

Teleste



INTERIM REPORT 1.1.-31.8.1999

TURNOVER AND PROFITABILITY

The group's turnover developed as anticipated in the previous interim report and came to 39,5 million euros, which was on last year's level. Operating profit increased 12,2 per cent to 4,7 million euros. Due to the decision received from arbitration at the end of June, the reservation made in 1997 was decreased by 1,0 million euros. Operating profit was burdened with especially heavy investments on R&D. Compared to the previous year goodwill depreciation increased by 471 thousand euros.

Orders received were slightly better than the previous year, 45,4 million euros. The order backlog increased to 15,0 million euros, which is 43 per cent higher than the same time last year. Due to the high seasonality of Teleste's operations the result for the first two tertials has always been weaker than the rest of the year. Last year the operating profit for the first eight months was 45 per cent of the full year of 1998 operating profit.

THE GROUP'S OPERATING PROFIT HAS INCREASED BY 12 PER CENT

THE GROUP'S TURNOVER WAS ON LAST YEAR'S LEVEL

THE GROUP'S ORDER BACKLOG HAS INCREASED BY 43 PER CENT COMPARED TO THE YEAR BEFORE

THE GROUP'S CORE DIVISION TELESTE ACCESS SYSTEMS' TURNOVER INCREASED BY 9 PER CENT

IMPORTANT ORDERS FROM GERMANY, THE NETHERLANDS AND CHINA

PERSONNEL

The group employed 585 people at the end of August (568 in the previous year), 392 of which are in Finland (366 the year before). Teleste Access Systems added professionals for R&D and marketing. In the production organization of Teleste Home Networks the number of personnel decreased significantly.

R&D AND INVESTMENTS

Teleste Access Systems continued its strong investments for R&D. R&D costs during the period came to 4,2 million euros or 10,7 per cent of the turnover (2,4 million euros and 6,1 per cent last year). The group's R&D personnel have increased from the beginning of the year by 21 people, consisting currently of 101 experts. The increase has mainly been software designers. R&D has concentrated in products and applications for digital fibre backbone and adapting

products for German standards. R&D costs are booked as annual expenses.

The group's investments came to 1,6 million euros (1,0 million euros last year). The largest single investment during the beginning of the year was Teleste Access Systems' new R&D center in Turku. The investments during the second tertial were mainly for information technology and for measuring equipment for production.

FINANCE

During the period the group's liquidity remained good. The group's interest bearing debt stood at 14,6 million euros at the end of August.

Liquid funds were 3,0 million euros. Key figures improved from those of the first tertial. The group's gearing was 73,3 per cent and the equity ratio was 37,7 per cent, as calculated from the balance sheet at the end of August. Teleste had unused credit facilities worth of 4,2 million euros.

YEAR 2000

The group's year 2000 project has proceeded according to plan. All the group's critical systems are year 2000 compliant. It is expected that the project would not cause substantial expenses.

TELESTE ACCESS SYSTEMS

Turnover was 27,4 million euros increasing with 9,3 per cent or 2,3 million euros. Operating profit was 3,6 million euros, which is worse than last year. Profitability was burdened by investments in sales and R&D in order to secure growth in the future. Teleste Access System's order intake increased to 32,5 million euros from last year's 29,4 million euros.

The turnover development during the period was still burdened by structural changes between international customers. These have slowed down projected projects among others in Scandinavia. Important orders were received

from Deutsche Telekom in Germany, Castel in the Netherlands and the first order from China. In the summer a frame agreement was made with NTL, which is after the structural changes the largest cable operator in the UK. This agreement is believed to strengthen Teleste's position on its traditionally strong market in the UK. During the period Teleste's own international sales organization was strengthened in Latvia and USA. Full year turnover is expected to develop positively and the profitability to remain good.

TELESTE EDUCATIONAL

Turnover was 6,1 million euros decreasing 12,3 per cent or 0,9 million euros. Operating profit was 0,5 million euros, which was on previous year's level. Teleste Educational's order intake was 6,3 million euros, last year's was 7,4 million euros.

Due to the technology change of the language learning environment, the demand for old products has decreased faster than expected and the demand for the newly developed software products has not yet started its expected rise. Measured by delivered pupil positions the volume was two per cent lower than last year; already half of the pupil positions delivered by Teleste are purely software based. This has had significant effect on turnover development. However, the software products, whose unit prices are cheaper, have improved margins and the profitability level is only slightly behind last year in spite of the decrease in turnover. The growth of the demand, which is generated by new technology, was expected to begin already this year. However, in this kind of significant technology change customers seem to postpone their decisions and the full year profitability will not reach last year's level.

TELESTE HOME NETWORKS

Turnover was 6,5 million euros decreasing 16,8 per cent or 1,3 million euros. Operating loss was 0,6 million euros and worse than the previous year. Teleste Home Networks' order intake was 7,2 million euros; last year's was 8,6 million euros.

Teleste Home Networks' loss of its second largest customer cannot be compensated during this year despite of the actions already taken. The total demand of products during the second tertial remained at a low level in the UK. Price competition from Far East imports creates more challenges to quickly improve the division's profitability. Full year turnover and profitability is expected to be clearly

lower than last year.

SHARES AND SHAREHOLDERS

Share price varied between 7,90 and 10,00 euros during the second tertial. The closing price at the end of August was 8,30 euros. According to the Finnish Central Security Depository the number of shareholders at the end of the period was 4319. The amount of foreign ownership was 26,8 per cent. Between the beginning of May and the end of August the value of shares traded at Helsinki Exchanges was 28,3 million euros and the number of shares was 3,1 million.

OUTLOOK FOR THE REST OF THE YEAR

The group will continue to invest strongly to both R&D and sales and marketing for its main division Teleste Access Systems. This is necessary to exploit the potential of current markets, but above all to ensure the growth targets for the coming years are met. Teleste Access Systems' full year turnover and profitability are expected to develop positively and to be better than last year. The still unclear market situation of Teleste Educational and Teleste Home Networks makes it difficult to estimate the development for the rest of the year. In spite of the market disappointments of Teleste Educational and Teleste Home Networks, the group's full year turnover and profitability are expected to improve from the previous year.

In the year 2000 Teleste Access Systems is expected to continue on its growth path. Surveillance network sales, which have developed well this year, is believed to support the growth. The strong growth of the other two divisions will require an improved market situation. Despite of this year's disappointment Teleste Educational is, with its software products, well positioned to take advantage of the technology change in the market place. The corrective actions, which are already made or are ongoing, are expected to bring results next year.

October 13, 1999

Teleste Corporation
Board of Directors

Timo Toiila
CEO

CONSOLIDATED
STATEMENT OF INCOME (teur = 1 000 euros)

| | 1-8/1999 | 1-8/1998 | Change % | 1-12/1998 |
|-------------------------------------|---------------|---------------|---------------|---------------|
| TURNOVER | 39 503 | 39 366 | 0,3 % | 66 106 |
| Other operating income | 691 | 212 | 225,9 % | 325 |
| Expenses | -33 195 | -33 712 | -1,5 % | -54 390 |
| Depreciation | -2 268 | -1 648 | 37,6 % | -2 667 |
| OPERATING PROFIT | 4 731 | 4 218 | 12,2 % | 9 374 |
| Financial income and expenses | -649 | -409 | 58,9 % | -548 |
| PROFIT AFTER FINANCIAL ITEMS | 4 082 | 3 809 | 7,2 % | 8 826 |
| Extraordinary items | 0 | 0 | | 925 |
| PROFIT BEFORE TAXES | 4 082 | 3 809 | 7,2 % | 9 751 |
| Taxes | -1 240 | -1 388 | -10,6 % | -2 725 |
| NET PROFIT | 2 842 | 2 422 | 17,3 % | 7 026 |

Taxes are computed on the basis of the tax on the profit for the period

CONSOLIDATED
BALANCE SHEET (teur)

| | 31.8.1999 | 31.8.1998 | 31.12.1998 |
|---|---------------|---------------|---------------|
| Fixed assets | 16 897 | 14 197 | 17 483 |
| Current assets | | | |
| Inventories | 8 171 | 8 088 | 7 318 |
| Other current assets | 14 132 | 10 284 | 12 515 |
| Liquid funds | 3 028 | 7 034 | 2 442 |
| TOTAL ASSETS | 42 228 | 39 603 | 39 758 |
| Shareholders' equity | 15 781 | 9 022 | 13 561 |
| Obligatory reserves | 1 698 | 3 357 | 3 379 |
| Non-current liabilities | 7 100 | 12 196 | 8 078 |
| Current liabilities | 17 649 | 15 029 | 14 740 |
| TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES | 42 228 | 39 603 | 39 758 |

TURNOVER

| BY DIVISION (teur) | 1-8/1999 | 1-8/1998 | Change % | 1-12/1998 |
|---------------------------|---------------|---------------|--------------|---------------|
| Access Systems | 27 400 | 25 061 | 9,3 % | 41 335 |
| Educational | 6 120 | 6 980 | -12,3 % | 11 847 |
| Home Networks | 6 549 | 7 868 | -16,8 % | 13 693 |
| Others and group items | -566 | -543 | 4,2 % | -769 |
| TOTAL | 39 503 | 39 366 | 0,3 % | 66 106 |

OPERATING PROFIT

| BY DIVISION (teur) | 1-8/1999 | 1-8/1998 | Change % | 1-12/1998 |
|---------------------------|--------------|--------------|---------------|--------------|
| Access Systems | 3 632 | 4 408 | -17,6 % | 7 392 |
| Educational | 507 | 521 | -2,7 % | 1 144 |
| Home Networks | -645 | -65 | -892,3 % | 800 |
| Others and group items | 1 237 | -646 | 291,5 % | 38 |
| TOTAL | 4 731 | 4 218 | 12,2 % | 9 374 |

KEY FIGURES (teur)

| | 1-8/1999 | 1-8/1998 | 1-12/1998 |
|--|----------|----------|-----------|
| Earnings per share | 0,18 | 0,15 | 0,38 |
| Earnings per share without goodwill depreciation | 0,23 | 0,17 | 0,42 |
| Return on equity | 29,1 % | 46,3 % | 60,3 % |
| Return on capital employed | 26,0 % | 25,2 % | 37,8 % |
| Equity ratio | 37,7 % | 23,0 % | 34,2 % |
| Gearing | 73,3 % | 106,0 % | 65,9 % |
| Investments | 1 588 | 1 043 | 10 596* |
| Orders received | 45 441 | 45 090 | 70 158 |
| Order backlog | 14 992 | 10 452 | 9 250 |
| Personnel, average | 574 | 555 | 563 |

* Includes 8544 thousand euros additional purchase price for Teleste Oy's shares

CONTINGENT LIABILITIES

AND PLEDGED ASSETS (teur)

| | | | |
|---------------------|--------------|---------------|--------------|
| For own debt | | | |
| Pledged assets | 0 | 16 557 | 0 |
| Mortgages | 2 985 | 4 886 | 2 985 |
| Guarantees | 310 | 167 | 205 |
| Leasing liabilities | 1 990 | 1 719 | 1 710 |
| Pension commitments | 0 | 89 | 0 |
| TOTAL | 5 285 | 23 418 | 4 900 |

DERIVATE INSTRUMENTS (teur)

| | | | |
|------------------------------------|--------|--------|--------|
| Foreign exchange forward contracts | 10 340 | 13 679 | 10 459 |
|------------------------------------|--------|--------|--------|

BUSINESS DEVELOPMENT

BY TERTIAL (teur)

| | 1-4/1999 | 5-8/1999 | 9-12/1998 | 1-12/1998 | 9/1998-8/1999 |
|--|----------|----------|-----------|-----------|---------------|
| Turnover | 18 939 | 20 564 | 26 740 | 66 106 | 66 243 |
| Operating profit | 1 359 | 2 723 | 5 156 | 9 374 | 9 238 |
| Operating profit without goodwill depreciation | 1 797 | 3 502 | 5 507 | 10 033 | 10 806 |
| Financial items | -399 | -250 | -139 | -548 | -788 |
| Profit before taxes | 960 | 3 122 | 5 942 | 9 751 | 10 024 |

LARGEST SHAREHOLDERS

PER 31.8.1999

| | |
|--|--------|
| Sponsor Fund I Ky | 41,5 % |
| Nominee registration | 26,8 % |
| Ilmarinen Mutual Pension Insurance Company | 3,2 % |
| Varma-Sampo Mutual Pension Insurance Company | 2,9 % |
| The Local Government Pensions Institute | 1,9 % |
| Sampo Life Insurance Company | 1,7 % |
| Mutual Insurance Company Pension Fennia | 0,9 % |
| Evli Nordic Small Co Fund | 0,9 % |
| Timo Toivila | 0,8 % |
| Suomi Mutual Life Assurance Company | 0,7 % |
| Others | 18,7 % |

The figures are not audited

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