



**ORBITAL
HALF YEAR
REPORT**

31 December 2003



ORBITAL
ENGINE CORPORATION LIMITED

ABN 32 009 344 058

Highlights

- Profit after taxation of \$2.1 million compared to a loss of \$2.9 million in the corresponding period last year.
- Continuing increase in engineering services, royalty and licence income.
- Overheads reduced by 32% to \$7.2 million.
- Record result by Synerject, contributing \$0.9 million to Orbital's result, an increase of 35% over the previous year.
- Successful share purchase plan generating \$3.3 million in July 2003.
- Improved cash flow.
- Continuing progress in new markets, particularly India and Taiwan.

STATEMENT OF FINANCIAL PERFORMANCE FOR THE HALF-YEAR ENDED 31 DECEMBER 2003

	2003 A\$'000	2002 A\$'000	Change
Revenue			
System sales	-	23,236	
Engineering services	6,141	4,856	+26%
Royalty and licencing income	1,947	1,620	+20%
	<u>8,088</u>	<u>29,712</u>	
Other Income			
Foreign exchange gain	808	248	
Proceeds on sale of fixed assets	138	80	
Other	606	65	
	<u>1,552</u>	<u>393</u>	
Total Revenue (excluding interest)	9,640	30,105	
System purchases	-	(21,696)	
Licence costs	(422)	-	
	<u>-</u>	<u>-</u>	
Gross Contribution	9,218	8,409	+10%
Overhead expenses	(7,221)	(10,561)	(32%)
Restructuring expenses	(12)	17	
Share of Synerject net profit	896	664	+35%
	<u>2,881</u>	<u>(1,471)</u>	
Earnings before Interest, Tax, Depreciation, and Amortisation	2,881	(1,471)	
Depreciation and amortisation	(947)	(1,158)	
Amortisation of prepaid marketing	-	(484)	
Net interest income	276	147	
	<u>2,210</u>	<u>(2,966)</u>	
Operating Profit/(Loss) before Tax	2,210	(2,966)	
Income tax (expense)/credit	(102)	67	
	<u>2,108</u>	<u>(2,899)</u>	
Operating Profit/(Loss) after Tax	2,108	(2,899)	

Revenue

As previously reported, the restructure of Synerject included the transfer of Orbital's marine and recreation systems sales business to Synerject with effect from 1 April 2003. This has resulted in a decrease in total revenue consolidated by Orbital, however the net result after elimination of system sales, cost of system sales and related overheads as well as the take up of an improved Synerject result is a positive contribution.

Engineering services and royalty and licence income have increased by 26% and 20% respectively over the previous year, despite the strengthening of the Australian dollar which has eroded royalty revenue by some \$200,000 compared to the prior year's exchange rate.

Engineering consulting revenue continues the improvements demonstrated last year as Orbital has expanded its sales and marketing focus beyond its traditional technology customers.

Royalty and licence revenue has continued to grow with the introduction of Mercury's 115 and 90 horsepower 3-cylinder OptiMax™ product range, launched over the last 9 months. The increase also reflects progress made in the introduction of OCP™ technology into new markets, including a licence fee instalment made by UCAL India.

Expenses

Orbital commenced a restructuring program in FY2001, resulting in progressive reduction of overhead expenses over the last few years. Overheads have decreased a further 32% to \$7.2 million in this half-year. The savings were derived primarily from the closure of Orbital's US office in April 2003, as a result of the transfer of the system sales business to Synerject noted above. In addition, all other business expenses have been subject to review and have contributed to the savings achieved.

Synerject

Synerject, Orbital's 50:50 joint venture with Siemens VDO Automotive, continues to achieve improved results with Orbital's share of Synerject's profit for the half-year increasing by 35% to \$0.9 million for the half-year. Synerject derives revenue in United States dollars and Euros, and the translation of Synerject's results into Australian dollars has eroded reported revenue by \$210,000 compared to the prior corresponding period.

Synerject realised the benefits of the transfer of Orbital's marine and recreation system sales and Siemens VDO's non-automotive systems business for the full half-year. In addition, sales volumes increased with the introduction of direct injection fuel systems to Mercury's 3-cylinder OptiMax™ range of engines. Mercury introduced the 115hp engine in April 2003, the 90hp engine in July 2003 with the 75hp due for introduction in early 2004.

Commercial Update

Orbital continues to expand its engineering customer base beyond traditional OCP™ customers.

This is reflected in the 26% improvement in engineering services revenue for the half-year, which includes, for instance, continued assessment of ethanol blends in petrol, and the provision of calibration and validation services for OEMs seeking to outsource engineering services.

In the marine sector, Mercury continued the introduction of 1.5 litre OptiMax™ 3-cylinder engines. The 115hp model which was released in April 2003 was followed by the 90hp in September 2003. It is anticipated that the 75hp model will be released in early 2004.

In October 2003 Kymco, a leading Taiwanese motorcycle manufacturer, announced the adoption of Orbital direct injection technology for the planned introduction of a 100cc scooter model scheduled for launch in 2004. Kymco have made further progress in production plans having received qualified EPA approval with initial launch volumes anticipated prior to the end of the financial year.

Whilst taking longer than originally envisaged, Orbital continues to make progress with 2-wheeler and 3-wheeler initiatives in India. As a precursor to any licence agreement, several engineering programs have been undertaken during the year with Indian motorcycle OEMs and UCAL, Orbital's licensed system supplier in India.

Outlook

Orbital is reasonably confident that the level of engineering consultancy services provided in the first half will continue for the remainder of the financial year. Cost reductions implemented in the last two years which relate primarily to this business sector are now finalised ensuring a stable business with secure returns.

Royalty and licence income, however, will most probably be affected by the unstable 50cc European scooter market. Delays in implementation of Euro III emissions legislation and escalating European manufacturing costs are contributing to the market uncertainty in this price sensitive sector.

Synerject will also be affected by the weakness in the motorcycle sector however the cyclical nature of the Synerject business should see continued growth in Synerject's profits in the second half as OEMs build inventory for the northern hemisphere summer.

Orbital's first half result had a net benefit from translation gains/losses arising from foreign exchange movements.

The Directors anticipate that the financial results in the second half will be in line with the first half, after excluding any foreign exchange gains or losses.

Cash

EBITDA reflects the steady improvement in the operating results and consequent cash flows, as illustrated in the accompanying graph.

Cash at bank at 31 December 2003 was \$12.0 million compared to \$9.0 million at 30 June 2003. In July 2003, Orbital received \$3.3 million arising out of a share purchase plan which was extremely well supported by existing shareholders.

Orbital has reduced net cash used in operating activities from \$6.1 million in the half-year to 31 December 2002 to \$0.3 million this year. Increased engineering revenue has required some additional working capital and final payments with respect to staff reductions arising out of the Synerject restructure were settled during the half-year.

Net cash requirements for investing activities are now minimal as Synerject is self-funding.

United States Generally Accepted Accounting Principles

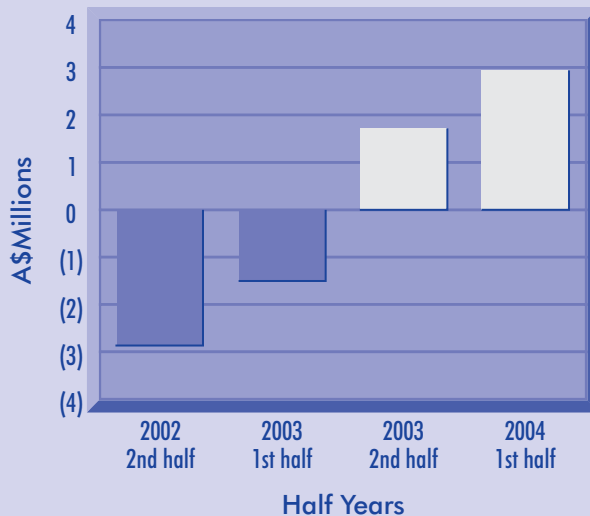
The financial result for the half-year ended 31 December 2003 under US GAAP is a profit after taxation of A\$10.0 million compared to a loss in the corresponding period last year of A\$2.6 million.

The most significant difference between Australian GAAP and US GAAP is the recognition under US GAAP of income tax losses not previously brought to account of A\$8.0 million. Under Australian GAAP tax losses can only be recognised when the realisation of the asset is virtually certain, however under US GAAP recognition is required if it is more likely than not that the tax losses will be utilised.

Orbital has total future tax benefits of approximately A\$38 million and the Directors have determined that it is more likely than not that Orbital will realise at least A\$8.0 million of available losses. The determination is supported by factors including: -

- Recent profits in Synerject and Orbital's US subsidiaries.
- Profit for the 6 months ended 31 December 2003 in Orbital's Australian operations.
- Forecast profits for Orbital going forward.

Orbital Engine Corporation EBITDA



Orbital CEO, Peter Cook, said that the Company had consolidated the turnaround demonstrated in the second half of last financial year: "This result is another step forward in our process of getting the fundamentals right. Over last year's corresponding period and after the Synerject restructuring, all business segments have shown improvement and a contribution to the bottom line."



1 Whipple Street, Balcatta,
Western Australia, 6021
Phone: 61 (08) 9441 2311
Fax: 61 (08) 9441 2111
Email: info@orbeng.com
Website: www.orbeng.com