliding scale between 25% and 100% of the awarded shares.

(v) Sharesave plan

A sharesave plan was approved by shareholders at the Annual General Meeting in September 2008. All employees including executive directors are eligible. The first offer under the sharesave plan was made in February 2009. A second offer under the sharesave plan was made in November 2010.

(c) Company policy on contracts of service

Hemant Mardia, Michael Brennan and Alan Needle, the executive directors, all have rolling service contracts. Under Hemant Mardia's service contract the notice period for termination by either party is twelve months. Under Michael Brennan's service contract the notice period for termination by either party is six months. Under Alan Needle's service contract the notice period for termination by either party is six months (but 12 months until 15 November 2012). There are no specific compensation commitments for early termination in the service contracts.

(d) Company pensions policy

The company's policy is to offer executives membership of the Filtronic plc Stakeholder Pension Plan on the same basis as all other employees of the company. The plan is a defined contribution scheme. The maximum contribution the company makes to the plan is 8% of pensionable salary, if the member makes a contribution of 6% of pensionable salary. Members of the plan are also entitled to death in service benefit of four times pensionable salary and long term disability insurance.

The pension scheme inherited from the Isotek acquisition is also a defined contribution scheme. The maximum contribution the company makes to the plan for UK employees is 10% of pensionable salary if the member makes a contribution of 5% pensionable salary. All employees are also entitled to death in service benefit of four times pensionable salary and long term disability insurance.

US employees contribute to a defined contribution plan under Section 401(k) of the Internal Revenue Code. 6% of pensionable salary is contributed by employees and this is matched by the company. All employees are also entitled to death in service benefit of two times salary to a maximum of \$100,000.

(e) Company policy on external appointments

The remuneration committee reviews any request by an executive director with regard to a proposed external appointment and deals with each request on its individual merits. The overriding requirement is for each executive, as a term of his contract, to devote substantially the whole of his time, skill and attention to the affairs of the group.



Remuneration Report

for the year ended 31 May 2011

Non-executive directors agreements for services and remuneration

The non-executive directors have rolling agreements for services with the company. These are terminable by the company or the non-executive director on six months notice for the Chairman and on three months notice for the other non-executive directors and are reviewed annually by the Board.

The Board determines the remuneration of the non-executive directors. Non-executive directors are not entitled to any share options, performance shares, bonuses or pension benefits.

The information on pages 20 and 21 has been audited.

Directors' remuneration

| | Salary or fees | Bonuses | Benefits | Total remuneration excluding pension contributions | |
|---|-------------------|--------------|--------------|--|--------------|
| | 2011 £000 | 2011 £000 | 2011 £000 | 2011 £000 | 2010 £000 |
| Executives | | | | | |
| Hemant Mardia | 180 | – | 18 | 198 | 225 |
| Michael Brennan | 100 | – | 7 | 107 | 95 |
| Stephen Mole (resigned 18 September 2009) | – | – | – | – | 111 |
| Alan Needle (appointed 16 November 2010) | 54 | – | – | 54 | – |
| Non-executives | | | | | |
| Howard Ford | 70 | – | 1 | 71 | 58 |
| Graham Meek | 40 | – | – | 40 | 39 |
| Reginald Gott | 40 | – | – | 40 | 39 |
| John Poulter (resigned 18 September 2009) | – | – | – | – | 104 |
| Total 2011 | 484 | – | 26 | 510 | 671 |
| Total 2010 | 599 | 42 | 30 | 671 | |

Benefits incorporate all assessable tax benefits arising from employment by the company and relate in the main to the provision of a fully expensed company car or car allowance and private medical insurance.

Directors' pension benefits

Company's pension contributions to defined contribution schemes.

| | Pension contributions | |
|---|--------------------------|--------------|
| | 2011 £000 | 2010 £000 |
| Hemant Mardia | 14 | 14 |
| Michael Brennan | 8 | 6 |
| Stephen Mole (resigned 18 September 2009) | – | 4 |
| Alan Needle (appointed 16 November 2010) | 5 | – |
| | 27 | 24 |

Remuneration Report

for the year ended 31 May 2011



Directors' shareholdings

| | 2011 | 2010 |
|-----------------|------------------|---------------|
| Alan Needle | 2,064,707 | – |
| Hemant Mardia | 159,813 | 54,249 |
| Michael Brennan | 40,400 | – |
| Howard Ford | 42,204 | – |
| Reg Gott | 28,515 | – |
| Graham Meek | 50,000 | – |
| | 2,385,639 | 54,249 |

All of the above shareholdings are held beneficially. Hemant Mardia, Graham Meek and Reg Gott's shareholdings include those of their wives.

Reg Gott's wife purchased 28,515 shares at 35.7p on 2 August 2010.

Howard Ford purchased 42,204 shares at 35p on 3 August 2010.

Graham Meek's wife purchased 50,000 shares at 38p on 4 August 2010.

Hemant Mardia and his wife each purchased 15,000 shares at 37.95p on 5 August 2010.

Hemant Mardia and his wife purchased 11,979 and 11,935 shares respectively at 37.99p on 6 August 2010.

Hemant Mardia and his wife each purchased 25,825 shares at 38p on 6 September 2010.

Michael Brennan purchased 40,400 shares at 35.5p on 29 October 2010.

Alan Needle received 2,064,707 shares as consideration for the Isotek acquisition on 16 November 2010.

Directors' interests in share awards

| | Vesting date | 2010 | Granted during the year | 2011 |
|-------------------------------|------------------|----------------|-------------------------|----------------|
| Performance share plan | | | | |
| Hemant Mardia | 29 July 2012 | 378,239 | – | 378,239 |
| | 29 November 2013 | – | 305,126 | 305,126 |
| Michael Brennan | 2 September 2012 | 108,108 | – | 108,108 |
| | 29 November 2013 | – | 114,286 | 114,286 |
| | | 486,347 | 419,412 | 905,759 |

Hemant Mardia's share awards include those of his wife, who is employed by the group.

Directors' interests in share options

| | Exercise period | Option price | 2010 | Granted during the year | Cancelled during the year | 2011 |
|-----------------------|-------------------------|--------------|---------------|-------------------------|---------------------------|---------------|
| Sharesave plan | | | | | | |
| Hemant Mardia | 01/04/2012 – 01/10/2012 | 25p | 62,400 | – | – | 62,400 |
| | 01/11/2013 – 30/04/2014 | 34.2p | – | 8,842 | – | 8,842 |
| Mike Brennan | 01/11/2013 – 30/04/2014 | 34.2p | – | 26,315 | – | 26,315 |
| Total all directors | | | 62,400 | 35,157 | – | 97,557 |



Remuneration Report

for the year ended 31 May 2011

Hemant Mardia's share options include those awarded to his wife, who is employed by the group.

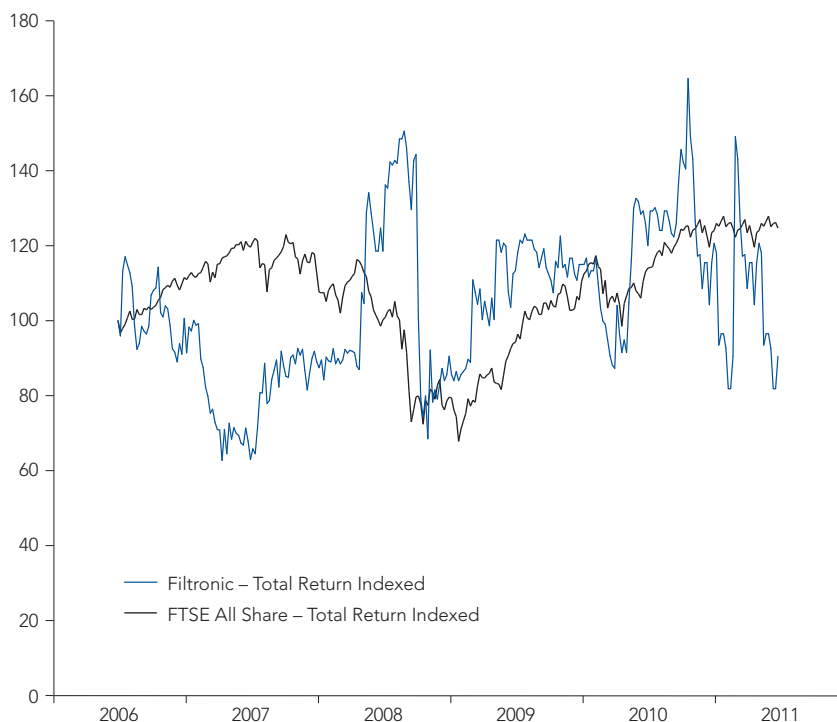
The closing middle market share price on 31 May 2011 was 23p, and on 31 May 2010 it was 26p. The range of closing middle market share prices during the year ended 31 May 2011 was 62p – 23p.

There were no changes to the directors' interests between 31 May 2011 and 2 August 2011. The company's register of directors' interests which is open to inspection at the registered office contains full details of directors' shareholdings.

Performance graph

This graph illustrates the performance of the company's shares measured by Total Shareholder Return (TSR) relative to a broad equity market index over the past five years. The FTSE All Share is considered to be the most appropriate index against which to measure performance, as the company has been a constituent of the FTSE All Share throughout the five-year period and the index is widely used. TSR is the measure of the returns that a company has provided for its shareholders, reflecting share price movements and assuming reinvestment of dividends.

Total Shareholder Return
1 June 2006 to 31 May 2011 Weekly Indexed



Source: Thomson Datastream

Note: Rebased to 100 as at 1 June 2006

Approved by the Board on 2 August 2011 and signed on its behalf by

M Moynihn
Company Secretary



Statement of directors' responsibilities in respect of the annual report and the financial statements

The directors are responsible for preparing the Annual Report and the group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare group and parent company financial statements for each financial year. Under that law they are required to prepare the group financial statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the parent company financial statements on the same basis.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and parent company and of their profit or loss for that period. In preparing each of the group and parent company 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;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group and the parent company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that complies with that law and those regulations.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.



Independent Auditor's Report

Independent auditor's report to the members of Filtronic plc

We have audited the financial statements of Filtronic plc for the year ended 31 May 2011 set out on pages 26 to 64. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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 auditor's 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 auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 23, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's website at www.frc.org.uk/apb/scope/private.cfm.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 May 2011 and of the group's loss for the year then ended;
- the group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU; and
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- information given in the Corporate Governance Statement set out on pages 14 to 17 with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures is consistent with the financial statements.



Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- a Corporate Governance Statement has not been prepared by the company.

Under the Listing Rules we are required to review:

- the directors' statement, set out on page 17, in relation to going concern;
- the part of the Corporate Governance Statement on page 14 relating to the company's compliance with the nine provisions of the June 2008 Combined Code specified for our review; and
- certain elements of the report to shareholders by the Board on directors' remuneration.

David Morritt (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor

Chartered Accountants
1 The Embankment
Neville Street
Leeds
LS1 4DW

2 August 2011



Consolidated Income Statement

for the year ended 31 May 2011

| | | | Group |
|---|------|----------------|---------|
| | | 2011 | 2010 |
| | | £000 | £000 |
| Continuing operations | note | | |
| Revenue | | 15,523 | 15,575 |
| Operating loss before amortisation and exceptional items | | (5,260) | (292) |
| Amortisation of intangibles | | (1,209) | – |
| Exceptional items | 6 | (611) | (842) |
| Operating loss | 5 | (7,080) | (1,134) |
| Finance income | 12 | 79 | 113 |
| Loss before taxation | | (7,001) | (1,021) |
| Taxation | 13 | 326 | – |
| Loss for the period from continuing operations | | (6,675) | (1,021) |
| Loss for the period from discontinued operations | 3 | (265) | – |
| Loss for the period | | (6,940) | (1,021) |
| Basic and diluted loss per share | | | |
| Continuing operations | 14 | (7.19)p | (1.37)p |
| Discontinued operations | 14 | (0.29)p | – |
| Basic and diluted loss per share | 14 | (7.48)p | (1.37)p |

The loss for the period is attributable to the equity shareholders of the parent company Filtronic plc.

Consolidated Statement of Comprehensive Income

for the year ended 31 May 2011



| | Group | |
|--|----------------|----------------|
| | 2011 £000 | 2010 £000 |
| Loss for the period | <u>(6,940)</u> | <u>(1,021)</u> |
| Currency translation movement arising on consolidation | <u>(32)</u> | <u>—</u> |
| | <u>(32)</u> | <u>—</u> |
| Total comprehensive income for the period | <u>(6,972)</u> | <u>(1,021)</u> |

The total comprehensive income for the period is attributable to the equity shareholders of the parent company Filtronic plc.

For the company, there were no other items of comprehensive income other than the loss for the year. Accordingly, no company statement of comprehensive income has been presented.



Consolidated Balance Sheet

at 31 May 2011

| | | 2011 £000 | Group 2010 £000 |
|--------------------------------|----|---------------|-----------------------|
| Non-current assets | | | |
| Goodwill and other intangibles | 16 | 13,330 | – |
| Property, plant and equipment | 17 | 2,485 | 1,998 |
| | | 15,815 | 1,998 |
| Current assets | | | |
| Inventories | 19 | 1,677 | 1,998 |
| Trade and other receivables | 20 | 5,763 | 3,361 |
| Tax receivable | | 114 | – |
| Cash and cash equivalents | | 4,120 | 16,245 |
| | | 11,674 | 21,604 |
| Total assets | | 27,489 | 23,602 |
| Current liabilities | | | |
| Trade and other payables | 21 | 5,485 | 2,886 |
| Provision | 23 | 437 | 706 |
| Deferred tax | 18 | 653 | – |
| Deferred income | 22 | 17 | 17 |
| | | 6,592 | 3,609 |
| Non-current liabilities | | | |
| Deferred tax | 18 | 1,959 | – |
| Deferred income | 22 | 108 | 108 |
| | | 2,067 | 108 |
| Total liabilities | | 8,659 | 3,717 |
| Net assets | | 18,830 | 19,885 |
| Equity | | | |
| Share capital | 25 | 9,287 | 7,432 |
| Share premium | 26 | 4,683 | – |
| Translation reserve | 27 | (32) | – |
| Retained earnings | 29 | 4,892 | 12,453 |
| Total equity | | 18,830 | 19,885 |

The total equity is attributable to the equity shareholders of the parent company Filtronic plc.

Company member 2891064

Approved by the Board on 2 August 2011 and signed on its behalf by

Hemant Mardia
Chief Executive Officer

Consolidated Statement of Changes in Equity

for the year ended 31 May 2011



| | Group | |
|---|---------------|---------------|
| | 2011 £000 | 2010 £000 |
| Opening total equity | 19,885 | 21,576 |
| Total comprehensive income for the period | (6,972) | (1,021) |
| New shares issued (net of issue costs) | 6,538 | – |
| Share-based payments | 122 | 73 |
| Dividends | (743) | (743) |
| Closing total equity | 18,830 | 19,885 |

Company Statement of Changes in Equity

for the year ended 31 May 2011



| | Company | |
|---|---------------|---------------|
| | 2011 £000 | 2010 £000 |
| Opening total equity | 14,066 | 16,683 |
| Total comprehensive income for the period | (1,557) | (1,929) |
| New shares issued, net of issue costs | 6,538 | – |
| Share-based payments | 91 | 55 |
| Dividends | (743) | (743) |
| Closing total equity | 18,395 | 14,066 |



Consolidated Cash Flow Statement

for the year ended 31 May 2011

| | | 2011 £000 | Group 2010 £000 |
|---|----|-----------------|-----------------------|
| Cash flows from operating activities | | | |
| Loss for the period | | (6,940) | (1,021) |
| Loss on sale of discontinued operations | | 265 | – |
| Taxation | | (326) | – |
| Finance income | | (79) | (113) |
| Operating loss | 35 | (7,080) | (1,134) |
| Share-based payments | | 122 | 73 |
| Loss on disposal of plant and equipment | | – | 35 |
| Depreciation | | 523 | 601 |
| Amortisation of intangibles | | 1,209 | – |
| Movement in inventories | | 476 | 2,533 |
| Movement in trade and other receivables | | (724) | 1,418 |
| Settlement of option premia debt acquired with Isotek | | 1,194 | – |
| Movement in trade and other payables | | 178 | (1,117) |
| Movement in provision | | (269) | (608) |
| Change in deferred income including government grants | | – | 125 |
| Net cash (used in)/from operating activities | 35 | (4,371) | 1,926 |
| Cash flows from investing activities | | | |
| Interest received | | 79 | 113 |
| Acquisition of plant and equipment | | (925) | (639) |
| Proceeds on sale of assets | | 19 | – |
| Acquisition of subsidiary, net of cash acquired | | (4,162) | – |
| Share issue costs | | (325) | – |
| Acquired loan repaid | | (1,400) | – |
| Sale of discontinued operations | 36 | (265) | (635) |
| Net cash used in investing activities | 35 | (6,979) | (1,161) |
| Cash flows from financing activities | | | |
| Dividends paid | | (743) | (743) |
| Net cash used in financing activities | 35 | (743) | (743) |
| Movement in cash and cash equivalents | | (12,093) | 22 |
| Currency exchange movement | | (32) | 5 |
| Opening cash and cash equivalents | | 16,245 | 16,218 |
| Closing cash and cash equivalents | | 4,120 | 16,245 |

Company Balance Sheet

at 31 May 2011



| | | Company 2011 £000 | 2010 £000 |
|-----------------------------|------|-------------------------|--------------|
| | note | | |
| Non-current assets | | | |
| Investments in subsidiaries | 15 | 10,564 | – |
| Current assets | | | |
| Trade and other receivables | 20 | 7,812 | 1,552 |
| Cash and cash equivalents | | 2,953 | 15,616 |
| | | 10,765 | 17,168 |
| Total assets | | 21,329 | 17,168 |
| Current liabilities | | | |
| Trade and other payables | 21 | 2,934 | 3,102 |
| Total liabilities | | 2,934 | 3,102 |
| Net assets | | 18,395 | 14,066 |
| Equity | | | |
| Share capital | 25 | 9,287 | 7,432 |
| Share premium | 26 | 4,683 | – |
| Retained earnings | 29 | 4,425 | 6,634 |
| Total equity | | 18,395 | 14,066 |

Approved by the Board on 2 August 2011 and signed on its behalf by

Company member 2891064

Hemant Mardia
Chief Executive Officer



Company Cash Flow Statement

for the year ended 31 May 2011

| | Company | |
|---|-----------------|--------------|
| | 2011 £000 | 2010 £000 |
| Cash flows from operating activities | | |
| Loss for the period | (1,557) | (1,929) |
| Finance costs | 61 | 459 |
| Finance income | (79) | (113) |
| Loss on sale of investment in subsidiary | 265 | – |
| Operating loss | (1,310) | (1,583) |
| Share-based payments | 91 | 55 |
| Movement in trade and other receivables | (5,730) | 2,488 |
| Movement in trade and other payables | (169) | (21) |
| Net cash from operating activities | (7,118) | 939 |
| Cash flows from investing activities | | |
| Interest received | 79 | 113 |
| Acquisition of subsidiary | (4,230) | – |
| Share issue costs | (325) | – |
| Sale of investment in subsidiary | (265) | – |
| Net cash from investing activities | (4,741) | 113 |
| Cash flows from financing activities | | |
| Dividends paid | (743) | (743) |
| Net cash used in financing activities | (743) | (743) |
| Increase/(decrease) in cash and cash equivalents | (12,602) | 309 |
| Currency exchange movement | (61) | (459) |
| Opening cash and cash equivalents | 15,616 | 15,766 |
| Closing cash and cash equivalents | 2,953 | 15,616 |

Notes to the Financial Statements

for the year ended 31 May 2011



1 Accounting policies

Reporting entity

Filtronic plc is a company registered in England and Wales, domiciled in the United Kingdom, and is listed on the London Stock Exchange.

Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS).

The directors have reviewed the projected cash flow and other relevant information and have a reasonable expectation that the group has adequate resources to continue in operational existence for the foreseeable future. For this reason the directors continue to adopt the going concern basis in preparing the annual report.

The financial statements have been prepared under the historical cost convention except for forward foreign exchange contracts that are accounted for on a fair value basis.

The accounting policies have been applied consistently throughout the group.

Basis of consolidation

The financial statements consolidate the income statements, balance sheets and cash flow statements of the company and all of its subsidiaries.

Subsidiaries are all entities over which the group has the power to govern the financial and operating policies. Subsidiaries are consolidated from the date on which control is transferred to the group, and are not consolidated from the date that control ceases. Intra group transactions and balances are eliminated on consolidation.

In publishing the Parent Company Financial Statements here together with the Group Financial Statements, the company has taken advantage of the exemptions in s408 of the Companies Act 2006 not to present its individual income statement and related notes that form part of these approved Financial Statements.

Foreign currency translation

The functional currency of each group company is the currency of the primary economic environment in which the group company operates. The financial statements are presented in sterling which is the functional and presentational currency of the company.

Transactions denominated in foreign currencies are translated into the functional currency of each group company at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange ruling at the balance sheet date.

Foreign exchange gains and losses arising on the settlement of such transactions and translation of monetary assets and liabilities are recognised in the income statement.

Forward foreign exchange contracts are recognised in the balance sheet at their market value at the balance sheet date, and the resulting gain or loss is recognised in the income statement.



Notes to the Financial Statements

for the year ended 31 May 2011

1 Accounting policies (continued)

Foreign currency translation (continued)

On consolidation, the financial statements of subsidiaries with a functional currency other than sterling are translated into sterling as follows:

- The assets and liabilities in their balance sheets plus any goodwill are translated at the rate of exchange ruling at the balance sheet date.
- The income statements and cash flow statements are translated at the average rate of exchange for the period, which approximates the rate of exchange ruling at the date of the transactions.

Currency translation movements arising on the translation of the net investments in foreign subsidiaries are recognised in the translation reserve, which is a separate component of equity.

Revenue

Revenue is recognised for goods and services during the periods when the risks and rewards of ownership have been transferred to the customer, there is no continuing management involvement and the amount of revenue can be measured reliably. Revenue excludes any related value added or sales tax. This policy also applies to the newly acquired Isotek business.

Research and development

All research costs are expensed as incurred.

Development costs chargeable to the customer are recognised as an expense in the same period as the associated customer revenue.

Development costs incurred on projects requiring product qualification tests to satisfy customer specifications are generally expensed as incurred, reflecting the technical risks associated with meeting the resultant product qualification test.

Development costs incurred on projects are capitalised where firstly the technical feasibility can be tested against relevant milestones, secondly the probable revenue stream foreseen over the life of the resulting product can support the development and thirdly sufficient resources are available to complete the development. These capitalised costs are amortised on a straight line basis over the expected life of the associated product.

Once a new product is qualified, further development costs are expensed as they arise because they are incurred in response to continual customer demand to enhance the product functionality and to reduce product selling prices.

Operating leases

Operating lease rentals are charged to the income statement on a straight line basis over the lease term.

Share-based payments

The group operated share option and share award schemes, under which share options and share awards were granted to certain employees. The granting of the share options and share awards are share-based payments.

The fair value of the share options at the date of grant was calculated using an option pricing model, taking into account the terms and conditions applicable to the option grant. The fair value of the number of share options or share awards expected to vest was expensed in the income statement on a straight line basis over the expected vesting period. Each reporting period these vesting expectations were revised as appropriate.

A credit was made to equity, equal to the share-based payment expense in the period.



1 Accounting policies (continued)

Exceptional items

Exceptional items are those significant items which are separately disclosed by virtue of their size or incidence to enable a full understanding of the financial results.

Business combinations

Business combinations are accounted for by applying the acquisition method.

Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the group takes into consideration potential voting rights that currently are exercisable. The acquisition date is the date on which control is transferred to the acquirer. Judgement is applied in determining the acquisition date and determining whether control is transferred from one party to another.

The group measures goodwill as the fair value of the consideration transferred including the recognised amount of any non-controlling interest in the acquiree, less the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed, all measured as of the acquisition date.

Consideration transferred includes the fair values of the assets transferred, liabilities incurred by the group to the previous owners of the acquiree, and equity interests issued by the group. Consideration transferred also includes the fair value of any deferred consideration, which is undiscounted.

A contingent liability of the acquiree is assumed in a business combination only if such a liability represents a present obligation and arises from a past event, and its fair value can be measured reliably.

Transaction costs that the group incurs in connection with a business combination, such as finder's fees, legal fees, due diligence fees, and other professional and consulting fees are expensed as incurred.

Investments in subsidiaries

Investments in subsidiaries are stated in the company's financial statements at cost less any accumulated impairment losses.

Investments in subsidiaries are tested for impairment when there is an indication of impairment.

Goodwill

Goodwill that arises upon the acquisition of subsidiaries is included in intangible assets.

Goodwill is measured at cost less accumulated impairment losses. In respect of equity accounted investees, the carrying amount of goodwill is included in the carrying amount of the investment, and an impairment loss on such an investment is not allocated to any asset, including goodwill, that forms part of the carrying amount of the equity accounted investee.

Goodwill, which is allocated to cash generating units, is tested for impairment annually and when there is an indication of impairment. If impaired, the goodwill carrying value is written down to its recoverable amount.



Notes to the Financial Statements

for the year ended 31 May 2011

1 Accounting policies (continued)

Other intangible assets

Other intangible assets that are acquired by the group and have finite useful lives are measured at cost less accumulated amortisation and accumulated impairment losses.

Amortisation is calculated over the cost of the asset, or other amount substituted for cost, less its residual value. Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill, from the date that they are available for use, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset.

The estimated useful lives for the current and comparative periods are as follows:

- Intangibles relating to the core technology and know-how 4.5 years.

Amortisation methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

Impairment charges

The carrying amounts of the group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill, and intangible assets that have indefinite useful lives or that are not yet available for use, the recoverable amount is estimated each year at the same time. The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. 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. For the purposes of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit, or CGU"). Subject to an operating segment ceiling test, for the purposes of goodwill impairment testing, CGUs to which goodwill has been allocated are aggregated so that the level at which impairment is tested reflects the lowest level at which goodwill is monitored for internal reporting purposes.

An impairment loss is recognised if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the units, and then to reduce the carrying amounts of the other assets in the unit (group of units) on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Notes to the Financial Statements

for the year ended 31 May 2011



1 Accounting policies (continued)

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and less any accumulated impairment losses.

Depreciation is provided on a straight line basis over the estimated useful lives of the assets as follows:

| | |
|---------------------|-----------------|
| Land | Not depreciated |
| Buildings | 50 years |
| Plant and equipment | 3 to 10 years |

Property, plant and equipment are tested for impairment when there is an indication of impairment. If impaired, the carrying values of the assets are written down to their recoverable amounts.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises weighted average cost of materials and components together with attributable direct labour and overheads. Net realisable value is the estimated selling price less estimated costs of completion and sale.

Trade and other receivables

Trade and other receivables are stated net of any provision for doubtful debts.

Cash and cash equivalents

Cash and cash equivalents comprises cash balances and bank deposits with an original maturity of three months or less.

Defined contribution pension schemes

Defined contribution pension schemes are operated for employees. Contributions are recognised as an expense in the income statement as incurred.

Deferred taxation

Deferred tax is provided using the balance sheet liability method. Provision is made for temporary differences between the carrying amounts of assets and liabilities in the financial statements and the amounts for taxation purposes.

Temporary differences are not provided for the initial recognition of assets or liabilities that affect neither accounting nor taxable profit. No provision is made for differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

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



Notes to the Financial Statements

for the year ended 31 May 2011

1 Accounting policies (continued)

Grants

Capital based grants are included within deferred income in the balance sheet and credited to the profit and loss account over the estimated useful economic lives of the assets to which they relate.

Grants that compensate the group for expenses incurred are recognised in profit or loss as other operating income on a systematic basis in the same periods in which the expenses are recognised.

Warranty provision

A provision is recognised in the balance sheet when there is a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. A warranty provision is recognised when products are sold. The provision is based on historical warranty data. The level of warranty provision required is reviewed on a product by product basis and adjusted accordingly in light of actual experience.

Share capital

Ordinary shares issued are classified as share capital in equity.

Dividends

Interim dividends are recognised in equity in the period they are paid. Final dividends are recognised in equity in the period they are declared by shareholders.

Discontinued operations

A discontinued operation is a component of the group's activities that represents a separate business operation. Classification as a discontinued operation occurs upon disposal or if earlier when the operation meets the criteria to be classified as held for sale.

New IFRS and amendments to IFRS

The following new standards have become effective from 1 June 2010 and hence have been reflected in the financial statements:

- IFRS 3 (revised) Business combinations and consequential amendments to IAS 27 Consolidated and separate financial statements are effective prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009. During the period, the Group has made one acquisition as set out in note 37, and the requirements of these standards have been applied in accounting for these transactions. The Group's accounting policy under the new standards is set out within significant accounting policies.
- Amendments to IAS 39 "Financial Instruments: Recognition and Measurement: Eligible Hedged Items" (mandatory for the year commencing on or after 1 July 2009). The amendments to IAS 39 clarify how to apply existing principles in determining eligible hedged risks and portions. These changes have had no material impact on the Consolidated Financial Statements.



1 Accounting policies (continued)

New IFRS and amendments to IFRS (continued)

- Amendments to IAS 39 "Reclassification of financial Assets: Effective Date and Transition" (mandatory for the year commencing on or after 1 July 2009). These changes have had no material impact on the Consolidated Financial Statements.
- Improvements to IFRSs (issued 16 April 2009) (adoption dates vary but certain improvements are mandatory for the year commencing on or after 1 July 2009). On 16 April 2009 the IASB published the Improvements to IFRSs 2009. The Improvements to IFRSs 2009 is the result of the IASB's second annual improvements project (AIP). This project has involved the IASB accumulating throughout the year what it believes are non-urgent but necessary improvements to IFRSs and then processing these amendments collectively. The Improvements to IFRSs 2009 contains 15 amendments to 12 standards. These changes have had no material effect on the Consolidated Financial Statements.

There are a number of standards and interpretations issued by the IASB that are effective for financial statements after this reporting period. The following have not been adopted by the Group:

- IAS 24 Related party disclosures (revised) (effective for accounting periods starting on or after 1 January 2011)
- IFRS 7 Amendment to Financial instruments: Disclosures on derecognition (effective for accounting periods starting on or after 1 July 2011)
- IAS 12 Amendment to Income taxes on deferred tax (effective for accounting periods starting on or after 1 January 2012)
- IFRS 9 Financial instruments (effective for accounting periods starting on or after 1 January 2013)

The application of these standards and interpretations is not anticipated to have a material effect on the Group's financial statements.

2 Accounting estimates and judgements

The preparation of the financial statements requires the use of accounting estimates and judgements, that affect the application of accounting policies and reported amounts of assets and liabilities, income and expenses. The accounting estimates and judgements are continually evaluated. They are based on historical experience and other factors, including expectations of the future, that are believed to be reasonable under the circumstances. Actual results may differ from the expected results.

The accounting estimates and judgements that have a significant effect on the financial statements are considered below.

Acquisition accounting

As part of the accounting for business combinations it is necessary to perform a purchase price allocation exercise to identify appropriate categories of intangible assets that have been purchased. Such exercise involves judgement with regards to those types of assets identified, the value of those assets and the useful economic lives applied with regards to amortisation rates. The amounts recognised are calculated by reference to management forecasts and assumed discount rates.



2 Accounting estimates and judgements (continued)

Goodwill and other intangibles impairment

Goodwill and other intangibles are tested for impairment by reference to the expected cash generated by the business unit. This is deemed to be the best approximation of value, but is subject to the same uncertainties as the cash flow forecast being used.

Inventory

Inventories are stated at the lower of cost and net realisable value. The assessment of the net realisable value of inventory requires forecasts of the future demand and selling prices of inventory.

Deferred tax asset

The recognition of the deferred tax assets relating to tax losses carried forward depends on forecasts of the future taxable profits of the company and its subsidiaries. These forecasts require the use of estimates and judgements about the future performance of the company and its subsidiaries.

Warranty provision

Warranties are given to customers on products sold to them. A warranty provision is recognised when products are sold. The provision is based on historical warranty data. Actual warranty costs in the future may differ from the estimates based on historical performance. The level of warranty provision required is reviewed on a product by product basis and adjusted accordingly in light of actual experience.

Capitalisation of Development Costs

Development costs incurred on projects requiring product qualification tests to satisfy customer specifications are generally expensed as incurred, reflecting the technical risks associated with resultant product qualification test.

Other certain research and development costs are likely to meet the definition of enhancement type costs, as they do not substantially improve the product, and therefore do not meet the definition of development costs to be capitalised.

The process is to be continually reviewed to ascertain whether any development costs meet the criteria for capitalisation. This requires various judgements by management as to whether the various criteria have been met.

3 Loss for period from discontinued operations

The loss of £265,000 relates to a warranty issue arising post sale of the Defence UK business to Teledyne. This payment has now been settled and no further exposure is expected.

Notes to the Financial Statements

for the year ended 31 May 2011



4 Segmental analysis

Operating Segments

IFRS 8 requires consideration of the chief operating decision maker ('CODM') within the group. In line with the group's internal reporting framework and management structure, the key strategic and operating decisions are made by the CEO, who reviews internal monthly management reports, budget and forecast information as part of this. Accordingly the CEO is deemed to be the CODM.

Operating segments have then been identified based on the interim reporting information and management structures within the group. The group has two customers representing individually over 10% each and in aggregate over 75% of revenue.

In the period the group acquired the entire share capital of Isotek (Holdings) Limited. Prior to this the group operated within one trading business segment involving the design and manufacture of transceiver modules and filters for backhaul microwave linking of base stations used in wireless telecommunication networks (Broadband). Subsequent to the acquisition the enlarged group is also involved in the design of radio frequency conditioning product for base stations used in wireless telecommunication networks (Basestation). Accordingly the group (continuing operations) now operates within two trading business segments. The group also contains a central services segment that provides support to the trading businesses.

The Defence Electronics business was sold on 15 August 2008 (please refer to note 3).

In the table below reportable segment assets and liabilities include inter segment balances. This has been included to reflect the assets and liabilities of the segment as monies are freely moved around the group to provide funding for working capital where required.

| | Broadband | | Basestation | | Central Services | | Defence Electronics (Discontinued) | | Total | |
|--|--------------|--------------|--------------|--------------|------------------|--------------|------------------------------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| External revenue | 12,136 | 15,575 | 3,387 | – | – | – | – | – | 15,523 | 15,575 |
| Finance income | – | – | – | – | 79 | 113 | – | – | 79 | 113 |
| Depreciation and amortisation | 487 | 601 | 36 | – | – | – | – | – | 523 | 601 |
| Reportable segment loss before exceptional items | (2,463) | 667 | (1,955) | – | (842) | (959) | (265) | – | (5,525) | (292) |
| Reportable segment loss before income tax | (2,584) | 444 | (1,976) | – | (1,232) | (1,461) | (265) | – | (6,057) | (1,017) |
| Reportable segment assets | 7,409 | 7,806 | 6,007 | – | 18,777 | 15,796 | – | – | 32,193 | 23,602 |
| Capital expenditure | 663 | 639 | 263 | – | – | – | – | – | 926 | 639 |
| Reportable segment liabilities | 6,693 | 4,538 | 8,838 | – | 383 | 1,729 | – | – | 15,914 | 6,267 |



Notes to the Financial Statements

for the year ended 31 May 2011

4 Segmental analysis (continued)

Reconciliation of reportable segment revenues, profit or loss, assets and liabilities and other material items

| | 2011 £000 | 2010 £000 |
|--|----------------|----------------|
| Depreciation and amortisation | | |
| Reportable segment totals | 523 | 601 |
| Adjustments/amortisation of intangibles | 1,209 | – |
| Consolidated depreciation and amortisation | <u>1,732</u> | <u>601</u> |
| Loss before taxation | | |
| Total loss for reportable segments | (6,057) | (1,017) |
| Elimination of discontinued operations | 265 | – |
| Group/unallocated | (1,209) | – |
| Consolidated loss before taxation | <u>(7,001)</u> | <u>(1,017)</u> |
| Assets | | |
| Total assets for reportable segments | 32,193 | 23,602 |
| Inter company | (7,255) | (2,551) |
| Group/unallocated | 2,551 | 2,551 |
| Consolidated total assets | <u>27,489</u> | <u>23,602</u> |
| Liabilities | | |
| Total liabilities for reportable segments | 15,914 | 6,267 |
| Inter company | (7,255) | (2,551) |
| Consolidated total liabilities | <u>8,659</u> | <u>3,716</u> |

Notes to the Financial Statements

for the year ended 31 May 2011



4 Segmental analysis (continued)

Geographical information

In presenting information on the basis of geographical segments, segment revenue is based on geographical location of customers. Segment assets are based on the geographical location of the assets.

Revenue by destination

| | 2011 £000 | 2010 £000 |
|-------------------|---------------|---------------|
| United Kingdom | 838 | 35 |
| Europe | 11,256 | 14,451 |
| Americas | 620 | 7 |
| Rest of the world | 2,809 | 1,082 |
| | <u>15,523</u> | <u>15,575</u> |

Split of non-current assets by location

| | 2011 £000 | 2010 £000 |
|----------------|---------------|--------------|
| United Kingdom | 11,611 | 1,998 |
| Americas | 4,204 | – |
| | <u>15,815</u> | <u>1,998</u> |

Non-current assets relate to property, plant and equipment and intangible assets.

Acquisitions in the period

As described in note 37, the Basestation segment was acquired in the year. The Disclosures above show the split of the group income statement (to profit before tax) between acquisitions and the existing business of the group.



Notes to the Financial Statements

for the year ended 31 May 2011

5 Operating loss

| | note | 2011 £000 | 2010 £000 |
|-------------------------------|------|----------------|--------------|
| Continuing operations | | | |
| Revenue | | 15,523 | 15,575 |
| Other operating income | | (326) | (531) |
| Raw materials and consumables | | 10,435 | 7,570 |
| Wages and salaries | | 5,016 | 4,528 |
| Social security costs | | 509 | 450 |
| Pension costs | | 277 | 211 |
| Share-based payments | 32 | 122 | 73 |
| Staff costs | | 5,924 | 5,262 |
| Amortisation of intangibles | | 1,209 | – |
| Depreciation | | 523 | 601 |
| Depreciation and amortisation | | 1,732 | 601 |
| Other operating charges | | 4,838 | 3,807 |
| Operating costs | | 22,603 | 16,709 |
| Operating loss | | (7,080) | (1,134) |

The operating loss is stated after the exceptional items in note 6.

Other operating income represents the amount claimed from Yorkshire Forward towards a research and development programme.

Notes to the Financial Statements

for the year ended 31 May 2011



6 Exceptional items

Operating loss is stated after charging exceptional items as follows:

| | 2011 £000 | 2010 £000 |
|---|--------------|--------------|
| Directors' resignation costs | – | 146 |
| Pension scheme closure costs | – | 116 |
| Acquisition related costs | 694 | 320 |
| Vendor contribution towards acquisition costs | (300) | – |
| Integration costs relating to acquisition | 75 | – |
| Redundancy costs | 142 | 260 |
| | 611 | 842 |

Professional fees were incurred in the acquisition of Isotek (Holdings) Ltd. This includes legal and professional, non-audit and corporate finance fees. The prior year fees include the costs of an opportunity that Filtronic decided not to proceed with.

Under the terms of the Isotek acquisition, the vendor agreed to pay a contribution of £300,000 towards acquisition costs.

As part of the integration of Isotek into the Filtronic group costs have been incurred in harmonising systems and processes with the aim of achieving synergies.

7 Operating items

| | 2011 £000 | 2010 £000 |
|--|--------------|--------------|
| Operating loss is stated after charging: | | |
| Continuing operations: | | |
| Research and development costs | 3,531 | 2,313 |
| Operating lease rentals | 138 | 79 |

8 Auditors' remuneration

The company auditors are KPMG Audit Plc. The auditors' remuneration was as follows:

| | 2011 £000 | 2010 £000 |
|--|--------------|--------------|
| Company auditors: | | |
| Audit of the group and company financial statements | 6 | 7 |
| Company auditors and their associates: | | |
| Audit of subsidiaries financial statements pursuant to legislation | 34 | 18 |
| Other services pursuant to such legislation | 10 | 9 |
| Taxation services | 5 | 7 |
| Other services including acquisitions | 150 | 57 |
| | 205 | 98 |



Notes to the Financial Statements

for the year ended 31 May 2011

9 Employees

The average number of employees comprised:

| | 2011 Number | 2010 Number |
|--------------------------|----------------|----------------|
| Manufacturing | 95 | 105 |
| Research and development | 49 | 31 |
| Sales | 1 | – |
| Administration | 14 | 13 |
| | <u>159</u> | <u>149</u> |

10 Compensation of directors

Details of the remuneration, pension entitlements and share options of the individual directors are set out in the remuneration report on pages 18 to 22. The compensation of the directors was:

| | 2011 £000 | 2010 £000 |
|---|--------------|--------------|
| Salary or fees | 484 | 599 |
| Bonuses | – | 42 |
| Benefits | 26 | 30 |
| Total remuneration excluding pension contributions and share-based payments | <u>510</u> | <u>671</u> |
| Pension contributions | 27 | 24 |
| Share-based payments | 93 | 46 |
| | <u>630</u> | <u>741</u> |

The directors are related parties.

11 Related party transaction

Chief Executive Officer, Hemant Mardia's wife is employed by the group. Her salary, car allowance and pension contributions amounted to £96,000 (2010 £96,000).

Notes to the Financial Statements

for the year ended 31 May 2011



12 Finance income

| | 2011 £000 | 2010 £000 |
|-----------------|--------------|--------------|
| Interest income | <u>79</u> | <u>113</u> |

13 Taxation

The reconciliation of the effective tax rate is as follows:

| | 2011 £000 | 2010 £000 |
|--|-----------------|----------------|
| Loss before taxation | | |
| Continuing operations | <u>(7,001)</u> | <u>(1,021)</u> |
| Loss before taxation | <u>(7,001)</u> | <u>(1,021)</u> |
| | 2011 £000 | 2010 £000 |
| Loss before taxation multiplied by standard rate of corporation tax in the UK | 27% (1,925) | 28% (286) |
| Disallowable items | (2%) 114 | (12%) 108 |
| Non-taxable consolidation adjustment | – – | 13% (130) |
| Depreciation in advance of capital allowances | (2%) 142 | (17%) 178 |
| Defined benefit pension | – – | 3% (26) |
| Pension contributions brought forward utilised | 19% (1,322) | 166% (1,688) |
| Tax losses carried forward | (37%) 2,665 | (181%) 1,843 |
| Taxation | <u>5% (326)</u> | <u>– –</u> |



Notes to the Financial Statements

for the year ended 31 May 2011

14 Loss per share

| | 2011 £000 | Group 2010 £000 |
|--|----------------|-----------------------|
| Loss for the period | | |
| Continuing operations | (6,675) | (1,021) |
| Discontinued operations | (265) | – |
| Loss for the period | (6,940) | (1,021) |
| | 000 | 000 |
| Basic and diluted weighted average number of shares | 92,873 | 74,323 |
| Basic and diluted loss per share | | |
| Continuing operations | (7.19)p | (1.37)p |
| Discontinued operations | (0.29)p | – |
| Basic and diluted loss per share | (7.48)p | (1.37)p |

There was no difference in the weighted average number of shares used for the calculation of basic and diluted loss per share as the effect of all potentially dilutive shares outstanding was anti-dilutive.

Notes to the Financial Statements

for the year ended 31 May 2011



15 Investments in subsidiaries

| | Company Investments in subsidiaries £000 |
|---------------------------------------|---|
| Cost | |
| At 1 June 2009 | 21,639 |
| Dissolved | (11,093) |
| At 31 May 2010 | 10,546 |
| Additions | 10,564 |
| At 31 May 2011 | 21,110 |
| Impairment | |
| At 1 June 2009 | 21,639 |
| Dissolved | (11,093) |
| At 31 May 2010 | 10,546 |
| At 31 May 2011 | 10,546 |
| Carrying amount at 1 June 2009 | — |
| Carrying amount at 31 May 2010 | — |
| Carrying amount at 31 May 2011 | 10,564 |

The company's subsidiaries are related parties.

The subsidiaries at 31 May 2011, which were directly owned by Filtronic plc, were as follows:

| Name of subsidiary | Country of incorporation | Description of equity held | Proportion held | Activity |
|---|--------------------------|----------------------------|-----------------|--|
| Filtronic Broadband Limited | UK | 1p ordinary shares | 100% | Design and manufacture of microwave products for telecommunication systems |
| Filtronic Holdings UK Limited | UK | £1 ordinary shares | 100% | Holding company |
| Isotek (Holdings) Limited | UK | 1p ordinary shares | 100% | Holding company |
| Owned by Isotek (Holdings) Limited: | | | | |
| Isotek Electronics Limited | UK | 1p ordinary shares | 100% | Design and manufacture of Filtronic products for telecommunication systems |
| Isotek Inc | USA | \$1 ordinary shares | 100% | Design and manufacture of Filtronic products for telecommunication systems |
| Isotek Limited | UK | 1p ordinary shares | 100% | Dormant company |
| Owned by Isotek Electronics Limited: | | | | |
| Isotek Hong Kong Holdings Limited | Hong Kong | HK \$1 ordinary shares | 100% | Holding company |



Notes to the Financial Statements

for the year ended 31 May 2011

16 Goodwill and other intangibles

| | Goodwill £000 | Other intangibles (core technology) £000 | Total £000 |
|---------------------------------------|------------------|--|----------------|
| Cost | | | |
| At 1 June 2010 | – | – | – |
| Additions | 3,655 | 10,884 | 14,539 |
| At 31 May 2011 | 3,655 | 10,884 | 14,539 |
| Amortisation | | | |
| At 1 June 2010 | – | – | – |
| Provided in year | – | (1,209) | (1,209) |
| At 31 May 2011 | – | (1,209) | (1,209) |
| Carrying amount at 1 June 2010 | – | – | – |
| Carrying amount at 31 May 2011 | 3,655 | 9,675 | 13,330 |

Goodwill and other intangibles have arisen in the period relating to the acquisition referred to in note 37.

Goodwill is allocated to the Basestation cash generating unit (CGU) and this CGU represents the lowest level within the group at which the goodwill is monitored for internal management purposes, which is not higher than the group's operating segments as reported in note 4. The group tests goodwill annually for impairment or more frequently if there are indications that goodwill may be impaired.

The carrying value of intangible assets and goodwill has been assessed for impairment by reference to its value in use. Value in use was determined by discounting the future cash flows generated from the continuing use of the unit. The calculation of the value in use was based on the following key assumptions:

- Cash flows were projected to 31 May 2013 based on past experience and actual operating results;
- Cash flows for a further 8-year period were extrapolated. A growth factor was not applied to the projections as the value in use exceeded the carrying amounts before any such assumption was applied;
- A pre-tax discount rate of 20% was applied in determining the recoverable amount of the unit, being the estimated weighted average cost of capital.

Based on this testing the directors do not consider any of the goodwill or intangible assets to be impaired even allowing for a reasonable degree of sensitivity to the underlying assumptions, including the discount rate.

Notes to the Financial Statements

for the year ended 31 May 2011



17 Property, plant and equipment

| | Group Plant and equipment £000 |
|---|---|
| Cost | |
| At 1 June 2009 | 6,789 |
| Additions | 639 |
| Disposals | (1,579) |
| At 31 May 2010 | 5,849 |
| Assets acquired through acquisition of Isotek | 260 |
| Additions | 926 |
| Disposals | (115) |
| At 31 May 2011 | 6,920 |
| Depreciation and impairment | |
| At 1 June 2009 | 4,793 |
| Depreciation | 601 |
| Disposals | (1,543) |
| At 31 May 2010 | 3,851 |
| Depreciation of assets acquired through acquisition of Isotek | 157 |
| Depreciation | 523 |
| Disposals | (96) |
| At 31 May 2011 | 4,435 |
| Carrying amount at 1 June 2009 | 1,996 |
| Carrying amount at 31 May 2010 | 1,998 |
| Carrying amount at 31 May 2011 | 2,485 |



Notes to the Financial Statements

for the year ended 31 May 2011

18 Deferred tax

| | Group | | Company | |
|------------------------|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Deferred tax liability | 2,612 | – | – | – |

The deferred tax liability relates to the intangible assets arising upon acquisition. The original liability was £2,938,000 with £326,000 released to the income statement during the year.

Deferred tax classified as current consists of the element that will be recognised as income in the next year. Deferred tax classified as non-current will be released to the income statement over the remaining life.

Deferred tax assets which have not been recognised:

| | Group | | Company | |
|---|---------------|--------------|---------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Depreciation in advance of capital allowances | 1,823 | 1,811 | 507 | 546 |
| Pension contributions carried forward | – | 1,346 | – | 1,346 |
| Tax losses carried forward | 15,431 | 12,065 | 12,666 | 12,065 |
| | 17,254 | 15,222 | 13,173 | 13,957 |

The deferred tax assets have not been recognised where the directors consider that it is unlikely that the underlying temporary differences will reverse in the foreseeable future.

On 23 March 2011 the Chancellor announced the reduction in the main rate of UK corporation tax to 26 per cent with effect from 1 April 2011. This change became substantively enacted on 29 March 2011. The effect of the rate reduction is reflected in the figures above. The Chancellor also proposed changes to further reduce the main rate of corporation tax by one per cent per annum to 23 per cent by 1 April 2014, but these changes have not yet been substantively enacted and therefore are not included in the figures above.

19 Inventories

| | Group | | Company | |
|---|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Raw materials | 897 | 1,403 | – | – |
| Work in progress | 342 | 346 | – | – |
| Finished goods | 438 | 249 | – | – |
| | 1,667 | 1,998 | – | – |
| Inventories are stated net of provision | 1,775 | 1,332 | – | – |

Notes to the Financial Statements

for the year ended 31 May 2011



20 Trade and other receivables

| | Group | | Company | |
|---|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Trade receivables | 4,671 | 2,598 | – | – |
| Group receivables | – | – | 7,255 | 1,373 |
| Other receivables and prepayments | 1,061 | 763 | 557 | 179 |
| Forward foreign exchange contracts | 31 | – | – | – |
| | <u>5,763</u> | <u>3,361</u> | <u>7,812</u> | <u>1,552</u> |
| Trade receivables are stated net of provision | – | – | – | – |

21 Trade and other payables

| | Group | | Company | |
|-----------------------------|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Trade payables | 4,197 | 1,544 | 46 | 6 |
| Group payables | – | – | 2,551 | 2,551 |
| Other payables and accruals | 1,288 | 1,342 | 337 | 545 |
| | <u>5,485</u> | <u>2,886</u> | <u>2,934</u> | <u>3,102</u> |

22 Deferred income

Deferred income classified as current consists of a capital grant made by a customer that will be recognised as income in the next year. Deferred income classified as non-current consists of the non-current portion that will be released to the income statement over the life of the asset.

23 Provision

| | Group | | Company | |
|---|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Warranty provision | | | | |
| Opening balance | 706 | 1,314 | – | – |
| Provision acquired through Isotek acquisition | 40 | – | – | – |
| Used during the year | (44) | (285) | – | – |
| Released unused during the year | (441) | (542) | – | – |
| Charge for the year | 176 | 219 | – | – |
| Closing balance | <u>437</u> | <u>706</u> | <u>–</u> | <u>–</u> |

24 Pension costs

| | Group | | Company | |
|------------------------------|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Defined contribution schemes | <u>277</u> | <u>211</u> | <u>14</u> | <u>15</u> |



Notes to the Financial Statements

for the year ended 31 May 2011

25 Share capital

| | Group and Company | |
|-----------------------|---------------------------------|--------------|
| | Ordinary shares of 10p each | |
| | Issued and fully paid Number | £000 |
| At 1 June 2009 | 74,323,093 | 7,432 |
| At 1 June 2010 | 74,323,093 | 7,432 |
| Shares issued in year | 18,550,000 | 1,855 |
| At 31 May 2011 | 92,873,093 | 9,287 |

Holders of the ordinary shares are entitled to receive dividends when declared, and are entitled to one vote per share at meetings of the company.

The group issued 18.55m shares of nominal value 10p in part consideration for the entire share capital of Isotek Holdings Limited.

In compliance with the Companies Act 2006 the company has adopted articles of association that has dispensed with the requirement for authorised share capital.

26 Share premium

| | Group and Company |
|------------------------|----------------------|
| At 1 June 2010 | – |
| Premium on share issue | 5,008 |
| Share issue costs | (325) |
| At 31 May 2011 | 4,683 |

The shares issued as part of the consideration of Isotek (Holdings) Ltd were issued at a premium of 27p reflecting the market value of the shares at the date of acquisition net of issue costs of £325,000.

27 Translation reserve

| | Group £000 |
|--|---------------|
| At 1 June 2010 | – |
| Currency translation movement arising on consolidation | (32) |
| At 31 May 2011 | (32) |

Notes to the Financial Statements

for the year ended 31 May 2011



28 Dividends

The dividends recognised in equity and paid during the year were as follows:

| | | Group and Company | |
|--|-----------|----------------------|--------------|
| | Per share | 2011 £000 | 2010 £000 |
| Annual dividend year ended 31 May 2009 | 1.00p | – | 743 |
| Annual dividend year ended 31 May 2010 | 1.00p | 743 | – |
| | | <u>743</u> | <u>743</u> |

The directors are not proposing to pay a dividend for the year ended 31 May 2011.

29 Retained earnings

| | Group £000 | Company £000 |
|-----------------------|---------------------|---------------------|
| At 1 June 2009 | 14,144 | 9,251 |
| Loss for the period | (1,021) | (1,929) |
| Share-based payments | 73 | 55 |
| Dividends | (743) | (743) |
| At 31 May 2010 | 12,453 | 6,634 |
| Loss for the period | (6,940) | (1,557) |
| Share-based payments | 122 | 91 |
| Dividends | (743) | (743) |
| At 31 May 2011 | <u>4,892</u> | <u>4,425</u> |



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for the year ended 31 May 2011

30 Share options

There are two sharesave plans that have been offered to employees. Under both plans employees who join the plan save up to £250 per month for three years. The members of the plan were granted a number of share options based on the amount they would save over the three years. At the end of the three years the members have a six month period in which they can exercise the share options. The exercise price for an option was the middle market quotation of Filtronic plc's ordinary shares as derived from the Official List of the United Kingdom Financial Services Authority on the dealing day immediately prior to the plan offer date.

Sharesave Plan – Scheme 1

| | Weighted average exercise price | Number of options | Weighted average exercise price | Number of options |
|--|--|----------------------|--|----------------------|
| | 2011 | 2011 | 2010 | 2010 |
| Outstanding at the beginning of the period | 25p | 615,450 | 25p | 857,100 |
| Granted during the period | 25p | – | 25p | – |
| Cancelled during the period | 25p | (82,350) | 25p | (241,650) |
| Outstanding at the end of the period | 25p | <u>533,100</u> | 25p | <u>615,450</u> |
| Exercisable at the end of the period | | <u>–</u> | – | <u>–</u> |

The first sharesave plan was offered to employees in February 2009.

The options outstanding at 31 May 2011 for Scheme 1 have a weighted average remaining contractual life of 1.3 years.

The share options granted under this scheme have an exercise price of 25p and have an exercise period from 1 April 2012 to October 2012.

Sharesave Plan – Scheme 2

| | Weighted average exercise price | Number of options |
|--|--|----------------------|
| | 2011 | 2011 |
| Outstanding at the beginning of the period | 34.2p | – |
| Granted during the period | 34.2p | 321,981 |
| Cancelled during the period | 34.2p | (34,208) |
| Outstanding at the end of the period | 34.2p | <u>287,773</u> |
| Exercisable at the end of the period | | <u>–</u> |

The second sharesave plan was offered to employees in November 2010.

The options outstanding at 31 May 2011 for Scheme 2 have a weighted average remaining contractual life of 2.9 years.

The share options granted during the year to May 2011 have an exercise price of 34.2p and have an exercise period from 1 November 2013 to 30 April 2014.

Notes to the Financial Statements

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31 Share awards

| | Number of share awards 2011 | Number of share awards 2010 |
|--|-----------------------------------|-----------------------------------|
| Performance Share Plan | | |
| Outstanding at the beginning of the period | 569,388 | – |
| Awarded during the period | 497,709 | 569,388 |
| Outstanding at the end of the period | 1,067,097 | 569,388 |

The share awards awarded during the year to 31 May 2010 have a weighted average remaining contractual life of 1.2 years.

The share awards awarded during the year to 31 May 2011 have a weighted average remaining contractual life of 2.5 years.

Under the plan in the year to 31 May 2010 share awards were made to executive directors and senior managers. The vesting of the awards is subject to performance targets based on growth in earnings per share (EPS) over a three year period. If growth in EPS exceeds growth in the Retail Price Index (RPI) by 3% per year (on a compound basis) then 25% of the awarded shares will vest. If growth in EPS exceeds growth in RPI by 10% per year (on a compound basis) then 100% of the awarded shares will vest. If growth in EPS falls between these two targets, then the awarded shares will vest on a sliding scale between 25% and 100% of the awarded shares.

Under the plan in the year to 31 May 2011 further share awards were made to executive directors and senior managers. The vesting of the share awards is subject to performance targets based on growth in earnings per share (EPS) over a three year period. If EPS grows such that for the year to 31 May 2013 it exceeds a figure corresponding to £5.5m of earnings before intangible amortisation, exceptionals, interest and tax, then 25% of the awarded shares will vest. If EPS grows such that for the year to 31 May 2013 it exceeds a figure corresponding to £7.0m of earnings before intangible amortisation, exceptionals, interest and tax, then 100% of the awarded shares will vest. If EPS grows to be between these two targets then the awarded shares will vest on a sliding scale between 25% and 100% of the awarded shares.

32 Share-based payments

| | Group | | Company | |
|-----------------------|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Share options expense | 34 | 19 | 3 | 1 |
| Share awards expense | 88 | 54 | 88 | 54 |
| | <u>122</u> | <u>73</u> | <u>91</u> | <u>55</u> |

The share options expense was the fair value of the share options at the date of grant spread over the expected vesting period of the share options. The fair value of the share options at the date of grant was measured using the Black-Scholes model.



Notes to the Financial Statements

for the year ended 31 May 2011

32 Share-based payments (continued)

The inputs to the Black-Scholes model and the weighted average fair value of the share options granted during the year were as follows:

| | Group | | Company | |
|---------------------------------|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Number of share options granted | 321,981 | – | 30,736 | – |
| Weighted average share price | 38p | – | 38p | – |
| Weighted average exercise price | 34.2p | – | 34.2p | – |
| Expected volatility | 60% | – | 60% | – |
| Expected life | 3.1 years | – | 3.1 years | – |
| Risk free interest rate | 3% | – | 3% | – |
| Weighted average fair value | 12p | – | 12p | – |

Expected volatility is the estimate of the volatility of the share price over the expected life of the share options.

The share awards expense was the fair value of the share awards at the date of award spread over the expected vesting period of the share awards. The fair value of the share awards at the date of award was the market price of the shares on that day.

The fair value of the share awards awarded during the year were as follows:

| | Group | | Company | |
|--------------------------------|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Number of share awards awarded | 497,709 | 569,388 | 157,944 | 154,411 |
| Weighted average share price | 32p | 34p | 32p | 36p |
| Expected life | 3.0 years | 3.0 years | 3.0 years | 3.0 years |
| Weighted average fair value | 32p | 34p | 32p | 36p |

33 Operating lease commitments

At the balance sheet date there were commitments for lease payments under non-cancellable operating leases, which fall due as follows:

| | Group | | Company | |
|----------------------------|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Less than one year | 149 | 159 | 110 | 105 |
| Between one and five years | 219 | 324 | 190 | 280 |
| | 368 | 483 | 300 | 385 |

Operating leases are for land and buildings and motor vehicles and the lease terms are for periods of one to three years.

Notes to the Financial Statements

for the year ended 31 May 2011



34 Capital expenditure commitments

| | Group | | Company | |
|---|--------------|--------------|--------------|--------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Capital expenditure contracted for at the balance sheet date but not provided in the financial statements | <u>284</u> | <u>165</u> | <u>-</u> | <u>-</u> |

35 Note to the consolidated cash flow statement

| | | Group | |
|---|------|----------------|----------------|
| | note | 2011 £000 | 2010 £000 |
| Operating loss | | | |
| Continuing operations | | <u>(7,080)</u> | <u>(1,134)</u> |
| Net cash (used in)/from operating activities | | | |
| Continuing operations | | <u>(4,371)</u> | <u>1,926</u> |
| Net cash used in investing activities | | | |
| Continuing operations | | <u>(6,714)</u> | <u>(526)</u> |
| Sale of discontinued operations | 36 | <u>(265)</u> | <u>(635)</u> |
| | | <u>(6,979)</u> | <u>(1,161)</u> |
| Net cash used in financing activities | | | |
| Continuing operations | | <u>(743)</u> | <u>(743)</u> |

36 Net cash from sale of discontinued operations

| | | Group | |
|-------------------------|--|--------------|--------------|
| | | 2011 £000 | 2010 £000 |
| Tax paid | | - | (635) |
| Historic warranty claim | | <u>(265)</u> | <u>-</u> |
| | | <u>(265)</u> | <u>(635)</u> |



Notes to the Financial Statements

for the year ended 31 May 2011

37 Acquisition in year

On 16 November 2010 Filtronic acquired the share capital of Isotek (Holdings) Limited ("Isotek"). Isotek employs approximately 51 staff predominantly in the United Kingdom and in the United States, and develops and markets leading edge telecoms products for a range of wireless infrastructure telecoms applications.

The consideration is made up of:

| | £000 |
|--|---------------|
| Share consideration (18,550,000) at completion date market value | 6,864 |
| Cash consideration | 4,230 |
| Total consideration for Isotek | 11,094 |
| Estimated working capital adjustment to consideration | (530) |
| Estimated final consideration for Isotek | 10,564 |

As at 31 May 2011 the fair value of the acquired assets, liabilities and goodwill has been determined on a provisional basis pending finalisation of the working capital adjustment.

The Offer to Isotek shareholders included an adjustment to consideration based on the level of working capital and net cash on the date of acquisition. The estimate above is based upon the working capital data included in the Isotek companies opening balance sheets used to prepare these accounts but cannot be final until the working capital adjustment is agreed.

There were no significant fair value adjustments arising on the acquisition other than the recognition of intangible assets and deferred tax noted below.

The goodwill arising on the acquisition relates to the skills and talents of the acquired business workforce and the benefits of future market expansion. These benefits are not recognised separately from goodwill as the future economic benefits arising cannot be reliably measured.

Intangibles relating to the core technology and know-how are being amortised over a period of 4.5 years.

Since the acquisition Isotek has carried revenues of £3.4m, and has made losses from operations of £2.0m excluding exceptional items and amortisation.

| | Book value pre acquisition £000 | Fair value adjustments £000 | Fair value of net assets £000 |
|---|--|--|--|
| Intangibles on acquisition | – | 10,884 | 10,884 |
| Deferred tax liability | – | (2,939) | (2,939) |
| Tangible fixed assets | 105 | – | 105 |
| Current assets | 2,573 | (20) | 2,553 |
| Current liabilities | (3,585) | (109) | (3,694) |
| | (907) | 7,816 | 6,909 |
| Goodwill arising on acquisition | | | 3,655 |
| Total consideration (as above) | | | 10,564 |
| Non-cash consideration (shares issued and provisional working capital adjustment) | | | (6,334) |
| Cash (acquired) | | | (68) |
| Net cash outflow | | | 4,162 |

Notes to the Financial Statements

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37 Acquisition in period (continued)

The following summary presents the group as if Isotek was acquired on 1 June 2010. The amounts include the results of the acquired business but do not include any exceptional items or any amortisation of separately identified intangibles, which are being amortised over 4.5 years. In addition the amounts do not include any possible synergies from the acquisition. The results of the acquired companies for the period before acquisition have not been adjusted to reflect Filtronic accounting policies nor to reflect fair value adjustments made on acquisition. The information is provided for illustrative purposes only and does not necessarily reflect the actual results that would have occurred, nor is it necessarily indicative of the future results of the combined entities.

| | Pro forma group £000 |
|---|----------------------------|
| Revenue | 16,646 |
| Loss before tax, amortisation and exceptional items | (6,755) |

38 Financial instruments

Fair value

The carrying amount of all the financial assets and liabilities approximate to their fair value as described below.

Cash and cash equivalents comprise bank balances and bank deposits with a maturity of three months or less.

Trade and other receivables are all receivable in less than one year. Trade receivables are generally receivable within 90 days.

Trade and other payables are all payable in less than one year. Trade payables are generally payable within 90 days.

Liquidity risk

The group and company hold significant cash balances and have no debt. Cash is held on bank deposit for varying periods from overnight to six months to ensure all liabilities can be met as they fall due. The amount of the cash balances results in liquidity risk being very low.

Credit risk

The exposure to credit risk is limited to the carrying amount of cash and cash equivalents and trade and other receivables in the balance sheet as follows:

| | Group | | Company | |
|-----------------------------|--------------|---------------|---------------|---------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Cash and cash equivalents | 4,120 | 16,245 | 2,953 | 15,616 |
| Trade and other receivables | 5,763 | 3,361 | 7,812 | 1,552 |
| | <u>9,883</u> | <u>19,606</u> | <u>10,765</u> | <u>17,168</u> |



Notes to the Financial Statements

for the year ended 31 May 2011

38 Financial instruments (continued)

The cash and cash equivalents in the balance sheet were on deposit with large banks with high credit ratings as follows:

| | Group | | Company | |
|-----------------|--------------|---------------|--------------|---------------|
| | 2011 £000 | 2010 £000 | 2011 £000 | 2010 £000 |
| Barclays Bank | 3,312 | 11,245 | 2,413 | 10,616 |
| Santander Bank | 540 | 5,000 | 540 | 5,000 |
| Bank of America | 227 | – | – | – |
| HSBC | 41 | – | – | – |
| | <u>4,120</u> | <u>16,245</u> | <u>2,953</u> | <u>15,616</u> |

The credit risk related to cash and cash equivalents is considered to be low due to the banks being large with high credit ratings.

Credit risk is primarily related to trade receivables. The group's businesses are concentrated on long term relationships with a small number of larger and long established original equipment manufacturers. Overdue receivables are regularly monitored and appropriate action is taken to collect payment. The group has historically incurred only low levels of unrecoverable receivables. Therefore credit risk is considered to be low.

The company has no trade receivables.

Trade receivables included the following amounts for the group's largest customers.

| | Group | |
|-----------------|--------------|--------------|
| | 2011 £000 | 2010 £000 |
| Customer one | 2,147 | 2,154 |
| Customer two | 1,481 | – |
| Customer three | 222 | – |
| Other customers | 821 | 444 |
| | <u>4,671</u> | <u>2,598</u> |

The age of trade receivables that have not been provided for was as follows:

| | Group | |
|---------------------------------|--------------|--------------|
| | 2011 £000 | 2010 £000 |
| Not past due | 4,609 | 2,515 |
| Past due less than three months | 62 | 83 |
| | <u>4,671</u> | <u>2,598</u> |

The age of trade receivables that have been provided for was as follows:

| | Group | |
|---------------------------------|--------------|--------------|
| | 2011 £000 | 2010 £000 |
| Past due less than three months | – | – |

Notes to the Financial Statements

for the year ended 31 May 2011



38 Financial instruments (continued)

The movement in the provision for doubtful trade receivables was as follows:

| | 2011 £000 | Group 2010 £000 |
|------------------------|--------------|-----------------------|
| Opening balance | - | 15 |
| Release for the year | - | (15) |
| Closing balance | - | - |

Interest rate risk

Cash is held on short term bank deposits which earn interest at variable money market deposit rates. At 31 May 2011 £1,986,000 was held in Barclays on short term deposit; £1,000,000 with an interest rate of 1.25% and £986,000 with an interest rate of 0.7%. A further £540,000 was held in Santander on short term deposit with an interest rate of 1.25%. Sterling interest rates are very low and therefore interest rate risk is considered to be low.

The interest rate sensitivity of the expected annual interest income assuming a balance on deposit of £2,500,000 is as follows:

| Interest rate | Expected annual interest income £000 |
|---------------|---|
| 1.5% | 38 |
| 1.0% | 25 |
| 0.5% | 13 |

Foreign currency risk

The group's and company's reporting currency is sterling, which is also the company's functional currency. The functional currencies of the subsidiaries are sterling and US dollar.

The group's results and financial position are affected by fluctuations in foreign currency exchange rates.

The group generates a surplus of US dollars as most customers are now invoiced in US dollars. The nature of the group's businesses means that there is limited visibility of future revenues in US dollars. Therefore when forward foreign exchange contracts are used to reduce the currency risk on the surplus currency expected to be generated, they are usually only for short term periods of no more than six months. If sterling were to strengthen significantly this could materially reduce the group's revenue and operating result.

Forward foreign exchange contracts may also be used to reduce the foreign currency risk on other transactions.

At 31 May 2011 there were three outstanding forward foreign exchange contracts.

Nearly all cash is held in sterling.



Notes to the Financial Statements

for the year ended 31 May 2011

38 Financial instruments (continued)

The group's exposure to foreign currency risk for cash and cash equivalents, trade receivables and trade payables was as follows:

| | Group | | | | | |
|---------------------------|-------------|---------------------|-------------|-------------|---------------------|-------------|
| | EUR £000 | 2011 SEK £000 | USD £000 | EUR £000 | 2010 SEK £000 | USD £000 |
| Cash and cash equivalents | 446 | – | 659 | 535 | 82 | – |
| Trade receivables | 143 | – | 4,358 | 405 | 9 | 5 |
| Trade payables | (425) | – | (4,057) | (392) | – | (57) |
| Net exposure | 164 | – | 960 | 548 | 91 | (52) |

The sensitivity of the group operating profit from continuing operations to US dollars to sterling exchange rate, assuming all other variables remain constant, is as follows:

If the US dollar had been one per cent stronger/weaker against sterling throughout the year ended 31 May 2011 then the group operating profit from continuing operations would have been £46,000 higher/lower.

The company has no significant exposure to foreign currency risk.

Capital management

The group's and company's capital is the total equity which comprises ordinary share capital and retained earnings. The group and company have no debt or undrawn debt facilities. At 31 May 2011 the group had a cash balance of £4,120,000 and the company had a cash balance of £2,953,000. The group and company have sufficient cash to cover working capital requirements and capital expenditure plans.

The group's objectives when managing capital are to safeguard the group's ability to continue as a going concern in order to provide future returns for shareholders.

39 Forward-looking statements

Certain statements in this annual report are forward-looking. Where the annual report includes forward-looking statements, these are made by the directors in good faith based on the information available to them at the time of their approval of this report. Such statements are based on current expectations and are subject to a number of risks and uncertainties, including both economic and business risk factors that could cause actual events or results to differ materially from any expected future events or results referred to in these forward-looking statements. Unless otherwise required by applicable law, regulation or accounting standard, the group undertakes no obligation to update any forward-looking statements whether as a result of new information, future events or otherwise.



Annual General Meeting

The Annual General Meeting of Filtronic plc will be held at Pinsent Masons LLP, 1 Park Row, Leeds LS1 5AB on Friday 23 September 2011 at 11.00 am. The notice of meeting, together with details of business to be conducted at the meeting and a form of proxy, is being circulated to shareholders with this report.

Financial calendar

Provisional dates for the announcement of results:

Interim results to 30 November 2011

30 January 2012

Final results to 31 May 2012

30 July 2012

Website

The company's website address is www.filtronic.co.uk

The website includes company news and investor sections. The annual and half-yearly reports of the company can be downloaded from the website. The company's share price is also available on the website.

Shareholder enquiries and change of address

Shareholders should direct all enquiries regarding their shareholdings and notification of change of address to the company's registrars:

Capita Registrars
The Registry
34 Beckenham Road
Beckenham
Kent
BR3 4TU
Tel: 0870 162 3100

Capita Registrars also provide a range of online shareholder services at www.capitashareportal.com which shareholders may find useful.

**Company secretary**

M Moynihan

Company number

2891064

Registered office

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Registrars

Capita Registrars
The Registry
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Beckenham
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