

## Message from the President

Kudelski Group  
Annual report 2004

In 2004 the Kudelski Group delivered record results, both in growth and in absolute figures, with total revenues increasing by more than 50% to reach CHF 619 million, EBIT passing the CHF 100 million threshold for the first time, and net profit reaching CHF 77.2 million.

However, beyond these figures, 2004 will remain a milestone in the history of the Group. Management as well as all teams demonstrated their ability to deal with a large number of challenges successfully, while paving the way for the Group's future growth.

All of our activities, aside from Nagra Public Access, achieved a very good performance. Lysis in particular stood out as a key player in Europe in VOD program management solutions. Nagra Audio, for its part, saw its best year since 1990, when it was the company's core business.

### Digital television

2004 marked the success of the Group's strategy to both become the N°1 supplier of DTV conditional access systems and expand to promising new sectors at the crossroads of the digital television, internet and mobile worlds.

The growth of the digital television business in 2004 was particularly satisfying: all the strategic objectives were reached and the Group took full advantage of new development opportunities.

By increasing its revenues by 50% organically, this division confirmed its ability to grow on the strength of its own merits and its own resources in a highly competitive environment and under constantly moving market conditions.

The acquisition of the conditional access activity of Canal+ Technologies – MediaGuard – as well as strong organic growth have enabled the Kudelski Group to multiply its digital TV revenues in Europe by three, while in America they increased by 90% purely through organic growth.

In parallel with efforts made to address customer needs, a special task force worked on integrating the MediaGuard activity (rolled into Nagra France) within the Group's digital television division. Today integration has been achieved, and the Nagra France and NagraVision teams are collaborating actively in the development of new technologies. Nagra France has become a competence center for several promising projects such as securing access to Pay TV services on broadband networks.

While the Kudelski Group has built its worldwide reputation by developing new technologies, it has always sought to release new business models combined with state-of-the-art technology at the right time.

2004 was no exception as the Group launched prepaid, disposable smartcards for digital terrestrial television. This new business model, chosen by the Italian media giant Mediaset, creates a truly new choice for digital terrestrial television viewers. The operator's new offering met with immediate public success: close to 1.6 million cards had been distributed in Italy at the end of the first quarter of 2005.

High potential innovations released by the digital television R&D teams also include:

- Broadband (DSL) television security solutions, already chosen in 2004 by French operator neuf telecom.
- Solutions for digital video recorders (DVR) that not only enable digital TV programs to be recorded securely but also offer Push VOD functionalities, offering an instant pay-per-view choice of films on demand, coupled with an exceptional comfort of use. Premiere and EchoStar have already chosen this solution, which they will offer to their customers in 2005.
- A security concept especially designed for the secure distribution of video content on mobile devices, enabling digital TV subscribers to access programs when and where they want.

Recurring business, which includes more than 11.5 million smartcards sold on a rental basis in 2004, new contracts as well as technological developments opening new markets provide a solid base for the future growth of the DTV division.

### Public access

Despite a large number of new contracts, the public access business saw a difficult year in 2004. In an adverse environment, several major medium and long term cost-cutting measures were launched which should deliver first tangible results in the second half of 2005. In parallel, the Group decided to accelerate the development of new products and expand geographically instead of focusing only on short-term profitability. Some patience will be needed until these efforts come to full fruition, given that business cycles in this sector are longer than in digital television.

The public access market is faced with new challenges that offer many opportunities but also entail a few risks. This will require repositioning of the offer, leading to several technological innovations. As in the past, the Kudelski Group is determined to emerge stronger than before from this type of situation.

### Investing in the future

Since its foundation in 1951, Kudelski has never paid dividends, preferring to reinvest all of its profits into the development of its activities. Today more than ever, we have strategic development projects to prepare the future growth of the Group that will require reinvesting most of the profits.

As an example, 29.5% of turnover of the digital television division is reinvested in R&D, which demonstrates, among many other instances, the commitment of the Group to develop its future business.

However, in response to the expectations of a growing number of shareholders, the Board of Directors has decided to propose the payment of a dividend of 20 Swiss centimes per bearer share and 2 centimes per registered share, corresponding to 2% of nominal value.

While this dividend may appear to be low, one must bear in mind the need to maintain the Group's long-term solidity and ability to grow. Development opportunities have never been as numerous as they are today, and at the same time the need to stay at the cutting-edge of technology has never been greater.

In a rapidly changing world, to move more slowly than the market is to go backward, and thereby to risk forfeiting our leadership position. It is not just a matter of defining the right targets, but of being quicker off the mark than our competitors and hard-hitting when necessary. Rather than increased dividends in 2004, this approach will certainly contribute to delivering a better return on investment to shareholders in the long run.

André Kudelski