



Meeting the growing global demand for mobile telecoms infrastructure

**Filtronic plc**

Annual report and accounts  
for the year ended 31 May 2014  
Stock code: FTC

[www.filtronic.com](http://www.filtronic.com)





# Welcome to Filtronic plc

**Filtronic plc is a world leader in the design and manufacture of a broad range of customised RF, microwave and millimetre-wave components and subsystems.**

**The company's products are used in mobile wireless communication equipment, point-to-point communication systems and adjacent defence sectors.**

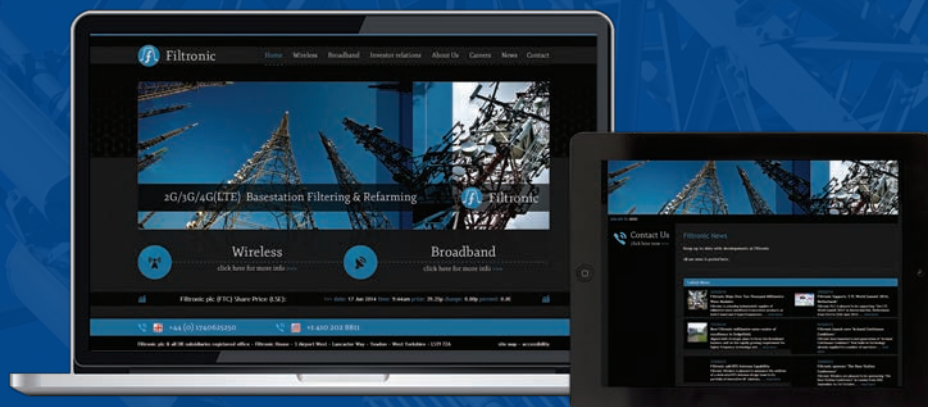
**Filtronic's customers include leading international original equipment manufacturers (OEMs) as well as a wide range of mobile phone network operators.**

Filtronic's strategic objective is to become one of the world's leading RF electronics subsystems companies in the wireless infrastructure sector by utilising its proprietary technologies and engineering expertise and applying them to markets that offer opportunities for significant, sustainable rates of growth and shareholder return. Filtronic addresses these opportunities by designing and supplying sophisticated and customised RF filter and microwave subsystems, antennas and millimetric transceiver products to customers' requirements and by continuing to develop and support its global relationships with these customers.

The group's operations include two separately reported trading business segments: Broadband (which has been transitioned from the traditional point to point (PTP) backhaul business) and Wireless.

Filtronic Broadband is an established leading designer and manufacturer to the OEM mobile telecommunications industry for millimetre-wave products as well as providing build to print manufacturing and testing services for microwave and millimetre-wave products at its state of the art highly automated UK facility. The product range includes transceiver modules and multi-chip, surface mountable transceiver packages at microwave, E-band and V-band frequencies.

Filtronic Wireless is a world leader in the design and manufacture of RF filters, combiners, tower mounted amplifiers (TMAs), microwave subsystems, and Ultra Wide Band (UWB) antennas for the mobile telecommunications industry focusing on equipment for OEMs and network operators.





# Contents

## Strategic Report

Glossary	02
Financial highlights	04
Operational highlights	04
Chairman's letter	05
Chief executive's statement	06
Market overview	08
Objective and strategy	12
Our business model	14
Financial review	16
Key performance indicators	17
Risk management	18
Corporate responsibility report	20

## Governance Report

Introductory letter from the chairman of the board on the governance report	24
Governance framework: board and committees, membership, remit and activities	25
Statement of compliance with the 2012 UK corporate governance code (the "Code")	27
Audit committee report	28
Nominations committee report	30
Directors' remuneration report	31
Directors' report	43

## Financials

Independent auditor's report to the members of Filtronic plc only	46
Consolidated income statement	48
Consolidated statement of comprehensive income	49
Consolidated balance sheet	50
Consolidated statement of changes in equity	51
Company statement of changes in equity	51
Consolidated cash flow statement	52
Company balance sheet	53
Company cash flow statement	54
Notes to the financial statements	55

## Shareholder Information 81

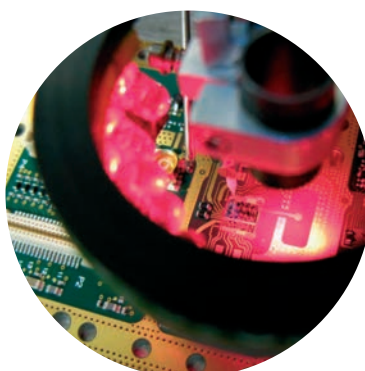
# What's inside:



## 05

### Chairman's letter

Investment in the 4G equipment infrastructure market continues to grow and offer significant opportunities for both Wireless and Broadband.



## 06

### Chief executive's statement

The next few years will see a continuance of increased demand for data with operators looking to differentiate themselves by offering seamless coverage and improvements in quality of service.



## 12

### Objective and strategy

Our objective is to be a major supplier of RF and microwave products to the global telecommunications equipment infrastructure market.



## 14

### Our business model

Our business model has been developed around close working relationships with both our customers and suppliers to maintain a dialogue at multiple levels to cover all aspects of the business.



# Glossary

<b>3G:</b>	3rd generation mobile networks
<b>4G:</b>	4th generation mobile networks
<b>5G:</b>	5th generation mobile networks
<b>CDMA:</b>	Code Division Multiple Access
<b>Cloud RAN:</b>	Cloud radio access network, a new cellular network architecture
<b>dBm:</b>	an abbreviation for the power ratio in decibels (dB) of the measured power referenced to one milliwatt (mW)
<b>Diplexer:</b>	A diplexer is a passive device that implements frequency domain multiplexing.
<b>E-band:</b>	71 GHz to 86 GHz
<b>EDGE:</b>	Enhanced Data Rates for Global Evolution
<b>Gbit/s:</b>	Gigabit per second
<b>GHz:</b>	Gigahertz $10^9$ Hertz
<b>Gigabit:</b>	$10^9$ bits
<b>GSM:</b>	Global System for Mobile Communications
<b>HSPA:</b>	High Speed Packet Access
<b>Hz:</b>	the international standard symbol for Hertz, the unit of frequency
<b>LTE:</b>	Long Term Evolution
<b>MHz:</b>	$10^6$ Hertz
<b>MMIC:</b>	Monolithic Microwave Integrated Circuit
<b>Mobile PC:</b>	Defined as laptop or desktop PC devices with built-in cellular modem or external USB dongle
<b>Mobile router:</b>	A device with a cellular network connection to the internet and Wi-Fi or ethernet connection to one or several clients (such as PCs or tablets)
<b>Multiplexing:</b>	A method by which multiple analogue message signals or digital data streams are combined into one signal over a shared medium.
<b>OEM:</b>	Original Equipment Manufacturer
<b>OFCOM:</b>	The Office of Communications; the government approved regulatory and competition authority for the broadcasting, telecommunications and postal industries of the United Kingdom.
<b>PetaByte:</b>	$10^{15}$ bytes
<b>RAN:</b>	Remote Access Radio
<b>RF:</b>	Radio Frequency, a rate of oscillation in the range of around 3 kHz to 300 GHz
<b>Smartphone:</b>	Mobile phones with data processing capabilities, e.g. iPhones, Android OS phones, Windows phones but also Symbian and Blackberry OS
<b>TMA:</b>	Tower Mounted Amplifier
<b>UWB:</b>	Ultra Wide Band
<b>V-band:</b>	57 GHz to 66 GHz
<b>WCDMA:</b>	Wideband Code Division Multiple Access



# Strategic report

A photograph of a person standing in a large anechoic chamber, working on a large antenna system. The chamber's walls, floor, and ceiling are covered in dark, pyramid-shaped electromagnetic absorbers designed to eliminate reflections. The person is positioned in the center-right of the frame, facing away from the camera towards the antenna. The antenna is a complex structure with a long, vertical, white cylindrical component at the top, mounted on a blue and silver mechanical base. The lighting is dramatic, with a strong light source from above creating highlights on the absorbers and the antenna.

Pictured: Filtronic antenna test range, Täby, Sweden



# Strategic report

## Financial highlights

	2014	2013
Sales revenue	<b>£32.9m</b>	£40.0m
Operating (loss)/profit (before amortisation and exceptional items)	<b>(£0.4m)</b>	£3.1m
(Loss)/profit before taxation	<b>(£3.7m)</b>	£0.2m
Basic (loss)/earnings per share	<b>(2.90p)</b>	0.29p
Diluted (loss)/earnings per share	<b>(2.90p)</b>	0.29p
Net cash balance as at 31 May	<b>£2.5m</b>	£1.9m
Cash in/(out) flow from operating activities	<b>£1.6m</b>	(£0.3m)

## Operational highlights

- Acquired antenna capability which has subsequently achieved four design wins for antennas that are expected to generate revenue in FY2015.
- Successfully increased the number of OEM customers in both Broadband and Wireless.
- Broadband completed move to a new facility at North East Technology Park, Sedgefield, County Durham reducing Broadband's fixed cost base.
- Introduced a new Filtronic designed high power MMIC Amplifier for use on E-band platform.
- Successfully completed customer trial of an E-band transceiver to achieve 1 Gbit/s in 250MHz RF channel with output power of 16dBm.



Pictured: Reconfigurable notch filter

# Chairman's letter

The year ended 31 May 2014 (FY2014) was an important developmental year for Filtronic. The group saw the introduction of several new products and was involved in a number of custom projects which have led to design wins with both original equipment manufacturers (OEMs) and network operators. Disappointingly, sales revenue reduced to £32.9m (2013: £40.0m) with an operating loss before exceptional items and the amortisation of intangibles of £0.4m (2013: £3.1m). The reduction in sales revenue and profit resulted from the conclusion of a significant project to deliver 4G (LTE) interference mitigation filters, which completed in the first half of FY2014, and a longer lead time for expected contracts from new design wins with OEMs.

Sales revenue in the Wireless business was £23.2m (2013: £31.9m) and £9.7m (2013: £8.1m) for the Broadband business. Operating profit before exceptional items and intangible amortisation was split between Wireless £2.6m profit (2013: £6.4m profit), Broadband £2.3m loss (2013: £2.4m loss) and central costs of £0.8m (2013: £0.9m). Net cash at 31 May 2014 was £2.5m compared with £1.9m; the increase in net cash resulted from the unwinding of working capital associated with projects at the previous year end and the improving shipments and lower inventory holding in Broadband.

## Wireless business

During FY2014 the Wireless business worked with a number of OEMs and operators to develop customised products, including various innovative filters, switchable filters, combiners and antennas to support the roll-out of LTE. A number of these projects have led to design wins that are anticipated to enter production in 2015/16.

In September 2013, the business acquired certain antenna assets and with the recruitment of an engineering team, predominantly located in Sweden, the group has developed a capability to design and manufacture the next generation of ultra wideband (UWB) antennas that cover existing and yet to be released frequency spectrum. We are pleased to report that design wins at four customers have been achieved for antennas and these are anticipated to be revenue-generating in the second half of FY2015.

The increased market complexity resulting from 4G LTE and the need for a heterogeneous network has resulted in a far more complex technology landscape. It is expected that OEMs will take an ever increasing role in the development of integrated equipment which may in the longer term reduce the number of operator specific projects available to Filtronic and further underscores the rationale of Filtronic working more closely with OEMs.

## Broadband business

Sales revenues from E-band and V-band backhaul transceiver modules have increased through the year and are replacing lower margin, legacy product. Sales in the year included a last time buy of materials of £2.5m at cost by a long term customer to service their potential requirements until 2017, which suppressed the profit (as a percentage of sales) for Broadband. The current E-band transceiver modules are predominantly for 'carrier grade' mobile backhaul required by larger global operators to connect base stations into the mobile communications network. The V-band product is primarily used in enterprise solutions and 'small cell' opportunities. The business also won contracts for the supply of microwave devices used in phased array radars in the military aerospace market.

Broadband successfully relocated its operations to a new location at North East Technology Park (NETPark) in County Durham. The relocation has enabled the business to reduce its fixed costs and focus its manufacturing capabilities to its core competencies. The increased sales revenue and lower overheads resulted in a reduced operating loss for the year and at the conclusion of the period the business attained profitability on a monthly run rate basis.

## Dividend

The board does not recommend a dividend for 2014 (2013: nil).

## Board of directors

Mike Brennan left the board in April 2014 and Rob Smith was appointed as chief financial officer and director subsequent to the year end.

## Outlook

Investment in the 4G equipment infrastructure market continues to grow and offer significant opportunities for both Wireless and Broadband. The number, scale and quality of new opportunities continues to be strong and whilst the timing and volume of contracts from design wins remains uncertain, we expect Wireless to return to growth and with the upturn we have seen in Broadband the board is confident about the prospects for the business.

Finally, I should like to thank all staff in the business for their contribution over the past year and our shareholders for their patience as we continue to position the business to take advantage of the significant market growth forecast over the next several years.

## Howard Ford

Chairman

14 August 2014

# Chief executive's statement

## Summary of year performance

Over the previous few years Filtronic has supplied custom Wireless product to a number of operator projects. These projects included combiners, tuneable filters and LTE mitigation filters that resulted in a rapid growth in sales in FY2013.

The sales revenue from these projects has been tremendously beneficial for the group and has allowed us the time and resources to develop and expand our product offering and now, with the addition of tower mounted amplifiers and ultra wideband (UWB) antennas, we are able to target the OEMs with a more complete product range to establish a more stable underlying base level of business.

In Broadband it has enabled the company to transition away from low margin legacy products and concentrate its efforts on the supply of transceiver modules to the E-band and V-band markets.

However, as these projects came to their natural conclusion and follow on projects were delayed, sales revenue and operating profit receded in the second half of FY2014. In Wireless, it was our expectation that the take up of potential new projects would coincide with the conclusion of some of the operator projects. Unfortunately, this has not been the case and consequently the sales revenue in Wireless was lower than the previous year.

**£23.2m**

Wireless sales revenue.  
(2013: £31.8m)

**£9.7m**

Broadband sales revenue.  
(2013: £8.1m)

## Wireless performance

In the year, Wireless achieved sales revenue of £23.2m (2013: £31.9m) and a profit of £2.6m (2013: £6.4m).

With customer expectations demanding a seamless user experience in a heterogeneous network, where all network layers need to be integrated together to an unprecedented degree, it is our belief that integrated systems of this complexity can only be satisfied by the major OEMs. It is this market dynamic that has increased our desire to access more OEM programmes.

In line with this desire we have now achieved a significant number of design wins at key OEMs and expect these to enter production through FY2015. Our decision to prioritise OEM activity is key to providing the business with a more stable and sustainable growth pattern. Whilst we expect to be involved in several operator projects we see these as being incremental to the base OEM programmes in the longer term.

As stated in the chairman's letter, we have established an antenna business near Stockholm in Sweden. The antenna assets acquired included both compact and spherical near field antenna measurement ranges and the latest electrical and mechanical modelling tools which will enable Wireless to design and manufacture a range of UWB antennas for the mobile infrastructure market. The addition of antennas to the Filtronic product portfolio enables Wireless to combine a number of its existing technologies into a system level offering that is relevant to the future system requirements of our customers. We are pleased to report that design wins at four customers have been achieved for antennas and these are anticipated to be revenue-generating in the second half of FY2015.

## Broadband performance

In the year, Broadband achieved sales revenue of £9.7m (2013: £8.1m) and a £2.3m loss (2013: £2.4m loss). Sales in the year included £2.5m of materials supplied to a customer to cover future production needs.

As the business developed, Broadband has been focused on its capability to design, manufacture and supply E-band and V-band transceiver modules. The E-band modules are required for 'carrier grade' backhaul applications to connect high capacity base stations into the network. As network density increases with ever higher capacities, backhaul becomes more critical to avoid creating problems. The V-band transceiver modules are primarily for enterprise and small cell applications.

Our new products are at the leading edge of what is currently technically achievable and during FY2014 we have been improving our production processes and product designs to improve yield and capacity. By the end of the year, yields and output had considerably improved and the business achieved a profitable monthly run rate. The demand for E-band and



V-band products is growing and we are embedded in a number of OEM programmes which are at the early stage of market development. In the year we delivered the 10,000th millimetre-wave module and successfully completed a customer trial which achieved 1 Gbit/s in a 250MHz RF channel with an output power of 16dBm.

In addition to E-band and V-band, Filtronic Broadband continues to supply to a major defence contractor with transmit and receive modules for aerospace, military grade phased array radar programmes. This is a long term relationship that has required Broadband to develop an expertise in high reliability manufacturing and testing techniques, which has the added benefit that relates to the manufacture and test of E-band and V-band modules.

During the year, Broadband completed the move to a new facility at NETPark, Sedgefield, UK. The relocation has enabled the business to rationalise a number of its processes and enabled us to concentrate on our core competencies. This rationalisation has been a major contributor to the improved production yields achieved through the year and has also resulted in a significant reduction in our fixed cost.

Prospects for Broadband have been enhanced by the development of E-band and V-band capabilities and the reduced cost base. The markets for the business's products are growing rapidly and we look forward to Broadband being a major player in its field.

**“As part of our research and development activities we are working to develop solutions which support the market trend towards smaller, more compact products encompassing the use of alternative materials including ceramic.”**

**Pictured: Transceiver module**

### Future developments

The next few years will see a continuance of increased demand for data with operators looking to differentiate themselves by offering seamless coverage and improvements in quality of service. This is likely to see the development of heterogeneous networks, networks that are composed of multiple radio access technologies, architectures, transmission solutions, and base stations of varying transmission power to create a seamless user experience. This development will drive both of our businesses, with every new frequency release providing opportunities for Wireless and the increasing requirement for 'carrier grade' mobile backhaul providing additional opportunities for Broadband.

As part of our research and development activities we are working to develop solutions which will support the market trend towards smaller, more compact products encompassing the use of alternative materials including ceramic.

With Cloud RAN and later 5G, which is forecasted to commence roll-out in 2020, we expect to see another dramatic increase in data volumes and speed of connection.

Filtronic is ideally placed to participate in this market and continues to develop its technology roadmap to support these opportunities.

### Alan Needle

Chief Executive Officer  
14 August 2014



# Market overview

## Market overview

The wireless telecommunications infrastructure equipment sector is a \$100 billion plus market experiencing significant growth due to the increasing demand for data.

## Network infrastructure

This demand for infrastructure is being driven by the growth in mobile broadband subscriptions and the increasing volume of data being consumed. End user expectations are for high quality services that allow them to consume data, and in particular streaming video, seamlessly whilst on the move. The network operators are competing to supply a comprehensive seamless network and are investing in infrastructure to meet this demand.

The original mobile networks were designed primarily for voice traffic. Today's networks are being designed to provide a seamless user experience for customers. Operators will be judged on whether the various applications available can be accessed and whether the application works as expected by the user.

**“ LTE continues to grow strongly and has reached 240 million subscriptions, with around 35 million additions in Q1 2014. WCDMA/HSPA had the highest net additions during the quarter at around 70 million. Almost all of these 3G/4G subscriptions have access to GSM/EDGE as a fallback. The number of GSM/EDGE-only subscriptions remained flat.”**

(Ericsson, June 2014)

**“ The number of mobile subscriptions worldwide grew approximately 7 per cent year-on-year during Q1 2014. The number of mobile broadband subscriptions grew even faster over this period – at a rate of 35 per cent year-on-year, reaching 2.3 billion. The amount of data usage per subscription also continued to grow steadily. Around 65 per cent of all mobile phones sold in Q1 2014 were smartphones. Together, these factors have contributed to a 65 per cent growth in mobile/cellular data traffic between Q1 2013 and Q1 2014.”**

(Ericsson, June 2014)

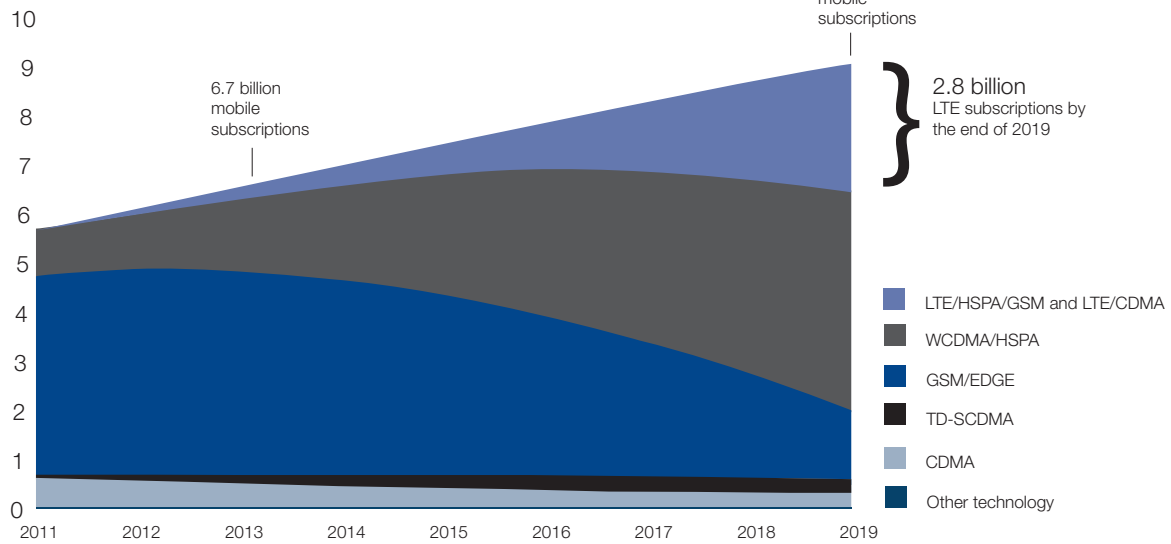
Mobile data traffic is projected to increase at a compound annual growth rate of approximately 45 per cent between 2013 and 2019. This growth level will result in a 10-fold increase by the end of 2019. As smartphone subscriptions increase data traffic will accelerate and data per subscription, especially driven by streaming video, will add to this rise in data volume.

Smartphones are already generating more data traffic than mobile PCs, tablets and mobile routers. It is projected that smartphone subscriptions will treble by 2019, resulting in rapid traffic growth. The aggregate growth in traffic generated by more subscriptions and more data per subscription is expected to result in an overall increase in traffic by 10 times between 2013 and 2019.

The largest and most significant driver of data traffic growth is video. Ericsson are forecasting that this segment will grow by 13 times by 2019 and will account for 50 per cent of all global data traffic. Social networking currently accounts for 10 per cent of data traffic and is forecast to grow in line with the overall 10-fold increase. Music streaming although gaining in popularity, is expected to see slightly slower growth rates than the overall rate and is expected to increase 8-fold by the end of 2019; this is due to the ease of caching content and the ability to create offline playlists. Web browsing is expected to increase 6-fold over the same period and its relative share of overall data traffic will reduce as other activities grow more rapidly.

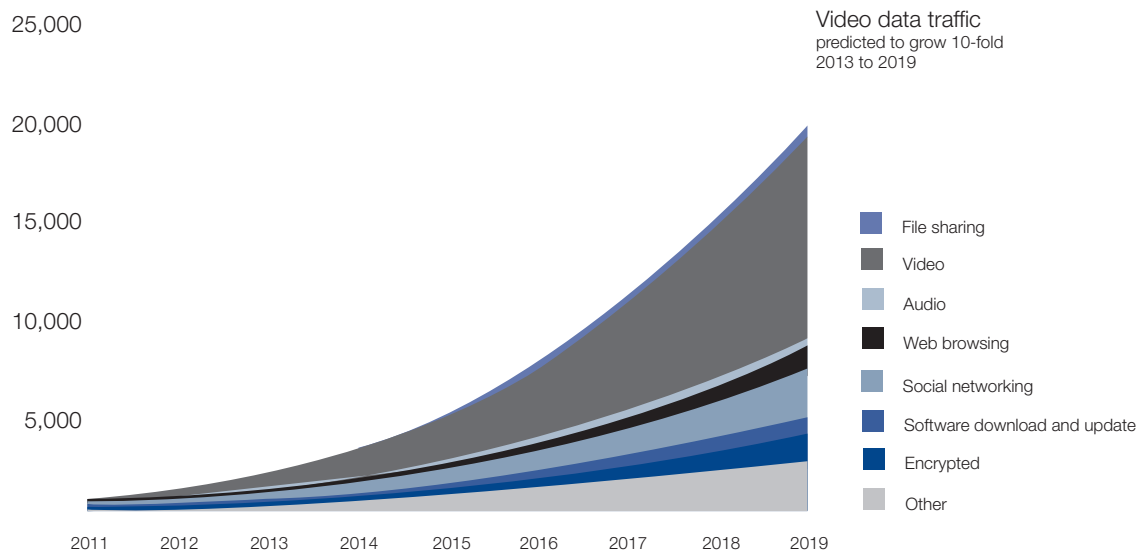


Mobile subscriptions (billions)



Source: Ericsson, June 2014

Global mobile data traffic by application (PetaBytes / month)



Source: Ericsson, June 2014



## Market overview continued

There is a wide disparity in the data usage between different networks, markets and user types. A minority of users are generating a significant proportion of the traffic. The factors influencing user data traffic include operator volume caps, tariff plans, and the screen size and resolution of the user's device.

The improved speed and increased capacity resulting from the introduction of HSPA networks and roll-out of LTE in Western Europe is expected to lead to an 8-fold increase in mobile data traffic between 2013 and 2019 as the user experience is enhanced.

European markets were among the first to adopt wireless technology. In the early 1990s GSM was deployed and WCDMA was rolled out 10 years later. The early introduction of infrastructure has resulted in high population coverage estimated currently at 90 per cent for GSM/EDGE and 75 per cent for WCDMA/HSPA. Ericsson predict that by 2019 coverage will increase to 95 per cent and 90 per cent respectively.

The early introduction of mobile networks in Europe has meant that there is a legacy of older base stations compared to regions where infrastructure was rolled out subsequently. This has resulted in the need to modernise base stations in recent years as more efficient infrastructure is required to handle multi-standard technologies such as GSM/EDGE and WCDMA/HSPA. Other regions have seen modernisation programmes driven by the introduction of LTE.

**“ Mobile backhaul—Backhaul plays an important role in providing a good user experience and overall network performance. As network density increases with higher capacities, backhaul becomes more critical, as it needs to be aligned with the radio access capacities to avoid creating bottlenecks.”**

(Ericsson, June 2014)

### Network backhaul

Mobile broadband backhaul capacity is predicted to see further expansion as demand continues to grow. Capacity per base station will vary by site depending on population density and target data rates. By 2019, high capacity base stations are predicted to require backhaul in the 1 Gbit/s range.

Microwave currently accounts for 60 per cent of base station connections and Ericsson predict that this technology will continue to connect approximately 50 per cent of such connections in 2019.

Smart mobile devices such as smartphones and tablets running various applications account for the majority of data traffic over mobile broadband networks. Ericsson predict that the evolution of devices and applications with more complexity will fuel further growth in traffic.

Pictured: MMIC

**“ Microwave technology evolution —Microwave technology has improved in terms of capacity and spectrum efficiency. Gigabit capacities can now be made available anywhere.**

**In recent years, microwave products have pushed capacity limits using multiple technologies such as higher order modulation, wider channels and carrier aggregation. They have also evolved to work more efficiently using built-in packet aggregation and adaptive modulation to minimize costs for initial rollout or network upgrade.”**

(Ericsson, June 2014)

### Future developments

Early mobile networks pre-date the development of smart mobile devices and were designed primarily to service voice traffic. Mobile network operators have been forced to invest in modernisation of their infrastructure and to adopt new technologies such as HSPA and LTE. The modernisation process has resulted in the development of seamless heterogeneous networks capable of handling multiple technologies.

The development of heterogeneous networks is resulting in the requirement for complex hardware solutions combining multiple technologies. OEMs are developing integrated product solutions to address this requirement and these standardised products will address multiple operators in multiple territories.

### Conclusion

The wireless telephony infrastructure market, including mobile backhaul, is set to grow over the coming years as network operators upgrade their networks to provide platforms capable of delivering the capacity and speed required to service the growing data traffic generated by users of smart mobile devices. Streaming video is the single most important driver and the delivery of a seamless service is imperative to meet consumer expectations.

**“ Heterogeneous networks— Heterogeneous network is a term used for a network that is typically composed of multiple radio access technologies, architectures, transmission solutions, and base stations of varying transmission power. The main objective of deploying heterogeneous networks is to create a seamless user experience. This implies the use of various access nodes in a wireless network.**

**Such a network can use a combination of macro cells, micro cells, and pico cells deployed in a variety of environments. The degree of integration that can be achieved between the macro cell and the small cell layers will to a large extent determine the overall network performance.”**

(Ericsson, June 2014)

It is this growth that will drive demand for both the Wireless and Broadband business and Filtronic is positioned to be a key supplier to OEMs and operators as they develop and supply products required to upgrade networks to satisfy end user demand.

Data and information in the market overview has been sourced from the June 2014 Ericsson Mobility Report that is available at <http://www.ericsson.com/res/docs/2014/ericsson-mobility-report-june-2014.pdf>.



## Objective and strategy

Our objective is to be a major supplier of RF and microwave products to the global telecommunications equipment infrastructure market. There is a growing need for suppliers to provide solutions to satisfy technically difficult specifications to support the increasing complexity within the wireless telecommunications market. Filtronic is well positioned to capitalise on this need.

The group comprises two divisions.

### Wireless

This division designs and manufactures bespoke filters, combiners, tower mounted amplifiers, antennas and RF microwave subsystems for the mobile telecommunications market supplying both the OEM market and network operators.

### Broadband

This division designs and manufactures, for the OEM mobile backhaul market, E-band and V-band transmit and receive modules. Additionally, Broadband supplies modules for phased array radars and offers a build to print, design and test manufacturing service for precision hybrid/surface mount technology at microwave, E-band and V-band.

“The Mobile Radio Access Network LTE equipment market for both macro and small cell radios will witness tremendous growth over the next five years, with LTE RAN revenue levels expected to outdo the RAN revenue peaks of GSM in 2007 and WCDMA in 2011.”

(Dell'Oro Group quarterly report, July 2014)

### Key group strategic drivers

The demand for infrastructure equipment is being driven by the growth in mobile broadband subscriptions and the increasing volume of data being consumed. Our customers include the network operators and more recently the large OEMs that supply these network operators. In Wireless we are focused on achieving 'design wins' onto the major equipment platforms that will be needed to support this equipment roll-out. Increasingly, our revenues are generated by expanding our market access for microwave filters, combiners and RF subsystems and the introduction of new products such as TMAs and antennas. Importantly, we are now able to offer a more complete product portfolio and this maximises our opportunity per customer whether operator or OEM. In Broadband the focus is on introducing the next generation of E-band and V-band modules. By 2019, high capacity base stations are predicted to require mobile backhaul to achieve a data traffic rate of 1 Gbit/s and then, with the adoption of C-RAN, a rate of up to 10 Gbit/s.



## Market strategy

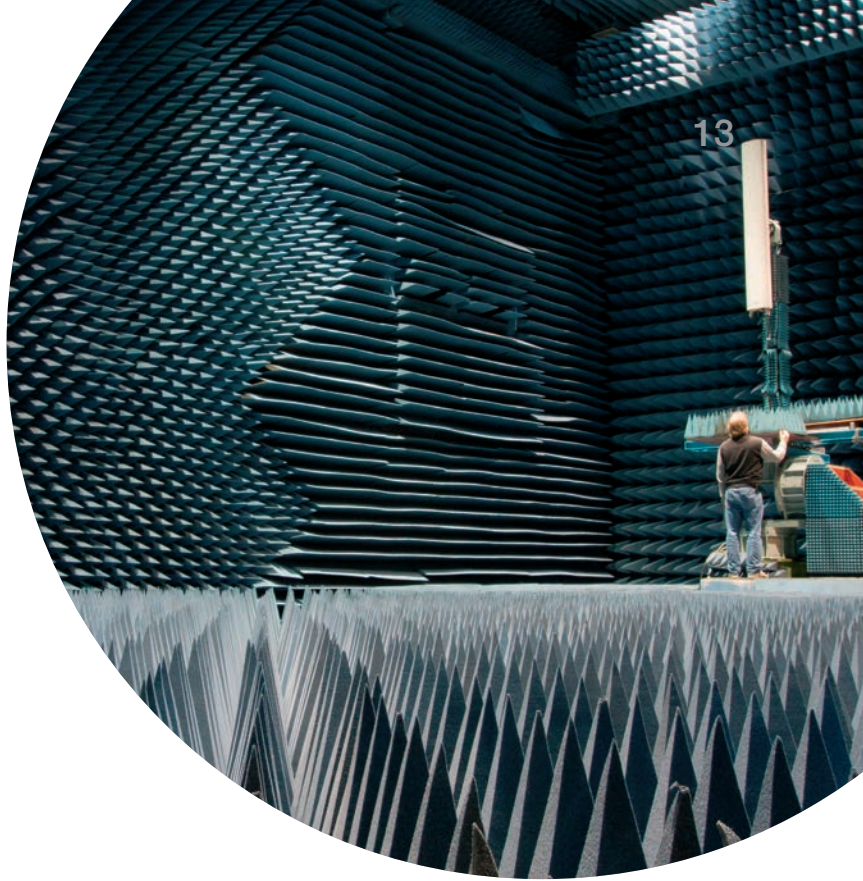
### Wireless

Initially, the Wireless business predominantly focused on the mobile operators and in providing combiner solutions to enable new networks to be integrated into the existing networks and products to manage cell site interference and capacity improvements. Additionally, the time to market when supplying operators is significantly faster than the OEM market where the development of products for their mainstream platforms can take up to 18 months before volume manufacture commences. Due to the project nature of the business to operators, revenues can be extremely variable and subject to last minute change and it is therefore difficult to forecast and resource for this customer base. With OEM business, forecasting tends to be more straightforward due to the OEM having multiple end customers. As the product range and the business reach has grown we are now involved with many OEMs and have a number of design wins which include, frequency diplexers, antennas, RF subsystems, TMAs, combiners and small cell developments.

The majority of these major platform developments commence production within the next 12 months and are forecast to expand, year-on-year, for the foreseeable future.



Pictured: E-band transceiver testing



Pictured: Filtronic antenna test range, Täby, Sweden

### Broadband

The Broadband business supplies OEMs with E-band and V-band, transmit and receive modules, for point to point backhaul solutions. Broadband's engineering team is experienced in the design of MMICs. This, coupled with our system design knowledge and capability, has enabled Broadband to design the RF transmit and receive modules that are required for 'carrier grade' mobile backhaul applications at E-band frequencies. Broadband also provides build to print services at V-band and E-band which take advantage of the in-house expertise that has been developed. The build to print product usually has some key component or design feature that creates intellectual property, protects our sourcing position and enables a higher yield manufacture.

Over the year, Broadband has successfully improved production yields for what is technically difficult product to manufacture, delivering the 10,000th millimetre-wave transceiver module. The focus now is on introducing the next generation of E-band transceivers, increasing the OEM customer base and expanding the possible applications to other market sectors such as small cell and other enterprise opportunities to take advantage of this developing market.



## Our business model

### Filtronic Wireless

Filtronic Wireless is a designer and manufacturer of RF filters, combiners, TMAs, microwave subsystems and antennas for the mobile telecommunications industry, focusing on equipment for OEMs and network operators.



Filtronic Wireless provides a range of products to support global customers in the mobile telecommunications industry such as Ericsson AB, Alcatel Lucent, Nokia Siemens Networks, Motorola, O2, Sprint and Metro PCS as well as numerous smaller companies. Filtronic Wireless has its headquarters in Leeds, UK and has major design and engineering sites in the UK, Sweden and the US. With certified management systems and cost effective new product introduction and development processes, our experienced staff are able to support the needs of our customers for manufacturable high performance products.

Volume manufacturing is sourced from our manufacturing partner who is based in Suzhou, China where we have our own dedicated staff on site. We can provide the complete manufacturing process in house to minimise potential lead times, whilst maintaining the highest quality.

Filtronic Wireless has continued to develop new designs and products and now offers the following range of solutions for network operators and OEMs;

- Custom filtering for interference suppression and blocking protection
- Remote radio head products for the OEM base station market
- Innovative combining solutions which enable the rapid deployment of new systems maximising the use of available spectrum in the most compact and cost effective way
- TMAs to improve base station capacity
- UWB antennas to support the need to reduce the environmental impact of mobile phone telecommunication towers and support the introduction of new transmission frequencies

Solutions must also minimise the need for capital outlay, the need for extra antennas and avoid as far as possible planning permission for civil works.

### Filtronic Broadband

Filtronic Broadband is a designer and manufacturer of 60 to 90GHz millimetre-wave products for mobile broadband backhaul, defence applications as well as providing build to print manufacturing at its state of the art, highly automated UK facility.



Our key offerings are:

- Design and manufacture of E-band and V-band transceiver modules
- Design and manufacture of microwave and millimetric filters and diplexers
- Design and manufacture of customised MMICs for multi-chip module applications and advanced packaging
- Build to print and design for cost/manufacture services for precision hybrid/surface mount technology at 60 to 90GHz

Broadband products support global OEM customers for 'carrier grade' mobile backhaul and a number of smaller second tier OEM customers that supply the enterprise mobile backhaul market. Modules for phased array radars and has build to print and test contracts for complex microwave modules at 4 to 90GHz.

Filtronic Broadband offers a vertically integrated design, manufacture and test capability for E-band and V-band transceivers for the mobile broadband backhaul market. The 'carrier grade' transceiver performance results from the use of proprietary MMICs. These MMICs have been designed in-house, for manufacture on the processes of leading foundries, and offer a differentiating capability in the market. The build to print projects involve some element of design for manufacture and rely on the vast experience that has been developed to achieve and support volume manufacture.

### Investing in research and development

Filtronic operates in a fast moving, technology driven market place where generating our own proprietary technology is key to maintain our competitive advantage. The group therefore invests in research and development and where appropriate obtains patents to protect our intellectual property.

From time to time, the group also benefits from grants, schemes and other incentives to carry out research and development. In FY2014 the group received £nil (2013: £36,000).

As part of our research and development activities we are working to develop solutions which support the market trend towards smaller, more compact products encompassing the use of alternative materials including ceramic.



### Strategic relationships

Our business model has been developed around close working relationships with both our customers and suppliers to maintain a dialogue at multiple levels to cover all aspects of the business.

Wireless continues to develop its long-standing relationship with its manufacturing partner in Suzhou, China where Wireless has its own specialist staff on site to ensure close co-operation and good communication.

When there is a customer requirement to dual source production, for reasons of security of supply, Filtronic will, where economically viable, use more than one source of supply.





# Financial review

## Financial results

Sales revenue in the year ended 31 May 2014 was £32.9m (2013: £40.0m) and operating loss before interest, intangible amortisation and exceptional items was £0.4m (2013: £3.1m profit). The group net loss before taxation for the year was £3.7m (2013: £0.2m profit). Amortisation of intangible assets arising from the acquisition of Isotek (Holdings) Limited charged in the year was £2.4m (2013: £2.4m). Exceptional costs, primarily relating to the relocation of the Broadband business of £0.8m (2013: £0.4m) were recognised in the year.

During the year, Broadband recognised sales revenue of £2.5m in respect of a last time buy to secure materials for a customer programme for legacy product. The customer ordered the material from Filtronic against their forecast requirement for finished product. No margin was made on the sale of the last time buy material and consequently the operating profit percentage to sales for Broadband and the group were reduced.

## Key performance indicators (KPIs)

The directors set budgets for the year which are reviewed against the management accounts on a monthly basis. In addition to these results the directors review a number of KPIs to assess the performance of the group and assist in decision making. Historically, revenue and operating results by segment (note 3) have been the main KPIs used by the group.

In line with industry practice, a more comprehensive set of financial KPIs has been introduced to monitor business performance. These KPIs are set out on page 17.

## Taxation

A tax credit of £0.9m (2013: £0.05m) has been recognised for the year, see note 12, to the financial statements.

## Funding and cash flow

The group ended the year with net cash of £2.5m (2013: £1.9m), the increase in net cash resulted from the unwinding of working capital associated with projects completed in the year and a reduction in inventory in Broadband. Cash in/(out) flow from operating activities was £1.6m (2013: £(0.3m)).

Filtronic has an invoice discounting facility with Barclays Bank plc of £2.0m. As at 31 May 2014 no funds were drawn down against this facility (2013: £0.5m).

## Inventory provision

Inventory is valued at the lower of cost or net realisable value. It is the group's policy to regularly review the carrying value of its inventories and to make a provision for excess and obsolete inventory. As at 31 May 2014 the inventory provision was £1.6m (2013: £1.5m).

## Warranty provision

In line with industry practice the group provides warranties to customers over the quality and performance of products it sells. The group's policy is to make a provision, calculated as a percentage of sales revenue, after reviewing costs associated with faulty products returned.

In Broadband, sufficient data has existed to enable the group to establish a reliable calculation of warranty provision.

In the case of our Wireless business, no historic data was available to the group when it acquired the business and consequently up to 31 May 2013 the group has provided a cautious estimate of the provision likely to be required. By the year ended 31 May 2014 sufficient warranty returns data had been accumulated to enable the business to calculate a more reliable value required to cover the cost of any warranty returns for product supplied and still under warranty. This recalculation of warranty and normal adjustments resulted in a reduction of overall provision of £0.5m which was credited to the income statement in the year.

## Capital expenditure

Capital expenditure of £1.1m (2013: £1.5m) included £0.7m for the Wireless business and £0.3m in Broadband.

## Research and development costs

Research and development costs in the year were £6.4m (2013: £5.4m). In line with the requirements of IFRS, the group's policy is to capitalise development expenditure as intangible assets when all the qualifying criteria set out in note 2 to the financial statements have been met. After considering the criteria no research and development costs were capitalised in the balance sheet in the year (2013: £nil).

## Working capital

At 31 May 2014 net working capital was £8.0m (2013: £9.0m). Net working capital comprised inventories of £3.9m (2013: £5.4m), receivables of £9.9m (2013: £17.2m) and payables of £7.4m (2013: £13.6m).

## Rob Smith

Chief Financial Officer  
14 August 2014

# Key performance indicators




	Group		Broadband		Wireless	
	FY2014	FY2013	FY2014	FY2013	FY2014	FY2013
<b>Operating (loss)/profit per employee</b> Filtronic recognises that employees are a critical asset in our business and we monitor the profit per employee to measure productivity.	<b>£(2,376)</b>	£17,636	<b>£(24,837)</b>	£(29,155)	<b>£30,103</b>	£75,929
<b>Research and development to sales per cent</b> The board recognises that the group needs to invest in new products, capabilities and technologies to participate in a technology driven market and monitors the investment made in research and development as a proportion of sales.	<b>19.3%</b>	13.6%	<b>10.4%</b>	16.4%	<b>23.0%</b>	12.9%
<b>Operating (loss)/profit to sales per cent</b> The board monitors profitability to ensure that an acceptable return is being made on operating activities in the year.	<b>(1.3)%</b>	7.6%	<b>(23.5)%</b>	(30.1)%	<b>11.3%</b>	20.0%
<b>Inventory turns</b> The group maintains inventory so that it can meet customer demand for scarce and long lead-time items and to fulfil customer orders where deliveries are scheduled over a number of months or years.	<b>7.4</b>	8.6	<b>1.7</b>	1.4	<b>9.8</b>	18.4
<b>Trade receivables days</b> In line with other companies in the sector the group extends credit facilities to customers that have an acceptable credit rating.	<b>94</b>	61	<b>83</b>	93	<b>122</b>	59
<b>Trade payables days</b> The group receives credit from a number of suppliers and recognises the importance of paying its suppliers on time.	<b>62</b>	85	<b>55</b>	90	<b>79</b>	84



# Risk management

Effective risk management is key to our success against the characteristics both of the industry that we operate in and within our chosen business model. Filtronic supplies microwave, base station filter products and antennas for the wireless telecommunications market. The group operates 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.

The directors recognise that risk is inherent in any business and seek to manage risk in a controlled manner. The key business risks are set out as follows: -

Risk	Nature	Mitigation	Change in year
<b>Market</b>	We supply a range of niche products to a small number of large OEM customers for both the Broadband and Wireless businesses as well as a number of network operators in the Wireless business. The loss of any of these customers, 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.	<p>The group seeks to mitigate this risk by working closely with OEMs, on an engineer to engineer basis, to ensure that we are designed in to their products at an early stage. The group is actively seeking to increase the number of design wins across a range of OEM products. This strategy is designed to diversify market risk.</p> <p>The relationship that the group maintains with OEMs is key to ensuring that we are involved in the early stages of product design.</p>	
<b>Manufacturing</b>	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 consistently 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.	<p>The group's internal and outsourced manufacturing processes are certified to ISO9001.</p> <p>Our Broadband division has relocated to a new facility. This move provided us with the opportunity to take greater control over our in house processes and where appropriate we have outsourced non-core processes to suppliers who can offer better quality and consistency of manufacturing.</p> <p>All our products are provided to customers after detailed qualification testing. We work closely with our customers to ensure that the test process employed ensure that all the products are supplied compliant to the customer's specification.</p>	
<b>Technology</b>	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.	<p>Our ability to remain competitive in terms of technology and product design is underpinned by retaining key staff.</p> <p>We work closely with our customers and suppliers to gain a thorough knowledge of the technology being developed in the marketplace. By staying close to the market we position ourselves to react quickly to any technology changes that develop.</p>	



Risk	Nature	Mitigation	Change in year
<b>Financial management</b>	The group has a specific exposure to credit risk, interest rate and exchange rate fluctuations.	The group has established a number of policies to mitigate these risks, further details of which are presented in note 36 to the financial statements.	↑
<b>Legacy disposals</b>	We have sold four divisions of the group in the past 10 years and have provided warranties in support of these transactions. These warranties typically cover matters such as product liability, environmental impact risks on freehold property and tax risks. We may receive claims in future related to these current and future commitments.	Following a review, the group has made financial provisions for potential liabilities and periodically reviews its potential liability in respect of these disposals.	↓

The board has established a continuous process for identifying, evaluating, and managing the significant risks the group faces which has operated throughout the year and up to the date of this report. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance with respect to the preparation of financial information and the safeguarding of assets and against material misstatement or loss.

In compliance with the UK Corporate Governance Code, the board regularly reviews (at least annually) the effectiveness of the group's system of internal control. The board's monitoring covers all controls, including financial, operational and compliance controls and risk management systems. It is based principally on reviewing reports from management to consider whether significant risks are identified, evaluated, managed and controlled and whether any significant weaknesses are promptly remedied and indicate a need for more extensive monitoring. The board has also performed a specific assessment for the purpose of this annual report. This assessment considers all significant aspects of internal control arising during the period covered by the report. The audit committee assists the board in discharging its review responsibilities.

During the course of its review of the risk management and internal control systems, the board has not identified or been advised of any failings or weaknesses which it has determined to be significant. Therefore, a confirmation in respect of necessary actions has not been considered appropriate.



# Corporate social responsibility report

Acting with integrity and behaving responsibly is central to the execution of our strategy and underpins our business model. This report covers how Filtronic interacts with a range of key groups, stakeholders and its approach to key issues and its aims for the future.

## Employees

The group's success depends on its employees and the board recognises that it is their commitment and contribution that is vital to the execution of the group's strategy.

With an international workforce, it is important that we provide an environment where we attract, motivate and reward high quality employees.

### Employee development

Employee development is an important element of employee retention and motivation. 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.

### Employee communications

The group believes in keeping employees fully informed on matters which affect them through various communication forums. 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. The group culture is one which encourages openness and interaction between all members of staff.

## Equal opportunities

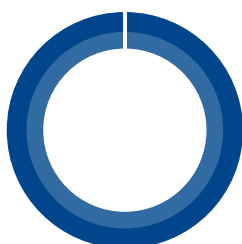
The group is committed to a policy of equal opportunities by which the group ensures that all employment related activities are based on merit and suitability for the job alone. Further information on our equal opportunities policy may be found on our website [www.filtronic.com](http://www.filtronic.com).

### Diversity and inclusion

Although Filtronic currently has no specific policy on diversity, including gender diversity, it is one of the group's core values (expected of employees, suppliers and other stakeholders) that all individuals are treated with dignity and respect. Our policies and practices emphasise the importance of treating people in a non-discriminatory manner across the full employment life cycle, including hiring, reward, development, promotions, mobility and departure. In the event that an employee becomes disabled the group will make reasonable adjustments, and so far as is practicable; will continue to provide employment. Training is provided to those making decisions on these factors so that no individual is disadvantaged and to prevent discrimination on the grounds of gender, religion, belief, race, creed, age, disability, sexual orientation, ethnic origin, or marital status. The board recognises the importance and benefit of ensuring diversity throughout the business and is considering whether a specific policy on diversity, equality and inclusion is required. The diagrams below illustrate what the gender split is at various levels within the group.

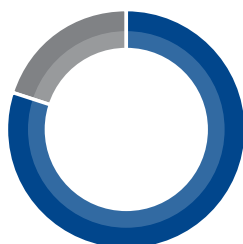
The chief executive officer is the board member responsible for human resources.

**Board of Directors' Diversity**



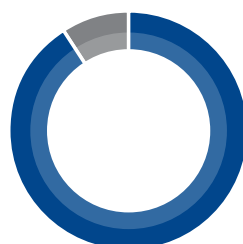
● Male 100%  
● Female 0%

**Executive Level Diversity**



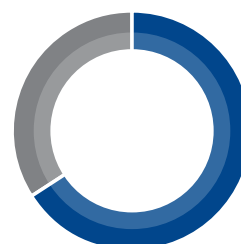
● Male 80%  
● Female 20%

**Management Diversity**

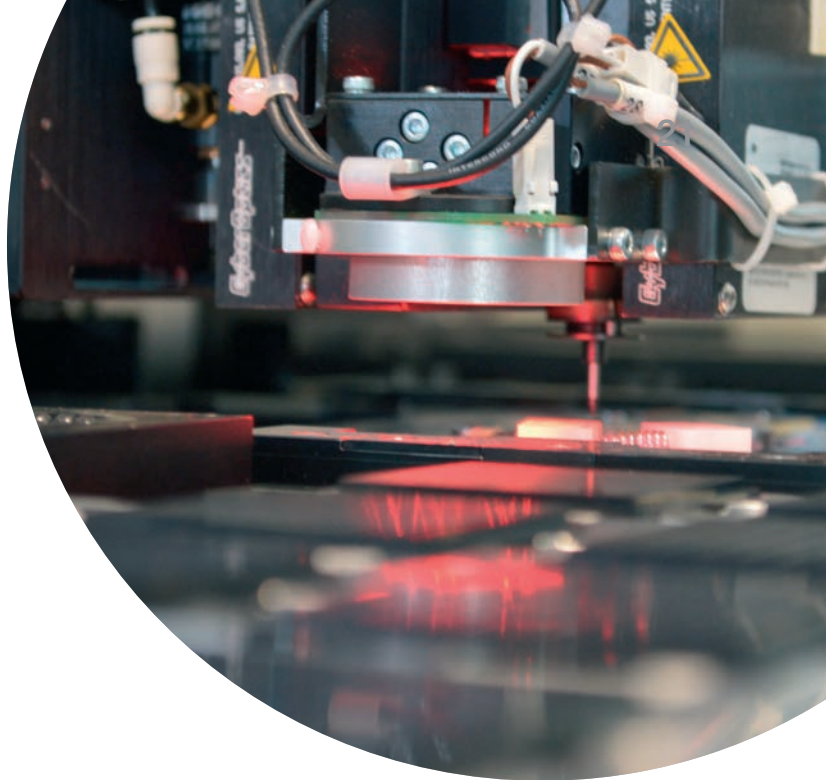


● Male 91%  
● Female 9%

**Total Workforce Diversity**



● Male 66%  
● Female 34%



**Pictured: High precision, automated die attach machine**

## Human rights

Filtronic applies human rights considerations to the way it does business, for example through our supplier and anti-bribery and anti-corruption policies, our code of ethics which is an integral part of our management policies, our practices in relation to health and safety, equal pay and employees' freedom to join trade unions. At present the group does not have a specific policy on human rights but will continue to review whether such a policy is needed in the future.

## 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.



**Pictured: Visual inspection at NET Park**

Filtronic Wireless has streamlined its processes into an integrated management system to encompass the requirements of both the ISO9001 and ISO14001 international standards. This integration will allow for a more cost effective monitoring system to ensure compliance to the highest level of quality and environmental standards in our industry. Filtronic Broadband is adopting the same approach.

Currently we have three sites which are certified to ISO9001 standard – Salisbury, Maryland, USA, Leeds, West Yorkshire and Sedgefield, County Durham. The Leeds site is certified to the ISO14001 standard with the Sedgefield site currently in the process of re-establishing its certification after its move from Newton Aycliffe. Efforts are ongoing to obtain certifications at other sites in FY2015 including our Shrewsbury and Sweden sites.

## Emissions statement

Filtronic calculated its global greenhouse gas (GHG) emissions statement using an operational control consolidation approach as described in the Greenhouse Gas: Protocol: A Corporate Accounting and Reporting Standard (Revised Edition, 2004), which reflects the Defra Environmental Reporting Guidelines (Revised October 2013).



# Corporate social responsibility report continued

Scope 1 emissions occur from sources that are owned or where Filtronic has operational control. This includes direct emissions from gas combustion in our buildings and fuel used in leased company vehicles. Actual and estimated gas consumption data has been collected from each of the leased properties under the control of the Filtronic group, from data sources including direct meter readings, meter readings from suppliers included on invoices and estimations where required based on available information from property management suppliers and other sources. Actual mileage data has been collected from the company vehicle fleet.

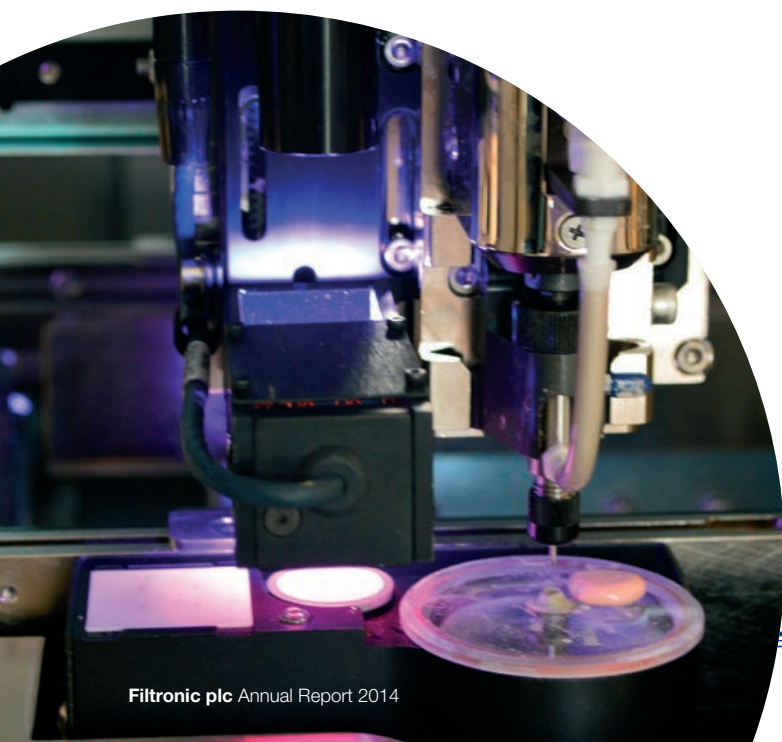
Scope 2 refers to indirect emissions from the consumption of purchased electricity (also including any purchased heat, steam or cooling) from facilities owned or under the operational control of Filtronic. Actual and estimated data has been collected from each of the leased properties under the control of the Filtronic group, from data sources including direct meter readings, meter readings from suppliers included on invoices and estimations where required based on available information from property management suppliers and other sources.

Assessment Parameters	
Baseline year	1 June 2013 to 31 May 2014
Consolidation approach	Operational control
Boundary summary	All entities and facilities under operational control included subject to the materiality threshold applied
Consistency with financial statements	The only variation is that leased properties deemed to be under the operational control have been included in scope 1 and 2 emissions
Materiality threshold	Materiality has been set at group level at 5 per cent*
Assessment methodology	Greenhouse Gas Protocol and ISO14064-1 (2006)
Intensity ratio	Emissions per £m turnover excluding royalties

\* The total of any excluded emission sources are estimated to be less than 5 per cent of Filtronic plc's total reporting emissions.

GHG emission source	(tCO <sub>2</sub> e)	(tCO <sub>2</sub> e/£m)
Scope 1	189	5.7
Scope 2	1,174	35.7
<b>Statutory total (scope 1 and 2)</b>	<b>1,363</b>	<b>41.4</b>

The GHG emissions statement includes emissions data from leased assets that are not included in the rest of the consolidated financial statements, other than in note 32, operating lease arrangements.



Pictured: Epoxy dispenser



### Supply chain

The adoption of a new, advanced product life cycle management software system has allowed for group-wide management and control of our documentation to include product design, suppliers and change management as well as a module to address specific quality processes. Supply chain management is working to develop partnerships with our main suppliers to ensure they have systems in place that focus on quality, environment, corporate social responsibility and health and safety. This includes new initiatives from our customers on reporting of use of conflict minerals in our supply chain.

The implementation of these management systems, which are designed to monitor and control processes such as quality, environment and health and safety will provide Filtronic Wireless with the confidence that each and every product that is delivered to our customers is an appropriate level of quality, and has been designed and manufactured in a way that considers our impact on the environment and the ultimate health and safety of our employees who contribute to our success. Filtronic Broadband will be adopting the same approach.

### 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. Due to recent expansion and addition of sites, we have refocused our efforts within each location on developing a robust health and safety programme that emphasises risk management to ensure our employees have a safe and healthy work environment. Our goal is to align our programme with the OHSAS 18001 international standard.

### Charitable and community support

The group has a history of supporting charities. In the majority of cases this involves matching employee sponsorship for their chosen charity events which have included, in the past year, 'The Stroke Association' and 'Mind' and 'Mind the Gap' (a charity for learning disabilities based in Bradford).

For us, helping out is not necessarily just about raising funds or making donations; it also includes practical help. The group donated PCs to a local primary school, and large amounts of office and lab equipment to educational establishments, following the relocation of the Broadband business to Sedgefield, County Durham earlier this year.

Opportunities are provided annually, across all divisions, for work experience and student placements.

To support engineering and technology we have developed partnerships with local universities; sponsoring a PhD student, awarding a group sponsored prize to 'outstanding undergraduate student' in electronic communications and knowledge sharing events.



# Governance report

## Introductory letter from the chairman of the board on the governance report

### Dear Shareholder

At Filtronic, we believe that good governance is about helping to run the company well whilst promoting its success for the benefit of all of its shareholders. In practice, it is about setting clear goals and expectations not only for the company's strategy but for its conduct and business performance and being honest in our business dealings.

We are conscious that the board sets the tone for the company. The way in which it conducts itself, its attitude to ethical matters, its definition of success, the setting of goals and strategy and its assessment of risk, all define the environment in which the executive members implement the company's strategy. We continue to measure the effectiveness of our directors, the board itself and its committees and the outcome from this exercise invariably generates constructive suggestions. The board is aware that it must continually develop its skills and knowledge so that it can respond to changing market conditions.

During a year of considerable change on the board (Michael Roller joined as a non-executive director in June 2013 and Rob Smith joined in June 2014 replacing Mike Brennan as CFO) our board committees have continued to perform effectively. The focus of the nominations committee's activities this year has been on succession planning and the search for a new CFO.

The remuneration committee completed an extensive review and benchmarking exercise on the short, medium and long term incentives for our UK-based executive directors and senior staff. It considered guidance from investor bodies and from the Department of Business, Innovations and Skills. The audit committee considered a number of key risks within the business and the exposure to risk within the business.

In the pages that follow, we describe the corporate governance framework in more detail. We start by describing the board and its committees, their remit and operation, ending with the directors' corporate governance statement. Separate reports from each of the committees are included followed by the directors' report.

The detailed statement below sets out how the company applied the principles of good governance set out in the UK Corporate Governance Code issued in September 2012 by the Financial Reporting Council ("The Code"). I hope you will find this report helpful in understanding our commitment to good governance.

Yours sincerely

**Howard Ford**

Chairman

14 August 2014

\* During the reporting period ending 31 May 2014, the company has been deemed to be a 'smaller company' in terms of code provisions including B.7.1 and directors are subject to re-election at intervals of no more than three years after initial election by shareholders with the exception of Graham Meek who is subject to annual re-election by shareholders.

## Governance framework: Board and committees, membership, remit and activities

### Board Membership

The board is currently comprised of six directors as follows: the chairman, three non-executives and two executive directors.

### Executive directors

**Alan Needle** (aged 59) has been an executive director since November 2010 and chief executive officer since July 2012. Prior to the acquisition of the Wireless business he was head of Wireless Infrastructure of Isotek Electronics Limited. Previously, he had been an executive director of Filtronic plc from flotation in 1994, until 1997 and chief executive of the Wireless Infrastructure Division of Filtronic plc from 2002 until January 2006. He is a Chartered Engineer and a Fellow of the Institute of Electrical Engineers.

**Robert (Rob) Smith** (aged 50) was appointed as an executive director and chief financial officer with effect from 16 June 2014. Prior to joining Filtronic, Rob was Finance Director at APC Technology Group PLC, a distributor of specialist electronic components and smart energy saving products and services provider. Rob has also served as finance director at Densitron Technologies plc, a manufacturer and distributor of electronic displays. Rob's earlier career was spent principally in the electronic components industry working for GEC, Centronic and International Rectifier. He is a Chartered Management Accountant and a Fellow of the Chartered Institute of Management Accountants.

### Non-executive directors

**Howard Ford** (aged 63) 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 is currently the non-executive chairman of Cambridge Semiconductor Limited, Light Blue Optics Limited, Pyreos Limited and ZBD Displays Limited and 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 67) has been a non-executive director since 1999. Since 2006 he has been designated the senior non-executive director and is chairman of the audit committee. He is a non-executive director of Capital Gearing Trust plc and is vice-chairman of King's College Hospital NHS Foundation Trust.

**Reginald (Reg) Gott** (aged 57) 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 Resource Group Limited. From 2002 to 2008 he was an executive director of FKI plc, an international diversified engineering group, and from 2009 to 2012 he was chief executive of Nuaire Group. He has an extensive background in the machinery, automation and controls segments of the capital goods markets across Europe and North America.

**Michael Roller** (aged 49) was appointed as a non-executive director on 1 June 2013. In March 2014 he joined the board of Bioquell plc as group finance director. He has previously been finance director of a number of quoted companies, most recently Corin Group plc. He has also held a number of other senior finance roles in a broad range of listed and private companies. He qualified as an accountant with KPMG.

## Framework of governance: corporate duties, operation of the board and its committees

### Leadership

The board is accountable to the company's shareholders for good corporate governance. It is also responsible for providing leadership to the group within an effective framework of authority and accountability. It sets the strategy and oversees its implementation. It ensures that the right people and resources are in place in order to deliver long term value to shareholders through the proper management of risk in parallel with the promotion of innovation and entrepreneurship. In June 2013, Michael Roller joined the board as a non-executive director and in June 2014, Rob Smith joined as chief financial officer of the group, replacing Mike Brennan who stepped down in April 2014. Howard Ford, the chairman is responsible for the running of the board ensuring, together with the company secretary, that it receives timely and clear information to enable it to discharge its duties.

### Effectiveness

During the year, the board carried out a rigorous evaluation exercise involving an internal review process. The board did consider appointing an independent facilitator for the evaluation process but chose not to do so this year. The methodology used was as follows.

Separate questionnaires based on the provisions of the UK Corporate Governance Code 2012 were prepared, with tailored questions for (i) the board and its committees; (ii) the chairman; (iii) the non-executive directors and the (iv) the executive directors.

The board effectiveness questionnaires were completed by all directors. Contributions were submitted anonymously to the company secretary to facilitate candour. The results were reviewed initially by the chairman with a view to sharing and making recommendations shortly thereon with the board as a whole. The evaluation of the chairman was completed by all directors. Again contributions were submitted anonymously. In this case, the results were reviewed initially by the senior



# Governance report continued

non-executive director, Graham Meek with a view to sharing with the entire board. The evaluation of executive and non-executive directors was completed by all directors. Again, contributions were submitted anonymously and results will be reviewed initially by the chairman with a view to sharing with the entire board.

The recommendations from this exercise will be formally considered by the board with a view to improving effectiveness.

The board considers all of its non-executive directors to be independent. Although Graham Meek does not meet the criteria for independence as set out in the Code, the board considers him in character and judgement to be independent. Mr Meek, having been invited by the board to continue to serve as a non-executive director has agreed to continue, subject to re-election by the company's shareholders at the AGM on 26 September 2014. All members of the board have access to the advice and services of the general counsel and company secretary and are able to take independent professional advice at the company's expense in the discharge of their duties. The company has procedures to deal with directors' conflicts of interest and the board is satisfied that these procedures operate effectively.

## Accountability

The UK Corporate Governance Code states that the board should present a balanced assessment of the company's position and prospects including the significant risks facing the company. The strategic report and the audit committee report set out these assessments in detail.

## Remuneration

The remuneration committee report is set out on pages 31 to 42 complies with the new regulations governing the reporting of directors' remuneration by UK public companies. The directors' remuneration policy will be proposed as a shareholder resolution at the AGM in September and will be the subject of a binding vote. The annual remuneration report will similarly be proposed as a shareholder resolution at the AGM but will be subject to an advisory (i.e. non-binding) vote.

## Relations with shareholders

The chairman is chiefly responsible for ensuring that there is a satisfactory dialogue with shareholders. All of the directors recognise the importance of having clear communication with shareholders and the role of clear narrative reporting in particular to aid this communication. Meetings with shareholders are usually scheduled after the announcements of the preliminary results in July and the interim results in January each year. Shareholders are encouraged to attend the company's AGM. 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.com](http://www.filtronic.com).

## Remit of the board

Whilst day to day operational matters are managed by the chief executive officer, other matters, including those listed below, are reserved for the board:

- Strategy and oversight of the management of the company;
- Approval of company and consolidated financial statements;
- Approval of major corporate transactions and commitments;
- Succession planning (appointment/removal of directors and the company secretary);
- Approval of all terms of reference for the committees of the board and delegation of authority to the chief executive officer;
- Review of the group's overall corporate governance arrangements including systems of internal controls and risk management;
- Approval of the delegation of authority to the chief executive officer or where appropriate to the relevant board committee;
- Approval of the terms of reference of all committees of the board.

The board has established the following committees, each of which has written terms of reference specifying its authority:

## Audit committee

The primary function of the audit committee is to assist the board in fulfilling its financial and risk oversight responsibilities. During the year, it met three times. The committee reviews items such as the half and full year results and then makes a recommendation to the board. The audit committee is chaired by Graham Meek and is comprised of all of the non-executive directors. Further details of the role and responsibility of the committee can be found later in this section in the audit committee report.

## Nominations committee

The nominations committee is chaired by Howard Ford, and the other members are the independent non-executive directors: Graham Meek, Reginald Gott and Michael Roller. The nominations committee's duties are confined to the nomination of appointments, reappointments and termination of employment or engagement of directors and the company secretary. Further details of the role and activities of the committee can be found later in this section in the nominations committee report.

### Remuneration committee

The remuneration committee is chaired by Reginald Gott and the other independent non-executive directors, Graham Meek and Michael Roller together with Howard Ford, the chairman of the board, are members. The members of the committee have no personal interest in the matters considered other than as shareholders. No potential conflicts of interest exist in relation to any of the member of the committee and their duties. The remuneration committee's responsibilities include ensuring that the remuneration policy of the company and its implementation are appropriate. It ensures that levels of remuneration are sufficient to attract, retain and motivate directors of the quality required to run the company successfully whilst avoiding paying more than is necessary for this purpose. Further details of the role and responsibility of the committee can be found later in this section in the remuneration report. The remuneration committee met three times during the year.

### Executive committee

The chief executive has established an executive committee.

The committee aims to meet monthly either by teleconference or face to face. The routine matters on the agenda include, operational matters (trading, customers, suppliers), site specific issues in the UK, Sweden, China and the USA, risk management, health and safety, human resources and environmental matters.

### Directors' attendance table FY2014

The board normally schedules at least 10 meetings during the year. Last year the board met 13 times. Attendance at board meetings and committee meetings during the year ended 31 May 2014 was as follows:

	Board	Audit	Remuneration	Nominations
Total meetings in year	13	3	3	4
<b>Director attendance</b>				
Howard Ford (Chairman)	13	3	3	4
Reginald Gott	13	3	3	4
Graham Meek	12	3	2	4
Michael Roller	13	3	3	4
Mike Brennan	10/10	n/a	n/a	n/a
Alan Needle	12	n/a	n/a	n/a

Table Governance Report: Attendance at board (and committee) meetings held in FY2014

### Statement of compliance with the 2012 UK Corporate Governance Code (the Code)

The company is committed to the principles of corporate governance contained in the Code.

Notwithstanding the circumstances set out in provision B.1.1 of the Code, the board believes that Graham Meek continues to be independent in character and judgement despite the fact that he has served on the board for more than three terms of three years. He continues to demonstrate his independence at each board meeting with the originality and acuity of his views not only in relation to the executive directors but also the view of the other non-executive directors.

In respect of code provision C.3.3 (relating to the audit committee's role in monitoring the company's internal audit function) as explained in the company's audit committee report, the company outsources its internal audit activity to third parties as it is not deemed appropriate given, the company's size, to have its own internal audit function. The audit committee considers annually whether there is a need for an in house internal audit function to be established and were it to conclude that this would be more appropriate than the current arrangements, would recommend this to the board.

Except for the foregoing, the directors consider that throughout the year ended 31 May 2014 the company has been in compliance with the code provisions set out in the Code.



# Audit committee report

During the year the audit committee comprised four independent non-executive directors:

Graham Meek (chairman), Howard Ford, Reg Gott and Michael Roller.

The audit committee's terms of reference include the following roles and responsibilities:

- monitoring and making recommendations to the board in relation to the company's published financial statements and other formal announcements relating to the company's financial performance;
- advising the board on whether the committee believes the annual report and accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the company's performance, business model and strategy;
- monitoring and making recommendations to the board in relation to the company's internal financial controls and financial risk management systems;
- annually considering the need for an internal audit function;
- making recommendations to the board in relation to the appointment, reappointment and removal of the external auditor and approving the remuneration and terms of engagement of the external auditor;
- reviewing and monitoring the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements;
- monitoring the extent to which the external auditor is engaged to supply non-audit services; and
- ensuring that the company has arrangements in place for the investigation and follow-up of any concerns raised confidentially by staff in relation to the propriety of financial reporting or other matters.

The committee reviews its terms of reference and its effectiveness annually and recommends to the board any changes required as a result of the review. The terms of reference are available on request from the company secretary and on the company website, [www.filtronic.com](http://www.filtronic.com). The audit committee meets at least three times a year and has direct access to KPMG LLP ("KPMG"), the company's external auditor. The board considers that the members of the committee are independent and have collectively the skills and

experience required to discharge their duties effectively, and that the chairman of the committee meets the requirements of the UK Corporate Governance Code as to recent and relevant financial experience.

The company outsources its internal audit activity to third parties as it is not deemed appropriate given the size of the company to have its own internal audit function. However, the committee considers annually whether there is a need for an in-house internal audit function to be established and, were it to conclude that this would be more appropriate than the current arrangements, would recommend this to the board.

During the year ended 31 May 2014 the audit committee met three times and discharged its responsibilities by:

- reviewing and approving the external auditor's terms of engagement, remuneration and independence;
- reviewing the external auditor's plan for the audit of the company's financial statements, including identification of key risks;
- reviewing the company's internal financial controls operated in relation to the business and assessing the effectiveness of those controls in minimising the impact of key risks;
- reviewing the appropriateness of the company's accounting policies;
- reviewing the company's draft annual report and accounts, interim report and interim management statements prior to board approval;
- reviewing the external auditor's detailed report to the committee on the annual financial statements;
- reviewing the need for an internal audit function, and determining what aspects of the company's operations should be subject to outsourced internal audit scrutiny.

The following key areas of risk and judgement have been identified and considered by the audit committee in relation to the business activities and financial statements of the company:

- inventory valuation
- warranty provisions

These issues were discussed with management and the auditor, in particular at the pre-year end audit planning meeting and at the conclusion of the audit of the financial statements.

**Inventory valuation:** Filtronic operates in an industry where developments in product technology and the highly customer-specific nature of some inventory may result in inventory becoming slow-moving or obsolete. This in turn may mean that inventory cannot be sold or that sales prices for such inventory are discounted to less than the relevant inventory's book value.

The majority of Filtronic's inventory relates to the Broadband division. The committee considered a paper from senior management analysing this inventory by customer and looking at projected future usage relative to current inventory on hand. It reviewed the provision for excess and obsolete inventory and noted that the level of provision and the methodology applied were appropriate and consistent.

**Warranty provisions:** Filtronic maintains a provision to recognise the risk of warranty claims being made against it by its customers. The level of warranty provision varies and is dependent on the customer and the complexity of the product. In Broadband the warranty provision rate can be up to 0.9 per cent of sales value whereas in Wireless the warranty provision is set at a fixed level of 0.32 per cent of sales value. The level of any such provision is necessarily judgemental because many of the group's product ranges are new and there is no extended history of warranty claims upon which to base the level of ongoing provisioning.

The committee considered the provision for warranty claims in light of the claims experience in the current and recent years and the mix of new and established products sold in the year and concluded that the level of provision was appropriate.

The company's management confirmed to the audit committee that they were not aware of any material misstatements. Having reviewed the reports received from management and the auditor, the committee is satisfied that the key areas of risk and judgement have been appropriately addressed in the financial statements and that the significant assumptions used in determining the value of assets and liabilities have been properly appraised and are sufficiently robust. The committee considers that KPMG has carried out its duties as auditor in a diligent and professional manner.

As part of the review of auditor independence, KPMG has confirmed that it is independent of the company and has complied with applicable auditing standards. KPMG has held

office as auditor for 12 years; in accordance with professional guidelines the engagement partner is rotated after at most five years and the current partner is in his first year on the engagement.

In assessing the auditor's effectiveness, the committee:

- challenged the work done by the auditor to test management's assumptions and estimates in the key risk areas;
- reviewed reports received from the auditor on these and other matters;
- received and considered feedback from management; and
- held private meetings with the auditor that provide the opportunity for open dialogue and feedback between the committee and the auditor without management being present.

In addition, the chairman of the committee has discussions by telephone and in person with the audit partner outside the formal committee process throughout the year.

Having completed its review, the audit committee is satisfied that KPMG remained effective and independent in carrying out its responsibilities up to the date of signing this report and believes that it would not be appropriate to put the audit appointment out to tender at the present time although this is kept under review. Accordingly, KPMG LLP will be proposed for reappointment as auditor at the annual general meeting.

After careful consideration of the advice of the audit committee, the board has concluded that the 2014 annual report is fair, balanced and understandable and provides the necessary information for the company's shareholders to assess the group's risks, performance, business model and strategy.

# Nominations committee report

## Nominations committee responsibilities

The terms of reference for the nominations committee are formally approved by the board and are available on the company's website. The principal duties and responsibilities of the committee include: reviewing the structure, size and composition of the board, ensuring that succession planning is considered, reviewing the leadership requirements of the company (both executive and non-executive), keeping up to date and informed about strategic issues and commercial changes affecting the company and the market in which it operates.

The committee is required to meet twice during the year. The nominations committee met four times during the year to consider succession planning, board composition and balance of skills on the board.

## Activities of the committee

Early in 2014, the committee undertook a recruitment process to recruit a new chief financial officer ("CFO") to replace the outgoing CFO. The committee was assisted in the search and recruitment activities by an independent search agency. The nominations committee continues to review the size, composition and structure of the board. At the start of the financial year 2014, the board was strengthened by the addition of a new non-executive director, Michael Roller, who has a wealth of recent and relevant financial experience. The committee considers that the current composition is appropriate to provide the proper governance, composition and guidance to the company's business. The committee recommends that Graham Meek, subject to re-election by shareholders at the annual general meeting in September 2014, continues to serve as the senior independent non-executive director.

## Boardroom diversity

Although the company has no separate specific policy on diversity (other than its employment policy for non-discrimination), diversity (including gender) is considered when the board is evaluating its performance and its balance of skills, experience, knowledge and independence and especially when recruiting new members to the board. In the two most recent recruitment exercises, the final short lists were comprised in equal measure of male and female candidates. However, the successful candidates were appointed solely on merit. The company, the board and the nominations committee values and supports the aims of the Davies Report on women on boards and noting that there is currently no female representation at board level (other than the general counsel and company secretary), the committee will keep under review whether a formal measurable objective should be set for female representation at board level.

There is always room for improvement and in the coming year the committee will be concentrating on our longer term vision and ensuring that the board (both executive and non-executive) has the optimal range of skills, experience, diversity and personalities to succeed.

Yours sincerely

**Howard Ford**

Chairman nominations committee  
14 August 2014



# Directors' remuneration report

## Annual statement on remuneration

### Dear fellow Shareholder,

I am pleased to present the Filtronic directors' remuneration report for the year ended 31 May 2014. This report describes how the board has applied the principles of the UK Corporate Governance Code relating to directors' remuneration and is split into two constituent parts:

The directors' remuneration policy sets out the policy for 2014-15 and the key factors that were taken into account in setting the policy. The 2014-15 directors' remuneration policy will be subject to a binding shareholder vote at the AGM to be held on 26th September 2014.

The annual report on remuneration (ARR) sets out payments and awards made to the directors and senior management and details the link between company performance and remuneration for the 2013-14 financial year. The ARR is subject to an advisory shareholder vote at the AGM.

The remuneration committee comprises all non-executive directors, plus the chairman. It defines the company's policy on remuneration, benefits and terms of employment for executive directors and senior management. The committee also reviews and approves general increases in staff salaries and bonus arrangements and takes these into account when setting remuneration packages for executive directors and senior management.

The committee has reviewed the remuneration packages of

the executive directors and senior management to ensure these continue to attract, retain and motivate talented people, while recognising wider shareholder interests. The committee reviews all incentive-based rewards before they are awarded and has full discretion to adjust awards downwards if deemed appropriate.

As a consequence of this review, the remuneration committee is proposing, for approval at the AGM, a slightly revised long term incentive framework which it believes better reflects 'best practice' going forward.

The board has also reviewed the terms of reference of the remuneration committee and made minor changes to accommodate the recently updated ICSA Approved Remuneration Committee Terms of Reference. The new remuneration committee terms of reference are available to view at [www.filtronic.com](http://www.filtronic.com).

The remuneration committee met three times formally during the year and ad hoc when needed.

### Reg Gott

Chairman, remuneration committee  
14 August 2014

## Directors' remuneration policy

The Filtronic FY2015 directors' remuneration policy ("the Policy") will come into effect, if approved by binding vote, at the AGM on 26 September 2014. The main aim of the group's remuneration policy is to align the interests of executive directors and senior management with the group's business strategy and the creation of long term shareholder value. It is the intention of the committee that the Policy should run, in principle, for three years. The Policy is comprised of four parts: (i) a future policy table for executive directors; (ii) a chart illustrating the relationship between Filtronic's performance and the resulting remuneration using various scenarios; (iii) other policies relating to executive director remuneration, recruitment, service contracts and termination; and (iv) remuneration policies for the chairman and non-executive directors.

The Policy aims to provide the directors and senior management with competitive remuneration packages, taking into account the remuneration practices of other international companies of similar size and scope within our industry sector and within the context of the current economic climate and the applicable regulatory and governance framework.

The remuneration policy review identified above was undertaken with the assistance of Ernst & Young LLP (E&Y) who completed a best practice benchmarking study against a comparator group of companies and advised on current and trend-line best practice that would be most appropriately applied to Filtronic within the context of the company's business growth strategy and aspirations. The comparator group selection, being a very critical part of this process, was reviewed jointly by the remuneration committee chairman, the CEO and E&Y. The group was selected to also include some similar profile businesses that were larger in revenue, profit and market capitalisation terms. These larger companies were not taken directly into account in the review process but were included in order to provide 'boundary guidance' to ensure the proposed Filtronic Policy and framework would be aligned with the target 'direction and rate of travel' of the company and thereby provide robust continuity beyond the year ahead. The fees paid to E&Y for this work amounted to £15,000.

The study concluded that the current Filtronic plc executive remuneration policy, introduced in 2008, was still essentially fit for purpose but that minor adjustments would be appropriate to reflect latest best practice.

The key change in remuneration policy recommended for FY2015 was an increase in the LTIP potential to adjust the focus of executive and senior management remuneration toward longer term shareholder value creation and the introduction of an element of deferral (non-matching) to further focus on delivering long term strategy.

Our objective is to ensure that our remuneration structure provides a fair reward to all executive management, senior management and staff for the performance delivered and an incentive to continue to deliver our strategy and develop our business over the long term. We believe the Policy we are asking you to approve does this whilst also giving the committee the flexibility to respond to changes in circumstances and opportunities.

We therefore submit the remuneration policy to a binding vote on 26 September 2014.

The following table applies to executive directors and senior management (as deemed appropriate by the remuneration committee).

### Future policy table — executive directors

Element	Purpose and Link to Strategy	Operation	Opportunity	Performance Measures and Period
<b>Base Salary</b>	This element is set to reflect expected contribution to delivering the company's business plans and to allow Filtronic to recruit and retain executive directors of the calibre needed to develop and deliver the company's strategy.	Reviewed annually with any change effective from 1 July, or following a significant change in responsibilities.  When setting salary, the committee considers the level of increase for employees in general, market data, business performance, external economic factors, the complexity of the business and the role, and the director's experience and performance.	The board retains discretion to make exceptional salary increases above inflation and the general level of increases throughout the group in situations, for example, where the executive has been promoted or gains a clear increase in responsibility.	The performance of an executive director is taken into account by the board during annual salary reviews.

Element	Purpose and Link to Strategy	Operation	Opportunity	Performance Measures and Period
<b>Benefits</b>	To provide reasonable benefits which are competitive in the market.	The taxable benefits in kind comprise principally a fully expensed company car (or cash equivalent) and private healthcare. Life assurance and income support are also part of the benefits on offer but are conditional on the employee joining the Filtronic stakeholder pension scheme. Relocation assistance and other benefits that are customarily provided, in the relevant location, are included, where applicable.	Benefits will vary by role, and the level is determined to be appropriate for the role and circumstances, including country of domicile, of each individual executive director.  It is not anticipated that the current cost of benefits will increase materially over the term of this policy, but the board retains the discretion to approve additional benefits in exceptional circumstances (e.g. relocation expenses or an expatriation allowance on recruitment, etc.).	None.
<b>Pension contribution</b>	To provide retirement provision, on the same basis as that available to other employees.	The company contributions are set as a percentage of base salary and overall contributions are paid monthly.  Only base salary is pensionable. The company also operates a cash alternative scheme, (which is at no additional cost to the company), when life time allowances are reached.  The company has implemented pension auto-enrolment during 2014 and executive directors as well as other employees will be assessed and, where eligible, will be subject to auto-enrolment in line with the regulations.	Under the Filtronic plc Stakeholder Pension Plan (a defined contribution plan) the maximum contribution the company makes is 8% of base salary if the employee makes a contribution of 6%.  The pension scheme inherited from the acquisition of the Wireless business in 2010 is also a defined contribution scheme. The maximum contribution the company makes to those who were employed by the acquired entity at the time of acquisition is 10% of base salary if the member makes a contribution of 5%.  It is not anticipated that the current cost of executive pensions will increase materially over the term of this policy.	None.



# Directors' remuneration policy continued

Element	Purpose and Link to Strategy	Operation	Opportunity	Performance Measures and Period
<b>Annual bonus</b>	To retain, incentivise and reward performance against annual financial, strategic and operational objectives which are consistent with the medium term goals of Filtronic.	<p>The award of annual bonus is assessed after the financial year end (when audited results are available) by the committee based on performance against the targets set at the beginning of the year.</p> <p>Historically, annual bonus targets have principally been financial targets (operating profit and cash generation targets), equally weighted in terms of bonus opportunity.</p> <p>The committee believes this to remain an appropriate structure for the annual bonus and will continue to apply it.</p> <p>Threshold vesting occurs (i.e. starting at 0%), if the threshold target is achieved, rising on a straight line basis to the maximum bonus opportunity in the event that the maximum performance targets are achieved.</p>	For performance in line with expectations (the lower threshold): 0%, up to a maximum: 50% of salary for achieving the upper threshold.	<p>The board continues to hold the view that, at this stage in the development of the business, operating profit and operating cash generation remain appropriate measures of performance for annual bonus purposes.</p> <p>Annual targets will be set to reflect the momentum in the business, the potential market opportunity, shareholder expectations and strategic plans but will always require management to deliver a stretching performance.</p> <p>In exceptional circumstances the board retains the discretion to change measures or targets at the half year to ensure alignment of pay with the underlying objectives and performance of the business during the year. The committee will provide a full explanation of why such discretion was applied in the following year's remuneration report.</p>
<b>ESOP</b>	To incentivise long term value creation through aligning the interests of executives and shareholders through the grant of share options.	<p>The committee can make share option awards to executive directors under the Filtronic plc employee share option plan.</p> <p>These take the form of awards of an option to acquire shares in the company at the market price on the date of grant of the option.</p> <p>The share options are subject to performance criteria being met over a vesting period.</p> <p>Awards may be adjusted to reflect a change in the capital structure of the company.</p>	Options over shares up to a maximum value of 100% of salary based on the market value of shares at the date of the grant of option.	<p>Performance measures are selected for each grant to reflect strategic priorities.</p> <p>The share options have a three year vesting period.</p>

Element	Purpose and Link to Strategy	Operation	Opportunity	Performance Measures and Period
<b>Long Term Incentive Plan ('LTIP')</b>	<p>To incentivise long term value creation through aligning the interests of executives and shareholders through the grant of an award in shares.</p> <p>The selected performance targets support the long term strategy of Filtronic and aid retention of executive directors.</p>	<p>The committee can make annual share-based awards to executive directors under the Filtronic plc performance share plan approved by shareholders in September 2008. These awards can take the form of conditional awards or nil cost options.</p> <p>The committee usually grants awards annually and performance targets are measured on company performance over a three year period.</p> <p>Directors are encouraged but not required to hold the relevant awards for at least a two year period, subject to satisfying any associated tax liabilities.</p> <p>The board proposes to introduce an element of deferral into the LTIP scheme such that 50% of any awarded shares will be subject to deferred exercise for two years. Executive directors are encouraged to achieve within five years and maintain thereafter a shareholding of at least their equivalent annual salary.</p> <p>Awards may be adjusted to reflect a change in the capital structure of the company.</p>	<p>Maximum potential value: 100% of base salary.</p> <p>Historically for the CEO and CFO, the maximum value of the award has been 50% and 40% of base salary respectively.</p> <p>It is proposed to set the normal maximum level at 50% of salary for both the CEO and CFO with an exceptional circumstances maximum level at 100% being available to award at the remuneration committee's discretion. If this discretion is applied, a full explanation will be provided in the following year's remuneration report.</p> <p>On-target performance will result in 25% vesting of the LTIP award.</p>	<p>In 2008 when the current LTIP scheme was introduced, the performance measure adopted was an increase in EPS over a three year period.</p> <p>The board believes this remains an appropriate measure of long term performance for the purpose of an LTIP.</p>
<b>Participation in other all employee share-based plans</b>	To encourage executive share ownership using HMRC approved schemes.	<p>Executive directors can choose to participate in the company's approved Save As You Earn Share Option Scheme on the same terms as other UK employees. In accordance with the scheme and UK tax rules, share options may be granted with an exercise price that is set at a discount (currently up to 20%) to the market value of Filtronic's shares at the date of invitation.</p> <p>Options may be adjusted to reflect a change in the capital structure of the company.</p>	Up to the maximum monthly saving amount as permitted by HMRC.	None.

### Performance measures and targets

The committee believes that, due to commercial sensitivity, it would not be in the best interests of shareholders if it publicly declared company performance targets for bonuses for the year ahead. Consequently, the performance targets for 2014-15 will not be declared in this report but will be declared retrospectively in the FY2015 annual report.

In terms of the LTIP scheme awards, the committee has determined that EPS growth compounded over three years will remain the performance target for determining LTIP vesting. Lower and upper targets will be set each year an LTIP is launched and if the lower target is not met after the three years the LTIP will lapse. On achieving the lower target the LTIP will vest at 25% of the maximum potential award and then continue to vest on a straight line basis until the upper target is achieved, at which point the maximum LTIP potential will vest. The committee believes this scheme will clearly align the motivation of the executive directors with shareholder interests.

# Directors' remuneration policy continued

## Illustration of application of Filtronic's remuneration policy for FY2015 (on the basis that the grant of LTIPs will be 50% of salary)

### Alan Needle



	Minimum	Lower threshold	Upper threshold
Salary and benefits	£223,462	£223,462	£223,462
Bonus	—	—	£100,000
LTIP	—	£25,000	£100,000

### Rob Smith



	Minimum	Lower threshold	Upper threshold
Salary and benefits	£173,200	£173,200	£173,200
Bonus	—	—	£75,000
LTIP	—	£18,750	£75,000

In order to illustrate the potential opportunity available to the executive directors and the sensitivity of pay to performance, the charts above set out outcomes for three performance levels:

- Minimum: Pay is limited to fixed elements of salary, pension allowance and taxable benefits and no vesting under any of the long term incentive plans.
- Achievement of lower threshold: Fixed pay and long term incentives vest at 50% of the maximum.
- Achievement of upper threshold: Fixed pay plus bonuses at the maximum opportunity and long term incentives vest at 100% of the maximum.

It is our intention to reward success. The policy is for a significant proportion of executive directors' total remuneration to be capable of being earned from variable, performance-based incentives. The objective of this policy is to provide rewards and incentives for success. Nearly half of each director's potential remuneration is variable and can only be earned by good group performance reflected in achievement of measurable objectives.

### General remuneration policy for employees

All Filtronic employees are entitled to an annual pay review, pension participation and Sharesave plan participation. Depending upon role and seniority, some employees may also benefit from private healthcare, an annual bonus plan and use of a company leased car (or cash equivalent allowance). In addition, the most senior management staff may also benefit from participation in the executive LTIP. The levels of participation in all bonuses and LTIPs are determined by the board via the remuneration committee in consideration of role responsibility and individual performance contribution.

### Recruitment policy

The committee recognises the importance of attracting the best talent available to the company in order to deliver company strategy and long term shareholder value. The company will, therefore, on recruitment of executive directors or senior management staff, or on the promotion of internal staff to an executive or senior management role, apply the remuneration policy in full. The committee will not approve joining bonuses but will retain the discretionary authority to set first year annual bonus performance targets for new recruits different to those for the other participants in order to reflect a commencement period after budgets have been set and to offer, also at commencement, immediate participation in the then current year LTIP plan.

### Exit payments

When determining any loss of office payment for a departing executive director or senior manager the committee will ensure that a consistent approach is adopted so that there is no reward for poor performance and the liabilities of the group are minimised where appropriate. The underlying principle to be applied is that an individual shall not receive more remuneration benefits as



a consequence of their departure than they would have been contractually entitled to had they continued in employment with the company in the same capacity for their full notice period, with the exception that, for 'good leavers' the committee will retain discretionary authority over the grant of pro-rata LTIP, Sharesave and ESOP awards.

No severance payment shall be made to any employee who is dismissed for serious breach of contract, serious misconduct or under-performance or any acts or omissions that bring the company into disrepute.

### Executive directors' service agreements

The executive directors have service contracts with an indefinite term with notice periods of no more than 12 months. The committee considers these notice periods to be reasonable and proper and in the best interests of all stakeholders.

Executive directors can accept appointments as non-executive directors of other companies and retain any fees received, provided such an appointment does not conflict with their duties to the company. Specific approval of the board is required in each case. Neither of the executive directors currently serves as non-executive directors of other companies.

### Future policy table – non-executive directors

Alignment with strategic objectives	Operation	Maximum Level	Performance Measures and Targets
<b>Chairman and non-executive director fees</b>  To attract and retain high calibre individuals who have the experience to conduct both statutory duties of directors as well as advise on company strategy and oversee its implementation.	Fee reviews are conducted annually, and take into account economic conditions, market levels and the time commitment and contribution of each individual as well as the affordability for the company.  The chairman and the non-executive directors are paid an inclusive fee regardless of whether they serve as chairman or a member of the remuneration committee and / or audit committee, or if they are elected as senior independent director.  Fees are payable entirely in cash. Neither the chairman nor the non-executive directors are permitted to participate in the company's performance-based incentive plans.  The last fee increase was in September 2009.	It is anticipated that any increases to fee levels will typically be in line with market levels of fee inflation. In exceptional circumstances (e.g. material misalignment with the market or a change in the complexity, responsibility or time commitment required to fulfil a non-executive director role) the board retains the discretion to make appropriate adjustments to fee levels to ensure they remain market competitive and fair to the director.	None.

### Non-executive directors' terms of appointment

Non-executive directors are appointed for an initial period of three years with subsequent three year reviews and can be terminated with three months' notice. The chairman's appointment can be terminated by the company on six months' notice.

### Consideration of shareholder views

When determining remuneration, the committee takes into account the views of the company's shareholders and guidelines set by shareholder representative bodies such as the Association of British Insurers. The Board always welcomes feedback from shareholders on the company's remuneration policy and commits to undertaking shareholder consultation in advance of any significant changes to policy. Detail on the votes received on the directors' remuneration report at the AGM is provided in the following year's ARR.

The committee did not consult with employees when preparing the directors' remuneration policy for this report.

# Annual report on remuneration

Details of the service contracts currently in place for directors are as follows:

Name	Executive service agreement appointment date	Key current terms
<b>Alan Needle CEO</b>	Appointed to the board on purchase of Isotek (Holdings) Limited on 16 November 2010  Appointed CEO on 1 August 2012	Base salary £200,000  Annual bonus potential 50% of salary  Potential LTIP 50% of salary  Health insurance  Car allowance  Pension
<b>Rob Smith CFO</b>	Appointed to the board on 16 June 2014	Base salary £150,000  Annual bonus potential 50% of salary  Health insurance  Potential LTIP 50% of salary  Car allowance  Pension

Name	Role	Non-executive terms of appointment date	Fee
Howard Ford	Chairman	Appointed to the board on 5 December 2008 Appointed to chairman on 18 September 2009	£70,000
Graham Meek	Senior non-executive director and audit committee chairman	Appointed to the board on 5 November 1999	£40,000
Reg Gott	Remuneration committee chairman	Appointed to the board on 13 July 2007	£40,000
Michael Roller		Appointed to the board on 1 June 2013	£40,000

Certain sections of the remuneration report constitute the audited part of the reports of the remuneration committee.

The committee sought external independent advice from Ernst & Young in reviewing and revising the executive director and senior management remuneration policy which it proposes to implement for the 2014-2015 financial year.

## Total single figure of remuneration for directors - audited

The executive directors' total remuneration in respect of the year under review are shown below and compared to the previous year. The information in these tables has been audited by the company's independent auditors.

£000's	Salary or fee		Bonus		Benefits		Total remuneration excluding pension contributions and share based payments	
	FY2014	FY2013	FY2014	FY2013	FY2014	FY2013	FY2014	FY2013
<b>Executive directors</b>								
Alan Needle	199	179	—	90	9	9	208	278
Hemant Mardia	—	78	—	—	—	3	—	81
Michael Brennan* (resigned 15 April 2014)	222	123	—	38	8	8	230	169
<b>Non-executive directors</b>								
Howard Ford	70	70	—	—	1	1	71	71
Graham Meek	40	40	—	—	—	—	40	40
Reginald Gott	40	40	—	—	—	—	40	40
Michael Roller	40	—	—	—	—	—	40	—
<b>Total</b>	<b>611</b>	<b>530</b>	<b>—</b>	<b>128</b>	<b>18</b>	<b>21</b>	<b>629</b>	<b>679</b>

\* Michael Brennan received exit payments as part of his remuneration in the year, see 'payments to past directors and exit payments', page 39.

## Notes to the single figure table of remuneration for directors - audited

### Taxable benefits

Taxable benefits in kind were unchanged in FY2014 and comprised car allowance and private health insurance.

In addition to these taxable benefits, the executive directors are provided with life assurance.

### Incentive outcomes for FY2014

Neither the profit nor the operating cash targets required to trigger an annual bonus payment were achieved in FY2014, therefore no performance incentive payments were made.

There was no LTIP scheme launch in FY2011 and therefore no LTIP shares vested in respect of FY2014.

### Payments to past directors and exit payments

Michael Brennan, formerly the CFO, resigned during the year. Michael, at the request of the Board, worked and provided continuing full service until the date of his departure, 15th April 2014. Consequently, Mr Brennan was considered a good leaver and in accordance with policy, he left with a proportion of his share options remaining exercisable. Payments to Mr Brennan include pay in lieu of notice of £69,483 and a compensation payment in respect of potential claims of £41,200, both of which are included in the salary column in the table entitled 'total single figure for remuneration for directors'. In accordance with policy no other exit payments were made.

### Appointment of a new director

Following the resignation of Michael Brennan, Rob Smith was recruited and appointed to the role of CFO and commenced his service with the company on 16 June 2014. Given the disappointing performance of the company in FY2014 and the challenging strategic growth targets the board has set for the business, the board considered that a CFO of exceptional talent, and with a proven track record of achievement with a listed company in the sector was essential. The board was therefore pleased to secure Rob to serve in the role and considered his salary of £150,000 (an increase of 17 per cent over his predecessor) to be appropriate and reasonable.

### Statement on voting at the 2013 annual general meeting

The voting on the directors' remuneration report at the 2013 AGM was as follows:

		Shares
For/discretionary	92.3%	53,738,044
Against	6.1%	3,572,701
Withheld		896,728

### Statement of implementation of remuneration policy in 2014 -15

The remuneration policy, as set out on pages 33 to 37, will be implemented, subject to shareholder approval, with effect from the AGM in 2014 as follows:

### General pay increase

A general pay increase, including the executive and non-executive directors of zero has been implemented. This decision will be reviewed at the beginning of December, subject to first half performance.

### Base salary

Base salaries for the CEO and CFO in FY2015 will be £200,000 and £150,000 respectively.

Executive director	Base salary* as of 1 July 2014	Base salary as of 1 July 2013	% change
Alan Needle	£200,000	£200,000	nil %
Rob Smith	£150,000	n/a	n/a

\*Base salary is the only pensionable portion of the remuneration package

### Pension and benefits

The executive directors will continue to receive pension contributions and benefits in line with the existing policy as described on pages 32 to 37 of the directors' remuneration policy.



# Annual report on remuneration continued

## Annual cash bonus

In line with the proposed policy changes, the maximum bonus for all executive directors will be 50 per cent of base salary.

Fifty per cent of bonus potential will be based on delivering operating profit performance and 50 per cent on delivering operating cash generation performance. Performance against each target will be independently measured and paid accordingly, i.e. the non-performance against one target will not affect payment for achieving the other target.

## Executive directors

FY2015 annual cash bonus targets (as percentage of basic salary):

Metric	On-target cash bonus	Maximum cash bonus
Operating profit	nil%	25%
Operating cash generation	nil%	25%
Total FY2015 cash bonus potential	nil%	50%

## Long term incentive plan (award as a percentage salary)

Conditional awards or nil-cost options will be made under the proposed revised LTIP in FY2015. The vesting of awards will be dependent on EPS growth over the period FY2015 to FY2018. The performance targets are summarised below:

Metric	On-target bonus	Maximum bonus
Operating profit	12.5%	25%
Operating cash generation	12.5%	25%
Total FY2015 cash bonus potential	25%	50%

The awards will be made during FY2015, dependent upon first half performance and full year outlook, but will be subject to approval of the directors' remuneration policy by the shareholders at the 2014 AGM.

Vested shares will be subject to a 50 per cent deferral for two years.

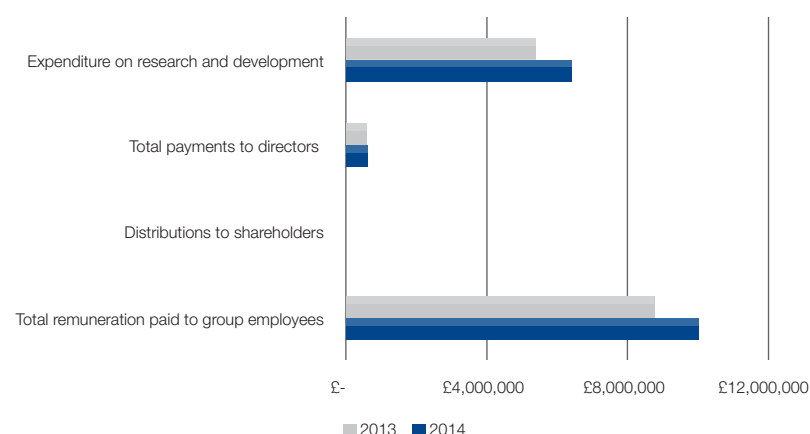
## Non-executive directors

The fees payable to the non-executive directors in FY2015 will be:

Non-executive director	Fee
Howard Ford	£70,000
Graham Meek	£40,000
Reg Gott	£40,000
Michael Roller	£40,000

\* Fees are flat fees and include payments for chairing any committees

## Relative spend on pay



## Percentage change in the remuneration of the chief executive officer compared with the average remuneration of employees

	2014 £000	2013 £000	% change
CEO total remuneration	208	278	-33.7%
Average employee total remuneration	49	51	-4.1%

## Five year chief executive officer total emoluments

Financial year ended 31 May	CEO	Single total figure of remuneration £000	Annual variable element (% of maximum, including deferred element)	PSP/share options vesting outcome (% of maximum)
2014	Alan Needle	208	0%	0%
2013*	Alan Needle	232	90%	0%
2013	Hemant Mardia	81	0%	100%
2012	Hemant Mardia	219	49%	n/a
2011	Hemant Mardia	198	0%	n/a
2010	Hemant Mardia	225	50%	n/a

\* Pro-rata from date of appointment as Chief Executive on 1 August 2012.

## Directors' and relevant senior management holdings of Filtronic shares - audited

The interests of the directors, who were serving as at 31 May 2014, in the company's 0.1 pence ordinary shares, which exclude interests under the share option schemes, are set out below:

	2014		2013	
	Shares	%	Shares	%
Alan Needle	2,246,142	2.3%	2,196,142	2.3%
Howard Ford	106,422	0.1%	93,626	0.1%
Reg Gott	102,159	0.1%	102,159	0.1%
Graham Meek	89,722	0.1%	89,722	0.1%
Michael Roller	26,212	0.0%	—	0.0%
	2,570,657	2.6%	2,481,649	2.6%

All of the above shareholdings are held beneficially and include holdings of directors' connected parties.

Michael Brennan resigned as a director on 15 April 2014. At 31 May 2013 he held 98,165 shares.

## Directors' interests in Filtronic share schemes and option plans

Directors are not required but encouraged to have holdings in the ordinary share capital of the company.

The information in the following tables has been audited by the company's independent auditors.

## Long term incentive scheme: performance shares and nil-cost options - audited

	Vesting Date	2014	Granted during the year	Cancelled during the year	2013
Michael Brennan	29/Nov/13	—	—	114,286	114,286
	02/Sep/16	—	136,986	136,986	—
Alan Needle	02/Sep/16	253,425	253,425	—	—
		253,425	390,411	251,272	114,286

# Annual report on remuneration continued

The performance conditions that apply to conditional awards granted in FY2014 were based on the company's earnings per share (EPS) (calculated as set out below) over a three year performance period comprising the company's financial years: 2013, 2014 and 2015.

The performance condition will be assessed in July 2015 following the completion of the audit of the company for FY2015, and any awarded shares will vest in July 2016.

Each award will vest as follows:

- if the group's earnings before tax, interest, intangible amortisation and exceptional items (EBIT) for FY2015 is equal to £6m giving an EBIT EPS figure (using 96,997,993 shares in issue) of 6.19p per share then 25% of the award will vest;
- if the group's earnings before tax, interest, intangible amortisation and exceptional items for FY2015 is equal to or exceeds £7.5m giving an EBIT EPS figure (using 96,997,993 shares in issue) of 7.73p per share then 100% of the award will vest;
- between threshold vesting at 25% and full vesting at 100%, awards will vest on a pro-rata straight line basis, so that, for example, 50% of the award will vest if the group's earnings before tax, interest, intangible amortisation and exceptional items for FY2015 is equal to £6.5m giving an EBIT EPS figure (using 96,997,993 shares in issue) of 6.70p per share, and 75% of the award will vest if the group's earnings before tax, interest, intangible amortisation and exceptional items for FY2015 is equal to £7m giving an EBIT EPS figure (using 96,997,993 shares in issue) of 7.22p per share.

## All employee share option scheme (Sharesave plan) - audited

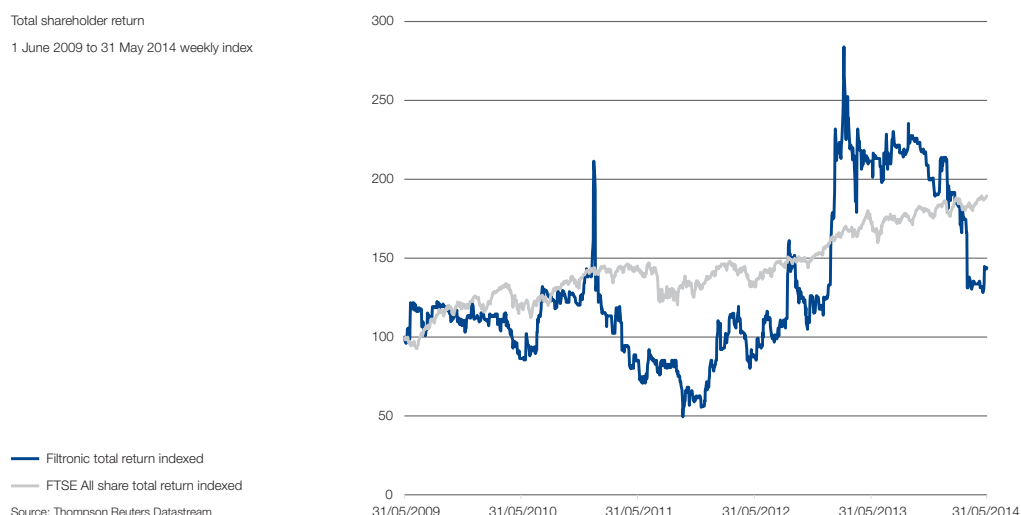
	Exercise period	Option price	2014	2013
Michael Brennan	01/05/2015–31/10/2015	22.6p	<b>30,106</b>	30,106
	01/05/2016–31/10/2016	56.4p	<b>3,893</b>	3,893
			<b>33,999</b>	33,999

The closing middle market price on 30 May 2014 was 42.25p, and on 31 May 2013 it was 62p. The range of middle market share prices during the year ended 31 May 2014 was 69p – 37.62p.

There were no changes in directors' interests between 31 May 2014 and 26 July 2014. The company's register of directors' interests, which is open to inspection at the registered office, contains full details of directors' shareholdings.

## Total shareholder return 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.





# Directors' report

The directors present their report together with the audited consolidated financial statements for the year ended 31 May 2014. The corporate governance statement set out earlier in the governance report forms part of this directors' report and is incorporated by reference.

## Going concern

The group's business, together with the factors likely to affect its future development, performance and position are set out in the strategic report. The group has sufficient financial resources to cover budgeted future cash flows together with contracts with its customers and suppliers across different geographic areas and industries. At 31 May 2014 the group had a cash balance of £2.5m and no interest bearing borrowings. The directors believe that the group is well placed to manage its business risks despite the current trading conditions. In arriving at this conclusion, the board undertook a review of its forecasts for the following two years and, accepting the inherent risks associated with the business, reviewed a number of scenarios and sensitivities. On completion of this process the board was satisfied that the going concern principle was appropriate for the preparation of the financial statements.

In accordance with the corporate governance requirements and the statement of directors' responsibilities on page 44 to 45, the directors confirm that they have a reasonable expectation that the group has adequate financial resources to continue to trade for the foreseeable future. Thus, they continue to adopt the going concern basis in preparing the financial statements.

## Directors and their interests

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

Alan Needle  
Michael Brennan (resigned 15 April 2014)  
Howard Ford  
Graham Meek  
Reginald Gott  
Michael Roller

Details of directors' interests in the share capital of the company are set out in the remuneration report on page 41.

Alan Needle retires by rotation and, being eligible, offers

himself for re-election at the annual general meeting.

Rob Smith, having been appointed by the board on 16 June 2014, offers himself for 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

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

## Research and development expenditure

Research and development costs were £6.4m (2013: £5.4m). Grant income of £nil (2013: £0.1m) was received to assist with part of these costs.

## Cash balances

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.

## Substantial shareholdings

Up to 31st May 2014 the company had been notified, in accordance with chapter 5 of the disclosure and transparency rules, of the following voting rights as a shareholders of the company. An analysis of shareholders as at 31 May 2013 (as disclosed by shareholders via TR1), is set out in the table below.

As at 31 May 2014 the company had issued share capital of 97,160,986 10p ordinary shares.

Shareholder	Shareholding (number of 10p ordinary shares)	Percentage of issued share capital
Aberforth Partners LLP	18,664,173	19.2 %
Legal & General Investment Management	17,062,172	17.6%
Prudential plc	3,863,785	4.0%
John David Rhodes	3,794,769	3.9%
Church of England Commissioners	2,945,964	3.0%

# Directors' report continued

## Financial results and dividend

The results for the year are set out in the income statement on page 48. The position at the end of the year is shown in the balance sheet on page 50.

The directors are not recommending payment of a dividend (2013: nil).

## Share capital

The company's share capital consists of 10p ordinary shares. The rights and obligations attached to each share are equal. Each share carries the right to one vote at general meeting of the company and carries no right to fixed income. 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 in September 2013.

## Emissions statement

All disclosures concerning the group's greenhouse gas emissions required by the mandatory carbon regulations are contained in the corporate social responsibility report which forms part of the strategic report on pages 21 to 22.

## Political and charitable contributions

No contributions were made for political purposes. The group donated £100 (2013: £nil) to various charities.

## Equal opportunities

The directors are committed to ensuring that there are equal opportunities throughout the group for all employees with no discrimination on account of race, gender, age, sexual orientation, disability, political views or religious beliefs.

## Disabled employees

Applications for employment by disabled persons are always welcome and fully considered bearing in mind the skills and aptitude of the applicant concerned. Where an employee becomes disabled, all reasonable efforts are made to ensure that employment with the group continues and that appropriate training is arranged. It is the policy of the group to ensure that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other members of staff.

## Employee communication

Employee engagement with its strategy and values is vital to the success of the group. The directors place great importance on keeping employees informed on matters that affect them as employees as well as matters that affect the performance of the group. This is achieved through formal and informal meetings as well as through group communications sessions.

## Annual general meeting

The annual general meeting of the company will be held on 26 September 2014 at the offices of Pinsent Masons LLP, 1 Park Row, Leeds, LS1 5AB. Full details of the business to be transacted at the meeting will be set out in the notice of annual general meeting.

## 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 strategic report, 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.

The directors, as at the date of this report, whose names and functions are listed in the board of directors on page 25 confirm that, to the best of their knowledge:

- the financial statements, which have been 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 strategic report includes a fair review of the development of the business and the position of the company and the undertakings included in the consolidation taken as a whole, together with a description of the risks and uncertainties they face.

### Statement of directors' responsibilities

#### Disclosure of information to the auditor

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 auditor is 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 auditor is aware of that information.

#### Auditor

KPMG LLP has expressed a willingness to continue in office as auditor and a resolution to reappoint KPMG LLP will be proposed at the forthcoming annual general meeting.

#### Maura Moynihan

Company secretary  
14 August 2014

# Independent auditor's report to the members of Filtronic plc only

## Opinions and conclusions arising from our audit

### 1 Our opinion on the financial statements is unmodified

We have audited the financial statements of Filtronic Plc for the year ended 31 May 2014 set out on pages 48 to 80. 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 2014 and of the group's loss for the year then ended;
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- 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.

### 2 Our assessment of risks of material misstatement

In arriving at our audit opinion above on the financial statements the risks of material misstatement that had the greatest effect on our audit were as follows:

#### Carrying amounts of inventories (carrying amount of £3,933,000)

Refer to pages 28 to 29 (Audit Committee Report), 58 (accounting policy) and page 69 (financial disclosure).

- The risk: The risk relating to the carrying amount of inventories arises from both the high value of inventory held by the Group and the judgement required to record inventory at the lower of cost and net realisable value. Products are hi-tech and often specific to individual customers which means that net realisable value is determined by the Directors' estimate of forecast customer demand and selling price. The nature of the business means that there can be inherent uncertainty in customer forecasts because the timing of contracts is not always certain.
- Our response: Our audit procedures included, among others, considering the extent to which the Directors' estimates take into account a balanced assessment of the latest available information in respect of inventory valuation, specifically forecast sales. For this purpose, we have tested the Group's budgeting process upon which forecasts are based and the principles and integrity of the assumptions and methodology used, in particular revenue growth. In assessing the level of provision required to record inventory at the lower of cost and net realisable value, we considered the ageing profile of stock and the accuracy of the inventory provision in previous years by comparing the assumptions made for inventory lines included in the provision to

subsequent sales activity for these products. We considered all the individual components of the current year inventory provision and assessed whether the assumptions applied in their calculation, specifically in respect of related sales forecasts, are underpinned by forecasts prepared for the Group for the next two years. We have also considered the adequacy of the Group's disclosures about the degree of estimation involved in arriving at the provision and movements in that provision.

#### Warranty provisions (carrying amount of £108,000)

Refer to pages 28 to 29 (Audit Committee Report), 59 (accounting policy) and page 71 (financial disclosure).

- The risk: The Group's products are sold with warranties. As the Group is constantly developing new products, there can be limited historical evidence available regarding warranty claims and return rates. The products are usually hi-tech in nature. Determining the amount of provision to be recognised requires the Group to make judgements and estimates that are inherently subjective. The basis of provisioning in respect of certain products has been refined this year and there is a risk that the provision could be materially misstated.
- Our response: Our audit procedures included, among others, considering the extent to which the Directors' estimates of the costs of future warranty claims take into account the latest available information regarding costs of historical warranty claims recorded for the underlying products. We have performed analytical procedures comparing the cost of warranty claims to cost of sales for the last three years, and assessed whether the balances in the current year fall within the trend. We also considered the Group's historical experience in assessing the level of provision required by comparing warranty costs incurred with provisions made. We have also considered the adequacy of the Group's disclosures about the degree of estimation involved at arriving at the provision.

### 3 Our application of materiality and an overview of the scope of our audit

The materiality for the financial statements as a whole was set at £650,000. This has been determined with reference to a benchmark of Group Revenue (of which it represents 2%) which we consider to be one of the principal considerations for members of the company in assessing the financial performance of the Group.

We agreed with the audit committee to report to it all corrected and uncorrected misstatements we identified through our audit with a value in excess of £32,500 in addition to other audit misstatements below that threshold that we believe warranted reporting on qualitative grounds.



Audits for group reporting purposes were performed by the Group audit team at the key reporting components in the UK, China and Sweden and by component auditors in the United States of America,. These audits covered 100% of total Group revenue, Group profit before taxation and total Group assets.

The audits undertaken for group reporting purposes at the key reporting components of the Group were all performed to materiality levels set by, or agreed with, the Group audit team. These materiality levels were set individually for each component and ranged from £100,000 to £500,000.

Detailed audit instructions were sent to the overseas auditors in the United States of America. These instructions covered the significant audit areas that should be covered by this audit (which include the relevant risks of material misstatement detailed above) and set out the information required to be reported back to the Group audit team. Regular e-mail contact was maintained with the overseas audit team throughout the process, including discussions on issues as they arose.

#### 4 Our opinion on other matters prescribed by the Companies Act 2006 is unmodified

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 Strategic Report and 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 Report set out on pages 27 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.

#### 5 We have nothing to report in respect of the matters on which we are required to report by exception

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the annual report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

In particular, we are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our audit and the Directors' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy; or
- the Audit Committee Report does not appropriately address matters communicated by us to the audit committee.

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' report, set out on page 43, in relation to going concern; and
- the part of the Corporate Governance Statement on page 27 relating to the company's compliance with the nine provisions of the 2010 Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

#### Scope of report and responsibilities

As explained more fully in the Directors' Responsibilities Statement set out on page 44, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at [www.frc.org.uk/auditscopeukprivate](http://www.frc.org.uk/auditscopeukprivate). This report is made solely to the company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at [www.kpmg.com/uk/auditscopeukco2013a](http://www.kpmg.com/uk/auditscopeukco2013a), which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

#### Johnathan Pass

for and on behalf of KPMG LLP, Statutory Auditor  
Chartered Accountants  
1 The Embankment  
Neville Street  
Leeds  
LS1 4DW  
14 August 2014

# Consolidated income statement

for the year ended 31 May 2014

		Group	
	Note	2014 £000	2013 £000
<b>Revenue</b>		<b>32,900</b>	39,976
<b>Operating (loss)/profit before amortisation and exceptional items</b>		<b>(442)</b>	3,051
Amortisation of intangibles		(2,419)	(2,419)
Exceptional items	5	(825)	(392)
<b>Operating (loss)/profit</b>	4	<b>(3,686)</b>	240
Finance income/(costs) — net	11	13	(2)
<b>(Loss)/profit before taxation</b>		<b>(3,673)</b>	238
Taxation	12	858	46
<b>(Loss)/profit for the period</b>		<b>(2,815)</b>	284
<b>Basic (loss)/earnings per share</b>	13	<b>(2.90p)</b>	0.29p
<b>Diluted (loss)/earnings per share</b>	13	<b>(2.90p)</b>	0.29p

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

The above results are all as a result of continuing operations.

# Consolidated statement of comprehensive income

for the year ended 31 May 2014

		Group	
	Note	2014 £000	2013 £000
<b>(Loss)/profit for the period</b>		<b>(2,815)</b>	284
<b>Other comprehensive income</b>			
<b>Items that are or may be subsequently reclassified to profit and loss:</b>			
Currency translation movement arising on consolidation	26	(474)	54
		(474)	54
<b>Total comprehensive income for the period</b>		<b>(3,289)</b>	338

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 2014

		Group	
	Note	2014 £000	2013 £000
<b>Non-current assets</b>			
Goodwill and other intangibles	15	5,653	8,072
Property, plant and equipment	16	2,865	3,005
Deferred tax	19	485	302
		<b>9,003</b>	11,379
<b>Current assets</b>			
Inventories	17	3,933	5,356
Trade and other receivables	18	9,941	17,237
Cash and cash equivalents		2,531	2,375
		<b>16,405</b>	24,968
<b>Total assets</b>		<b>25,408</b>	36,347
<b>Current liabilities</b>			
Trade and other payables	20	7,447	13,611
Provisions	21	333	605
Deferred income	22	169	229
Interest bearing borrowings	35	—	496
		<b>7,949</b>	14,941
<b>Non-current liabilities</b>			
Deferred tax	19	485	1,112
Deferred income	22	75	96
		<b>560</b>	1,208
<b>Total liabilities</b>		<b>8,509</b>	16,149
<b>Net assets</b>		<b>16,899</b>	20,198
<b>Equity</b>			
Share capital	24	9,716	9,700
Share premium	25	5,145	5,111
Translation reserve	26	(436)	38
Retained earnings	28	2,474	5,349
<b>Total equity</b>		<b>16,899</b>	20,198

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

Company number 2891064

Approved by the Board on 14 August 2014 and signed on its behalf by

## Alan Needle

Chief Executive Officer  
14 August 2014



# Consolidated statement of changes in equity

for the year ended 31 May 2014

	Note	Group	
		2014 £000	2013 £000
Opening total equity		<b>20,198</b>	19,841
Total comprehensive income for the period	26,28	<b>(3,289)</b>	338
New shares issued (net of issue costs)	24,25	<b>50</b>	47
Share-based payments	31	<b>(60)</b>	163
Exercise of share awards		—	(191)
<b>Closing total equity</b>		<b>16,899</b>	20,198

# Company statement of changes in equity

for the year ended 31 May 2014

		Company	
		2014 £000	2013 £000
Opening total equity		<b>18,281</b>	18,994
Total comprehensive income for the period	26	<b>(1,038)</b>	(656)
New shares issued (net of issue costs)	24,25	<b>50</b>	47
Share-based payments	31	<b>(132)</b>	87
Exercise of share awards		—	(191)
<b>Closing total equity</b>		<b>17,161</b>	18,281

# Consolidated cash flow statement

for the year ended 31 May 2014

		Group	
	Note	2014 £000	2013 £000
<b>Cash flows from operating activities</b>			
(Loss)/profit for the period		(2,815)	284
Taxation		(858)	(46)
Finance (income)/costs — net		(13)	2
<b>Operating (loss)/profit</b>	34	<b>(3,686)</b>	240
Share-based payments		(60)	163
Loss/(profit) on disposal of plant and equipment		27	(24)
Depreciation		1,083	875
Amortisation of intangibles		2,419	2,419
Movement in inventories		1,315	(2,158)
Movement in trade and other receivables		6,950	(6,960)
Movement in trade and other payables		(6,048)	5,189
Movement in provision		(272)	40
Change in deferred income including government grants		(81)	(58)
Tax paid		(32)	—
<b>Net cash from/(used in) operating activities</b>	34	<b>1,615</b>	(274)
<b>Cash flows from investing activities</b>			
Interest received		13	8
Acquisition of plant and equipment		(1,058)	(1,532)
Proceeds on sale of assets		32	55
<b>Net cash used in investing activities</b>	34	<b>(1,013)</b>	(1,469)
<b>Cash flows from financing activities</b>			
Proceeds from exercise of share options		50	47
Exercise of share awards		—	(191)
Interest paid		—	(10)
Movement in interest bearing borrowings		(496)	496
<b>Net cash (used in)/from financing activities</b>	34	<b>(446)</b>	342
<b>Movement in cash and cash equivalents</b>		<b>156</b>	(1,401)
Currency exchange movement		—	31
Opening cash and cash equivalents		2,375	3,745
<b>Closing cash and cash equivalents</b>		<b>2,531</b>	2,375

# Company balance sheet

at 31 May 2014

		Company	
	Note	2014 £000	2013 £000
<b>Non-current assets</b>			
Investments in subsidiaries	14	10,569	10,564
<b>Current assets</b>			
Trade and other receivables	18	12,840	10,792
Cash and cash equivalents		277	118
		<b>13,117</b>	10,910
<b>Total assets</b>		<b>23,686</b>	21,474
<b>Current liabilities</b>			
Trade and other payables	20	6,300	3,193
Provision	21	225	—
<b>Total liabilities</b>		<b>6,525</b>	3,193
<b>Net assets</b>		<b>17,161</b>	18,281
Equity			
Share capital	24	9,716	9,700
Share premium	25	5,145	5,111
Retained earnings	28	2,300	3,470
<b>Total equity</b>		<b>17,161</b>	18,281

Approved by the Board on 14 August 2014 and signed on its behalf by

Company number 2891064

## Alan Needle

Chief Executive Officer

14 August 2014

# Company cash flow statement

for the year ended 31 May 2014

	Company	
	2014	2013
	£000	£000
<b>Cash flows from operating activities</b>		
<b>Loss for the period</b>	<b>(1,038)</b>	(656)
Finance costs	200	10
Finance income	(13)	(38)
<b>Operating loss</b>	<b>(851)</b>	(684)
Share-based payments	(132)	87
Movement in trade and other receivables	(2,248)	(389)
Movement in trade and other payables	3,107	27
Movement in provision	225	—
<b>Net cash from/(used in) operating activities</b>	<b>101</b>	(959)
<b>Cash flows from investing activities</b>		
Interest received	13	8
Interest paid	—	(10)
Set up costs in new subsidiary	(5)	—
<b>Net cash from/(used in) investing activities</b>	<b>8</b>	(2)
<b>Cash flows from financing activities</b>		
Proceeds from exercise of share options	50	47
Exercise of share awards	—	(191)
<b>Net cash from/(used in) financing activities</b>	<b>50</b>	(144)
<b>Decrease in cash and cash equivalents</b>	<b>159</b>	(1,105)
Currency exchange movement	—	30
Opening cash and cash equivalents	118	1,193
<b>Closing cash and cash equivalents</b>	<b>277</b>	118



# Notes to the financial statements

for the year ended 31 May 2014

## 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).

In accordance with the corporate governance requirements and the statement of directors' responsibilities, the directors confirm that they have a reasonable expectation that the group has adequate financial resources to continue to trade 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. Intragroup 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.

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.

### 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.

# Notes to the financial statements

for the year ended 31 May 2014

## 1 Accounting policies (continued)

### 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.

The timing of the transfers of risks and rewards varies depending on the individual terms of the contract of sale. The majority of sales are made at the point the product leaves the Filtronic production facility but there are sales where the revenue is recognised once the product is delivered to the customer. In addition some customers require Filtronic to store items on their behalf, in this instance, revenue is recognised when the goods have been invoiced and when the products have been moved to a stock location for customer property.

### 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 operates share option and share award schemes, under which share options and share awards are 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. At each reporting period these vesting expectations were revised as appropriate.

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

### 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.

## 1 Accounting policies (continued)

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.

### 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 an 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 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.

# Notes to the financial statements

for the year ended 31 May 2014

## 1 Accounting policies (continued)

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.

### 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.

### Financial liabilities

Other current financial liabilities comprise borrowings and trade and other payables, and are recognised initially at fair value and subsequently measured at amortised cost.

### Current tax

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

### 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.

Deferred tax assets of £302,000 have been reclassified as non-current from current in the year.



## 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.

### Dilapidations and onerous leases

A provision for dilapidations and onerous leases is recognised in the balance sheet on a lease by lease basis and are based on the group's best estimates of the required cost to settle the obligations.

### 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.

### Accounting developments

- (a) A number of new standards, amendments to standards and interpretations are effective for the year ended 31 May 2014.
  - IFRS 13 'Fair Value Measurement'. IFRS 13 establishes a single framework for measuring fair value and making disclosures about the fair value measurements when such measurements are required or permitted by other IFRSs. It unifies the definition of fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It replaces and expands the disclosure requirements about fair value measurements in other IFRSs, including IFRS 7. As a result, the Group has included additional disclosures in this regard.
  - 'Presentation of items of Other Comprehensive Income' (Amendments to IAS 1). As a result of the amendments to IAS 1, the Group has modified the presentation of items of OCI in its statement of profit or loss and OCI, to present separately items that would be reclassified to profit or loss from those that would not be. Comparative information has been re-presented accordingly.
- (b) There are also a number of new standards, amendments to standards and interpretations that are effective for financial statements after this reporting period, but the group has not adopted them early. None of these is expected to have a material impact on the results or financial position of the group.

The following adopted IFRSs have been issued but have not been applied by the group in these consolidated financial statements:

- IFRS 10 'Consolidated financial statements, (2011)
- IFRS 12 'Disclosures of involvement with other entities, (2011)
- IAS 27 'Separate financial statements (revised 2011)' has been amended for the issuance of IFRS 10 but retains the current guidance for separate financial statements; and
- IAS 28 'Investments in associates and joint ventures (revised 2011)' has been amended for conforming changes based on the issuance of IFRS 10 and IFRS 11.

Each of these standards has an effective date for periods beginning on or after 1 January 2014. The impact of these new standards is not expected to have a significant impact on the group.

# Notes to the financial statements

for the year ended 31 May 2014

## 1 Accounting policies (continued)

### Forward currency contracts

Forward currency contracts are held at fair value. The gain or loss on re-measurement to fair value is recognised immediately in the consolidated income statement.

## 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.

### 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.

### Debtors

In line with industry practice Filtronic extends credit terms to its customers. Due to the concentration of debtors the effect of any one debtor defaulting would be material on the group's financial statements. Estimates and judgements are made when valuing the debtor as to the recoverability. A bad debt provision is created when it is unlikely the debt will be recovered.

### 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

In line with the requirements of IFRS, the group's policy is to capitalise development expenditure as intangible assets when all the following criteria are met:

- the technical feasibility of completing the asset so that it will be available for use or sale;
- the intention to complete the asset and use or sell it;
- the ability to use or sell the asset;
- the asset will generate probable future economic benefits and demonstrate the existence of a market or the usefulness of the asset if it is to be used internally;
- the availability of adequate technical, financial and other resources to complete the development and to use or sell it; and
- the ability to measure reliably the expenditure attributable to the intangible asset.

This process is 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 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 reporting information and management structures within the group. The group has four customers representing individually over 10 per cent each and in aggregate over 74 per cent of revenue. This is split as follows:

- Customer A (Wireless) — 24%
- Customer B (Wireless) — 19%
- Customer C (Broadband) — 18%
- Customer D (Wireless) — 13%

The group operates in two trading business segments:

- The design and manufacture of transceiver modules and filters for backhaul microwave linking of base stations used in Wireless telecommunications networks (Broadband).
- The design of radio frequency conditioning product for base stations used in Wireless telecommunication networks (Wireless).

The group also contains a central services segment that provides support to the trading businesses.

In the table below reportable segment assets and liabilities include intersegment balances. These have 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		Wireless		Central services		Total	
	2014 £000	2013 £000	2014 £000	2013 £000	2014 £000	2013 £000	2014 £000	2013 £000
Revenue	9,736	8,127	23,164	31,849	—	—	32,900	39,976
Finance income	—	—	—	—	13	8	13	8
Finance costs	—	—	—	—	—	(10)	—	(10)
Depreciation	605	621	478	254	—	—	1,083	875
Reportable segment (loss)/profit before amortisation of intangibles and exceptional items	(2,285)	(2,449)	2,619	6,378	(776)	(878)	(442)	3,051
Reportable segment (loss)/profit before amortisation of intangibles and income tax	(2,749)	(2,720)	2,563	6,378	(1,068)	(1,001)	(1,254)	2,657
Reportable segment assets	10,861	7,293	9,005	20,499	13,032	16,734	32,898	44,526
Capital expenditure	326	595	732	937	—	—	1,058	1,532
Reportable segment liabilities	14,422	8,298	3,340	16,824	788	1,757	18,550	26,879

# Notes to the financial statements

for the year ended 31 May 2014

## 3 Segmental analysis (continued)

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

	2014 £000	2013 £000
<b>Depreciation and amortisation</b>		
Reportable segment totals	1,083	875
Adjustments/amortisation of intangibles	2,419	2,419
Consolidated depreciation and amortisation	3,502	3,294
<b>(Loss)/profit before taxation</b>		
Total (loss)/profit for reportable segments	(1,254)	2,657
Group/unallocated	(2,419)	(2,419)
Consolidated (loss)/profit before taxation	(3,673)	238
<b>Assets</b>		
Total assets for reportable segments	32,898	44,526
Intercompany	(10,041)	(10,730)
Group/unallocated	2,551	2,551
Consolidated total assets	25,408	36,347
<b>Liabilities</b>		
Total liabilities for reportable segments	18,550	26,879
Intercompany	(10,041)	(10,730)
Consolidated total liabilities	8,509	16,149

### 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.

	2014 £000	2013 £000
<b>Revenue by destination</b>		
United Kingdom	10,429	14,083
Europe	4,351	7,880
Americas	15,081	6,001
Rest of the world	3,039	12,012
	32,900	39,976
<b>Split of non-current assets by location</b>		
United Kingdom	5,963	8,016
Europe	173	—
Americas	2,635	3,048
Rest of the world	232	315
	9,003	11,379

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



#### 4 Operating (loss)/profit

	2014 £000	2013 £000
<b>Revenue</b>	<b>32,900</b>	39,976
Other operating income	(21)	(58)
Raw materials and consumables	18,838	23,047
Wages and salaries	7,784	7,417
Social security costs	867	654
Pension costs	456	382
Share-based payments	(60)	125
Exceptional redundancy costs	—	180
Staff costs	9,047	8,758
Amortisation of intangibles	2,419	2,419
Depreciation	1,083	875
Depreciation and amortisation	3,502	3,294
Other operating charges	5,220	4,695
<b>Operating costs</b>	<b>36,586</b>	39,736
<b>Operating (loss)/profit</b>	<b>(3,686)</b>	240

The operating (loss)/profit is stated after the exceptional items in note 5. Exceptional items have all been charged through other operating charges in 2014.

#### 5 Exceptional items

Operating (loss)/profit is stated after charging exceptional items as follows:

	2014 £000	2013 £000
Management reorganisation	—	212
Redundancy costs	—	180
Dilapidation of premises of discontinued operations	310	—
Filtronic Broadband relocation	463	—
Swedish entity set up costs	52	—
	<b>825</b>	392

There is a charge for dilapidations of premises (£310,000) which relates to a liability for dilapidations following the termination of two leases relating to the disposal of the group's former UK defence business. The charge reflects recent negotiations with the landlords and is based on the company's best estimate of the liability.

During the year Filtronic Broadband Limited relocated to the North East Technology Park in Sedgefield, significantly lowering the fixed cost base of the entity.

Costs of £52,000 were incurred in setting up a Swedish entity for the group to enter the antenna market.

#### 6 Operating items

	2014 £000	2013 £000
Operating (loss)/profit is stated after charging/(crediting):		
Research and development costs	6,339	5,432
Operating lease rentals	243	194
Foreign exchange loss	168	12

# Notes to the financial statements

for the year ended 31 May 2014

## 7 Auditor's remuneration

The company's auditor is KPMG LLP. The auditor's remuneration was as follows:

	2014 £000	2013 £000
Company auditor:		
Audit of the group and company financial statements	10	10
Company auditor and their associates:		
Audit of subsidiaries' financial statements pursuant to legislation	35	39
Other services pursuant to such legislation	7	7
Taxation services	24	16
Other services	13	5
	<b>89</b>	<b>77</b>

## 8 Employees

The average number of employees comprised:

	2014 Number	2013 Number
Manufacturing	85	93
Research and development	80	62
Sales	3	2
Administration	18	16
	<b>186</b>	<b>173</b>

## 9 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 31 to 42. The compensation of the directors was:

	2014 £000	2013 £000
Salary or fees	500	530
Loss of office	111	—
Bonuses	—	128
Benefits	18	21
Total remuneration excluding pension contributions and share-based payments	629	679
Pension contributions	24	29
Share-based payments	1	30
	<b>654</b>	<b>738</b>

The directors are related parties.

## 10 Related party transaction

### Identity of related parties

The group has a related party relationship with its subsidiaries and with its directors.

### Transactions with subsidiaries

The main transactions between the company and its subsidiaries are management administration recharges to its subsidiaries of £432,000 (2013: £432,000) and a royalty charge of 1 per cent of Wireless sales to the Wireless business of £230,000 (2013: £314,000). The royalty charge is eliminated on consolidation.

The company also acts as a central service to distribute money around the group to ensure subsidiaries are adequately funded to meet obligations and to invest funds from subsidiaries where surplus cash exists. The total figures for these transactions along with the management and royalty charge can be seen in notes 18 and 20 through the movement in the company's intercompany receivables and payables.

### Transactions with key management personnel

Key management personnel is considered to be the executive directors of the company. The remuneration given to these individuals is disclosed in the directors' remuneration report on pages 38 to 42.

## 11 Finance income/(costs) — net

	2014 £000	2013 £000
Interest income	13	8
Interest costs of borrowing	—	(10)
	13	(2)

## 12 Taxation

	2014 £000	2013 £000
Recognised in the income statement		
<b>Current tax (credit)/charge</b>		
Overseas taxation in the period	43	15
Adjustment in respect of prior year — R&D tax credit	(65)	—
Total current tax (credit)/charge	(22)	15
<b>Deferred tax credit</b>		
Release from deferred tax liability	(627)	(648)
(Origination) and reversal of temporary differences	(209)	587
Total deferred tax	(836)	(61)
Income tax credit	(858)	(46)

# Notes to the financial statements

for the year ended 31 May 2014

## 12 Taxation continued

The reconciliation of the effective tax rate is as follows:

		<b>2014</b>		2013
		<b>£000</b>		£000
(Loss)/profit before taxation		<b>(3,673)</b>		238
		<b>2014</b>		2013
		<b>£000</b>		£000
(Loss)/profit before taxation multiplied by standard rate of corporation tax in the UK	<b>(23%)</b>	<b>(833)</b>	24%	57
Disallowable items	<b>4%</b>	<b>164</b>	12%	28
Tax relief for share options exercised	<b>—</b>	<b>—</b>	(25%)	(59)
Income not taxable	<b>(6%)</b>	<b>(205)</b>	(1%)	(3)
Deferred tax not recognised	<b>11%</b>	<b>405</b>	102%	243
Trading losses utilised	<b>—</b>	<b>—</b>	(104%)	(248)
Impact of rate change on deferred tax	<b>(1%)</b>	<b>(32)</b>	(17%)	(41)
Adjustment in respect of prior years — R&D credit	<b>(2%)</b>	<b>(65)</b>	—	—
R&D tax credit	<b>(8%)</b>	<b>(276)</b>	—	—
FX rate change of deferred tax	<b>1%</b>	<b>25</b>	—	—
Foreign tax not at UK rate	<b>(1%)</b>	<b>(41)</b>	15%	36
Deferred tax liability write off	<b>—</b>	<b>—</b>	(8%)	(19)
Recognition of capital allowances	<b>—</b>	<b>—</b>	(17%)	(40)
<b>Taxation</b>	<b>(23%)</b>	<b>(858)</b>	(19%)	(46)

## 13 (Loss)/earnings per share

		<b>Group</b>
	<b>2014</b>	2013
	<b>£000</b>	£000
<b>(Loss)/profit for the period</b>	<b>(2,815)</b>	284
	<b>000</b>	000
<b>Basic weighted average number of shares</b>	<b>97,078</b>	96,951
Dilution effect of share options	<b>—</b>	592
Dilution effect of share awards	<b>—</b>	70
<b>Diluted weighted average number of shares</b>	<b>97,078</b>	97,613
<b>Basic (loss)/earnings per share</b>	<b>(2.90p)</b>	0.29p
<b>Diluted (loss)/earnings per share</b>	<b>(2.90p)</b>	0.29p

## 14 Investments in subsidiaries

	Company investments in subsidiaries £000
<b>Cost</b>	
At 1 June 2012 and 31 May 2013	21,110
Additions	5
<b>At 31 May 2014</b>	<b>21,115</b>
<b>Impairment</b>	
At 1 June 2012, 31 May 2013 and May 2014	10,546
Carrying amount at 1 June 2012 and 31 May 2013	10,564
Carrying amount at 31 May 2014	10,569

The company's subsidiaries are related parties.

The subsidiaries at 31 May 2014, 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
<b>Owned by Filtronic Holdings UK Limited:</b>				
Filtronic Wireless AB	Sweden	SEK1 ordinary shares	100%	Design and manufacture of Filtronic products for telecommunication systems
<b>Owned by Isotek (Holdings) Limited:</b>				
Filtronic Wireless Limited	UK	1p ordinary shares	100%	Design and manufacture of Filtronic products for telecommunication systems
Filtronic Wireless Inc	USA	\$1 ordinary shares	100%	Design and manufacture of Filtronic products for telecommunication systems
Isotek Limited	UK	1p ordinary shares	100%	Dormant company
<b>Owned by Filtronic Wireless Limited:</b>				
Isotek Hong Kong Holdings Limited	Hong Kong	HK \$1 ordinary shares	100%	Holding company
<b>Owned by Isotek Hong Kong Holdings Limited:</b>				
Isotek Suzhou	China	USD \$350,000 paid in share capital	100%	Design and manufacture of Filtronic products for telecommunication systems
Filtronic Wireless Suzhou	China	USD \$162,000 paid in share capital	100%	Design and manufacture of Filtronic products for telecommunication systems



# Notes to the financial statements

for the year ended 31 May 2014

## 15 Goodwill and other intangibles

	Goodwill £000	Other intangibles (core technology) £000	Total £000
<b>Cost</b>			
At 1 June 2012, 31 May 2013 and 31 May 2014	3,235	10,884	14,119
<b>Amortisation</b>			
At 1 June 2012	—	3,628	3,628
Provided in year	—	2,419	2,419
At 31 May 2013	—	6,047	6,047
Provided in year	—	2,419	2,419
<b>At 31 May 2014</b>	<b>—</b>	<b>8,466</b>	<b>8,466</b>
Carrying amount at 1 June 2012	3,235	7,256	10,491
Carrying amount at 31 May 2013	3,235	4,837	8,072
<b>Carrying amount at 31 May 2014</b>	<b>3,235</b>	<b>2,418</b>	<b>5,653</b>

Goodwill and other intangibles relate to the acquisition of Isotek (Holdings) Limited.

Goodwill is allocated to the Wireless 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 3. 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:

- budgets incorporating cash flows have been prepared to 31 May 2015 based on past experience and actual operating results;
- cash flows for a further 6 years have been extrapolated from the second half of FY2015. A revenue growth factor of 5 per cent was applied to the projections together with cost inflation of 3 per cent; and
- a pre-tax discount rate of 12 per cent was applied in determining the recoverable amount of the unit, being the estimated weighted average cost of capital for the wireless CGU.

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.

## 16 Property, plant and equipment

	Group plant and equipment £000
<b>Cost</b>	
At 1 June 2012	7,486
Additions	1,532
Disposals	(108)
Currency translation movement	5
At 31 May 2013	8,915
Additions	1,058
Disposals	(146)
Currency translation movement	(89)
<b>At 31 May 2014</b>	<b>9,738</b>
<b>Depreciation and impairment</b>	
At 1 June 2012	5,111
Depreciation	875
Disposals	(78)
Currency translation movement	2
<b>At 31 May 2013</b>	<b>5,910</b>
Depreciation	1,083
Disposals	(89)
Currency translation movement	(31)
<b>At 31 May 2014</b>	<b>6,873</b>
Carrying amount at 1 June 2012	2,375
Carrying amount at 31 May 2013	3,005
<b>Carrying amount at 31 May 2014</b>	<b>2,865</b>

## 17 Inventories

	Group		Company	
	2014 £000	2013 £000	2014 £000	2013 £000
Raw materials	1,968	3,940	—	—
Work in progress	1,445	669	—	—
Finished goods	520	747	—	—
	<b>3,933</b>	5,356	—	—
Inventories are stated net of provision	<b>1,596</b>	1,542	—	—

The amount charged to the income statement in the year in respect of write downs of inventories is £200,000 (2013: £375,000). The amount credited to the income statement in the year in respect of reversals of write downs of inventories is £146,000 (2013: £221,000), principally resulting from the subsequent sale of inventory previously provided for. These amounts are classified within cost of sales in the consolidated income statement.

# Notes to the financial statements

for the year ended 31 May 2014

## 18 Trade and other receivables

	Group		Company	
	2014 £000	2013 £000	2014 £000	2013 £000
Trade receivables	8,908	16,514	—	—
Group receivables	—	—	12,818	10,729
Other receivables and prepayments	1,033	723	22	63
	9,941	17,237	12,840	10,792
Trade receivables are stated net of provision	—	16	—	—

## 19 Deferred tax

	Group	
	2014 £000	2013 £000
<b>Deferred tax liability</b>		
Opening balance	1,112	1,762
Release to income statement	(627)	(650)
<b>Closing balance</b>	485	1,112

The deferred tax liability largely relates to the intangible assets arising upon acquisition of the Wireless business. The liability at acquisition was £2,938,000 and at 31 May 2014 was £485,000. This will be released to the income statement in the next financial year.

Deferred tax assets of £302,000 have been reclassified as non-current from current in the year.

	Group	
	2014 £000	2013 £000
<b>Deferred tax assets</b>		
Opening balance	302	887
Tax losses recognised/(used)	192	(585)
Effect of change in UK corporation tax rate	(9)	—
<b>Closing balance</b>	485	302

The deferred tax assets relate to the recognition of tax losses and capital allowances in the Wireless business.

Deferred tax assets which have not been recognised:

	Group		Company	
	2014 £000	2013 £000	2014 £000	2013 £000
Depreciation in advance of capital allowances	1,880	1,831	435	448
Tax losses carried forward	11,204	11,550	10,880	11,216
Share options deferment	80	80	—	—
	13,164	13,461	11,315	11,664

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. There is no expiry date for these unrecognised assets.

A reduction in the UK corporation tax rate from 23 per cent to 21 per cent (effective from 1 April 2014) was substantively enacted on 2 July 2013, together with a further reduction to 20 per cent (effective from 1 April 2015) on the same date. This will reduce the company's future current tax charge accordingly. The deferred tax liability at 31 May 2014 has been calculated based on the rate of 20 per cent substantively enacted at the balance sheet date.

This is not expected to have a material impact on the group's tax position.

## 20 Trade and other payables

	Group		Company	
	2014	2013	2014	2013
	£000	£000	£000	£000
Trade payables	5,922	9,906	86	64
Group payables	—	—	5,738	2,551
Other payables and accruals	1,525	3,698	476	578
Forward exchange contracts	—	7	—	—
	7,447	13,611	6,300	3,193

## 21 Provisions

	Group		Company	
	2014	2013	2014	2013
	£000	£000	£000	£000
<b>Warranty provision</b>				
Opening balance	605	565	—	—
Used during the year	(41)	(126)	—	—
Released unused during the year	(487)	(94)	—	—
Charge for the year	31	260	—	—
<b>Closing balance</b>	108	605	—	—

The provision for warranty relates to the units sold during the last two financial years. The provision is based on estimates made from historical warranty data.

	Group		Company	
	2014	2013	2014	2013
	£000	£000	£000	£000
<b>Dilapidation provision</b>				
Opening balance	—	—	—	—
Used during the year	(85)	—	(85)	—
Charge for the year	310	—	310	—
<b>Closing balance</b>	225	—	225	—

The provision for dilapidation relates to a liability for the termination of two leases retained following the disposal of the group's UK defence business in 2009.

## 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 Pension costs

	Group		Company	
	2014	2013	2014	2013
	£000	£000	£000	£000
Defined contribution schemes	456	432	30	34

# Notes to the financial statements

for the year ended 31 May 2014

## 24 Share capital

	Group and Company Ordinary shares of 10p each Issued and fully paid	
	Number	£000
At 1 June 2012	96,814,993	9,681
Shares issued in year	183,000	19
At 1 June 2013	96,997,993	9,700
Shares issued in year	162,993	16
<b>At 31 May 2014</b>	<b>97,160,986</b>	<b>9,716</b>

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 162,993 shares due to employees exercising share options from SAYE schemes and the management incentive plans.

## 25 Share premium

	Group and Company
	£000
At 1 June 2012	5,083
Premium on share issue	28
At 1 June 2013	5,111
Premium on share issue	34
<b>At 31 May 2014</b>	<b>5,145</b>

The shares issued to employees in the year were issued at an average premium of 20p.

## 26 Translation reserve

	Group
	£000
At 1 June 2012	(16)
Currency translation movement arising on consolidation	54
At 1 June 2013	38
Currency translation movement arising on consolidation	(474)
<b>At 31 May 2014</b>	<b>(436)</b>

## 27 Dividends

The directors are not proposing to pay a dividend for the year ended 31 May 2014 (2013: nil).

## 28 Retained earnings

	Group	Company
	£000	£000
At 1 June 2012	5,093	4,230
Profit/(loss) for the period	284	(656)
Share-based payments	163	87
Exercise of share awards	(191)	(191)
At 31 May 2013	5,349	3,470
(Loss) for the period	(2,815)	(1,038)
Share-based payments	(60)	(132)
<b>At 31 May 2014</b>	<b>2,474</b>	<b>2,300</b>



## 29 Share options

There are four sharesave plans that have been offered to employees. Under these plans employees who join the plan save up to £250 per month (which limit was increased to £500 per month in FY2014) for three years. The members of the plans 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 2014	Number of options 2014	Weighted average exercise price 2013	Number of options 2013
Outstanding at the beginning of the period	—	—	25p	276,450
Exercised during the period	—	—	25p	(183,000)
Cancelled during the period	—	—	25p	—
Lapsed during the period	—	—	25p	(93,450)
Outstanding at the end of the period	—	—	25p	—
Exercisable at the end of the period	—	—	—	—

The first sharesave plan was offered to employees in February 2009 and has now closed.

### Sharesave Plan — Scheme 2

	Weighted average exercise price 2014	Number of options 2014	Weighted average exercise price 2013	Number of options 2013
Outstanding at the beginning of the period	34.2p	98,520	34.2p	113,677
Exercised during the period	34.2p	(95,888)	34.2p	—
Cancelled during the period	34.2p	(2,632)	34.2p	(15,157)
Outstanding at the end of the period	34.2p	—	34.2p	98,520
Exercisable at the end of the period	—	—	—	—

The second sharesave plan was offered to employees in November 2010 and has now closed.

### Sharesave Plan — Scheme 3

	Weighted average exercise price 2014	Number of options 2014	Weighted average exercise price 2013	Number of options 2013
Outstanding at the beginning of the period	22.6p	989,505	22.6p	1,040,478
Exercised during the period	22.6p	(49,183)	22.6p	—
Cancelled during the period	22.6p	(57,064)	22.6p	(50,973)
Outstanding at the end of the period	22.6p	883,258	22.6p	989,505
Exercisable at the end of the period	22.6p	30,106	22.6p	—

The third sharesave scheme was offered to employees in April 2012.

The options outstanding at 31 May 2014 for Scheme 3 have a weighted average remaining contractual life of 1.5 years. The share options granted during the year to May 2012 have an exercise price of 22.6p and have an exercise period from 1 May to 31 October 2015.

# Notes to the financial statements

for the year ended 31 May 2014

## 29 Share options (continued) Sharesave Plan — Scheme 4

	Weighted average exercise price 2014	Number of options 2014	Weighted average exercise price 2013	Number of options 2013
Outstanding at the beginning of the period	56.4p	278,848	56.4p	—
Granted during the period	56.4p	—	56.4p	278,848
Exercised during the period	56.4p	(1,730)	56.4p	—
Cancelled during the period	56.4p	(129,813)	56.4p	—
Outstanding at the end of the period	56.4p	147,305	56.4p	278,848
Exercisable at the end of the period		—		—

The fourth sharesave scheme was offered to employees in March 2013.

The options outstanding at 31 May 2014 for Scheme 4 have a weighted average remaining contractual life of 2.5 years. The share options granted during the year to May 2013 have an exercise price of 56.4p and have an exercise period from 1 May to 31 October 2016.

### Management incentive plans

Under this plan some managers were granted options vesting in three years time. At the end of the three years the employees' options have an exercise price of 18p and 23.5p. 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.

	Weighted average exercise price 2014	Number of share options 2014	Weighted average exercise price 2013	Number of share options 2013
Outstanding at beginning of the period	21.8p	428,677	21.8p	454,428
Exercised during the period	23.5p	(16,192)	21.8p	—
Cancelled during the period	23.5p	(6,280)	21.8p	(25,751)
Outstanding at the end of the period	21.7p	406,205	21.8p	428,677
Exercisable at the end of the period		—		—

The share options awarded during the year to 31 May 2012 have a weighted average remaining contractual life of 0.25 years.

## 30 Share awards

	Number of share awards	
	2014	2013
<b>Performance share plan</b>		
Outstanding at the beginning of the period	157,943	1,019,471
Exercised during the year	—	(569,389)
Granted during the year	512,634	—
Cancelled during the year	(294,929)	(292,139)
Outstanding at the end of the period	375,648	157,943

### 30 Share awards (continued)

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 per cent 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 per cent 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 per cent and 100 per cent of the awarded shares.

The 157,943 remaining share awards awarded during the year to 31 May 2011 were cancelled in the year as the performance targets of the scheme were not met.

Under the plan in the year to 31 May 2014 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 2015 it exceeds a figure corresponding to £6m of earnings before intangible amortisation, exceptionals, interest and tax, then 25 per cent of the awarded shares will vest. If EPS grows such that for the year to 31 May 2015 it exceeds a figure corresponding to £7.5m of earnings before intangible amortisation, exceptionals, interest and tax, then 100 per cent 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 per cent and 100 per cent of the awarded shares.

### 31 Share-based payments

	Group		Company	
	2014 £000	2013 £000	2014 £000	2013 £000
Share options expense	76	60	4	3
Share awards expense	20	65	20	63
Exceptional share-based payments	—	38	—	21
Non-vesting LTIP share award	(156)	—	(156)	—
	(60)	163	(132)	87
Exercise of share awards	—	(191)	—	(191)

The share options expense is 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.

The share awards made to executives and senior managers in the year to 31 May 2011 did not vest due to performance targets not being met. As a consequence a credit has been made to the income statement to reverse the charge previously made.

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	
	2014 £000	2013 £000	2014 £000	2013 £000
Number of share options granted	512,634	278,848	512,634	7,786
Weighted average share price	63.0p	70.5p	63.0p	70.5p
Expected volatility	60%	60%	60%	60%
Expected life	3.0 years	3.0 years	3.0 years	3.0 years
Risk free interest rate	3%	3%	3%	3%
Weighted average fair value	24p	21p	24p	21p

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.

# Notes to the financial statements

for the year ended 31 May 2014

## 32 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	
	2014 £000	2013 £000	2014 £000	2013 £000
Less than one year	425	319	2	111
Between one and five years	1,360	701	—	2
More than five years	408	346	—	—
	<b>2,193</b>	1,366	<b>—</b>	113

The group leases a number of facilities, offices and vehicles under non-cancellable operating leases. The lease terms are for periods of one to ten years.

## 33 Capital expenditure commitments

	Group		Company	
	2014 £000	2013 £000	2014 £000	2013 £000
Capital expenditure contracted for at the balance sheet date but not provided in the financial statements	—	7	—	—

## 34 Note to the consolidated cash flow statement

	Group	
	2014 £000	2013 £000
Operating (loss)/profit	(3,686)	240
Net cash used in operating activities	1,615	(274)
Net cash used in investing activities	(1,013)	(1,469)
Net cash from financing activities	(446)	342

## 35 Analysis of net funds

	1 June 2013 £000	Cash flow £000	31 May 2014 £000
Cash and cash equivalents	2,375	156	2,531
Interest bearing borrowings	(496)	496	—
	1,879	652	2,531

### Reconciliation of cash flow to movement in net funds

	2014 £000	2013 £000
Movement in cash and cash equivalents	156	(1,401)
Cash flow from decrease/(increase) in debt financing	496	(496)
Effect of exchange rate fluctuations	—	31
Movement in net funds	652	(1,866)
Net funds at 1 June	1,879	3,745
Net funds at 31 May	2,531	1,879

The £496,000 was secured against the debtors as per the Barclays sales financing agreement. This has now been repaid with no charge remaining against debtors.

## 36 Financial instruments

### Fair value

The carrying amount of all the financial assets and liabilities approximates 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 also have access to a £2m sales invoicing facility with Barclays Bank. 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.

The sales invoicing facility with Barclays allows the company to borrow 60% of the UK entities debtors denominated in US dollars and sterling up to a value of £2m.

### 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	
	2014	2013	2014	2013
	£000	£000	£000	£000
Cash and cash equivalents	2,531	2,375	277	118
Trade and other receivables	9,941	17,237	12,840	10,792
	12,472	19,612	13,117	10,910

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

	Group		Company	
	2014	2013	2014	2013
	£000	£000	£000	£000
Barclays Bank	2,384	1,789	277	118
China Citic Bank	92	336	—	—
Bank of America	1	208	—	—
Bank of Delmarva	29	37	—	—
Industrial and Commercial Bank of China	16	3	—	—
SEB	8	—	—	—
ABC Bank China	1	2	—	—
	2,531	2,375	277	118

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.



# Notes to the financial statements

for the year ended 31 May 2014

## 36 Financial instruments (continued)

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

	Group	
	2014	2013
	£000	£000
Customer one	2,402	9,245
Customer two	1,482	2,284
Customer three	829	938
Other customers	4,195	4,047
	<b>8,908</b>	<b>16,514</b>

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

	Group	
	2014	2013
	£000	£000
Not past due	7,914	14,849
Past due less than three months	577	973
Past due more than three months	417	692
	<b>8,908</b>	<b>16,514</b>

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

	Group	
	2014	2013
	£000	£000
Past due more than three months	—	16

### Interest rate risk

Cash is held on short term bank deposits which earn interest at variable money market deposit rates. At 31 May 2014 £65,000 was held in Barclays on short term deposit with an interest rate of 0.3%. The remaining cash in the group is held in very low interest rate accounts. 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/(costs) assuming a balance on deposit or loan of £1,000,000 is as follows:

Interest rate	Expected annual interest income £000	Expected annual interest costs £000
1.5%	15	(15)
1.0%	10	(10)
0.5%	5	(5)

### 36 Financial instruments (continued)

#### 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, US dollar, Chinese Yuan and Swedish Krona.

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

The group has generated a surplus of US dollars during the year due to an increasing number of projects being supplied in US dollars. Whilst the group's major supplier invoices in US dollars, giving some degree of a natural hedge, it is not adequate to offset the exposure on currency risk. Therefore, the group has used forward foreign contracts and a 'vanilla option' to reduce the currency risk from surplus US dollars. The nature of the group's businesses means there is limited visibility of the currency required in US dollars. Therefore, when forward contracts are used to reduce currency risk, they are usually only for short periods of no more than six months. If the US dollar was to weaken significantly this could materially reduce the group's revenue and operating profit.

At 31 May 2014, the group had a vanilla option in place to cover expected sales receipts of \$3.2m. The fair value of the option was a favourable £40,000 at 31 May 2014.

Financial instruments measured at fair value are classified by the following fair value hierarchy based on the valuation technique used to determine fair value.

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The group's forward foreign exchange contract has been determined to represent a level 2 instrument characterised by the existence of quoted prices in active markets for an identical asset. The fair value is calculated by reference to fair values provided by financial institutions.

Cash is mainly held in sterling and US dollars.

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

	Group							
	2014				2013			
	SEK £000	EUR £000	RMB £000	USD £000	SEK £000	EUR £000	RMB £000	USD £000
Cash and cash equivalents	13	303	110	1,750	—	10	341	925
Interest bearing borrowings	—	—	—	—	—	—	—	(496)
Trade receivables	—	246	211	7,384	—	236	1,311	5,594
Trade payables	(53)	(186)	(198)	(2,247)	—	(360)	(1,920)	(6,477)
Net exposure	40	363	123	6,887	—	(114)	(268)	(454)

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 2014 then the group operating profit from continuing operations would have been £65,000 higher/lower.

The company has exposure to foreign currency risk through an intercompany loan with Filtronic Wireless Inc. This is cancelled out on Group consolidation.

### Capital management

The group's and company's capital is the total equity which comprises ordinary share capital and retained earnings. The group currently has a sales financing agreement in place for £2m which is not currently being utilised. At 31 May 2014 the group had net funds of £2,531,000 and the company had a cash balance of £277,000. 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.

### 37 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.

# Shareholder information

## Directors

*(All of Filtronic House, 3 Airport West, Yeadon, West Yorkshire, LS19 7ZA, UK)*

Howard Ford — Non Executive  
Chairman

Alan Needle — Chief Executive Officer

Rob Smith — Chief Financial Officer

Graham Meek — Senior Non-Executive  
Director

Reg Gott — Non-executive Director

Michael Roller — Non-executive Director

## Company secretary

M Moynihan

## Company number

2891064

## Registered office

Filtronic plc  
Filtronic House  
3 Airport West  
Lancaster Way  
Yeadon, Leeds  
West Yorkshire  
LS19 7ZA  
Tel: 0113 220 000

## Registrars

Capita Asset Services  
The Registry  
34 Beckenham Road  
Beckenham, Kent  
BR3 4TU

Tel: 0870 162 3100. (UK calls cost 10p per minute plus network extras). From overseas: +44 20 8639 3399. Lines are open 9.00am to 5.30pm, Monday to Friday, excluding public holidays.

## Auditor

KPMG LLP  
Chartered Accountants  
1 The Embankment  
Neville Street  
Leeds  
LS1 4DW

## Bankers

Barclays Bank PLC  
10 Market Street  
Bradford  
BD1 1NR

## Financial public relations

Walbrook PR Limited  
4 Lombard Street  
London  
EC3V 9HD  
Tel: 020 7933 8780

## Annual General Meeting

The Company's Annual General Meeting will be held at 11am on Friday, 26 September 2014 at the offices of Pinsent Masons LLP, No 1 Park Row, Leeds, LS1 5AB.

## Capita Asset Services

Enquiries regarding shareholdings, change of address or similar particulars should be directed in the first instance to our Registrars, Capita Asset Services whose address is: The Registry, 34 Beckenham Road, Beckenham, Kent, BR3 4TU, Kent, BR3 4TU or call 0871 664 0300 ( UK calls cost 10p per minute plus network extras). From overseas: +44 20 8639 3399. Lines are open 9.00am to 5.30pm, Monday to Friday, excluding public holidays.

## Filtronic website

Shareholders are encouraged to visit our website: [www.filtronic.com](http://www.filtronic.com) which has more information about the company.

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