

GOING THE DISTANCE



SINGAPORE TECHNOLOGIES ENGINEERING
ANNUAL REPORT 2003

"The demand for heavy commercial and specialty vehicles for the rapidly growing construction industry in China is vast. As a strategic partner, ST Kinetics contributes skill sets and technologies that bring tremendous value to our business. They have been both proactive and professional, and we look forward to reaping tremendous results in the near future."

LIU WEN TAI

*General Manager
Beijing Heavy Duty Truck Plant*

"ST Kinetics brings outstanding product knowledge to our partnership on the Otokar Yavuz project. We have been greatly impressed by their experience and past performance in designing and producing armoured vehicles in record time. It has been a great pleasure working with them as they have shown positive team spirit, commitment and a dogged determination to overcome any challenge."

KUDRET ONEN

*General Manager
Otokar*

"With the new tools provided by ST Elect [through its subsidiary SES Systems] to enhance our criminal registration processes, I'm certain that crimes will be solved faster and more efficiently."

GOH LIANG KWANG

*Deputy Commissioner of Police
Singapore Police Force*

"We have been working with Agilis [ST Elect's subsidiary] for two and a half years now and hope to build on our strong business relationship for our future requirements."

PK GHATAK

*Chief Executive Officer
HFCL Satellite Communications Ltd*

"The CLWP Maintenance Department, along with a Herculean effort by ST Marine, was able to do something that many people said could not be done - a waterborne change out of USS Safeguard's (ARS 50) Ship Service Diesel Generator (SSDG) engine."

MERLION STAR NEWSLETTER

The US Navy

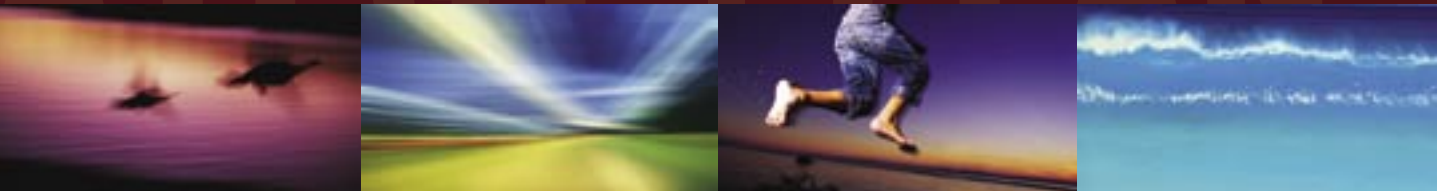
"ST Marine has regularly provided quality shiprepair services for our dredgers. Over the years, they have gained our trust and confidence with their high level of technical expertise. The Company's friendly, personalised approach also makes it very pleasant to work with ST Marine."

JACQUES CHR VAN DER PIJL

*Manager
Boskalis International BV*

To our shareholders, customers, partners and suppliers, our thanks for your support and sharing.

And to our staff, for making it all happen. We admire your energy and passion in going the distance.



The online version of "Going The Distance" can be found at
www.stengg.com/AR2003



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Foreword

A Letter To Our Shareholders

“For the year, the Group recorded an 8% improvement in turnover to S\$2.82b and comparable profit before tax of S\$412.7m. Profit after tax was 2% lower at S\$325.6m because of higher tax expense. Our market capitalisation ended the year at S\$5.89b, compared to S\$4.76b at the close of 2002.”

Dear Shareholders,

2003 began as another tough year globally. The war in Iraq and the invisible war, Severe Acute Respiratory Syndrome (SARS), hit Asia hard and severely affected regional economies.

As the year proceeded, the outlook for the world economy gradually improved. Business sentiment turned positive, although macroeconomic uncertainties kept international markets volatile.

As a growing global entity, ST Engg is not immune to the gyrations of the international economy. One thing came through clearly this year - our business is resilient, and this stems from the diversification of our operations across a good spread of industries and geographies. Despite the twin challenges of Iraq and SARS, we managed to maintain our profitability. Our robust business process, international customer base, networks and operations, and most importantly, the commitment of our people, enabled us to keep an even keel through turbulent waters.

Throughout the year, we continued to review our Group's businesses. We acquired and invested in more companies, expanded our capacity and rationalised some operations. We kept a tight rein on costs and implemented additional measures, including wage cuts for senior staff, to ensure we remained competitive in the international market.

For the year, the Group recorded an 8% improvement in turnover to S\$2.82b and comparable profit before tax (PBT) of S\$412.7m. Profit after tax (PAT) was 2% lower at S\$325.6m because

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of higher tax expense. Our market capitalisation ended the year at S\$5.89b, compared to S\$4.76b at the close of 2002.

Our Aerospace, Electronics and Marine sectors maintained a steady order book through the year. The Aerospace and Electronics sectors were successful in winning new customers and contracts, and the Marine sector's US operations performed according to plan. The Land Systems sector continued to transform itself in line with the changing needs of the global defence industry.

The Group's international thrust in 2003 focused on building new growth areas and capabilities, seeking new markets and in particular, increasing our presence in markets like China and the US. While there will always be short term financial impact from new ventures, investment in these areas is necessary to enable the Group to secure medium to long term growth.

Our commercial businesses increased their overall contributions as we continued to build growth through new opportunities and new markets, in our goal to become a global enterprise.

In line with the Group's aim to maintain a consistent dividend policy, the Board is recommending a total gross dividend of 11.3 cents, comprising an ordinary tax exempt dividend of 35% and a special tax exempt dividend of 78%.

REVIEWING FINANCIAL PERFORMANCE

PBT margins for the Group remained strong at 15%. Economic value added for 2003 was S\$240.9m, an increase of 27%. At the operating level, cash from operating activities improved by S\$252m from improvements in working capital.

The Aerospace sector recorded a 5% growth in turnover to S\$1.09b and a 6% increase in PBT to S\$225.2m. This was due to cost reductions as well as improved performance in US operations during the year.

The Electronics sector improved both its turnover and PBT by 7% and 8% to S\$614m and S\$61.4m respectively. This performance reflects its success in securing new contracts, both in Singapore and overseas.

The Marine sector achieved a 38% increase in turnover to S\$387m, with the inclusion of revenues from its US operations. However, PBT dropped by 14% to S\$35.2m primarily due to startup losses at its US operations, though overall US performance was better than expected.

The Land Systems sector posted a 1% increase in turnover to S\$717m, while the PBT of S\$96.4m was comparable to the previous year. Operating profits remained strong but PAT was lower due to the absence of tax writebacks and tax benefits as compared to 2002.

DIVIDEND

In line with the Group's aim to maintain a consistent dividend policy, the Board is recommending a total gross dividend of 11.3 cents, comprising an ordinary tax exempt dividend of 35% and a special tax exempt dividend of 78%. Discounting the one off special dividend in 2002, this final dividend of 113% represents 100% of net earnings and a dividend yield of 6.1%.

LOOKING BACK ON THE YEAR

Innovation

The SARS epidemic was a worrisome period for everyone. In the international battle against this scourge, we are proud to highlight the role of ST Elect's engineers who raced against time to adapt military surveillance technology in thermal imaging into equipment for temperature screening of large numbers of people at airports and other public places. Adoption of this technology started in Singapore and quickly spread across the globe, from Canada to the Middle East and North Asia. Named by TIME magazine as one of the Coolest Inventions in 2003, ST Elect's Infrared Fever Scanning System (IFss) is the first purpose built, non contact and mass temperature screening system in the world. It is a fine example of how we can quickly and innovatively adapt our advanced technology, whether in the defence or commercial sphere.

ST Aero, through innovative packaging of its services, was able to meet the needs of low cost carriers like AirAsia and Biman Bangladesh Airlines for total aviation support. ST Aero's early involvement with its customers to define requirements and share ideas enabled it to capture a new area of business growth.

Increasingly, the Group will exploit dual use technology to strengthen our capabilities and develop a broader product and sales base.

The key is to constantly innovate. We cannot cling to ways which may have served us well in the past but which are no longer relevant. Once upon a time, the saying was, "If it ain't broke, don't fix it." Then it became, "If it ain't broke, fix it now before it does break." The saying now goes, "If it ain't broke, break it before your competitors do." We must continually improve ourselves and achieve greater heights.

New Areas of Growth

We continued to broaden our geographical footprint in 2003, primarily in the key markets of China and the US.

We announced the formation of two joint ventures in China for the Aerospace and Land Systems sectors. ST Aero entered into a joint venture with China Eastern Airlines, one of China's three airline groups, to set up a commercial aircraft maintenance, repair and overhaul (MRO) facility in Shanghai. The joint venture company will be managed and operated under ST Aero's global network of MRO facilities, and leverage on ST Aero's total aviation support capabilities and global customer base. Another joint venture was set up in Beijing to engage in China's growing construction market. Known as Beijing Zhonghuan Kinetics Heavy Vehicles, it will focus on the design and manufacture of heavy commercial and industrial vehicles. Both joint ventures are awaiting regulatory approvals and are expected to be operational in 2004.

In the US, we acquired Miltope, a leading manufacturer of rugged computer equipment for military applications and computer related products for the commercial aerospace market. Miltope has a good strategic fit with ST Engg's businesses and will extend our reach in the US, giving us access to the growing defence market and the commercial business network of Miltope.

During the year, we made inroads into other new overseas markets by securing modest orders for our exports which we hope to build on in future. Some of our products and systems are also undergoing evaluation and trials in European countries, a step forward towards entry into these markets.

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TAN PHENG HOCK
President and CEO

PETER SEAH LIM HUAT
Chairman

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We also made a modest entry into the Central Asia market by signing an agreement to assist a state owned company develop into an industrial entity in the engineering sector.

ST Engg was awarded the Singapore Innovation Award 2003 – Innovative Organisation of the Year by the Singapore Innovation Council. This is testimony to our culture of innovation which is pivotal to the Group’s development of new capabilities and intellectual property.

Divestment

In 2003, we continued to rationalise our businesses. In reviewing our US Aerospace MRO facilities and the business outlook of each facility, we made the difficult decision to close down DalFort Aerospace in Texas in October after we were unable to overcome its limitations as a narrow-body facility. Subsequently in December, we sold the lease on DalFort Aerospace facility to Virginia Aerospace at a total consideration of US\$6.5m. We remain committed to growing our MRO business in the US through our two main facilities in Mobile, where we are adding two new hangars, and in San Antonio.

Business Excellence

Following the success of the Six Sigma programme in ST Kinetics, we extended the business leadership and performance system to the entire Group. Like Kaizen, this flexible system will help us inculcate in our workforce a determination to pursue excellence using every tool at our disposal and to constantly innovate and reinvent the way we do things. We continued to invest heavily in staff training and development throughout the year.

Awards

ST Engg was awarded the Singapore Innovation Award 2003 – Innovative Organisation of the Year by the Singapore Innovation Council. This is testimony to our culture of innovation which is pivotal to the Group’s development of new capabilities and intellectual property.

We continued to set industry standards in corporate transparency and governance by winning two key awards this year. We became the first company ever to be awarded the SIAS Transparency Excellence Award by the Securities Investors’ Association (Singapore). This honour comes from winning the SIAS Golden Circle Award for transparency across all categories for three consecutive years. We also won a Best Managed Boards award from The Singapore Institute of Directors, which recognises initiatives by company boards towards good corporate governance. These awards reflect ST Engg’s deep commitment to build and uphold best practices in corporate governance.

Going Forward

In the domestic market, we will maintain our focus in developing capabilities to stay relevant to MINDEF, and support and partner them as they transform and evolve.

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As we expand beyond the shores of Singapore to boost our growth, we will capitalise on our financial strength and brand name. These attributes put us in a unique position to acquire, collaborate and partner companies internationally.

Our efforts to enter new markets are starting to bear fruit as we secure and build on modest orders in some of these markets. We will continue to commit resources to grow our export markets and our international operations and networks.

We will continue to seek acquisition opportunities in the US, China and other parts of the world, and invest in technologies that will spearhead the development of new products and systems, and further integrate our global enterprise.

We are optimistic about the outlook for three of our sectors – Aerospace, Electronics and Marine – where current growth prospects are positive. The Land Systems sector will need more time to address structural changes and to reinvent capabilities through investments in research and development.

APPRECIATION

We would like to record our deep appreciation to our Directors – Lieutenant-General Lim Chuan Poh and Mr Philip Tan Yuen Fah – who retired this year from our Board. Their contributions will certainly be missed. We are happy to welcome Mr Koh Beng Seng, Major-General Ng Yat Chung, Dr Tan Kim Siew and Brigadier-General Bernard Tan Kok Kiang to our Board. They bring new ideas and fresh perspectives which will help the Board to guide the Group going forward.

To our shareholders, customers, partners and suppliers, our thanks for your support and sharing.

And to our staff, for making it all happen. We admire your energy and passion in going the distance.



PETER SEAH LIM HUAT

Chairman

28 January 2004



TAN PHENG HOCK

President and CEO