



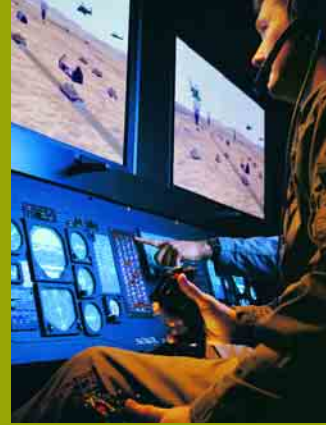
communications

**2000
Annual Report**



MOMENTUM

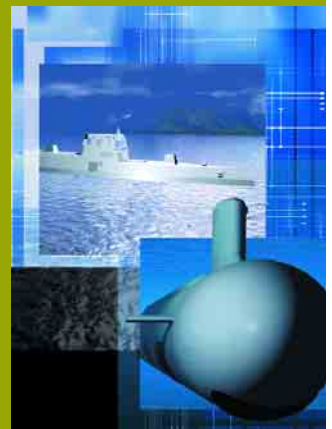
...READINESS, MOBILITY,



MODERNIZATION,



LEAPFROG TECHNOLOGY,



CAPITALIZING ON COMMERCIAL



OPPORTUNITIES...





L-3 Communications is a leading merchant

supplier of secure communications systems and

products, avionics and ocean products, training

products, microwave components and telemetry,

instrumentation, space and wireless products.

Its customers include the Department of Defense,

selected U.S. government intelligence agencies,

aerospace prime contractors and commercial

telecommunications and wireless customers.



Past: The P-51 Mustang, the most famous aircraft during World War II, was the long-range escort fighter that the Anglo-American bombing effort needed to end the war. The all-black 332nd Fighter Group – Tuskegee Airmen – flew their Mustangs in 200 escort missions and never lost a bomber to enemy aircraft.



Present: Decorated Air Force Pilot – Col. Eileen Collins – became the first woman to serve as commander of a space shuttle mission. She had participated in two earlier shuttle missions.



Future: Air Traffic Control Centers will be upgraded with new solid-state computer technology and the introduction of satellite-based navigation capabilities to provide dramatic breakthroughs in navigation precision.

Milestones

February 2000 L-3 acquires Raytheon's Training Devices and Training Services and renames it to reflect its heritage — Link Simulation & Training. Link is a leader in simulation and training products for a number of major aircraft and helicopter platforms, including the F-16, F/A-18, F-117 and F-22.

April 2000 L-3 adds Honeywell International's Traffic Alert and Collision Avoidance Systems (TCAS) business to its operations. Renamed Aviation Communications & Surveillance Systems (ACSS), this business is a leader in aviation safety systems and Mode S transponders in the world market.

SECURE COMMUNICATION SYSTEMS SEGMENT

- Secure communication links, satcom ground terminals
- Satellite communication & tracking; pointing, stabilization & command & control
- Shipboard communications
- Digital battlefield communications & communications software support services
- Secure voice, data & video, information processing (STE, OMNI™, LMD/KP)
- Military training devices & worldwide training services
- U-2, GUARDRAIL, Global Hawk, Predator, other aircraft, ships, unmanned aerial vehicles & satellites
- International Space Station, Earth Observing Satellite, Space Shuttle & NOAA weather satellites; Air Force Satellite Control Network, MELCO satellite ground stations, Delta launch vehicle guidance & ACTS
- AEGIS cruisers & destroyers, Trident & Attack (688) submarines, aircraft carriers, amphibious warfare & command ships
- U.S. Army C2V, ASAS, GUARDRAIL, future combat systems & UAV Risk Reduction Payload
- Armed forces & government agencies
- Flight simulators, maintenance trainers, aircrew training systems & distance learning

SPECIALIZED COMMUNICATION PRODUCTS SEGMENT

- Microwave, satellite & wireless components & RF safety products
- Cockpit voice & flight data recorders & Traffic Alert and Collision Avoidance Systems; reconnaissance
- Ultra-wide frequency antennas, rotary joints & radomes
- High performance displays and processors for airborne, shipboard and ground/vehicle applications
- Airborne dipping sonars, towed arrays; shipboard & submarine power delivery & conditioning systems
- Airborne, ground & space telemetry & flight testing
- Global satellite communications & transmission
- GPS receivers, translators, simulators & ruggedized displays
- Land navigation, fire control & missile guidance
- Turnkey automated data acquisition systems
- Cellular & PCS, commercial and military aircraft
- Commercial & military aircraft; SHARP
- Military aircraft, weather radar & air traffic control
- AH-64, A/MH-6J, C-130J, C-27J, C-5, EA-6B, E-2C, F-5B, F-14, Jaguar, JA-37, JAS-39, S-211, S-3B, SH-60J, T-38, U-2, LCAC, LOSAT & VISUAL
- SH-60, EH-101, NH-90, SSN, DDG-963 & FFG-7; DDG-51, NSSN & CVN-68
- JSF, F-15, F/A-18, F-22, Comanche, Nimrod (U.K.), Titan, EELV & BAe LIF
- Rural telephony, satellite news & private networks
- Armed Forces & Department of Defense
- MLRS, Dragonfire & CKEM
- Space Shuttle, Titan IV, EELV launch monitoring & U.S. Air Force jet engine test cells

EMERGING COMMERCIAL PRODUCTS*

- Prime Wave™ telecommunications equipment
- Privatel™ & Integrated Key Management System (IKMS™)
- eXaminer 3DX™ 3000 & 6000 explosive detection systems
- Power delivery & electrical products
- Event recorders
- Voyage data recorders
- Human Patient Simulator™
- Rural areas, developing nations & satellite based services
- Corporations, banking & e-commerce industries
- Domestic & international airlines & airports
- Transportation, utilities & web-based businesses
- Commercial rail transportation industry
- Cargo vessels & passenger ships
- Hospitals, medical schools, emergency medical services & military organizations

* L-3's Emerging Commercial Products are developed within its Secure Communication Systems and Specialized Communication Products business segments.

June 2000 MPRI, a leading teaching and training organization, is acquired by L-3. MPRI is staffed by accomplished, retired military officers and personnel and has a number of key domestic and international customers.

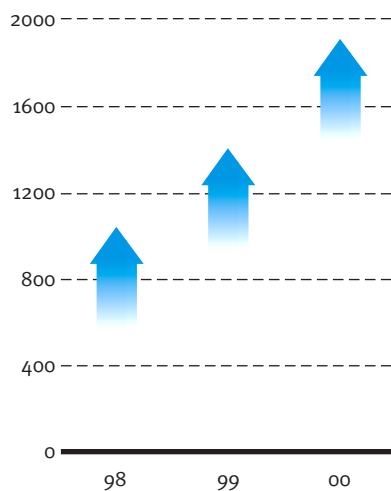
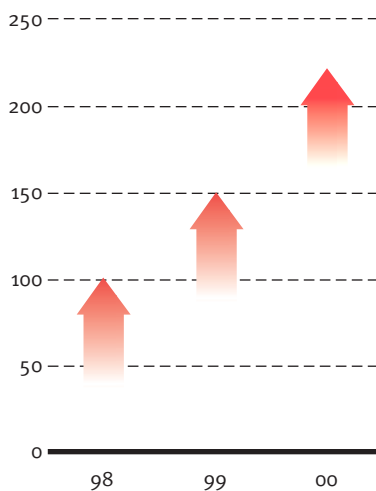
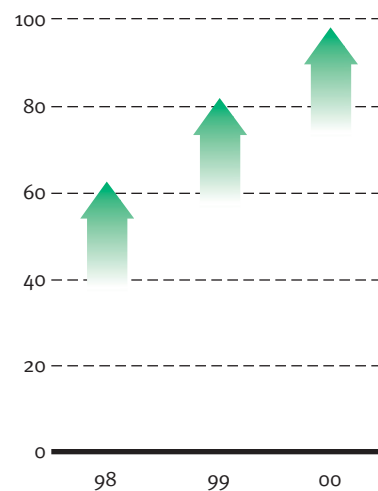
July 2000 L-3 acquires a 53.5% stake in LogiMetrics, Inc. and control of its operations. LogiMetrics has leadership technology for the emerging broadband wireless communications infrastructure market for Ka-band Point-to-Multipoint (PMP) distribution services, including high-speed Internet access, real-time multimedia file transfer, interactive video and other applications.

November 2000 L-3 sells \$300 million in 5.25% Convertible Senior Subordinated Notes due 2009 in a private placement. The notes are convertible into L-3 stock and the net proceeds from the offering were used to repay existing debt under its Senior Credit Facilities and for general corporate purposes, including acquisitions.

FINANCIAL HIGHLIGHTS

For the years ended December 31, (In thousands, except per share amounts)	2000	1999	1998
Sales	\$1,910,061	\$1,405,462	\$1,037,045
Operating income	222,718	150,486	100,349
Net income	82,727	58,689	32,551
Earnings per share (diluted)	2.37	1.75	1.26
Free cash flow ^(a)	98,285	82,275	62,623
Shareholders' equity	692,569	583,175	299,974

(a) Free cash flow is defined as cash flow from operating activities, less capital expenditures, net of dispositions.

Sales (in millions)**Operating Income** (in millions)**Free Cash Flow** (in millions)



(Left)
Frank C. Lanza
chairman and chief executive officer

(Right)
Robert V. LaPenta
president and chief financial officer



DEAR SHAREHOLDERS

L-3 Communications had another superlative year in 2000. For the fourth consecutive year, we exceeded key financial and operational measurements — growing greater than the 20% top- and bottom-line goals in 2000 and tripling in size since our inception in 1997.

We accomplished this with strong performance during the year in our core businesses, including secure communications, simulation and training products, ocean systems, displays and aviation products.

L-3 additionally won many program awards that extend our franchise businesses well into the future, including the Department of Defense's (DoD) decision to initiate Research and Development (R&D) on our next-generation data links to upgrade the U-2 program and other platforms, the award of several simulation and training programs, notable international and domestic sonar contracts and the expansion of our secure information products to mobile and wireless markets.

Our commercial transportation and telecommunications businesses have become key growth generators with significant potential over the next several years. We received important awards for fixed wireless access, gateway terminals, satellite ground station equipment, broadband mixed signal digital test and instrumentation products, explosive detection systems, hardened voyage recorders, aviation recorders and power equipment for trains, Internet data centers and air traffic control centers.

Letter to Shareholders

(cont'd)

In 2000, L-3 grew substantially by acquiring companies that are market leaders with proprietary assets and subsequently leveraging our marketing and R&D infrastructure and resources to increase their growth. This enabled us to broaden our already wide base of products, strengthen our relationship with DoD customers and prime contractors and outpace the growth of most defense companies.

As a result, we have created a unique company with significant momentum for this decade. One of the drivers of future growth is our major focus on R&D — developing products for planned platform upgrades and those platforms that are the blueprint for the future. Examples of L-3's R&D product development include revolutionary sonar technology, mobile collective simulation and training equipment and both commercial and military secure communications.

All these developments are very timely. Early in 2001, President George W. Bush began his efforts to implement an agenda that includes transforming the military and refocusing its future capabilities. He has noted that his highest priorities are improving the quality of life for the nation's armed forces, modernization and readiness and national missile defense. No matter which weapon platforms are subsequently authorized for recapitalization, L-3 will benefit. As a merchant supplier, L-3 provides state-of-the-art technology that can be used in both legacy modernization and futuristic platforms by any of the prime platform contractors. This is a unique and significant structural advantage for L-3 because it ensures that we can easily respond to changes in national priorities. It is one of the many reasons why L-3 is a momentum company for the decade ahead.

Record Sales

In 2000, our sales rose significantly to \$1.9 billion versus \$1.4 billion in 1999. This was a 35.9% increase over 1999 revenues.

Record Earnings

Operating income for L-3 increased 48.0% in 2000 to \$222.7 million from \$150.5 million in 1999.

Earnings before interest, taxes, depreciation and amortization (EBITDA) rose 45.4% to \$297.0 million from \$204.2 million in 1999. Net income in 2000 increased to \$82.7 million or \$2.37 per diluted share, compared to \$58.7 million or \$1.75 per diluted share in 1999.

Record Bookings

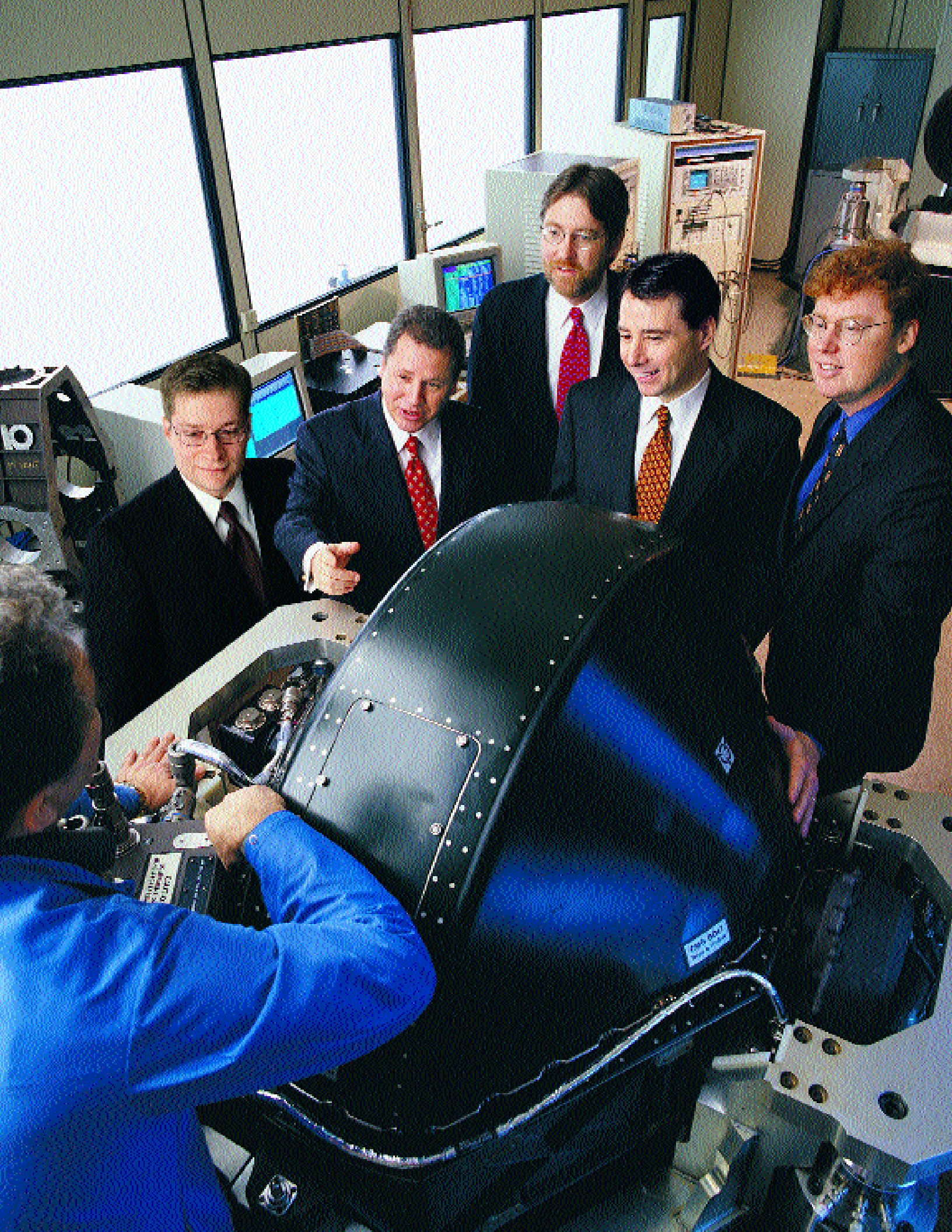
In 2000, we achieved a record \$2.0 billion in funded orders. In secure communications, L-3 had a banner year in data links, receiving contracts from the U.S. Air Force for next-generation data links for the U-2 high-altitude reconnaissance aircraft, contracts for Common High Bandwidth Data Link (CHBDL), Predator Unmanned Aerial Vehicle (UAV) and U.K. Airborne Stand-Off Radar (ASTOR). In addition, there was a new order for the VTUAV (Vertical Takeoff Unmanned Aerial Vehicle) platform.

We won an award which will have a long-term value of \$200 million from ITT, the prime contractor for the U.S. Air Force's Spacelift Range System, and an award from Raytheon Technical Services Company for L-3's Strategic/Tactical Airborne Recorder (S/TAR™) for the Shared Reconnaissance Pod (SHARP). L-3 also sold a record number of Secure Terminal Equipment (STE) products during the year and won an initial order for next-generation portable STEs as well as additional funding for classified signal intelligence programs and for the International Space Station (ISS) communication systems.

L-3's Link Simulation & Training business received a number of noteworthy contracts, including concurrency upgrades to the B-2 Weapon Systems and Maintenance Trainers, various upgrades for the F-117 Weapon Systems Trainer and continued funding for the F-22 Raptor Pilot and Maintenance Trainer Suites. In addition, there were awards for the C-17, E-3, F/A-18 and Battlefield Mobility and Target Acquisition programs.

At L-3 Space & Navigation with Control Moment Gyro: (l. to r.)

Ralph G. D'Ambrosio, controller, **Michael T. Strianese**, senior vice president of finance, **David T. Butler**, vice president of planning, **Christopher C. Cambria**, senior vice president, secretary and general counsel and **David M. Reilly**, assistant general counsel and assistant secretary.





L-3's teaching and training business — MPRI — was expanded with program support and information services for the Reserve Officer Training Corps (ROTC), growing from 25 to 217 universities. Support for the U.S. Army Recruiting Command also grew significantly.

Another important win for L-3 was the solid-state UHF Electronically Scanned Antenna, a next-generation phased array antenna for the carrier-based E-2C surveillance aircraft.

L-3's Aviation Recorder business is expanding its commercial business into the defense arena with contracts for the C-17, C-130 and F-22 aircraft as well as the next-generation Crash Survivable Memory Unit as a part of Boeing's Joint Strike Fighter (JSF) bid team. In addition, we secured orders for military recorders on the T-45 and B-1 platforms. On the commercial side, we were successful in obtaining orders for flight data recorders from Delta's fleet retrofit program, American and Continental Airlines and for Raytheon and Bombardier regional jets. We were also selected as the standard supplier for all new Airbus aircraft.

Ocean Products won key orders for towed array products for U.S. and international customers, dipping sonars for the Italian Navy's SH-3 helicopters and the U.S. Navy's SH-60 helicopters and strategically important orders for the Airborne Low Frequency Sonar and Multi-Purpose Processor retrofit programs.

Along with being a major supplier to the U.S. Navy for power distribution equipment, L-3 continued to expand into the commercial world with power transfer switches for transportation and web-based businesses. In 2000, there were orders from many high-profile companies, including AT&T, General Motors and AboveNet, a provider of fiber optic networks and Internet data centers.

In our Display business, L-3 won a key contract for its Warrior Vision™ flat panel displays on board the new Interim Armored

Vehicle and another to provide the shipboard workstations for the Virtual Imaging System for Approach and Landing (VISUAL) for U.S. Navy aircraft carriers and amphibious assault ships. In addition, we received important orders and follow-on awards for our Active Matrix Liquid Crystal Displays (AMLCDs) on the JAS-39, S-3, C-130J and U-2 as well as our ongoing work on the E-2C's Enhanced Main Display Unit (EMDU).

L-3's Microwave business posted strong orders, especially in the second half of the year, led by products for base station applications for customers ranging from Original Equipment Manufacturers (OEMs) to service providers.

The Telemetry, Instrumentation and Space businesses earned key awards from Boeing for encoders and transmitters for the Joint Direct Attack Munitions (JDAM) program, space transponders for the classified military satellite market, encoders and transmitters for Lockheed Martin on the Guided Multiple Launch Rocket System (GMLRS), a high data rate payload transmitter on the Coriolis spacecraft for Spectrum Astro, a telemetry system for the Maverick Weapon Systems Evaluation Platform for Redstone Arsenal and an integrated telemetry ground data processing system for the Royal Australian Air Force's (RAAF) Lead In Fighter program.

Finally, in our Explosive Detection System (EDS) business, L-3 signed a contract with the Federal Aviation Administration (FAA) for up to 60 eXaminer 3DX™ 6000 systems, with a potential value of \$89 million as well as developmental funds to add enhanced features and capabilities.

Next-Generation Products

A significant discriminator and key advantage that distinguishes L-3 from our competitors is our ability to funnel significant R&D funds into promising new product development. In 2000, L-3 devoted \$400 million of government and internally funded R&D to develop a host of next-generation products, product upgrades

Washington Operations: (l. to r.)

Seated — Jimmie V. Adams, vice president of Washington Operations, Robert W. RisCassi, vice president of Washington Operations and Carl E. Vuono, president of MPRI division.

Standing — Donald A. MacDonald, vice president - International, Larry L. Henry, vice president of Air Force Programs, Lawrence H. Schwartz, vice president of Business Development and Dennis A. Jones, vice president of Maritime Programs.

Letter to Shareholders (cont'd)

and new applications. The following are just a few highlights of new products and development work during the year:

- » **RADIS** (Rapid Acquisition Dispersive) modem technology that enables information to get through in a cluttered, wireless communications environment for commercial and defense applications. This technology allows for 160 times the communications traffic than is currently available.
- » **S/TAR™**, a solid-state recorder designed for the high performance, severe environments of airborne reconnaissance and flight tests. This product was selected by Raytheon for use in the U.S. Navy's Shared Reconnaissance Pod (SHARP).
- » **OMNI™**, a small, transportable voice and data communications security device for government users that leverages L-3's proprietary technology.
- » **Tsunami™**, a new major breakthrough multi-function ship hull sonar sensor system for advanced naval surface combatants that provides savings of up to 70% in acquisition, operation and maintenance costs over legacy systems. The system was successfully demonstrated at the Naval Undersea Warfare Center.
- » **Hardened Voyage Recorder (HVR) and Audio Acquisition and Microphone Mixer (AAMM)**, meeting the new data recorder requirements for passenger ships, ferries and cargo vessels using L-3's advanced data recorder technology.
- » **Broadband Wireless Instrumentation**, a full suite of new products and analysis tools that can be rack-mounted or portable for testing of all 2G and 3G wireless and satellite communications networks for telecommunications factories and R&D centers.
- » **Xcaliber GPS Receiver**, designed to meet requirements on a variety of U.S. DoD smart munition programs, features direct y-code and has the ability to withstand 15,500 Gs of shock when fired from a gun.
- » **Micro SCIRAS** (Micro-machined Silicon Coriolis Inertial Rate and Acceleration Sensor) for use in all systems requiring tactical-grade performance, including guided munitions, missiles and GPS-aided navigation systems.
- » **eXaminer 3DX™ 3000**, a more compact, lower-cost explosive detection system based on L-3's existing FAA-certified eXaminer 3DX™ 6000 for use in small and regional airports with less traffic.
- » **Prime Wave™**, an S-CDMA (Synchronous Code Division Multiple Access) system-based commercial telecommunications product for areas without conventional wireline infrastructure. The product was developed from technology used in international military applications and provides low-cost, secure wireless voice and data services.
- » **Transceivers for Local Multipoint Distribution Services (LMDS)**, which enables service providers to build a system that offers Point-to-Multipoint services, including high-speed Internet access, real-time multimedia file transfer, remote access to corporate local area networks and interactive video, among many other services. Production initiates in 2001.
- » **MarCom 2000**, an integrated digital switch that provides the U.S. Navy with a low-cost solution to the complex voice, video and data communications needs of present and future surface ships for internal and external communications.

At L-3 Space & Navigation with Position Navigation Unit: (l. to r.)

***Kenneth R. Goldstein**, director of taxes, **Kenneth W. Manne**, vice president of human resources, **Lawrence W. O'Brien**, vice president and treasurer, **Cynthia Swain**, vice president of corporate communications, **Joseph S. Paresi**, vice president of product development and president of Security Systems division and **Sheila Sheridan**, director of administration.*





» **FlyAway (Single Band) Satellite**

Terminal, enables service providers, traditional telecommunications providers and commercial and government users to quickly set up a transportable, high-speed backbone that offers voice, data, Internet and other applications from remote areas.

Major Acquisitions

In 2000, we once again demonstrated our financially disciplined approach to selecting acquisitions, making investments in other companies and developing cooperative relationships. L-3's acquisition strategy is to find hidden gems in the defense electronics arena that will be accretive, but are at the time undercapitalized or "under-managed." Once L-3 acquires the business, we immediately resize the company, improve margins, invigorate its management team, provide L-3's extensive marketing support and initiate synergies among complementary divisions.

There were a number of major acquisitions and partnerships at L-3 in 2000 including:

» **Raytheon's Training Devices and Training**

Services, now restored to its heritage name as **Link Simulation & Training**, a leader in simulation and training products on a host of high-profile platforms, including the F-16, F/A-18, F-117, F-22, B-2 and Army helicopter programs.

- » L-3 acquired **Honeywell International's Traffic Alert and Collision Avoidance Systems (TCAS)** business. The newly renamed **Aviation Communications & Surveillance Systems** division is the leader in avionics safety systems and Mode S transponders used on thousands of air transport, regional, corporate jet and military aircraft. L-3 also has agreed to create a joint venture company for this operating unit, in which Thales Avionics, formerly known as Sextant, will initially acquire a 30% equity interest. L-3 retains operating management of the joint ven-

ture and will utilize Thales' extensive international sales and support infrastructure to market its surveillance and safety products in the worldwide air transport market.

- » **MPRI**, a leader in providing teaching and training programs for domestic and international military and commercial customers, is poised for significant growth as the U.S. military increases its reliance on outsourcing to reduce costs and address personnel shortages.

- » **Coleman Research**, a leader in communications, intelligence and space instrumentation, simulation and training. Its high-fidelity custom targets are complementary to the administration's focus on theater and national missile defense and space programs.

- » L-3 acquired a 53.5% stake in **LogiMetrics**, a producer of broadband wireless communications transceivers for the emerging multi-billion-dollar market for Ka-band Point-to-Multipoint (PMP) distribution services for terrestrial and satellite markets.

- » L-3 acquired a minority equity interest in **Core Software Technology**, a leader in the growing commercial satellite imagery market and also became the exclusive provider to Core of high-speed broadband communications and networking products, including ground station uplinks and other products.

- » L-3 entered into a cooperative agreement with **Inmarsat**, a leading provider of global mobile communications, to offer advanced technologies for the spacecraft control marketplace and to provide satellite services for operators worldwide.

Letter to Shareholders

(cont'd)

Group and Division Presidents: (l. to r.)

*Standing — **Curtis Brunson**, corporate vice president and president of Communication Systems – West division, **James W. Dunn**, president of Link Simulation & Training division, **A.E. "Gene" Dotson**, president of SPD Technologies and general manager of Power Paragon division and **Steven T. Schorer**, president of Ocean Systems division.*

*Seated — **Gregory B. Roberts**, corporate vice president and president of Communication Systems – East division, **John S. Mega**, corporate vice president and president of Microwave Group, **Alan R. Dietrich**, corporate vice president and president of Telemetry Group and **Charles J. Schafer**, vice president of business operations and president of Products Group.*

Letter to Shareholders (cont'd)

Commercial Opportunities

One of the more difficult challenges for a defense company is to transfer its military technologies into the commercial world. Over the years, many big plans in the industry have translated into big losses, largely because of marketing and distribution shortcomings, high start-up costs and the punishing pace of technological and consumer change.

L-3's strategy has been to take measured steps by developing promising products in niche areas that were created with government funding and finding partners that have a strong commercial infrastructure in place. In addition, we make small strategic investments in businesses that in turn use L-3's technologies creating a win-win situation for all parties.

In our commercial transportation area, we offer explosive detection systems, hardened voyage recorders, power propulsion systems, power switches, displays and controls for the locomotive and transit industries, event recorders for rail transportation, power switches for Internet Service Providers, aviation recorders and collision avoidance systems.

Our commercial telemetry business has been strategically enhanced over the past year by key wins at Telemetry-East from Bombardier, Cessna and Embraer. These wins provide a firm foundation to pursue other similar business in the commercial aviation market.

Our EDS products won major awards in 2000 and in January 2001 from the FAA. L-3 was also funded for the development of a smaller version of our FAA-certified EDS technology. This gives L-3 a competitive advantage because we can provide products for both large and small airports.

By acquiring Aviation Communications and Surveillance Systems, L-3 has the premier traffic alert and collision avoidance technology in a billion-dollar market. We are also exploring an enhanced collision avoidance product that integrates Terrain Awareness Warning

System (TAWS) technology into the TCAS box. This will provide new and existing customers with functionality that is being mandated in many parts of the world, without having to accommodate an additional Line Replaceable Unit (LRU).

In telecommunications, L-3 supplies local wireless access equipment for voice, DSL and Internet access, transceivers for LMDS and a broad range of commercial components and digital test equipment for broadband communications providers.

We won a major endorsement of our fixed wireless access system with a contract to supply voice, Internet, leased-line and pay phone service in South America.

Investor Highlights

In 2000, L-3's focus on growth through performance and key acquisitions enabled us to raise capital in the financial markets at very attractive rates. In November of that year, L-3 sold \$300 million in 5.25% Convertible Senior Subordinated Notes due 2009 in a private placement. The notes are convertible into L-3 stock.

L-3 used the net proceeds from the offering to repay existing debt under its Senior Credit Facilities and for general corporate purposes, including acquisitions.

Throughout the year, L-3's executive team continued to participate in a number of high-profile investor conferences, reflecting our increasing prominence as a major defense company. In another sign of the increasing interest in L-3, we attracted additional analyst coverage in 2000.

Growth in 2001 and Beyond

As the Bush administration develops its national security strategy, we expect that it will be very positive for the defense industry. The 2001 defense budget has already been established, but it is too early to predict specifics on policy changes and how they will impact defense and commercial businesses.

There will be a host of issues to consider. They include national policy on whether to retain the core capability to fight and win two near simultaneous major theater wars in overlapping time frames, national missile defense, asymmetric threats and space operations. It is imperative that the DoD maintain a balance between legacy systems and advanced platforms.

The DoD will initiate a top-down review of these issues during Secretary of Defense Donald H. Rumsfeld's review culminating in the Quadrennial Defense Review, which will be announced in the second half of 2001. Its recommendations will form the basis for a bottom-up review that will shape the 2002 adjustments and future budgets.

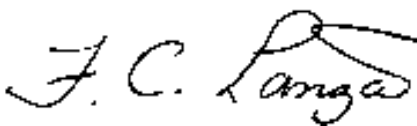
There is no question that President George W. Bush's administration believes that fundamental military reform and increased investment is an absolute. Generally speaking, the Bush administration has indicated the view that the U.S. military must make some substantial changes to reflect new realities. This includes resource adjustments to fund change that the U.S. military requires in order to leapfrog its increasingly outdated technology and move to more mobile, lighter and smarter weapons. Key areas that would benefit from such a shift include smart munitions, naval ship modernization, battlefield communications and fusion, all-weather execution of mission, space management and national and theater missile defense.

The 21st century environment and its associated defense trends are areas that would particularly benefit a defense electronics company such as L-3. We have high-technology data links and digital battlefield communications, simulation and training products, state-of-the-art sonar technology, solid-state power products for the U.S. Navy, GPS and TCAS products – each of which can play an important role in the military transformation ahead.

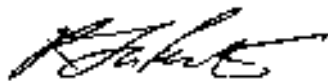
Industry consolidation will continue strong into 2001 and beyond. Though consolidation among prime contractors is largely concluded, there continues to be much opportunity below that level. There are assets from large defense companies, mid-caps and small defense firms on the market. L-3 has been and will continue to be the leader in the consolidation of smaller, specialty companies.

As for the economic outlook, we believe that the defense sector continues to be, on balance, a stable investment that largely resists the volatile swings that marked investment activity in 2000. By establishing ourselves as a core defense company with carefully selected, conservatively planned commercial opportunities, L-3 is structured to offer the advantages of solid growth, stability and commercial upside with minimal downside risk.

For these reasons, we believe that the environment for L-3 is exceptionally promising for 2001 and beyond. In the past four years, we have made extraordinary progress and achieved unrivaled growth in the defense industry. With the continued support of our highly talented employees and based on the momentum we have achieved, we see an extraordinary future ahead of us.



Frank C. Lanza
Chairman and Chief Executive Officer



Robert V. LaPenta
President and Chief Financial Officer



communications

▶▶ TELEMETRY & INSTRUMENTATION

WE HAVE TO BE AHEAD OF

▶▶ AVIONICS

▶▶ SECURE COMMUNICATIONS

▶▶ SPACE

A detailed view of the International Space Station (ISS) in space. The station's complex structure, including multiple modules and large solar panel arrays, is clearly visible against the black background of space. A bright blue light source, likely the Earth's horizon or a distant star, is visible in the upper left corner. The station is oriented diagonally across the frame.

▶▶ SIMULATION & TRAINING

▶▶ MICROWAVE

THE FUTURE EVERY DAY...

▶▶ NAVIGATION & GUIDANCE

▶▶ OCEAN SYSTEMS

▶▶ BROADBAND

*International Space Station is being navigated in space
and beaming down its audio and video communications —
all with L-3 Communications products.*





FUTURE PRODUCTS TODAY

To stay at the forefront as a merchant supplier, L-3 has to anticipate the requirements of the DoD and the primes for platforms that will be developed in the next few years. This also demands that L-3 plan products for those platforms that are on the drawing board for the future.

Operating on both new and future platform cycles requires L-3 to have solid relationships with the primes to understand their technological and cost issues to subsequently maximize its R&D funds to seed promising products. In addition, L-3 must develop an in-depth assessment of where Washington will direct the country's defense resources in the future and have a realistic view of which large venture commercial platforms will succeed. Having a long, proven record of success in developing the right products at the right time and cost is essential.



AVCATT-A Simulator (left) and Helmet Mounted Display (right):

Reconfigurable simulators being built by Link Simulation & Training for the U.S. Army will help develop the skills of new pilots, as well as prepare experienced aviators, crews and teams for specific combat or peacetime missions.

L-3's businesses have decades of experience in successfully responding to these requirements and developing state-of-the-art technologies that set standards in their particular niche. As a result, the company is resident on a number of new platforms.

Future Products Today

Digital Battlefield

In the new digital battlefield, sharing real-time data is crucial to responding quickly and effectively to threats. The nation's military forces must have the most advanced hardware and software to collect and relay information to the appropriate sources. L-3 provides airborne data links, antennas and ground and shipboard stations to convey this essential information to the fighters.

For decades, L-3 has been a supplier of data links for the premier surveillance and reconnaissance U-2 platform and, in fact, won two contracts to supply next-generation data links for the aircraft in 2000. In recent years, the DoD has also seen the success of its UAVs, which perform surveillance functions without risking military forces. As a result, UAVs are playing an increasing role in operations. L-3 has an extensive presence in the UAV market and has received a new data link contract for the VTUAV.

As digital and broadband communications continue to advance, display technology is pushing ahead to meet the increased needs of military planners. L-3's premier display is the Multiple Tile Video Display™ (MTVD), a lightweight, deployable, high-resolution unit with either four or nine large screen displays for commanders' situational awareness of the digital battlefield. This unit enables battlefield commanders to bring the full complexity of the battle scene together by displaying several digital and/or video inputs simultaneously, along with military symbology.

The need to replace outdated electro-mechanical instruments that provide horizontal and vertical situation data for navigation prompted the U.S. Naval Air Systems Command Headquarters (NAVAIR) to upgrade its S-3B Viking aircraft with L-3's Electronic Flight Instrument (EFI) flat panel displays. Boeing also enlisted L-3 to provide shipboard workstations for the Virtual Imaging System for Approach and Landing (VISUAL) program. This new product will assist the Landing Signal Officer (LSO) on board aircraft carriers and amphibious assault ships in assessing a pilot's performance on final approach.

For the past several years, military planners, U.S. agencies and high-level governmental officials have been using STE to ensure secure, encrypted communications around the world. Now they can take the technology with them when they travel.

L-3's OMNI™ is a small, portable terminal with Type 1 Security for voice and data communications, supporting desktop, network and portable wireline user requirements.

L-3 has also taken its secure technology to the commercial world. Traditionally, banks use manual keys to change the encryption in their ATMs to ensure their security. This is an expensive, labor-intensive process that can now be automated with L-3's Integrated Key Management System™ (IKMS). This is the only system of its kind available today and it reduces labor costs by up to 80%.



U-2: (above)

L-3 Communication Systems-West provides engineering, maintenance, special repair activity and field support for the U-2 data link programs.

Smart Weapons

There are two reasons why smart weapons are growing in importance for the U.S. military arsenal. First, the use of smart weapons by ground forces or in long distance air strikes can keep U.S. and allied casualties to a minimum. Second, the pinpoint accuracy of these weapons enables U.S. forces to limit collateral damage.

L-3 has decades of experience developing GPS guidance systems for the U.S. military and its technology will be used in both the Navy's Extended Range Guided Munition (ERGM) and the Army's Excalibur program. L-3's current system will process GPS, and eventually, inertial data from an L-3 developed silicon-based Micro-Machined Electro-Mechanical System Inertial Measurement Unit (MEMS IMU) as well as function as the navigation computer. With highly integrated GPS and inertial guidance, missiles will be more effective through enemy electronic jamming. The combination of GPS and MEMS IMU within one company uniquely qualifies L-3 to respond to the marketplace addressing both performance and cost-efficiency.



Naval Modernization

As the U.S. Navy begins its modernization efforts, there are many systems, subsystems and products that need to be upgraded. One area that will be transformed is hull sonars. For decades, naval surface combatants had large sonar hulls to house sensing technology. L-3 has revolutionized hull design with the development of the Tsunami™ Multi-Function Ship Hull Sonar, the culmination of ten years of R&D. This compact, long-range sensor system is one-third the size of conventional hull sonars, provides in-stride mine avoidance capability and saves the Navy up to 70% in acquisition, operation and maintenance costs over legacy systems.

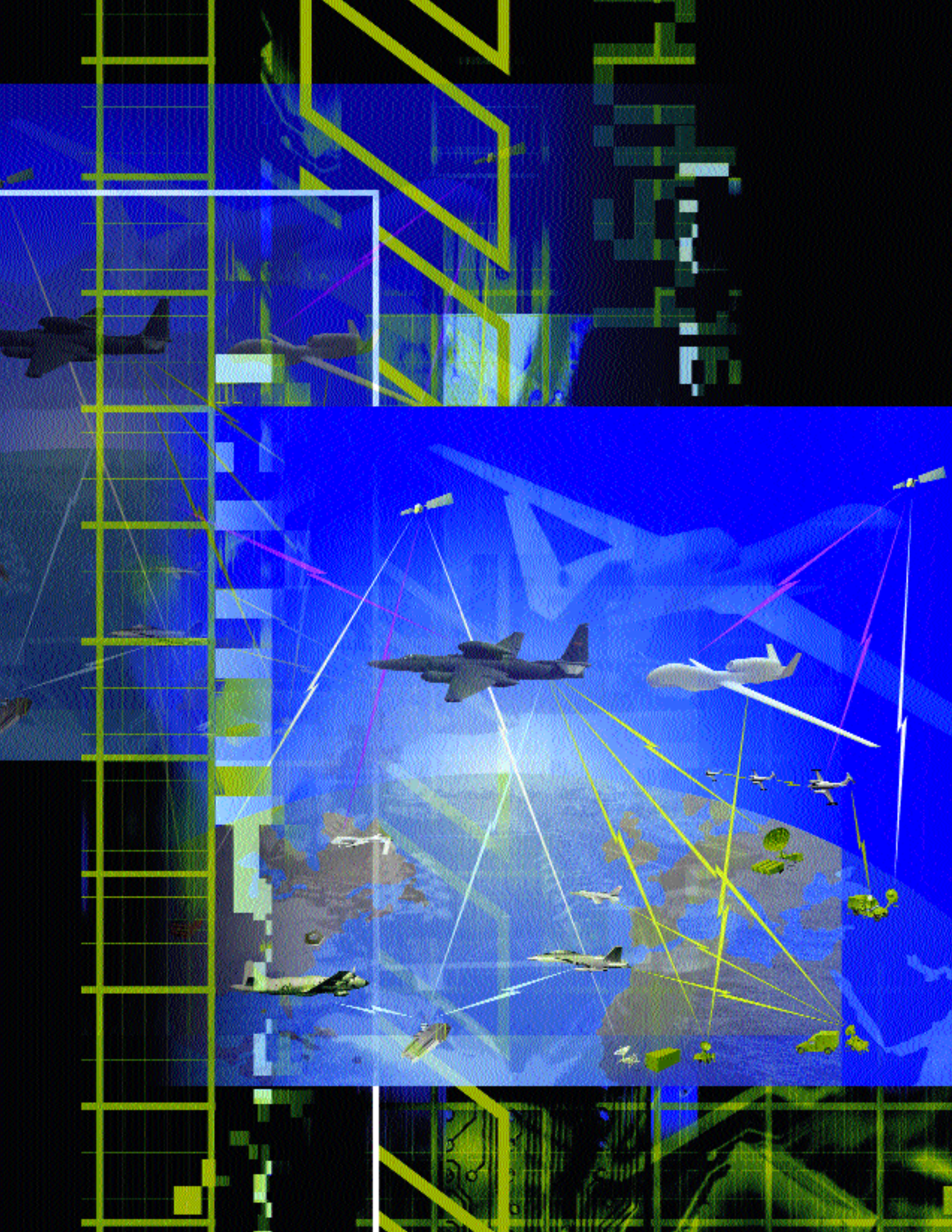
Another key upgrade is the move towards electrical power as the U.S. Navy converts its submarines from mechanical to the quieter and more efficient electrical power. L-3 is providing electric plant power conversion for the first Virginia class new attack submarine for the Navy and thirty more are planned over the next two decades.

ERGM: (above)

L-3 IEC's GPS receiver undergoes testing in its 15,500 G operational environment. After launch, the projectile is guided to a precise location at distances greater than those in use today.

OMNI™: (below left)

The OMNI™ secure terminal provides security for both voice and data communications by offering a versatile narrow band encryption solution that supports the desktop, network and portable wire-line government user requirements.



Along with a full catalog of state-of-the-art power delivery and conditioning products, L-3 has also developed ruggedized 150kW static air-cooled 60-400Hz Static Frequency Converters (SFC) for vital shipboard equipment. The SFC is derived from L-3's 288kW converter, which has become the class standard for the DDG-51 class AEGIS destroyer.

To save on costs, the U.S. Navy is also looking for state-of-the-art technology that is flexible and cost-efficient. L-3's MarCom 2000 is an integrated communication switch for command and control communications and radio room automation. This system is based on commercial-off-the-shelf (COTS) technology, a low-cost solution for complex voice, video and data requirements and can be used for present and future joint or allied missions. MarCom was successfully field tested on the USS Abraham Lincoln and the company also supplied its newest key switch integrated terminals to enhance the communications capability of the ship.

Avionics: New Capabilities, New Markets

Voice and data recorders have proven to be life-saving technologies for the airline industry and L-3 is upgrading them for commercial aircraft and expanding their use for other applications. For instance, the industry is looking to monitor an increased number of parameters on both rotary and fixed wing aircraft. L-3's FA2300 Modular Airborne Data Acquisition/Recording System (MADRAS) is a single-unit cockpit voice and flight data acquisition and recording system that will enable a plane to accommodate numerous



combinations of data and interface with aircraft sensors.

The catastrophic aircraft power failure of Swiss Air Flight 111 has led the FAA to propose new regulations requiring recorders to possess an independent power supply. L-3 was the first to develop technology that provides ten minutes of emergency backup power in all cases where normal aircraft power ceases.

There is still significant growth in the recorder market as it moves into new niches, including railroad, general aviation and maritime. In the rail transportation market, the company supplies event recorders for locomotives, which provide mishap analysis and evaluation of operating performance. For the emerging general aviation market, L-3 has developed a lower-cost FA2100 Cockpit Voice Recorder (CVR).

In addition, the International Maritime Organization (IMO) is instituting requirements for cruise ships to be equipped with recorders. As a result, the company has developed a Hardened Voyage Recorder (HVR) for the maritime market. This product records a range

Internet in the Sky: (left)

L-3 developed high-performance data link systems to transfer information to and from aircraft, ships, satellites and ground stations throughout the world for strategic and tactical operations.

MarCom 2000: (above)

Currently in production, the MarCom 2000 is the next-generation automated switch aboard the Los Angeles class attack submarines, AEGIS destroyers, and various international programs. The product provides a low-cost, integrated approach to the specialized voice and data communications needs of shipboard/ground force vehicle environments for internal and external communications, command and control and air traffic control.

Future Products Today

of data and audio and is fitted in a special Crash Protected Memory Unit (CPMU) with a device to aid in locating it in the event of a catastrophic incident.

L-3 participates in another key market that is being revolutionized by technological change. Aviation communications and surveillance technology, with its ability to make aircraft aware of oncoming intruders in their airspace and direct them away from potential danger, has fundamentally improved air travel safety.

The next revolution in this segment is the introduction of complete situational awareness, which will enable pilots to have a total understanding of potential threats in their surrounding airspace. L-3's TCAS 2000 is a second-generation product with superior intruder tracking performance and 360-degree, full-time surveillance coverage, which anticipates future "free flight" requirements and enhancements, thereby giving pilots full awareness and control of their present operating environment.

Finally, for the military market, L-3 has taken its decades of experience in space-based recording systems to develop S/TAR™. Along with numerous operational advantages, this ruggedized recorder has fast, random access to data, simultaneous read/write capability and a special feature that enables an aircrew to quickly pinpoint a key target. Raytheon Technical Services Company has awarded L-3 a contract to supply S/TAR™ for the U.S. Navy's premier tactical reconnaissance program, SHARP, to be flown on the F/A-18E/F Super Hornet.



Mobile Collective Training

In the simulation and training segment, economic pressures are placing enormous constraints on live field training exercises, so the military needs realistic trainers that can integrate pilots, crews and teams. These systems also need to be reconfigurable so that U.S. forces can be trained for changing real-world conditions and environments. The U.S. Army calls this collective training concept – "one Army, one simulator."

During 2000, Link Simulation & Training began developing suites of training devices that are the cornerstone of the U.S. Army's helicopter flight simulation and combined arms tactical training strategy. Known as the Aviation Combined Arms Tactical Trainer-Aviation Reconfigurable Manned Simulator (AVCATT-A) program, this initiative will enable the Army to enhance and sustain the skills of its helicopter pilots within simulated combat environments that present the challenge of interactive opposing forces. In addition, AVCATT-A's reconfigurable trainers – which will provide company-level collective training – will be interoperable with a family of existing and planned Army combined arms



Hardened Voyage Recorder: (above)

From the leader in "black box" technology – a solid-state, high-capacity, low-cost product line for maritime use. The L-3 Hardened Voyage Recorder provides over 12 hours of storage capacity for radar, sensor and audio data – all within a protective memory capsule. Units comply with all International Maritime Organization (IMO) requirements.

S/TAR™ RM-3000: (above right)

The Strategic/Tactical Airborne Recorder™ (S/TAR) product line is the most sophisticated and reliable family of solid-state recorders available on the market. Designed for high capacity, high data rate applications for airborne environments, the product was selected for use in the U.S. Navy's Shared Reconnaissance Pod (SHARP). Four successful flight certification tests of S/TAR™ have been demonstrated on the Global Hawk Unmanned Aerial Vehicle (UAV) being developed by Northrop Grumman.

training systems. These networked systems will create a virtual war gaming world in which simulators are used to train the full spectrum of warfare.

The awarded program has the potential to continue through 2007 and generate more than \$300 million in revenue. In addition, because this unique technology can be applied in the foreign military market, its international market potential is equal to that of domestic sales.



Space

The International Space Station's scope and complexity have been compared to the building of the pyramids — with sixteen nations cooperating to participate in the largest, non-military joint effort in history. When this station is completed, it will hold a habitation module for the crew as well as seven laboratories for research and eleven external payload locations for mounting experiments.

L-3 supplies a number of key products and systems for this extraordinary station, including the gyroscope that keeps the ISS in its orbit and its Warrior Vision™ display for the onboard Robotic Workstation (RWS).

When the world sees video of the activities of the space station and its crew, it will be as a result of L-3 products. L-3 is responsible for the Communication and Tracking System, which provides real-time, space-based communications and external video to earth through the Tracking and Data Relay Satellite System (TDRSS). In addition, L-3 will perform depot repairs and hardware upgrades to the ISS Orbital Replacement Units (ORU) returned from service.

TCAS: (above)

L-3's Traffic Alert and Collision Avoidance System computes range, relative altitude and bearing of aircraft to determine if nearby aircraft have collision potential.

Warrior Vision™: (below left)

L-3 IEC's ruggedized displays assist the astronaut specialist with remote vision for the Canadian Remote Manipulator Arm as it is used to construct major segments of the International Space Station.





communications

►► MISSILE

►► PLATFORMS OF THE FUTURE

►► AIRBORNE

►► NAVAL

►► GROUND

» 21ST CENTURY PLATFORMS

Even as the Cold War has ended, the number of potential threats to the U.S. and its allies has not diminished. The threats of cyberwar, weapons of mass destruction, nuclear threats from rogue nations, regional conflicts and terrorism have placed even greater demand on U.S. military forces to have more advanced technologies at their disposal.

These new technologies will demand extraordinary efforts from the defense industry, equivalent to the technological transformation missions that have altered the course of history, such as the race to place the first man on the moon. It will require a national and theater missile defense system, a lighter, more flexible and more lethal military force and all the technological tools necessary to outsmart and overpower the enemy and protect our people, borders and resources.

No matter which platform or system is selected as the nation assembles these tools to fight 21st century wars, L-3 is currently developing products and subsystems that will give America the edge in the conflicts to come. L-3's businesses have a tradition of anticipating what the state-of-the-art will be and exceeding those expectations.

» INTEGRATED COMMUNICATIONS

Information superiority will be the key to "full spectrum dominance" so that U.S. forces can make better decisions faster than the enemy can react. The threat to this dominance can come in the form of anti-satellite missiles or other weaponry designed to block access to the world's information assets. To combat these threats, the U.S. must maintain a strong presence in space to ensure that the U.S. and world economies and the flow of military data are not disrupted.

To make better use of information, military planners are looking ahead to reconnaissance architectures that link

numerous systems, including satellites, UAVs, remote sensors and soldiers on the ground. By creating such an integrated system, U.S. forces could have "dominant battle space awareness." This would provide reconnaissance, surveillance, intelligence gathering, battle management, communications, position location, terminal guidance and battle damage assessment. Dissemination of the tactical data will give the soldier, sailor and pilot a more complete view of the tactical environment. L-3's Enhanced National Tactical Receiver (ENTR) will provide this capability in a miniaturized, multichannel tactical receiver integrated into a laptop, desktop PC and airborne systems.

L-3's data communications operations were instrumental in building an "Internet in the sky" with its communication systems for intelligence collection, imagery processing and satellite

communications. This technology, which includes data link systems to transfer information to and from aircraft, ships, satellites and ground stations throughout the world, enables military planners to make strategic and tactical decisions in real time. This technology offers a sound base on which to build the integrated systems of the future.

The airborne integrated communication system produced by L-3 for Global Hawk Air Vehicle (photo above) permits worldwide secure command and control of the UAV and sensors as well as transmission of near real-time, high-resolution imagery. The Global Hawk supports the most robust communications suite flying on U.S. Government Intelligence, Surveillance and Reconnaissance (ISR) platforms today. Housing a total of four data links, L-3 provides two UHF line-of-sight (LOS) and beyond line-of-sight (BLOS) links for vehicle command and control and two wideband links for sensor data communication.



L-3 has also demonstrated a system that detects and locates both communications intelligence (COMINT) and electronic intelligence (ELINT) emitters using a UAV. The SKYHAWK 2000 UAV payload enables faster and more accurate transmission of information to a ground station.

The military is developing a new satellite communications network that replaces the current MILSTAR system and provides global jam-resistant communications for military users. L-3 will supply the Advanced Extremely High Frequency Communications Security (COMSEC) and Transmission Security (TRANSEC), known as ACTS.

►► MISSILE DEFENSE

Perhaps the most significant threat is the rise of emerging nuclear power nations and the possible use of biological, cyber and ballistic missile attack against other countries. To deal with this threat, the U.S. is currently developing a missile defense system to detect, track and destroy any incoming missile before it enters the atmosphere.

Much work needs to be done on the enabling technologies to make the vision of an effective missile defense system a reality. However, there is little doubt that it will play a major role in the defense posture of the U.S. within the next ten years. The elements include the National Missile Defense system (NMD), a land-based system slated to protect the entire U.S. and its allies, and the Theater Missile Defense system (TMD) to defend the nation's troops in conflicts or war. Also planned are advanced versions of the long-range standoff missile — Conventional Air-Launched Cruise Missile (CALCM) and the Extended Range Guided Munition (ERGM) projectile.

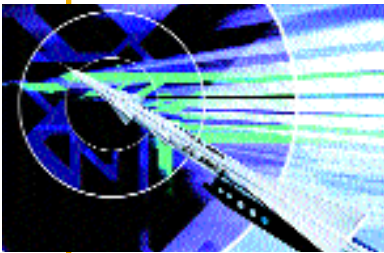
Much of the early work for NMD and TMD involves simulation work and prototype development of ballistic missile targets. L-3 is currently providing the U.S. government with high-fidelity custom targets that are important for NMD and space programs.

L-3 is an industry leader in GPS receivers and translator-based products for multiple aircraft, cruise missiles and precision-guided bombs and projectiles, and will continue to play an important role as the developmental work on missile defense advances (pictured left).

For the U.S. Army's Excalibur program, L-3 has developed a GPS Selective Availability Anti-Spoofing Module (SAASM) receiver, which is integrated with the company's MEMS-based Inertial Measurement Unit. SAASM, mandated by the GPS Joint Program Office, is essential for operation in a tactical, fast acquisition, high-jamming battlefield environment. This cost-effective, gun-launched guided projectile has all-weather condition accuracy and can withstand acceleration forces 15,000 times that of gravity, which makes it ideal for many other missile and projectile programs.

►► JOINT FORCES

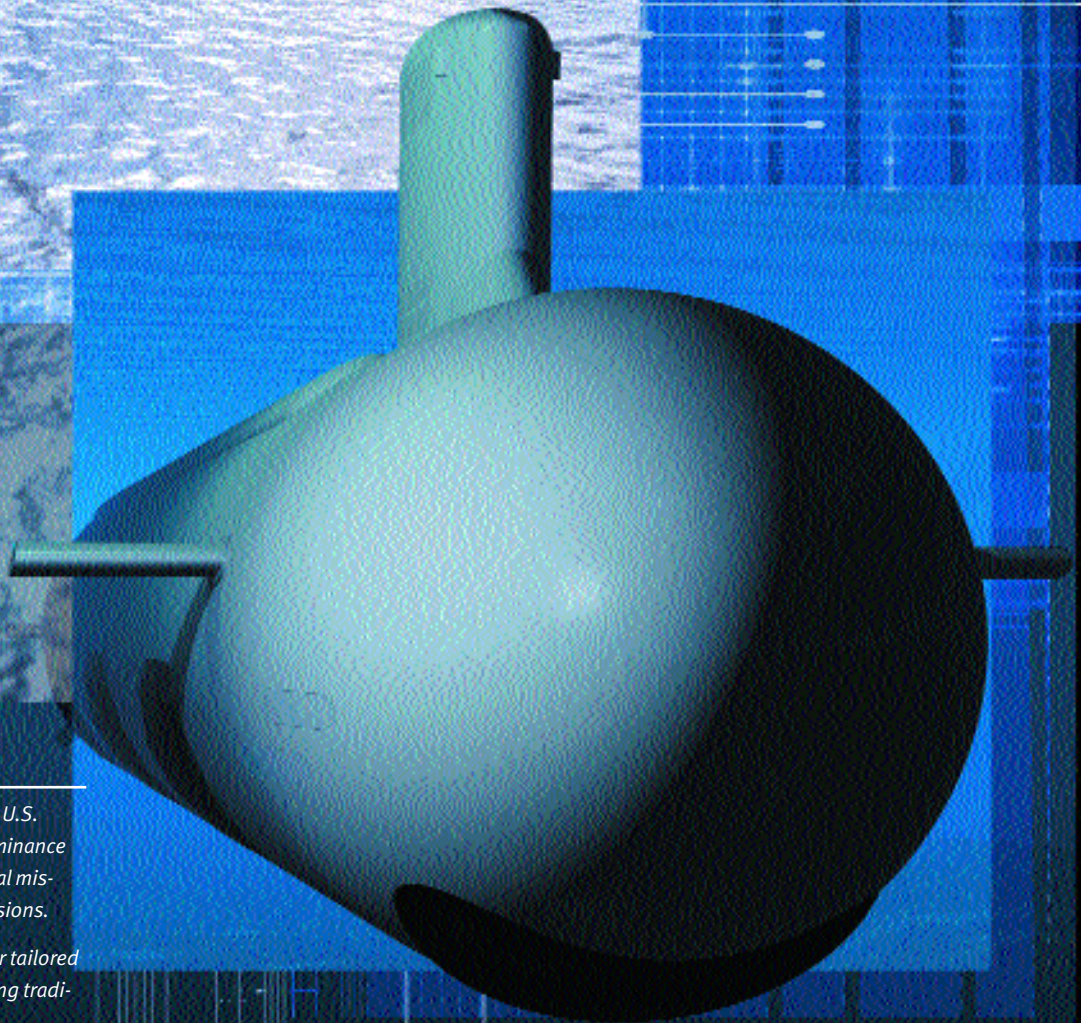
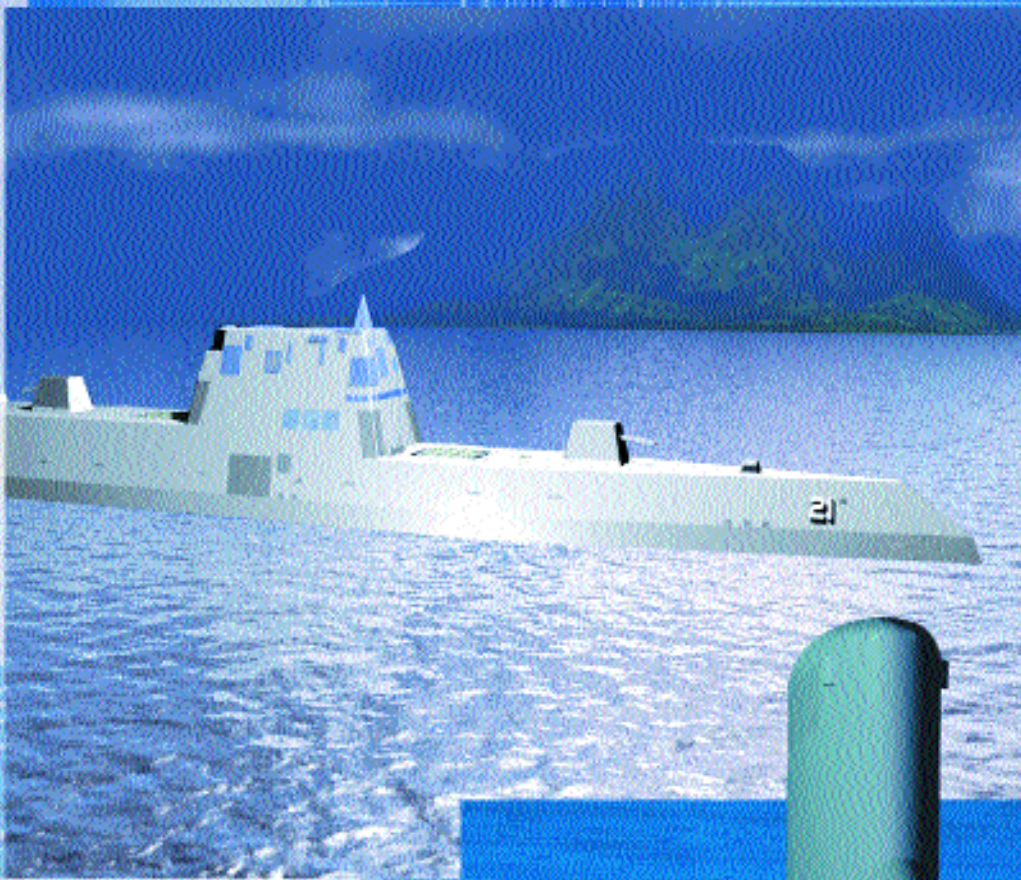
Another threat that military forces must plan for is the growing use of asymmetric warfare. For instance, in Kosovo, Serbian forces effectively employed mobility, camouflage, concealment and deception against NATO efforts. Although the Serbian leadership understood that it would not achieve tactical victory, it had hoped to stall allied forces in an effort to gain a political victory. These lessons will not be lost on other enemies both in regional conflicts or in humanitarian efforts involving U.S. forces.





Joint Strike Fighter (JSF):

The JSF is the next-generation strike aircraft weapon system for the U.S. Navy, Air Force, Marines and allies.



The Virginia class submarine (right) is the first U.S. submarine to be designed for battlespace dominance across a broad spectrum of regional and littoral missions as well as open-ocean "blue water" missions.

The DD-21 (above) is a multi-mission destroyer tailored for land attack warfare in addition to performing traditional destroyer missions.

As a result, U.S. military forces will increasingly have to rely on joint land, sea and aerospace forces that use speed, superior technology and surprise to defeat enemies quickly and with minimal U.S. casualties. It will require the Army to move towards more agile and strategic deployable equipment so that it can transport divisions within hours and days rather than weeks and months.

It will also require more high-technology equipment, superior intelligence, unmanned drones for reconnaissance and precision-guided, unitary warheads for the long-range Army Tactical Missile System (ATACMS). L-3 provides the guidance technology for ATACMS.

The U.S. Air Force will have to capitalize on stealth, advanced airborne and spaceborne sensors and highly precise all-weather munitions to engage adversary targets. With these technologies, U.S. and allied forces will be able to strike quickly and the enemy will no longer be able to hide at night or be protected by severe weather conditions or challenging terrain.

One of the platforms under consideration by the U.S. and its allies is the Joint Strike Fighter (JSF), a multi-role strike fighter that is more advanced, lethal and survivable than previous aircraft. L-3 is currently involved in a number of areas in the development of the JSF, including telemetry and instrumentation and the creation of displays and data recorders for this platform.

►► NAVAL SUPERIORITY

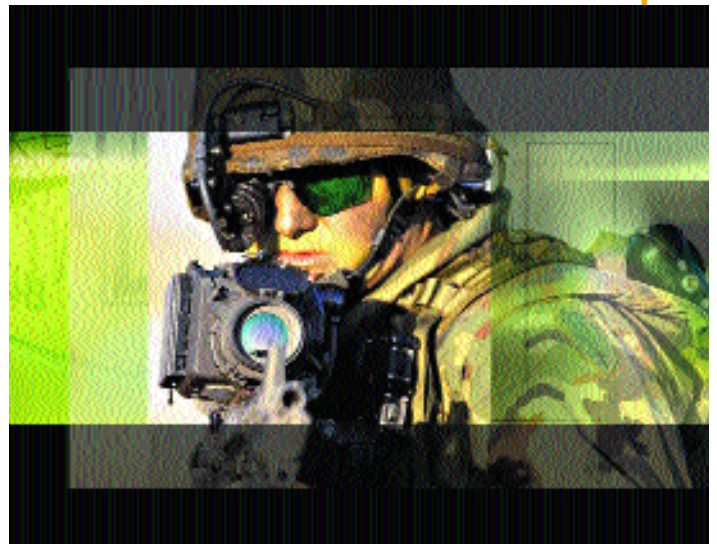
The U.S. Navy needs to maintain a robust forward presence and, in times of war, provide accurate and sustained fire support to ground forces in urban, desert and jungle environments. Ships will need dominant situational awareness of up to 1,000 miles on land as well as above and below the surface.

Communications will be at the heart of the U.S. Navy's new platforms. For the DD-21, L-3 has proposed a next-

generation, multi-function SATCOM terminal to support reconnaissance/surveillance missions, exterior communications as well as radomes.

The Virginia class new attack submarine is designed specifically to fight in the world's shallower coastal regions as well as in open ocean conflicts. The first of the 30 planned submarines will be powered by the quieter and more cost-efficient solid-state systems developed by L-3.

For the carrier fleet, the CVNX will be a large-deck, nuclear-powered ship with an electrical power distribution system that will have significantly improved warfighting capability for a wider range of missions. L-3 will be supplying the power distribution system for this new carrier.



Land Forces: (above)

21st century soldiers will have a plethora of high-technology equipment and superior sensor systems which will allow them to create the future environment that defines success.



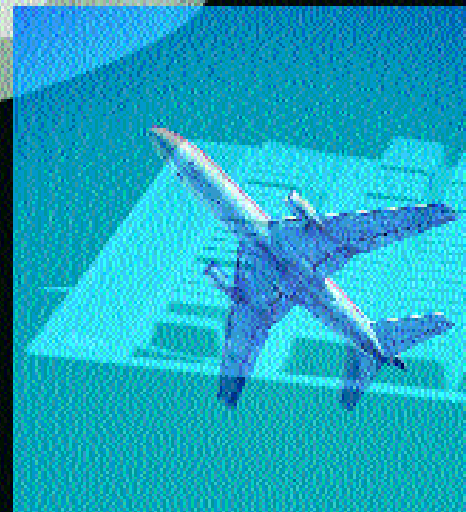
communications



►► TELECOMMUNICATIONS

►► CAPITALIZING ON
COMMERCIAL MARKETS

►► TRANSPORTATION



In 2000, L-3 achieved some significant successes in the commercial markets at a very difficult time for many technology companies. During the year, many Internet companies collapsed and telecommunications ventures struggled because of profitability issues and lack of investment community funding.

L-3 believes it has an advantage over other companies because it mines its products from technologies that have been developed in its defense businesses. The company's military Code Division Multiple Access (CDMA) products, scientific millimeter wave antennas, high-speed modems, baseband technology, radomes, Ka-band receivers, satellite communications, transceivers and spread spectrum technology all came from its defense businesses and have been translated into commercial applications.

The company further limits its risk by partnering with companies that have extensive marketing and distribution operations. In addition, L-3 is better able to weather the ups and downs of the market by balancing those products in immediate demand against those that have future potential. Having such a broad base of products significantly limits the company's exposure at any given time so that there is no material risk to achieving its financial goals.

» TELECOMMUNICATIONS

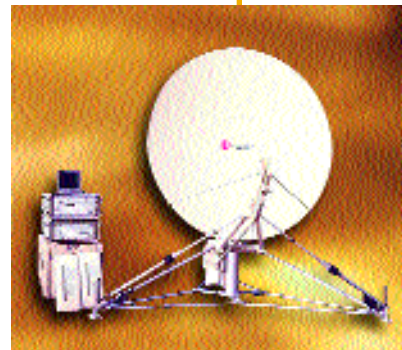
Despite the slowdown in telecommunications, the demand for broadband services showed no sign of abating in 2000 and it will grow substantially in the next several years. Terrestrial infrastructure will not be able to meet all this demand; space will be needed to supplement all the services that will be required. Clearly, space will increasingly be a viable option as content providers begin to demonstrate their commitment with new products, when next-generation satellites become a reality and as access devices are developed.

In fact, commercial launches are scheduled to increase in 2001 and into the next few years and content providers are beginning to invest in global broadband satellite programs. Liberty Media has invested in Astrolink, America Online is participating in the Hughes Spaceway and the AOL-TimeWarner merger is expected to result in a number of new applications. These developments should expand L-3's space business into areas such as commercial launch services, navigation, VSAT and services, including U.S. and international satellite TV, Internet, radio and telephony and satellite broadband.

For the space market, L-3 is participating in major ventures, featuring its uplinks/downlinks, antennas, satellite navigation, satellite payloads, satellite communications terminals, FlyAway Satellite Terminals, guidance and control products and converters. L-3 is providing terminals to United Pan-European Communications N.V. (UPC), which offers programming to European networks and a full suite of software products to Inmarsat, which provides voice and data communications services for a number of markets.

L-3 is also creating a satellite-based global infrastructure network for Core Software Technology, which is providing web distribution of images, audio, video and text for government, commercial and private customers.

In the area of telemetry, L-3 provides Telemetry, Tracking and Control (TT&C), including satellite operations centers, ground terminals and mission control centers. The company has supplied a ground control segment for the EarthWatch Quickbird, a high-resolution global commercial imaging



FlyAway Satellite Terminal:

L-3's FlyAway terminal will enable ISPs, traditional telecommunications providers, commercial and government users quick deployment of high speed satellite applications.

satellite collecting panchromatic and multi-spectral images over a broad area. For the Hughes ICO and 702 satellites, L-3 is supplying real-time payload monitoring and control of communications satellite payloads. L-3 is also providing telemetry ground systems to Mitsubishi Electric Corporation for strategic satellite ground station upgrades around the world.

There are many other space ventures on the horizon. Two major ones are SkyBridge, offering wireless Internet and phone service for small business and residential users and EuroSkyWay, providing bandwidth on demand to telecommunications companies, TV broadcasters and Internet Service Providers. L-3's plan is to select the most promising of these ventures and, in some cases, make a small investment in them and provide a considerable amount of product. This is a win-win for L-3 because it enables the company to sell its products, and as an added plus, potentially profit from its investments.

As Ka-band satellite technology becomes a commercial reality, it will open up a significant market for instrumentation that will replace the existing technology. L-3's Celerity Systems has developed a cost-effective product line that was successfully beta-tested and is being introduced in the first quarter of 2001. Industry analysts predict that this is a multi-billion-dollar market, since manufacturers will have to upgrade their facilities.

Ka-band satellites will also require equipment that provides Point-to-Multipoint equipment for high-speed Internet access, real-time multimedia file transfer, and remote access to corporate local area networks and interactive video. L-3 has developed transceivers and subscriber units for companies offering Local Multipoint Distribution Services (LMDS).

In addition to space products, there are some other niche markets that L-3 is focused on for growth opportunities. Many international areas without wireline infrastructure are demanding Internet capability and L-3 has a cost-

effective solution for these niche markets worldwide. L-3 had a major win for its spread spectrum technology with the contract to supply voice, Internet, leased-line and pay phone services in South America. In addition, L-3 developed Prime Wave™ fixed wireless access for countries and regional areas that do not have sufficient telecommunications infrastructure.

Finally, L-3 has taken its encryption technology and pioneered Privatel™. This small, portable device is being sold to individuals and businesses that want the strongest encryption and security technology in the industry to ensure the privacy of their phone conversations. Privatel™ enables users to speak securely from virtually any telephone in the world.

►► TRANSPORTATION

Another market area for L-3's commercial growth is transportation. It is clear that the number of passengers on the nation's airlines, trains and cruise and ferry ships has risen significantly in the past several years as economic prosperity has increased business, commuter and leisure travel. It is also clear that the nation's infrastructure is straining over this increased usage, which is prompting the need to modernize, and in some cases, meet new safety regulations. Because most of L-3's products have been used to upgrade military air, sea, space and ground platforms, they are particularly suited for the commercial market.

A case in point is the aviation recorder market. It is commonly noted in the industry that this technology has been instrumental in detecting aircraft problems, enabling regulatory agencies to recommend improvements that have been proven to save lives. In fact, these agencies have instituted a number of expanded requirements that will take hold in the next several years for upgraded systems.



Antenna Systems:

Antenna systems manufactured by EMP Systems support many applications including remote sensing satellite data acquisition, airborne vehicle telemetry and flight termination.



Commercial Transportation:

L-3's commercial transportation products include explosive detection systems, hardened voyage recorders, power propulsion systems, power switches, displays and controls for locomotive and transit industries, event recorders for rail transportation, power switches for Internet Service Providers, aviation recorders and collision avoidance systems.

L-3 has already anticipated and developed products for these new requirements. They include the demand for systems with ten minutes of independent power for recording whenever primary aircraft electrical systems cease to operate and the requirement for new and existing aircraft to have recorders with enough capacity to record rudder and aileron positions.

L-3's state-of-the-art solid-state recorders have no moving parts and utilize flash-memory chips to digitize flight and cockpit information that is then stored in a crash-survivable unit. The recorder is covered by a layer of armor that can withstand a crushing impact, extreme temperatures and other crash-related hazards that could jeopardize the stored data. No L-3 Communications solid-state recorder has ever failed to survive a crash.

The commuter train and maritime ship industries have opened up new markets for L-3 to take its existing technology and adapt it to their particular needs. L-3 is supplying solid-state propulsion control systems to the commuter rail industry and event recorders to train manufacturers in addition to companies producing cruise ships and ferries. In 2000, Samsung Heavy Industries Co., Ltd. gave L-3 a contract to supply its Hardened Voyage Recorders (HVRs) for new production ships, with the opportunity to provide these systems for ship retrofit or modernization projects.

The acquisition of Honeywell's Traffic Alert and Collision Avoidance System (TCAS) business gave L-3 the industry's premier collision avoidance product. It also enabled L-3 to initiate the creation of a joint venture with Thales Avionics U.S., a subsidiary of the European market leader Thales, which has a substantial marketing and support organization to sell TCAS to the global commercial air transport market.

The TCAS segment of the aviation industry is one of the fastest growing in all of aviation. There are many areas of growth for this technology as more airlines install TCAS systems to meet upcoming mandates by international govern-

ments and airspace regulatory agencies. Thousands of commercial air transport, regional, corporate, rotary wing, general aviation and military aircraft will put this technology to good use by avoiding possible in-air collisions. Industry forecasters predict that there will be approximately 12,000 aircraft installing a commercial TCAS system in the next five years. That constitutes a billion-dollar market opportunity.

In addition, there is much opportunity to upgrade the technology for the substantial installed base that L-3 has with flight management and eventual total situational awareness of airspace. Also, there is growth in integrating this technology into satellite communications.

Both U.S. and international governments are stepping up their efforts to ensure greater airline security by installing explosive detection systems in airports to monitor checked baggage. L-3 was the first to certify its eXaminer 3DX™ 6000 and then went on in 2000 to sell a number of systems internationally and to the FAA.

Because of its success, L-3 was funded by the FAA to develop the ARGUS version of the eXaminer for broader deployment applications. The addition of the ARGUS and the 3DX™ 3000, which was certified in 2001, gives L-3 a full product suite for all airports.

The threat of power disruption has the capacity to do great damage to the nation's flow of business information and electronic commerce over the Internet. L-3 has decades of experience in ensuring power delivery in its military platforms and has adapted that fail-safe technology to the commercial world. Many Internet providers, web-based businesses and government agencies that depend on the constant flow of power to deliver their services are using L-3's power transfer switches.



EDS:

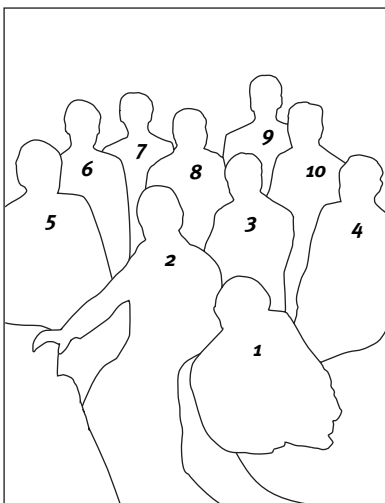
L-3's eXaminer 3DX™ 3000 explosive detection system, designed for smaller and regional airports, will use advanced CT scan technology to generate 3D images of checked baggage.





communications

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Board of Directors:

- 1 Frank C. Lanza**
Chairman and Chief Executive Officer
- 2 Robert V. LaPenta**
President and Chief Financial Officer
- 3 Robert B. Millard**
- 4 General (Ret.) John M. Shalikashvili**
- 5 Alan H. Washkowitz**
- 6 David J. Brand**
- 7 John E. Montague**
- 8 Arthur L. Simon**
- 9 Thomas A. Corcoran**
- 10 Alberto M. Finali**

SELECTED FINANCIAL DATA

The selected consolidated financial data presented below have been derived from our audited consolidated financial statements for the respective periods and should be read together with our “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our audited consolidated financial statements included elsewhere herein.

(in millions except per share data)	Company				Predecessor Company	
	Year Ended December 31,			Nine Months Ended	Three Months Ended	Year Ended
	2000 ⁽¹⁾	1999 ⁽¹⁾	1998 ⁽¹⁾	Dec 31, 1997 ⁽²⁾	Mar 31, 1997	Dec 31, 1996 ⁽³⁾
Statement of Operations Data:						
Sales	\$ 1,910.1	\$1,405.5	\$1,037.0	\$546.5	\$158.9	\$543.1
Operating income	222.7	150.5	100.3	51.5 ⁽⁴⁾	7.9	43.7
Interest expense, net of interest and other income	88.6	55.1	46.9	28.5	8.4	24.2
Provision (benefit) for income taxes	51.4	36.7	20.9	10.7	(0.2)	7.8
Net income (loss)	82.7	58.7	32.6	12.3 ⁽⁴⁾	(0.3)	11.7
Earnings per common share:						
Basic	\$ 2.48	\$ 1.83	\$ 1.32	\$ 0.62 ⁽⁴⁾		
Diluted	2.37	1.75	1.26	0.61 ⁽⁴⁾		
Weighted average common shares outstanding:						
Basic	33.4	32.1	24.7	20.0		
Diluted	35.0	33.5	25.9	20.0		
Balance Sheet Data (at period end):						
Working capital	\$ 360.9	\$ 255.5	\$ 157.8	\$ 143.2		\$ 98.8
Total assets	2,463.5	1,628.7	1,285.4	697.0		590.6
Long-term debt	1,095.0	605.0	605.0	392.0		
Invested equity						473.6
Shareholders’ equity	692.6	583.2	300.0	113.7		

(1) The results of operations are impacted significantly by our acquisitions described elsewhere herein.

(2) Reflects the acquisition of our predecessor company and the commencement of our operations effective April 1, 1997.

(3) Reflects our predecessor company’s ownership of nine business units acquired by Lockheed Martin from Loral Corporation effective April 1, 1996. Prior to April 1, 1996, the predecessor company was comprised only of one business unit.

(4) Includes a nonrecurring, noncash compensation charge of \$4.4 million (\$0.22 per share) related to our initial capitalization, which we recorded effective April 1, 1997.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITIONS

OVERVIEW

L-3 is a leading merchant supplier of sophisticated secure communication systems and specialized communication products. These systems and products are critical elements of virtually all major communication, command and control, intelligence gathering and space systems. Our customers include the U.S. Department of Defense ("DoD"), certain U.S. Government intelligence agencies, major aerospace and defense contractors, foreign governments and commercial customers. We have two reportable segments: Secure Communication Systems and Specialized Communication Products.

Our Secure Communication Systems segment provides secure, high data rate communications systems for military and other U.S. Government reconnaissance and surveillance applications. The Secure Communication Systems segment also produces advanced simulation and training products, and provides communication software support services and a full range of teaching, training, logistic and training device support services to domestic and international customers. Our Specialized Communication Products segment includes three product categories: avionics and ocean products, telemetry, instrumentation and space products and microwave components.

All of our domestic government contracts and sub-contracts are subject to audit and various cost controls, and include standard provisions for termination for the convenience of the U.S. Government. Multiyear U.S. Government contracts and related orders are subject to cancellation if funds for contract performance for any subsequent year become unavailable. Foreign government contracts generally include comparable provisions relating to termination for the convenience of the relevant foreign government.

ACQUISITIONS

In April 1997, we completed our acquisition of the predecessor company, and began operating as L-3. Our predecessor company was comprised of nine business units that Lockheed Martin acquired from Loral Corporation in April 1996 and one business unit purchased by Lockheed Martin as part of its acquisition of the aerospace business of General Electric Company in April 1993.

On February 5, 1998, March 4, 1998 and March 30, 1998 we purchased the assets of the Satellite Transmission Systems division of California Microwave, Inc., ILEX Systems and Ocean Systems business of the former AlliedSignal, Inc. for cash of \$26.1 million, \$54.3 million and \$68.8 million. On August 13, 1998, we purchased all of the outstanding stock of SPD Technologies, Inc. for cash of \$238.3 million. In August 1999, we issued 150,955 shares of our common stock valued at \$6.4 million as additional consideration for the ILEX acquisition based on the 1998 financial performance of ILEX. As of December 31, 2000, we had recorded a liability of \$17.7 million for shares of our common stock expected to be issued in 2001 as additional consideration for the ILEX acquisition based on the financial performance of ILEX in 1999 and 2000. There is no other remaining contingent consideration for the ILEX acquisition.

On January 8, 1999, we acquired all of the outstanding common stock of Microdyne Corporation for \$94.2 million in cash including expenses. On April 16, 1999, we acquired all of the outstanding common stock of Aydin Corporation for \$75.7 million in cash including expenses. On June 30, 1999, we acquired all of the outstanding common stock of Interstate Electronics Corporation from Scott Technologies Inc. for \$40.7 million in cash including expenses. On December 31, 1999, we completed our acquisition of the assets of Space and Navigation Systems from Honeywell Inc., for \$55.0 million in cash plus expenses, subject to adjustment.

On February 10, 2000, we acquired the assets of the Training Devices and Training Services (“TDTS”) business of the Raytheon Company for \$160.0 million in cash, plus expenses, subject to adjustment. Following the acquisition we changed TDTS’s name to L-3 Communications Link Simulation and Training. On February 14, 2000, we acquired the assets of Trex Communications Corporation for \$50.0 million in cash including expenses.

On April 28, 2000, we acquired the Traffic Alert and Collision Avoidance System (“TCAS”) product line from Honeywell for a purchase price of \$239.6 million in cash including expenses. In anticipation of the TCAS acquisition, on February 25, 2000, we entered into a Memorandum of Agreement with Thomson-CSF Sextant S.A., a subsidiary of Thomson-CSF, under which the parties agreed to create a limited liability corporation for TCAS, contribute 100% of the TCAS assets to be acquired from Honeywell to TCAS LLC, and sell a 30% interest in the TCAS LLC to Sextant for a cash purchase price equal to 30% of the final purchase price we paid to Honeywell for TCAS (approximately \$71.7 million). We will consolidate the financial statements of the TCAS LLC. We expect to complete this transaction during the first half of 2001.

On June 30, 2000, we acquired all of the outstanding stock of MPRI, Inc. for \$35.7 million in cash, including expenses, subject to additional consideration not to exceed \$4.0 million based on the financial performance of MPRI for the year ending June 30, 2001.

On July 11, 2000, we acquired 53.5% of the outstanding common stock of LogiMetrics, Inc. (“LogiMetrics”) for a purchase price of \$15.0 million, of which \$8.5 million was paid in cash at closing and the balance was paid in installments that were completed in the first quarter of 2001. We also agreed to invest an additional \$5.0 million in cash during 2001 for additional common stock.

On December 29, 2000, we acquired all of the outstanding common stock of Coleman Research Corporation (“Coleman”), a subsidiary of Thermo Electron Corporation for \$60.0 million in cash plus expenses, subject to adjustment and additional consideration not to exceed \$5.0 million based on the financial performance of Coleman for the year ending December 31, 2001.

Additionally, during 1998, 1999 and 2000 we purchased several other operations and product lines, which individually and in the aggregate were not material to our results of operations or financial position.

All of our acquisitions have been accounted for as purchase business combinations and are included in our results of operations from their respective effective dates.

We regularly evaluate potential acquisitions and joint venture transactions, but we have not entered into any agreements with respect to any material transactions at this time.

RESULTS OF OPERATIONS

The following information should be read in conjunction with our consolidated financial statements. Our results of operations for the periods presented are impacted significantly by our acquisitions. The table below provides selected income statement data for the years ended December 31, 2000, 1999 and 1998.

SEGMENT OPERATING DATA

(in millions)	Year Ended December 31,		
	2000	1999	1998
Sales⁽¹⁾:			
Secure Communication Systems	\$ 847.1	\$ 542.9	\$ 483.5
Specialized Communication Products	1,063.0	862.6	553.5
Total	\$1,910.1	\$1,405.5	\$1,037.0
Operating income:			
Secure Communication Systems	\$ 91.3	\$ 47.0	\$ 39.9
Specialized Communication Products	131.4	103.5	60.4
Operating income	\$ 222.7	\$ 150.5	\$ 100.3
Depreciation and amortization expenses included in operating income:			
Secure Communication Systems	\$ 26.4	\$ 18.4	\$ 17.3
Specialized Communication Products	47.9	35.3	23.1
Total	\$ 74.3	\$ 53.7	\$ 40.4
EBITDA⁽²⁾			
Secure Communication Systems	\$ 117.7	\$ 65.4	\$ 57.2
Specialized Communication Products	179.3	138.8	83.5
Total	\$ 297.0	\$ 204.2	\$ 140.7

(1) Sales are after intersegment eliminations. See Note 16 to the consolidated financial statements.

(2) EBITDA is defined as operating income plus depreciation expense and amortization expense (excluding the amortization of debt issuance costs). EBITDA is not a substitute for operating income, net income or cash flows from operating activities as determined in accordance with generally accepted accounting principles as a measure of profitability or liquidity. We present EBITDA as additional information because we believe it to be a useful indicator of our ability to meet debt service and capital expenditure requirements. EBITDA as we defined it may differ from similarly named measures used by other entities.

Year Ended December 31, 2000 Compared With Year Ended December 31, 1999. Sales increased \$504.6 million to \$1,910.1 million in 2000. Sales grew \$304.2 million in the Secure Communication Systems segment and \$200.4 million in the Specialized Communication Systems segment. Operating income increased \$72.2 million to \$222.7 million in 2000. Operating income as a percentage of sales (“operating margin”) improved to 11.7% from 10.7%. Depreciation and amortization expenses increased \$20.6 million to \$74.3 million in 2000, reflecting increased goodwill amortization associated with our acquisitions and additional depreciation related to our capital expenditures and acquired businesses. Our EBITDA for 2000 increased \$92.8 million to \$297.0 million. EBITDA as a percentage of sales (“EBITDA margin”) increased to 15.5% in 2000 from 14.5% in 1999. Basic earnings per share (“EPS”) grew 35.5% to \$2.48 in 2000 and diluted EPS grew 35.4% to \$2.37 in 2000. Basic weighted-average common shares outstanding increased 3.9% in 2000, and diluted weighted-average common shares outstanding increased 4.3% in 2000, primarily because of common stock issued for exercises of employee stock options.

Sales of our Secure Communication Systems segment increased \$304.2 million to \$847.1 million in 2000. Operating income increased \$44.3 million in 2000. Operating margin improved to 10.8% from 8.7%. We attribute the increase in sales principally to the acquisitions of Link Training and Simulation and MPRI and increased sales of secure telephone equipment (“STE”), wideband secure data link programs, communication software support services and airport security equipment. The increase in operating margin was principally attributable to improved margin on military communication systems and high data rate communications systems. These margin improvements arose from cost reductions and improved operating efficiencies. Additionally, during 2000 a larger percentage of our sales were generated from fixed-price contracts which generally have higher margins than sales generated from cost-plus contracts. EBITDA increased \$52.3 million to \$117.7 million in 2000 and EBITDA margin improved to 13.9% from 12.0% in 1999. We expect operating margins for our Secure Communications Systems segment in 2001 to remain relatively unchanged from those in 2000 and we do not expect a significant change in our mix of fixed-price and cost-plus contracts from that in 2000.

Sales within our Specialized Communication Products segment increased \$200.4 million to \$1,063.0 million in 2000. Operating income increased \$27.9 million in 2000. Operating margin improved to 12.4% from 12.0%. We attribute this increase in sales principally to the acquisitions of TCAS and Space and Navigation Systems and volume increases on airborne dipping sonar systems, aviation recorders, and display products. These increases in sales were partially offset by decreased shipments of naval power systems in 2000 compared with 1999, principally due to the slippage of certain sales into 2001 which were previously anticipated to occur in 2000. Sales of our telemetry products were essentially unchanged in 2000 compared with 1999 due to continued softness in the space and broadband commercial communications markets. We attribute our increase in operating margin principally to improved margins on avionics and ocean products. These margin improvements arose from sales volume increases, costs reductions and the higher margins from the TCAS business. Lower margins on our naval power systems due to less shipments and on our telemetry products and microwave components due to changes in product sales mix partially offset these operating margin improvements. EBITDA increased \$40.5 million to \$179.3 million in 2000 and EBITDA margin improved to 16.9% from 16.1% in 1999.

Interest expense increased \$32.4 million to \$93.0 million in 2000 principally because of the higher average outstanding debt during 2000. Interest and other income decreased \$1.1 million to \$4.4 million. Interest and other income for 2000 includes gains of \$14.9 million from the sales of our interests in certain businesses. These gains were largely offset by losses of \$12.4 million on the write-down in the carrying value of certain investments and intangible assets. The net gain contributed \$0.04 to our 2000 diluted EPS. Excluding the net gain, diluted EPS was \$2.33, an increase of 33.1% in 2000 compared with 1999. The income tax provision for 2000 reflects our effective income tax rate for 2000 of 38.3% compared with the effective tax rate of 38.5% for 1999.

Year Ended December 31, 1999 Compared with Year Ended December 31, 1998. Sales increased \$368.5 million to \$1,405.5 million in 1999. Sales in the Secure Communication Systems segment grew \$59.4 million and sales in the Specialized Communication Products segment grew \$309.1 million in 1999. Operating income increased \$50.2 million to \$150.5 million in 1999. Operating margin improved to 10.7% from 9.7%. Depreciation and amortization expenses increased \$13.3 million to \$53.7 million in 1999, reflecting increased goodwill amortization associated with our acquisitions and additional depreciation related to our capital expenditures and acquired businesses. Our EBITDA for 1999 increased \$63.5 million to \$204.2 million. EBITDA margin improved to 14.5% in 1999 from 13.6% in 1998. Basic earnings per common share grew 38.6% to \$1.83 in 1999 and diluted earnings per share grew 38.9% to \$1.75 in 1999. Basic weighted-average common shares outstanding increased 30.1% in 1999 and diluted weighted-average common shares outstanding increased 29.4% in 1999, principally because of the timing of the issuance of 5.0 million shares of common stock in connection with our February 1999 stock offering.

Sales within our Secure Communication Systems segment increased \$59.4 million to \$542.9 million in 1999. Operating income increased \$7.1 million to \$47.0 million in 1999. Operating margin improved to 8.7% from 8.3%. We attribute this increase in sales to greater sales on the U-2 Support Program, STE and airport security systems and our acquisition of Microdyne. Declines in sales on secure wide-band data link programs, communication subsystems for the ISS (International Space Station) and LMD/KP (Local Management Device/Key Processor) units which occurred from the scheduled phasedown of these programs partially offset our sales gains. We attribute the improvement in operating margin to military communication systems and high data rate communication systems. These margin improvements arose from cost reductions and operating efficiencies and sales volume increases on STE, and were partially offset by lower margins from our Microdyne acquired businesses and costs incurred for network security systems. EBITDA increased \$8.2 million to \$65.4 million in 1999 and EBITDA margin improved to 12.0% from 11.8% in 1998.

Sales within our Specialized Communication Products segment increased \$309.1 million to \$862.6 million in 1999. Operating income increased \$43.1 million to \$103.5 million in 1999, and operating margin increased to 12.0% from 10.9%. The increase in sales was principally attributable to the timing of our Aydin and IEC acquisitions in 1999 and the SPD and Ocean Systems acquisitions in 1998, as well as volume increases on ocean products, primarily for power distribution, control and conversion systems, aviation recorders and space and satellite control products. Lower volume on microwave components and decreased shipments of displays and antenna products partially offset our sales gains. We attribute the increase in operating margin to higher margins on ocean products and aviation recorders caused by volume increases and cost reductions, higher margins from the SPD business and improved margins in 1999 for the STS business acquired in February 1998. Lower operating margins from the Aydin and IEC businesses and lower margins due to declines in sales on microwave components and antenna products partially offset our operating margin improvements. EBITDA increased \$55.3 million to \$138.8 million in 1999, and EBITDA margin increased to 16.1% from 15.1% in 1998.

Interest expense increased \$11.0 million to \$60.6 million in 1999 because of the higher average outstanding debt during 1999 compared with 1998 principally because of the \$200.0 million of senior subordinated notes that we sold in December 1998. Interest and other income for 1999 included \$0.4 million for a gain on the sale of a business. The income tax provision for 1999 reflects our effective income tax rate for 1999 of 38.5%, compared with the effective tax rate of 39.1% for 1998.

LIQUIDITY AND CAPITAL RESOURCES

Balance Sheet

During 2000, contracts in process increased \$221.0 million to \$700.1 million at December 31, 2000. The increase included \$154.6 million related to acquired businesses, and the remaining increase of \$66.4 million was principally from:

- increases in unbilled contract receivables principally arising from an increase in programs in production phases, during which unbilled costs and profits generally exceed progress payments and advances received from the customers until contract shipments are completed; and

- increases in inventories for production on certain programs and products.

The increases in deferred tax assets, property, plant and equipment, intangibles, accrued employment costs, accrued expenses, other current liabilities and other liabilities during 2000 were principally related to acquired businesses. The increase in accounts payable was principally related to balances of acquired businesses and the timing of payments to vendors. The increase in other current liabilities was principally due to increases in estimated costs in excess of billings to complete contracts in process including the U.S. Army Aviation Combined Arms Tactical Trainer (“AVCATT”) contract that were assumed as part of the TDTS acquisition. The increase in accrued interest was attributable to higher outstanding debt balances and the timing of interest payments.

STATEMENT OF CASH FLOWS

The table below presents selected cash flow data.

(in millions)	Year Ended December 31,		
	2000	1999	1998
Net cash from operating activities	\$ 113.8	\$ 99.0	\$ 85.1
Net cash (used in) investing activities	\$(608.2)	\$(284.8)	\$(472.9)
Net cash from financing activities	\$ 484.3	\$ 202.4	\$ 336.4

OPERATING ACTIVITIES

During 2000, we generated \$113.8 million of cash from our operating activities, an increase of \$14.8 million from the \$99.0 million generated during 1999. Earnings adjusted for non-cash items and deferred taxes increased \$48.5 million to \$200.3 million in 2000 from \$151.8 million in 1999. During 2000 our working capital and operating assets and liabilities increased \$86.5 million compared with an increase of \$52.8 million in 1999. Our cash flows from operating activities during 2000 include uses of cash relating to performance on certain contracts in process including the AVCATT contract that were assumed in the TDTS acquisition for which the estimated costs exceed the estimated billings to complete these contracts. We expect to continue to experience negative impacts on our cash flows as a result of the completion of these TDTS acquired contracts in process during 2001, but to a lesser extent than in 2000. Additionally, we expect our working capital to increase during the first half of 2001 in connection with certain commercial programs and products.

During 1999, we generated \$99.0 million in cash from operating activities, an increase of \$13.9 million over 1998. Earnings adjusted for non-cash items and deferred taxes increased \$55.6 million to \$151.8 million in 1999 from \$96.2 million in 1998. During 1999 our working capital and other operating assets and liabilities increased \$52.8 million compared with an increase of \$11.1 million in 1998. The increase was principally related to the greater working capital requirements primarily for contracts in process.

INVESTING ACTIVITIES

We continued to pursue our acquisition strategy during 2000 and invested \$599.6 million to acquire businesses, compared with \$272.2 million in 1999. We used \$448.0 million in 1998 to acquire businesses.

We make capital expenditures for improvement of manufacturing facilities and equipment. We expect that our capital expenditures for the year ending December 31, 2001 will be between \$40.0 million and \$45.0 million, compared with \$33.6 million for the year ended December 31, 2000. The anticipated increase is principally due to capital expenditures for our acquired businesses. Dispositions of property, plant and equipment for 2000 includes net proceeds of \$13.3 million related to a facility located in Hauppauge, NY which we sold and leased back in December 2000.

In 2000, we sold our interests in two businesses for net cash proceeds of \$19.6 million, which are included in other investing activities.

FINANCING ACTIVITIES

At December 31, 2000, available revolver borrowings under our senior credit facilities were \$400.9 million after reductions for outstanding borrowings of \$190.0 million used principally to finance acquisitions and outstanding letters of credit of \$109.1 million. At December 31, 1999, there were no borrowings outstanding under our senior credit facilities.

On April 28, 2000 we entered into a new 364-day revolving senior credit facility for \$300.0 million that expires on April 27, 2001, which increased our senior credit facilities

to \$700.0 million. On April 28, 2000 we borrowed \$237.0 million under the facility to finance the TCAS acquisition. These borrowings were repaid in November 2000 with a portion of the proceeds from our offering of the convertible senior subordinated notes which are described below. At December 31, 2000, there were no borrowings outstanding under this credit facility. Additionally, on April 28, 2000 we amended all of the senior credit facilities to change the spreads used to calculate the interest rates on borrowings and commitment fees on the unused commitments under the senior credit facilities. The spreads are the same for all senior credit facilities, and the lenders all rank pari passu under our senior credit facilities.

In August 2000, the other outstanding revolving 364-day credit facility for \$200.0 million that was scheduled to expire was renewed for an additional 364 days and will expire on August 9, 2001. At that time, we may extend the term, with the consent of our lenders, for a period of 364 days and we also may exercise an option to convert 80% of the borrowings outstanding into term loans which fully amortize over an eighteen month period beginning September 30, 2001.

During the first half of 2001, we intend to restructure our \$300.0 million 364-day revolving credit facility that expires April 27, 2001 together with all of our senior credit facilities to extend their maturities.

In the fourth quarter of 2000 we sold \$300.0 million of 5.25% Convertible Senior Subordinated Notes due 2009 (the "Convertible Notes") in a private placement. The net proceeds from this offering amounted to \$290.5 million after debt issuance costs, and were used to repay revolver borrowings outstanding under our senior credit facilities. The Convertible Notes may be converted at any time into our common stock at a conversion price of \$81.50 per share. The Convertible Notes are jointly and severally guaranteed (the "Guarantees") by certain existing and future direct and indirect domestic subsidiaries. The Guarantees are subordinated in right of payment to all of our existing and future

senior debt and rank pari passu with our other senior subordinated debt, which is described below.

Pursuant to a registration rights agreement that we entered into with the initial purchaser of the Convertible Notes, we agreed to file a registration statement with the Securities and Exchange Commission ("SEC") by April 5, 2001, which is 135 days after the original issuance of the notes to cover resales by holders of the Convertible Notes and Guarantees, and our common stock issuable upon conversion of the notes. If we do not file the registration statement with the SEC on or before April 5, 2001, liquidated damages, in the form of additional interest, will accrue on the Convertible Notes from April 5, 2001 to but excluding the day on which the registration statement is filed. In no event will liquidated damages exceed 0.50% per annum of the principal amount outstanding under the notes. We expect to file the registration statement with the SEC by the end of March 2001.

On February 4, 1999, we sold 5.0 million shares of our common stock in a public offering for \$42.00 per share which generated net proceeds of \$201.6 million. In addition, as part of the same transaction 6.5 million shares of our common stock were sold by Lehman Brothers Capital Partners III, L.P. and its affiliates ("the Lehman Partnership") and Lockheed Martin in a secondary public offering. In October 1999, Lockheed Martin sold its remaining shares of our common stock. In December 1999, the Lehman Partnership distributed to its partners approximately 3.8 million shares of our common stock. On December 31, 2000 the Lehman Partnership owned approximately 16.4% of our outstanding common stock.

In April 1997, May 1998 and December 1998, we sold \$225.0 million of 10 3/8% Senior Subordinated Notes due 2007, \$180.0 million of 8 1/2% Senior Subordinated Notes due 2008, and \$200.0 million of 8% Senior Subordinated Notes due 2008 (collectively, the "Senior Subordinated Notes"), whose aggregate net proceeds amounted to \$576.0 million, after debt issuance costs.

The senior credit facilities, Senior Subordinated Notes and Convertible Notes contain financial covenants which remain in effect so long as we owe any amount or any commitment to lend exists thereunder. As of December 31, 2000, we have been in compliance with the covenants of the agreements governing our debt at all times. The borrowings under the senior credit facilities are guaranteed by us and by substantially all of our direct and indirect domestic subsidiaries. The payments of principal and premium, if any, and interest on the Senior Subordinated Notes are unconditionally guaranteed, on an unsecured senior subordinated basis, jointly and severally, by us and substantially all of our direct and indirect wholly owned subsidiaries. See Note 7 to our consolidated financial statements for a description of our debt and related financial covenants at December 31, 2000.

Based upon our current level of operations, we believe that our cash from operating activities, together with available borrowings under the senior credit facilities, will be adequate to meet our anticipated requirements for working capital, capital expenditures, research and development expenditures, program and other discretionary investments, and interest payments for the foreseeable future, including at least the next three years. There can be no assurance, however, that our business will continue to generate cash flow at current levels, or that currently anticipated improvements will be achieved. If we are unable to generate sufficient cash flow from operations to service our debt, we may be required to sell assets, reduce capital expenditures, refinance all or a portion of our existing debt or obtain additional financing. Our ability to make scheduled principal payments or to pay interest on or to refinance our indebtedness depends on our future performance and financial results, which, to a certain extent, are subject to general conditions in or affecting the defense industry and to general economic, political, financial, competitive, legislative and regulatory factors beyond our control. There can be no assurance that sufficient funds will be available to enable us to service our indebtedness, to make necessary capital expenditures and to make discretionary investments.

MARKET RISKS

All of our financial instruments that are sensitive to market risk are entered into for purposes other than trading.

Interest Rate Risk. Our financial instruments that are sensitive to changes in interest rates include borrowings under the senior credit facilities, purchased interest rate cap contracts and written interest rate floor contracts, all of which are denominated in U.S. dollars. The weighted average interest rate on our borrowings outstanding under the senior credit facilities at December 31, 2000 was 8.5%. The interest rates on the Senior Subordinated Notes and Convertible Notes are fixed-rate and are not affected by changes in interest rates.

To mitigate risks associated with changing interest rates on borrowings under the senior credit facilities that bear interest at variable rates we entered into interest rate cap and floor contracts. The interest rate cap contract provides protection against increases in interest rates on borrowings to the extent:

- those borrowings are less than or equal to the notional amount of the cap contract; and
- the interest rate paid on the borrowings rises above the sum of the cap reference rate plus our applicable borrowing spread.

However, the written interest rate floor limits our ability to enjoy decreases in interest rates on our borrowings to the extent:

- those borrowings are less than or equal to the notional amount of the floor contract; and
- the interest rate paid on those borrowings falls below the sum of the floor reference rate plus our applicable borrowing spread.

We attempt to manage exposure to counterparty credit risk by entering into interest rate agreements only with major financial institutions that are expected to perform fully under the terms of such agreements. Cash payments between us and the counterparties are made at the end of each quarter. Such payments are recorded as adjustments to interest expense and were not material to our interest expense or cash flows for 2000, 1999 or 1998. Additional data on our debt obligations, the borrowing spreads included in the inter-

est rates we pay on our borrowings under the senior credit facilities and interest rate agreements are provided in Notes 7 and 8 to our consolidated financial statements.

For the interest rate agreements, the table below presents significant contract terms and fair values on December 31, 2000.

(in millions)	Caps	Floors
Notional amount	\$100.0	\$50.0
Cap/floor interest rate	7.5%	5.5%
Reference rate	3 month LIBOR	3 month LIBOR
Designated maturity	Quarterly	Quarterly
Expiration date	March 28, 2002	March 28, 2002
Fair value	—	\$(0.1)

Foreign Currency Exchange Risk. We conduct some of our operations outside the U.S. in functional currencies other than the U.S. dollar. Additionally, some of our U.S. operations have contracts with foreign customers denominated in foreign currencies. To mitigate the risk associated with certain of these contracts denominated in foreign currency we have entered into foreign currency forward contracts. At December 31, 2000, the notional value of foreign currency forward contracts was \$6.9 million and the fair value of these contracts was \$0.4 million. We account for these contracts as hedges.

Equity Price Risk. Our investments in common equities are subject to equity price risk. Both the carrying values and estimated fair values of such instruments amounted to \$9.0 million at the end of 2000.

There were no significant changes in our market risks during 2000.

BACKLOG AND ORDERS

We define funded backlog as the value of contract awards received from the U.S. Government, which the U.S. Government has appropriated funds, plus the value of contract awards and orders received from customers other than the U.S. Government which have yet to be recognized as sales. Our funded backlog as of December 31, 2000 was \$1,354.0 million and as of December 31, 1999 was \$1,003.7 million. We expect to record as sales approximately 72% of our December 31, 2000 funded backlog during 2001. However, there can be no assurance that our backlog will become sales in any particular period, if at all. Our funded orders were \$2,013.7 million for 2000, \$1,423.1 million for 1999 and \$1,057.0 million for 1998.

Our funded backlog does not include the full value of our contract awards including those pertaining to multi-year, cost-plus reimbursable contracts, which are generally funded on an annual basis. Funded backlog also excludes the sales value of unexercised contract options that may be exercised by customers under existing contracts and the sales value of purchase orders that may be issued under indefinite quantity contracts or basic ordering agreements.

RESEARCH AND DEVELOPMENT

Company-sponsored research and development costs, including bid and proposal costs were \$101.9 million for 2000, \$76.1 million for 1999 and \$59.9 million for 1998. Customer-funded research and development costs were \$299.3 million for 2000, \$226.3 million for 1999 and \$181.4 million for 1998.

CONTINGENCIES

We are engaged in providing products and services under contracts with the U.S. Government and to a lesser degree, under foreign government contracts, some of which are funded by the U.S. Government. All such contracts are subject to extensive legal and regulatory requirements, and, periodically, agencies of the U.S. Government investigate whether such contracts were and are being conducted in accordance with these requirements. Under government procurement regulations, an indictment by a federal grand jury could result in the suspension for a period of time from eligibility for awards of new government contracts. A conviction could result in debarment from contracting with the federal government for a specified term. Additionally, in the event that U.S. Government expenditures for products and services of the type we manufacture and provide are reduced, and not offset by greater commercial sales or other new programs or products, or acquisitions, there may be a reduction in the volume of contracts or subcontracts awarded to us.

We continually assess our obligations with respect to applicable environmental protection laws. While it is difficult to determine the timing and ultimate cost to be incurred in order to comply with these laws, based upon available internal and external assessments, with respect to those environmental loss contingencies of which we are aware, we believe that

even without considering potential insurance recoveries, if any, there are no environmental loss contingencies that, individually or in the aggregate, would be material to our consolidated results of operations. Also, we have been periodically subject to litigation, claims or assessments and various contingent liabilities incidental to our business. We accrue for these contingencies when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated.

With respect to those investigative actions, items of litigation, claims or assessments of which we are aware, we are of the opinion that the probability is remote that, after taking into account certain provisions that have been made with respect to these matters, the ultimate resolution of any such investigative actions, items of litigation, claims or assessments will have a material adverse effect on our consolidated financial position or results of operations.

On December 27, 2000, we filed a complaint against Raytheon and Raytheon Technical Services Company in the Court of Chancery for the State of Delaware in and for New Castle County, alleging that Raytheon failed to disclose material liabilities in connection with the sale of TDTS to us in February 2000. Specifically, the complaint alleges that Raytheon misrepresented the financial liabilities associated with the AVCATT contract which will cause us to incur damages of approximately \$100 million. We assumed the AVCATT contract as part of our acquisition of TDTS from Raytheon which was completed in February 2000. The complaint seeks rescission of the TDTS Asset Purchase and Sale Agreement and, alternatively, rescission of the AVCATT contract, rescissory damages and breach of contract.

RECENTLY ISSUED ACCOUNTING STANDARDS

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* ("SFAS 133"), which establishes accounting and reporting standards for derivative instruments including certain deriva-

tive instruments embedded in other contracts and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value and is effective for all quarters of fiscal years beginning after June 15, 2000. We do not expect SFAS 133 to have a material impact on our consolidated results of operations or financial position.

In September 2000, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* ("SFAS 140"), which replaces SFAS 125. SFAS 140 revises the standards for accounting for securitizations and other transfers of financial assets and collateral and requires certain disclosures, but it carries over most of SFAS 125's provisions without reconsideration. SFAS 140 is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001. We do not expect SFAS 140 to have a material impact on our consolidated results of operations or financial position.

In March 2000, the Financial Accounting Standards Board issued Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation – An Interpretation of APB Opinion No. 25* ("FIN 44"). FIN 44 clarifies the definition of an employee for purposes of calculating stock-based compensation, the criteria for determining whether a plan qualifies as a noncompensatory plan, the accounting consequence of various modifications to the terms of previously fixed stock options or awards, and the accounting for an exchange of stock compensation awards in a business combination. FIN 44 is primarily effective July 1, 2000, with some provisions effective earlier. We have adopted the accounting and disclosures required by FIN 44 for all periods presented.

INFLATION

The effect of inflation on our sales and earnings has not been significant. Although a majority of our sales are made under long-term contracts, the selling prices of such contracts, established for deliveries in the future, generally reflect estimated costs to be incurred in these future periods. In addition, some contracts provide for price adjustments through escalation clauses.

FORWARD-LOOKING STATEMENTS

Certain of the matters discussed concerning our operations, cash flows, financial position, economic performance, and financial condition, including in particular, the likelihood of our success in developing and expanding our business and the realization of sales from backlog, include forward-looking statements within the meaning of section 27A of the Securities Act and Section 21E of the Exchange Act.

Statements that are predictive in nature, that depend upon or refer to events or conditions or that include words such as “expects,” “anticipates,” “intends,” “plans,” “believes,” “estimates” and similar expressions are forward-looking statements. Although we believe that these statements are based upon reasonable assumptions, including projections of orders, sales, operating margins, earnings, cash flow, research and development costs, working capital, capital expenditures and other projections, they are subject to several risks and uncertainties, and therefore, we can give no assurance that these statements will be achieved.

Our forward-looking statements will also be influenced by factors such as:

- our dependence on the defense industry and the business risks peculiar to that industry including changing priorities or reductions in the U.S. Government defense budget;
- our reliance on contracts with a limited number of agencies of, or contractors to, the U.S. Government and the possibility of termination of government contracts by unilateral government action or for failure to perform;
- the ability to obtain or the timing of obtaining future government contracts;
- the availability of government funding and customer requirements;

- economic conditions, competitive environment, international business and political conditions, timing of international awards and contracts;
- our extensive use of fixed price contracts as compared to cost plus contracts;
- our ability to identify future acquisition candidates or to integrate acquired operations;
- the rapid change of technology in the communication equipment industry;
- the high level of competition in the communications equipment industry;
- our introduction of new products into commercial markets or our investments in commercial products or companies;
- the significant amount of our debt and the restrictions contained in our debt agreements;
- collective bargaining agreements and labor disputes; and
- pension, environmental or legal matters or proceedings and various other market, competition and industry factors, many of which are beyond our control.

Readers of this document are cautioned that our forward-looking statements are not guarantees of future performance and the actual results or developments may differ materially from the expectations expressed in the forward-looking statements.

As for the forward-looking statements that relate to future financial results and other projections, actual results will be different due to the inherent uncertainties of estimates, forecasts and projections and may be better or worse than projected. Given these uncertainties, you should not place any reliance on these forward-looking statements. These forward-looking statements also represent our estimates and assumptions only as of the date that they were made. We expressly disclaim a duty to provide updates to these forward-looking statements, and the estimates and assumptions associated with them, after the date of this filing to reflect events or changes or circumstances or changes in expectations or the occurrence of anticipated events.

CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)	December 31,	
	2000	1999
Assets		
Current assets:		
Cash and cash equivalents	\$ 32,680	\$ 42,788
Contracts in process	700,133	479,143
Deferred income taxes	89,732	32,985
Other current assets	7,025	7,761
Total current assets	829,570	562,677
Property, plant and equipment, net	156,128	140,971
Intangibles, primarily goodwill	1,371,368	821,552
Deferred income taxes	57,111	56,858
Other assets	49,367	46,683
Total assets	\$2,463,544	\$1,628,741
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable, trade	\$ 159,901	\$ 98,693
Accrued employment costs	102,606	70,618
Accrued expenses	55,576	29,030
Customer advances	55,203	56,738
Accrued interest	16,335	12,683
Income taxes	7,251	2,715
Other current liabilities	71,797	36,680
Total current liabilities	468,669	307,157
Pension and postretirement benefits	105,523	110,262
Other liabilities	101,783	23,147
Long-term debt	1,095,000	605,000
Commitments and contingencies		
Shareholders' equity:		
Common stock \$.01 par value; authorized 100,000,000 shares, issued and outstanding 33,606,645 and 32,794,547 shares	515,926	483,694
Retained earnings	186,272	103,545
Unearned compensation	(2,457)	(1,661)
Accumulated other comprehensive loss	(7,172)	(2,403)
Total shareholders' equity	692,569	583,175
Total liabilities and shareholders' equity	\$2,463,544	\$1,628,741

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)	Year Ended December 31,		
	2000	1999	1998
Sales	\$1,910,061	\$1,405,462	\$1,037,045
Costs and expenses	1,687,343	1,254,976	936,696
Operating income	222,718	150,486	100,349
Interest and other income	4,393	5,534	2,659
Interest expense	93,032	60,590	49,558
Income before income taxes	134,079	95,430	53,450
Provision for income taxes	51,352	36,741	20,899
Net income	\$ 82,727	\$ 58,689	\$ 32,551
Earnings per common share:			
Basic	\$ 2.48	\$ 1.83	\$ 1.32
Diluted	\$ 2.37	\$ 1.75	\$ 1.26
Weighted average common shares outstanding:			
Basic	33,355	32,107	24,679
Diluted	34,953	33,516	25,900

See notes to consolidated financial statements.

L-3 Communications

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

For the Years Ended December 31, 2000, 1999 and 1998

(in thousands)	Common Stock Shares Issued	Par Value	Additional Paid-in Capital	Retained Earnings	Unearned Compensation	Accumulated Other Comprehensive Income (Loss)	Total
Balance December 31, 1997	17,056	\$171	\$101,191	\$ 12,305	\$ —	\$ —	\$ 113,667
Comprehensive income:							
Net income				32,551			32,551
Minimum pension liability adjustment, net of tax						(9,514)	(9,514)
Foreign currency translation adjustment						(137)	(137)
							22,900
Shares issued:							
Sale of common stock	6,900	69	139,431				139,500
Employee benefit plans	22	—	967				967
Exercise of stock options	480	5	3,887				3,892
Conversion of common stock subject to repurchase agreement	2,944	29	19,019				19,048
Balance December 31, 1998	27,402	\$274	\$264,495	\$ 44,856	\$ —	\$(9,651)	\$299,974
Comprehensive income:							
Net income				58,689			58,689
Minimum pension liability adjustment, net of tax						9,443	9,443
Unrealized loss on securities, net of tax						(970)	(970)
Foreign currency translation adjustment						(1,225)	(1,225)
							65,937
Shares issued:							
Sale of common stock	5,000	50	201,763				201,813
Employee benefit plans	163	2	6,991				6,993
Acquisition consideration	151	2	6,432				6,434
Exercise of stock options	79		1,764				1,764
Grant of restricted stock			1,921		(1,921)		—
Amortization of unearned compensation					260		260
Balance December 31, 1999	32,795	\$328	\$483,366	\$103,545	\$ (1,661)	\$(2,403)	\$ 583,175
Comprehensive income:							
Net income				82,727			82,727
Minimum pension liability adjustment, net of tax						(819)	(819)
Unrealized loss on securities, net of tax						(2,728)	(2,728)
Foreign currency translation adjustment						(1,222)	(1,222)
							77,958
Shares issued:							
Employee benefit plans	235	2	12,640				12,642
Exercise of stock options	577	6	18,056				18,062
Grant of restricted stock			1,512		(1,512)		—
Amortization of unearned compensation					716		716
Other			16				16
Balance December 31, 2000	33,607	\$336	\$515,590	\$186,272	\$(2,457)	\$(7,172)	\$692,569

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)	Year Ended December 31,		
	2000	1999	1998
Operating activities:			
Net income	\$ 82,727	\$ 58,689	\$ 32,551
Goodwill amortization	35,327	20,970	13,966
Depreciation and other amortization	38,927	32,748	26,389
Amortization of deferred debt issue costs	5,724	3,904	2,564
Deferred income tax provision	25,103	28,831	19,786
Other noncash items	12,517	6,617	967
Changes in operating assets and liabilities, net of amounts acquired:			
Contracts in process	(66,402)	(61,670)	(23,807)
Other current assets	(2,599)	(70)	48
Other assets	(416)	552	(376)
Accounts payable	38,065	2,896	23,480
Accrued employment costs	6,239	2,052	8,653
Accrued expenses	2,274	(6,280)	(90)
Customer advances	(17,087)	5,766	(12,132)
Accrued interest	3,637	5,985	2,279
Income taxes	13,161	3,917	331
Other current liabilities	(59,286)	(13,554)	(12,281)
Pension and postretirement benefits	(7,214)	1,788	18
Other liabilities	1,959	7,102	2,873
All other operating activities	1,149	(1,225)	(137)
Net cash from operating activities	113,805	99,018	85,082
Investing activities:			
Acquisition of businesses, net of cash acquired	(599,608)	(272,195)	(447,988)
Proceeds from net assets held for sale	—	—	6,653
Capital expenditures	(33,580)	(23,456)	(23,429)
Disposition of property, plant and equipment	18,060	6,713	970
Other investing activities	6,905	4,136	(9,069)
Net cash (used in) investing activities	(608,223)	(284,802)	(472,863)
Financing activities:			
Repayment of borrowings under term loan facilities	—	—	(172,000)
Borrowings under revolving credit facility	858,500	74,700	367,000
Repayment of borrowings under revolving credit facility	(668,500)	(74,700)	(367,000)
Proceeds from sale of senior subordinated notes	—	—	380,000
Proceeds from sale of convertible senior subordinated notes	300,000	—	—
Proceeds from sale of common stock, net	—	201,582	139,500
Debt issuance costs	(12,916)	(323)	(14,173)
Proceeds from exercise of stock options	8,954	658	3,110
Other financing activities	(1,728)	525	—
Net cash from financing activities	484,310	202,442	336,437
Net increase (decrease) in cash	(10,108)	16,658	(51,344)
Cash and cash equivalents, beginning of period	42,788	26,130	77,474
Cash and cash equivalents, end of period	\$ 32,680	\$ 42,788	\$ 26,130

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

1. DESCRIPTION OF BUSINESS

L-3 Communications Holdings, Inc. (“L-3 Holdings”) and subsidiaries (“L-3” or “the Company”), including its wholly owned subsidiary L-3 Communications Corporation (“L-3 Communications”) is a merchant supplier of sophisticated secure communication systems and specialized communication products. The Company produces secure, high data rate communication systems, training and simulation systems, avionics and ocean products, telemetry, instrumentation and space products and microwave components. These systems and products are critical elements of virtually all major communication, command and control, intelligence gathering and space systems. The Company’s systems and specialized products are used to connect a variety of airborne, space, ground- and sea-based communication systems and are used in the transmission, processing, recording, monitoring and dissemination functions of these communication systems. The Company’s customers include the U.S. Department of Defense (“DoD,”), certain U.S. Government intelligence agencies, major aerospace and defense contractors, foreign governments, commercial customers and certain other U.S. Government agencies. The Company has two reportable segments, Secure Communication Systems and Specialized Communication Products.

Secure Communication Systems. This segment provides secure, high data rate communications systems for military and other U.S. Government reconnaissance and surveillance applications. The major secure communication programs and systems include:

- secure data links for airborne, satellite, ground- and sea-based remote platforms for real time information collection and dissemination to users;
- strategic and tactical signal intelligence systems that detect, collect, identify, analyze and disseminate information;
- secure telephone and network equipment and encryption management;
- communication software support services; and

- communication systems for surface and undersea vessels and manned space flights.

The Secure Communication Systems segment includes the training and simulation business, which produces advanced simulation and training products, with high-fidelity representations of cockpits and operator stations for aircraft and vehicle system simulation. This segment also provides a full range of teaching, training, logistic and training device support services to domestic and international military customers, and ballistic targets for the DoD.

Specialized Communication Products. This segment supplies products to military and commercial customers, and focuses on niche markets in which the Company believes it can achieve a market leadership position. This reportable segment includes three product categories:

- avionics and ocean products including aviation recorders, airborne collision avoidance products, displays, antennas, acoustic undersea warfare products and naval power distribution, conditioning, switching and protection equipment;
- telemetry, instrumentation and space products including commercial off-the-shelf, real-time data collection and transmission products and components for missile, aircraft and space-based electronic systems; and
- microwave components including commercial off-the-shelf, high-performance microwave components and frequency monitoring equipment.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation: The consolidated financial statements of the Company include all wholly owned and significant majority-owned subsidiaries. Investments over which the Company has significant influence but does not have voting control are accounted for by the equity method.

Cash and Cash Equivalents: Cash equivalents consist of highly liquid investments with a maturity of three months or less at time of purchase.

Revenue Recognition: Sales on production-type contracts which are within the scope of the American Institute of Certified Public Accountants Statement of Position 81-1

Accounting for Performance of Construction-Type and Certain Production-Type Contracts (“SOP 81-1”) are recorded as units are shipped and profits applicable to such shipments are recorded pro rata based upon estimated total profit at completion of the contract. Sales and profits on cost reimbursable contracts which are within the scope of SOP 81-1 are recognized as costs are incurred. Sales and estimated profits under other long-term contracts which are within the scope of SOP 81-1 are recognized under the percentage of completion method of accounting using the cost-to-cost method. Amounts representing contract change orders or claims are included in sales only when they can be reliably estimated and their realization is reasonably assured. Losses on contracts are recognized when determined. The impact of revisions in profit estimates are recognized on a cumulative catch-up basis in the period in which the revisions are made. Sales which are not within the scope of SOP 81-1 are recognized in accordance with the Securities and Exchange Commission’s Staff Accounting Bulletin No. 101.

Contracts in Process: Costs accumulated on contracts in process include direct costs and manufacturing overhead costs, and for U.S. Government contracts and contracts with prime contractors or subcontractors of the U.S. Government, general and administrative costs, independent research and development costs and bid and proposal costs. Contracts in process contain amounts relating to contracts and programs with long performance cycles, a portion of which may not be realized within one year. Unbilled contract receivables represent accumulated recoverable costs and earned profits on contracts in process that have been recorded as sales, but have not yet been billed to customers. Inventoried contract costs represent recoverable costs incurred on contracts in process. Inventories other than inventoried contract costs are stated at the lower of cost or market primarily using the average cost method. Under the contractual arrangements on certain contracts with the U.S. Government, the Company receives progress payments as it incurs costs. The U.S. Government has a security interest in the unbilled contract receivables and inventoried contract costs to which progress payments have been applied, and such progress payments are reflected as an offset against the related unbilled contract receivables and inventoried contract costs. Other customer advances are classified as current liabilities.

Property, Plant and Equipment: Property, plant and equipment are stated at cost. Depreciation is computed by applying principally the straight-line method to the estimated useful lives of the related assets. Useful lives range substantially from 10 to 40 years for buildings and improvements and 3 to 10 years for machinery, equipment, furniture and fixtures. Leasehold improvements are amortized over the shorter of the lease term or the estimated useful life of the improvements.

Debt Issuance Costs: Costs incurred to issue debt are deferred and amortized as interest expense over the term of the related debt using a method that approximates the effective interest method.

Intangibles: Intangibles consist primarily of the excess of the purchase cost of acquired businesses over the fair value of net assets acquired (“goodwill”) and are amortized on a straight-line basis over periods ranging from 15 to 40 years. Accumulated goodwill amortization was \$76,001 at December 31, 2000 and \$40,147 at December 31, 1999. The carrying amount of goodwill is evaluated on a recurring basis. Current and estimated future profitability and undiscounted cash flows excluding financing costs of the acquired businesses are the primary indicators used to assess the recoverability of goodwill. For the years ended December 31, 2000 and 1999, there were no material adjustments to the carrying amounts of goodwill resulting from these evaluations.

Income Taxes: The Company provides for income taxes using the liability method prescribed by the Financial Accounting Standards Board (“FASB”) Statement of Financial Accounting Standards (“SFAS”) No. 109, *Accounting for Income Taxes*. Under the liability method, deferred income tax assets and liabilities reflect tax carryforwards and the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting and income tax purposes, as determined under enacted tax laws and rates. The effect of changes in tax laws or rates is accounted for in the period of enactment.

Research and Development: Research and development costs sponsored by the Company include bid and proposal costs related to government products and services. These costs generally are allocated among all contracts in progress under U.S. Government contractual arrangements. Customer-funded research and development costs incurred pursuant to contracts are accounted for as direct contract costs.

Stock Options: In accordance with Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (“APB 25”) and related interpretations, compensation expense for stock options is recognized in income based on the excess, if any, of L-3 Holdings’ fair value of the stock at the grant date of the award or other measurement date over the amount an employee must pay to acquire the stock. When the exercise price for stock options granted to employees equals or exceeds the fair value of the L-3 Holdings common stock at the date of grant, the Company does not recognize compensation expense. The Company has adopted the disclosure only provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of sales and costs and expenses during the reporting period. The most significant of these estimates and assumptions relate to contract estimates of sales and costs, estimated costs in excess of billings to complete contracts in process, estimates of pension and postretirement benefit obligations, recoverability of recorded amounts of fixed assets and goodwill, income taxes, litigation and environmental obligations. Actual results could differ from these estimates.

Recently Issued Accounting Standards: In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* (“SFAS 133”), which establishes accounting and reporting standards for derivative instruments including certain derivative instruments embedded in other contracts and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value and is effective for all quarters of fiscal years beginning after June 15, 2000. The Company does not expect SFAS 133 to have a material impact on its consolidated results of operations or financial position.

In September 2000, the Financial Accounting Standards Board issued Statement of Financial Accounting

Standards No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* (“SFAS 140”), which replaces SFAS 125. SFAS 140 revises the standards for accounting for securitizations and other transfers of financial assets and collateral and requires certain disclosures, but it carries over most of SFAS 125’s provisions without reconsideration. SFAS 140 is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001. The Company does not expect SFAS 140 to have a material impact on its consolidated results of operations or financial position.

In March 2000, the Financial Accounting Standards Board issued Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation – An Interpretation of APB Opinion No. 25* (“FIN 44”). FIN 44 clarifies the definition of an employee for purposes of calculating stock-based compensation, the criteria for determining whether a plan qualifies as a noncompensatory plan, the accounting consequence of various modifications to the terms of previously fixed stock options or awards, and the accounting for an exchange of stock compensation awards in a business combination. FIN 44 is primarily effective July 1, 2000, with some provisions effective earlier. The Company adopted the accounting and disclosures required by FIN 44 for all periods presented.

Reclassifications: Certain reclassifications have been made to conform prior-year amounts to the current-year presentation.

3. ACQUISITIONS AND DIVESTITURES

On January 8, 1999, the Company acquired all of the outstanding common stock of Microdyne Corporation (“Microdyne”) for \$94,228 in cash including expenses and the repayment of assumed debt, net of cash acquired. On April 16, 1999, the Company acquired all of the outstanding common stock of Aydin Corporation (“Aydin”) for \$60,034 in cash, including expenses, net of cash acquired. On June 30, 1999, the Company acquired all the outstanding common stock of Interstate Electronics Corporation (“IEC”) from Scott Technologies Inc. for \$40,610 in cash including expenses. On December 31, 1999, the Company acquired the assets of the Space and Navigation Systems business (“SNS”) of Honeywell International Inc. (“Honeywell”) for \$55,000 in cash, plus expenses, subject to adjustment based on closing date net assets, as defined.

On February 10, 2000, the Company acquired the assets of the Training Devices and Training Services (“TDTS”) business of Raytheon Company for \$160,000 in cash plus expenses, subject to adjustment based on closing date net working capital, as defined. Following the acquisition, the Company changed TDTS’s name to L-3 Communications Link Simulation and Training (“Link Simulation and Training”).

On February 14, 2000, the Company acquired the assets of Trex Communications Corporation (“TrexCom”) for \$50,210 in cash, plus expenses, subject to adjustment based on closing date net worth, as defined.

On April 28, 2000, the Company acquired the Traffic Alert and Collision Avoidance System (“TCAS”) product line from Honeywell for a purchase price of \$239,594 in cash, including expenses. In anticipation of the TCAS acquisition, on February 25, 2000, the Company entered into a Memorandum of Agreement with Thomson-CSF Sextant S.A. (“Sextant”), a subsidiary of Thomson-CSF, under which L-3 agreed to create a limited liability corporation for TCAS, contribute 100% of the TCAS assets to be acquired from Honeywell to the TCAS LLC, and sell a 30% interest in the TCAS LLC to Sextant for a cash purchase price equal to 30% of the final purchase price paid to Honeywell for TCAS (which is expected to be approximately \$71,738). L-3 will consolidate the financial statements of the TCAS LLC. The Company expects to complete this transaction during the first half of 2001.

On June 30, 2000, the Company acquired all the outstanding stock of MPRI, Inc. (“MPRI”) for \$35,686 in cash including expenses subject to additional consideration not to exceed \$4,000 based on the financial performance of MPRI for the year ending July 30, 2001.

On July 11, 2000, the Company acquired 53.5% of the outstanding common stock of LogiMetrics, Inc. (“LogiMetrics”) for \$15,000, of which \$8,500 of the purchase price was paid in cash at closing, and the balance was paid in installments that were completed in the first quarter of 2001. The Company also agreed to invest an additional \$5,000 in cash during 2001 for additional common stock.

On December 29, 2000, the Company acquired all of the outstanding common stock of Coleman Research Corporation (“Coleman”), a subsidiary of Thermo Electron Corporation for \$60,000 in cash, subject to adjustment based on closing date net working capital, and additional considera-

tion not to exceed \$5,000 based on the financial performance of Coleman for the year ending December 31, 2001.

All of the acquisitions were financed with cash on hand or borrowings on bank credit facilities.

All of the Company’s acquisitions have been accounted for as purchase business combinations and are included in the Company’s results of operations from their respective effective dates. The assets and liabilities recorded in connection with the acquisitions of SNS, TDTS, TrexCom, TCAS and Logimetrics were \$763,845 and \$247, 943. The assets and liabilities recorded in connection with the purchase price allocations for the acquisitions of MPRI and Coleman are based upon preliminary estimates of fair values for contracts in process, estimated costs in excess of billings to complete contracts in process, inventories, and deferred taxes. Actual adjustments will be based on the final purchase prices and final appraisals and other analyses of fair values which are in process. The Company has valued acquired contracts in process at contract price, less the estimated costs to complete and an allowance for normal profit on the Company’s effort to complete such contracts. The preliminary assets and liabilities recorded in connection with the acquisitions of MPRI and Coleman were \$118,611 and \$22,855. The Company does not expect the differences between the preliminary and final purchase price allocations for the acquisitions to be material. Goodwill is amortized on a straight-line basis over periods of 40 years for SNS, TDTS, TCAS, Coleman and MPRI and 20 years for LogiMetrics and TrexCom.

Had the acquisitions of TDTS, TCAS and Coleman and the related financing transactions occurred on January 1, 2000, the unaudited pro forma sales, net income and diluted earnings per share for the year ended December 31, 2000 would have been \$2,072,300, \$80,000 and \$2.29. Had the acquisitions of Microdyne, Aydin, IEC, SNS, TDTS, TCAS and Coleman and related financing transactions occurred on January 1, 1999, the unaudited pro forma sales, net income and diluted earnings per share for the year ended December 31, 1999 would have been \$2,058,900, \$43,200 and \$1.29. The pro forma results are based on various assumptions and are not necessarily indicative of the result of operations that would have occurred had the acquisitions and the related financing transactions occurred on January 1, 1999 and 2000.

Interest and other income for the year ended December 31, 2000 includes gains of \$14,940 from the sales of our interest in certain businesses. These gains were largely offset by losses of \$12,456 on the write-down in the carrying value of certain investments and intangible assets. The net proceeds from the sales were \$19,638, and are included in Other Investing Activities on the Statement of Cash Flows.

4. CONTRACTS IN PROCESS

The components of contracts in process are presented in the table below. The unbilled contract receivables, inventoried contract costs and unliquidated progress payments are principally related to contracts with the U.S. Government and prime contractors or subcontractors of the U.S. Government.

	December 31,	
	2000	1999
Billed receivables	\$319,780	\$258,054
Unbilled contract receivables, gross	279,474	123,969
Less: unliquidated progress payments	(52,153)	(10,351)
Unbilled contract receivables, net	227,321	113,618
Inventoried contract costs, gross	72,504	65,967
Less: unliquidated progress payments	(23,061)	(19,273)
Inventoried contract costs, net	49,443	46,694
Inventories at lower of cost or market	103,589	60,777
Total contracts in process	\$700,133	\$479,143

The Company believes that approximately \$203,000 of the unbilled contract receivables at December 31, 2000 will be billed and collected within one year.

The selling, general and administrative ("SG&A") cost data presented in the table below have been used in the determination of the costs and expenses presented on the statements of operations.

	Year Ended Dec 31		
	2000	1999	1998
SG&A costs included in			
inventoried contract costs	\$ 24,396	\$ 23,637	\$ 16,550
SG&A incurred costs	350,561	265,136	189,507
Independent research and development, including bid and proposal costs included in SG&A incurred costs	101,883	76,134	59,897

5. OTHER CURRENT LIABILITIES AND OTHER LIABILITIES

At December 31, 2000, other current liabilities includes \$31,737 of estimated costs in excess of billings to complete contracts in process principally related to contracts assumed as part of the TDTS business that was acquired from Raytheon in February 2000, including the U.S. Army Aviation Combined Arms Tactical Trainer ("AVCATT") contract. At December 31, 2000, other liabilities includes \$59,641 for the non-current portion of estimated costs in excess of billings to complete contracts in process, principally for the AVCATT contract. At December 31, 1999, other current liabilities did not include any items in excess of 5% of total current liabilities. At December 31, 2000 and 1999, other liabilities did not include any items in excess of 5% of total liabilities.

6. PROPERTY, PLANT AND EQUIPMENT

	December 31,	
	2000	1999
Land	\$ 11,242	\$ 9,658
Buildings and improvements	25,942	30,071
Machinery, equipment, furniture and fixtures	178,603	137,665
Leasehold improvements	23,852	14,015
Gross property, plant and equipment	239,639	191,409
Less: accumulated depreciation and amortization	83,511	50,438
Property, plant and equipment, net	\$156,128	\$140,971

Depreciation and amortization expense for property, plant and equipment was \$36,158 for 2000, \$29,554 for 1999, and \$22,463 for 1998.

7. DEBT

The components of long-term debt are presented in the table below.

	December 31,	
	2000	1999
Borrowings under Senior Credit Facilities	\$ 190,000	\$ —
10 ³ / ₈ % Senior Subordinated Notes due 2007	225,000	225,000
8 ¹ / ₂ % Senior Subordinated Notes due 2008	180,000	180,000
8% Senior Subordinated Notes due 2008	200,000	200,000
5.25% Convertible Senior Subordinated Notes due 2009	300,000	—
Total long-term debt	\$1,095,000	\$605,000

The borrowings under the Senior Credit Facilities, 10³/₈% Senior Subordinated Notes due 2007, 8¹/₂% Senior Subordinated Notes due 2008 and 8% Senior Subordinated Notes due 2008 are the indebtedness of L-3 Communications.

The 5.25% Convertible Senior Subordinated Notes due 2009 are the indebtedness of L-3 Holdings. Details on all of the outstanding debt of both L-3 Communications and L-3 Holdings are discussed below.

L-3 Communications has three bank credit facilities that comprise the Senior Credit Facilities and permit borrowings of up to \$700,000, of which \$400,946 is available after reductions for outstanding borrowings of \$190,000 and letters of credit of \$109,054. One facility for \$200,000 expires on March 31, 2003 (the “Revolving Credit Facility”), a second facility for \$200,000 expires August 9, 2001 (the “Revolving 364 Day Facility”), and a third facility for \$300,000 expires on April 27, 2001 (the “New Revolving 364 Day Facility”). A portion of the Revolving 364 Day Facility may be extended, with the consent of the lenders for a period of 364 days following August 9, 2001 and L-3 Communications may convert the outstanding principal amount of any or all of the loans outstanding under the Revolving 364 Day Facility to term loans. In the event that any or all of the outstanding principal amount under the Revolving 364 Day Facility is converted, L-3 Communications would have to repay 20% of the resulting term loans by August 16, 2001. L-3 Communications would have to repay the remaining 80% of the term loans in six consecutive quarterly installments commencing on September 30, 2001. During the first half of 2001, L-3 Communications intends to restructure the Revolving 364 Day Facility together with all of the Senior Credit Facilities to extend their maturities.

Borrowings under the Senior Credit Facilities bear interest, at L-3 Communications’ option, at either: (i) a “base rate” equal to the higher of 0.50% per annum above the latest federal funds rate and the Bank of America “reference rate” (as defined) plus a spread ranging from 1.75% to 0.375% per annum depending on L-3 Communications’ ratio of debt to EBITDA, as defined (the “Debt to EBITDA Ratio”) at the time of determination or (ii) a “LIBOR rate” (as defined) plus a spread ranging from 2.75% to 1.25% per annum depending on L-3 Communications’ Debt to EBITDA Ratio at the time of determination. At December 31, 2000 the weighted average interest rate on the borrowings outstanding under the Senior Credit Facilities was 8.5%. L-3 Communications pays commitment fees calculated on the daily amounts of the available unused commitments under the Senior Credit Facilities at a rate ranging from 0.50% to 0.20% per annum,

depending on L-3 Communications’ Debt to EBITDA Ratio in effect at the time of determination. L-3 Communications pays letter of credit fees calculated at a rate ranging from 1.375% to 0.625% per annum for performance letters of credit and 2.75% to 1.25% for all other letters of credit, in each case depending on L-3 Communications’ Debt to EBITDA Ratio at the time of determination.

In April 1997, L-3 Communications sold \$225,000 of 10³/₈% Senior Subordinated Notes due May 1, 2007 (the “1997 Notes”) with interest payable semi-annually on May 1 and November 1 of each year commencing November 1, 1997. The 1997 Notes are general unsecured obligations of L-3 Communications and are subordinated in right of payment to all existing and future senior debt of L-3 Communications. The 1997 Notes are subject to redemption at any time, at the option of L-3 Communications, in whole or in part, on or after May 1, 2002 at redemption prices (plus accrued and unpaid interest) starting at 105.188% of principal (plus accrued and unpaid interest) during the 12-month period beginning May 1, 2002 and declining annually to 100% of principal (plus accrued and unpaid interest) on May 1, 2005 and thereafter.

In May 1998, L-3 Communications sold \$180,000 of 8¹/₂% Senior Subordinated Notes due May 15, 2008 (the “May 1998 Notes”) with interest payable semi-annually on May 15 and November 15 of each year commencing November 15, 1998. The May 1998 Notes are general unsecured obligations of L-3 Communications and are subordinated in right of payment to all existing and future senior debt of L-3 Communications. The May 1998 Notes are subject to redemption at any time, at the option of L-3 Communications, in whole or in part, on or after May 15, 2003 at redemption prices (plus accrued and unpaid interest) starting at 104.250% of principal (plus accrued and unpaid interest) during the 12-month period beginning May 15, 2003 and declining annually to 100% of principal (plus accrued and unpaid interest) on May 15, 2006 and thereafter. In addition, prior to May 15, 2001, L-3 Communications may redeem up to 35% of the aggregate principal amount of the May 1998 Notes with the net proceeds of one or more equity offerings, at a price equal to 108.500% of the principal (plus accrued and unpaid interest) to the extent such proceeds are contributed (within 120 days of any such offering) to L-3 Communications as common equity, provided that at least

65% of the original aggregate principal amount of the May 1998 Notes remains outstanding thereafter.

In December 1998, L-3 Communications sold \$200,000 of 8% Senior Subordinated Notes due August 1, 2008 (the “December 1998 Notes”) with interest payable semi-annually on February 1 and August 1 of each year commencing February 1, 1999. The December 1998 Notes are general unsecured obligations of L-3 Communications and are subordinated in right of payment to all existing and future senior debt of L-3 Communications. The December 1998 Notes are subject to redemption at any time, at the option of L-3 Communications, in whole or in part, on or after August 1, 2003 at redemption prices (plus accrued and unpaid interest) starting at 104% of principal (plus accrued and unpaid interest) during the 12-month period beginning August 1, 2003 and declining annually to 100% of principal (plus accrued and unpaid interest) on August 1, 2006 and thereafter. In addition, prior to August 1, 2001, L-3 Communications may redeem up to 35% of the aggregate principal amount of December 1998 Notes with the net proceeds of one or more equity offerings, at a price equal to 108% of the principal (plus accrued and unpaid interest) and to the extent such proceeds are contributed (within 120 days of any such offering) to L-3 Communications as common equity, provided that at least 65% of the original aggregate principal amount of the December 1998 Notes remains outstanding.

In the fourth quarter of 2000, L-3 Holdings sold \$300,000 of 5.25% Convertible Senior Subordinated Notes (the “Convertible Notes”) due June 1, 2009 in a private placement. Interest is payable semi-annually on June 1 and December 1 of each year commencing June 1, 2001. The Convertible Notes may be converted at any time into L-3 Holdings common stock at a conversion price of \$81.50 per share. If all the Convertible Notes were converted, an additional 3,680,982 shares of L-3 Holdings common stock would have been outstanding at December 31, 2000. The Convertible Notes are general unsecured obligations of L-3 Holdings and are subordinated in right of payment to all existing and future senior debt of L-3 Holdings and L-3 Communications. The Convertible Notes are subject to redemption at any time, at the option of L-3 Holdings, in whole or in part, on or after December 1, 2003 at redemption

prices (plus accrued and unpaid interest) starting at 102.625% of principal (plus accrued and unpaid interest) during the 12-month period beginning December 1, 2003 and declining annually to 100% of principal (plus accrued and unpaid interest) on December 1, 2005 and thereafter.

Collectively the 1997 Notes, May 1998 Notes, December 1998 Notes comprise the “Senior Subordinated Notes”. The maturities on the Senior Subordinated Notes and Convertible Notes are, \$225,000 in 2007, \$380,000 in 2008 and \$300,000 in 2009.

The Senior Credit Facilities, Senior Subordinated Notes and Convertible Notes agreements contain financial and other restrictive covenants that limit, among other things, the ability of the Company to borrow additional funds, dispose of assets, or pay cash dividends. The Senior Credit Facilities contain the most restrictive financial covenants which require that (i) the Company’s Debt to EBITDA Ratio be less than or equal to 4.50 for the quarter ended December 31, 2000, and that the maximum allowable debt ratio, as defined, thereafter declining over time to less than or equal to 3.25 for the quarters ending September 30, 2002 and thereafter, and (ii) the Company’s interest coverage ratio, as defined, be greater than or equal to 2.50 for the quarter ended December 31, 2000, and that the minimum allowable interest coverage ratio, as defined, thereafter increasing over time to greater than or equal to at least 3.00 for the quarters ending September 30, 2002 and thereafter. For purposes of calculating the financial covenants under the Senior Credit Facilities, the Convertible Notes are considered debt of L-3 Communications. The Senior Credit Facilities also limit the payment of dividends by L-3 Communications to L-3 Holdings except for payment of franchise taxes, fees to maintain L-3 Communications legal existence, interest accrued on the Convertible Notes or to provide for operating costs of up to \$1,000 annually. Under the covenant, L-3 Communications may pay permitted dividends to L-3 Holdings from its excess cash flow, as defined, a cumulative amount of \$5,000, provided that the debt ratio is less than 3.5 to 1 as of the most recent fiscal quarter. As a result, at December 31, 2000, \$5,000 of L-3 Communications net assets were available for payment of dividends to L-3 Holdings. Through December 31, 2000 the Company was in compliance with these covenants at all times.

In connection with the Senior Credit Facilities, the Company has granted the lenders a first priority lien on the stock of L-3 Communications and substantially all of its domestic subsidiaries. The borrowings under the Senior Credit Facilities are guaranteed by L-3 Holdings and by substantially all of the domestic subsidiaries of L-3 Communications. The payment of principal and premium, if any, and interest on the Senior Subordinated Notes is unconditionally guaranteed, on an unsecured senior subordinated basis, jointly and severally, by all of L-3 Communications' restricted subsidiaries other than its foreign subsidiaries. Additionally, the Convertible Notes are jointly and severally guaranteed (the "Guarantees") by certain existing and future domestic subsidiaries of L-3 Holdings, including L-3 Communications (the "Guarantors"). The Guarantees are subordinated in right of payment to all existing and future senior debt of the Guarantors and rank pari passu with the other senior subordinated indebtedness of the Guarantors.

Pursuant to a registration rights agreement that L-3 Holdings entered into with the initial purchaser of the Convertible Notes, L-3 Holdings agreed to file a registration statement with the Securities and Exchange Commission ("SEC") within 135 days after the original issuance of the Convertible Notes to cover resales by holders of the Convertible Notes and the Guarantees and the L-3 Holdings common stock issuable upon conversion of the Convertible Notes. If L-3 Holdings does not file the registration statement with the SEC on or before April 5, 2001, liquidated damages, in the form of additional interest, will accrue on the Convertible Notes from April 5, 2001 to but excluding the day on which the registration statement is filed. In no event will liquidated damages exceed 0.50% per annum of the principal amount outstanding under the Convertible Notes. L-3 Holdings expects to file the registration statement with the SEC by the end of March 2001.

8. FINANCIAL INSTRUMENTS

Fair Value of Financial Instruments. The Company's financial instruments consist primarily of cash and cash equivalents, billed receivables, investments, trade accounts payable, customer advances, Senior Credit Facilities, Senior Subordinated Notes, Convertible Notes, foreign currency forward contracts,

and interest rate cap and interest rate floor contracts. The carrying amounts of cash and cash equivalents, billed receivables, trade accounts payable, Senior Credit Facilities, and customer advances are representative of their respective fair values because of the short-term maturities or expected settlement dates of these instruments. The fair value of the Company's investments are based on quoted market prices, as available, and historical costs which approximate fair value. The Senior Subordinated Notes are registered, unlisted public debt which are traded in the over-the-counter market and their fair values are based on quoted trading activity. The fair value of the Convertible Notes are based on quoted prices for the same or similar issues. The fair value of foreign currency forward contracts were estimated based on exchange rates at December 31, 2000 and 1999. The fair values of the interest rate caps and floor contracts were estimated by discounting expected cash flows using quoted market interest rates. The carrying amounts and estimated fair value of the Company's financial instruments are presented in the table below.

	December 31,			
	2000		1999	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Investments	\$ 8,985	\$ 8,985	\$ 12,068	\$ 12,068
Senior Subordinated Notes	605,000	586,300	605,000	582,000
Convertible Notes	300,000	331,350	—	—
Borrowings under				
Senior Credit Facilities	190,000	190,000	—	—
Interest rate caps	431	2	800	435
Interest rate floor	(74)	104	(137)	49
Foreign currency forward contracts	—	392	—	264

Interest Rate Risk Management. To mitigate risks associated with changing interest rates on borrowings under the Senior Credit Facilities, the Company entered into interest rate caps and interest rate floors (collectively, the "interest rate agreements"). The interest rate agreements are denominated in U.S. dollars and have designated maturities which occur every three months until the interest rate agreements expire in March 2002. Cash payments received from or paid to the counterparties on the interest rate agreements are the difference between the amount that the reference interest rates are greater than or less than the contract rates on the designated maturity dates, multiplied by the notional

amounts underlying the respective interest rate agreements. Cash payments or receipts between the Company and counterparties are recorded as a component of interest expense. The initial cost or receipt of these arrangements are deferred and amortized as a component interest expense over the term of the interest rate agreement. The Company manages exposure to counterparty credit risk by entering into the interest rate agreements only with major financial institutions that are expected to fully perform under the terms of such agreements. The notional amounts are used to measure the volume of these agreements and do not represent exposure to credit loss. The impact of the interest rate agreements was not material to interest expense or cash flows for 2000, 1999 and 1998.

Foreign Currency Exchange Risk Management.

Some of the Company's U.S. operations have contracts with foreign customers which are denominated in foreign currencies. To mitigate the risk associated with certain of these contracts denominated in foreign currency, the Company has entered into foreign currency forward contracts. The Company's activities involving foreign currency forward contracts are designed to hedge the foreign denominated cash paid or received, primarily Euro, Spanish Peseta and Italian Lira. The Company manages exposures to counterparty credit risk by entering into foreign currency forward contracts only with major financial institutions that are expected to fully perform under the term of such contracts. The notional amounts are used to measure the volume of these contracts and do not represent exposure to foreign currency losses.

Information with respect to the interest rate agreements and foreign currency forward contracts is presented in the table below.

	December 31,			
	2000		1999	
	Notional Amount	Unrealized Gains (Losses)	Notional Amount	Unrealized Gains (Losses)
Interest rate caps	\$100,000	\$(429)	\$100,000	\$(365)
Interest rate floor	50,000	(30)	50,000	88
Foreign currency forward contracts	6,863	(392)	7,290	(264)

9. COMMON STOCK

On February 4, 1999, L-3 Holdings sold 5.0 million shares of common stock in a public offering for \$42.00 per share (the "February 1999 Common Stock Offering"); the net proceeds amounted to \$201,582 and were contributed by L-3 Holdings to L-3 Communications. In addition, 6.5 million shares were also sold in the February 1999 Common Stock Offering by the Lehman Partnership and Lockheed Martin. In October 1999, Lockheed Martin sold its remaining interest in L-3 Holdings' common stock. In December 1999, the Lehman Partnership distributed to its partners approximately 3.8 million shares of its common stock of Holdings. At December 31, 2000 the Lehman Partnership owned approximately 16.4% of L-3 Holdings' common stock.

On May 19, 1998, L-3 Holdings sold 6.9 million shares of its common stock in an initial public offering ("IPO"). The net proceeds of the IPO amounted to \$139,500 and were contributed by L-3 Holdings to L-3 Communications. Prior to the IPO, the common stock of L-3 Holdings consisted of three classes: Class A, Class B, and Class C common stock. Immediately prior to the IPO, each authorized share of L-3 Holdings Class A common stock, Class B common stock and Class C common stock was converted into one class of common stock and the authorized L-3 Holdings common stock was increased to 100 million shares.

10. EARNINGS PER SHARE

A reconciliation of basic and diluted earnings per share ("EPS") is presented in the table below.

	Year Ended December 31,		
	2000	1999	1998
Basic:			
Net income	\$82,727	\$58,689	\$32,551
Weighted average common shares outstanding	33,355	32,107	24,679
Basic earnings per share	\$ 2.48	\$1.83	\$1.32
Diluted:			
Net income	\$82,727	\$58,689	\$32,551
Common and potential shares:			
Weighted average common shares outstanding	33,355	32,107	24,679
Assumed exercise of stock options	3,940	3,376	2,824
Assumed purchase of common shares for treasury	(2,342)	(1,967)	(1,603)
Common and potential common shares	34,953	33,516	25,900
Diluted earnings per share	\$ 2.37	\$ 1.75	\$ 1.26

The 3,680,982 shares of L-3 Holdings common stock that are issuable upon conversion of the Convertible Notes were not included in the computation of diluted EPS for the year ended December 31, 2000 because, after the assumed after-tax interest savings, the effect on conversion would have been anti-dilutive.

11. INCOME TAXES

Pretax income of the Company was \$134,079 for 2000, \$95,430 for 1999 and \$53,450 for 1998 substantially all of which was derived from domestic operations. The components of the Company's provision for income taxes are presented in the table below.

	Year Ended December 31,		
	2000	1999	1998
Current income tax provision, primarily federal	\$26,249	\$ 7,910	\$ 1,113
Deferred income tax provision:			
Federal	23,130	27,881	18,203
State and local	1,973	950	1,583
Subtotal	25,103	28,831	19,786
Total provision for income taxes	\$ 51,352	\$36,741	\$20,899

A reconciliation of the statutory federal income tax rate to the effective income tax rate of the Company is presented in the table below.

	Year Ended December 31,		
	2000	1999	1998
Statutory federal income tax rate	35.0%	35.0%	35.0%
State and local income taxes, net of federal income tax benefit	4.4	4.6	4.7
Foreign sales corporation benefit	(2.6)	—	—
Nondeductible goodwill amortization and other expenses	6.8	5.2	4.6
Research and experimentation and other tax credits	(6.1)	(7.1)	(6.8)
Other, net	0.8	0.8	1.6
Effective income tax rate	38.3%	38.5%	39.1%

The provision for income taxes excludes current tax benefits related to the exercise of stock options credited directly to shareholders' equity of \$9,108 for 2000 and \$1,011 for 1999 and \$782 for 1998.

The significant components of the Company's net deferred tax assets and liabilities are presented in the table below.

	December 31,	
	2000	1999
Deferred tax assets:		
Inventoried costs	\$ 14,868	\$ 11,033
Compensation and benefits	10,461	1,873
Pension and postretirement benefits	39,486	31,768
Property, plant and equipment	9,081	17,149
Income recognition on contracts in process	55,942	8,617
Accrued warranty costs	3,349	2,401
Net operating loss carryforwards	9,660	12,749
Tax credit carryforwards	18,444	16,576
Other, net	11,081	4,492
Total deferred tax assets	172,372	106,658
Deferred tax liabilities:		
Goodwill	(18,903)	(9,656)
Other, net	(6,626)	(7,159)
Total deferred tax liabilities	(25,529)	(16,815)
Net deferred tax assets	\$146,843	\$ 89,843

The net deferred tax assets are presented in the table below.

Current deferred tax assets	\$ 89,732	\$32,985
Long-term deferred tax assets	57,111	56,858
Total net deferred tax assets	\$146,843	\$89,843

At December 31, 2000 and 1999 the Company had \$28,104 and \$29,325 of tax carryforwards primarily related to U.S. federal net operating losses, alternative minimum tax credits, research and experimentation tax credits, and various state and local tax credits which primarily will expire, subject to various limitations and restrictions, if unused beginning in 2011. The Company believes that these carryforwards will be available to reduce future income tax liabilities and has recorded these carryforwards as non-current deferred tax assets.

12. STOCK OPTIONS

The Company adopted the 1999 Long Term Performance Plan in April 1999, and adopted the 1997 Option Plan in April 1997. As of December 31, 2000 and 1999, the number of shares authorized for grant of options or awards under these plans was 5,255,815 of L-3 Holdings' common stock. The grants may be awarded to employees of the Company in the form of

non-qualified stock options, incentive stock options, stock appreciation rights, restricted stock or other incentive awards. The price at which options may be granted shall not be less than 100% of the fair market value of L-3 Holdings common stock on the date of grant. In general, options expire after 10 years and are exercisable ratably over a 3 year period. As of December 31, 2000 the Company had 420,395 shares of L-3 Holdings' common stock available for awards under the these plans.

On January 1, 2000 and May 19, 1999, the Company awarded 42,896 and 40,339 shares of restricted stock of L-3 Holdings to employees which vest January 1, 2005 and 2004, respectively.

On April 5, 1999, the Company amended the performance options granted to Mr. Lanza and Mr. LaPenta on April 30, 1997 to purchase at \$6.47, 1,142,857 shares of L-3 Holdings common stock. Such amendment eliminated the performance target acceleration provisions and provided that the unvested portion of the performance options, which aggregated 914,286 options at April 5, 1999, became exercisable as of April 30, 2000. These performance options would have originally vested nine years after the grant date, but would have become exercisable with respect to 25% of the shares subject to such performance options on each of April 30, 1999, 2000, 2001 and 2002, to the extent certain targets for the Company's EBITDA were achieved.

The table below presents the Company's stock option activity.

(in thousands)	Number of Options	Weighted Average Exercise Price
Balance at December 31, 1997	2,971	\$ 6.47
Options granted	425	25.60
Options exercised	(481)	6.47
Options canceled	(37)	8.19
Balance at December 31, 1998	2,878	9.27
Options granted	1,004	39.10
Options exercised	(79)	8.37
Options canceled	(43)	29.99
Balance at December 31, 1999	3,760	17.02
Options granted	656	47.74
Options exercised	(577)	15.52
Options canceled	(221)	39.82
Balance at December 31, 2000	3,618	\$21.42

The table below summarizes information about stock options outstanding at December 31, 2000.

Range of Exercise Prices	Outstanding			Exercisable		
	Number of Options	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number of Options	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price
\$ 6.47	2,006	6.4	\$ 6.47	1,549	6.4	\$ 6.47
\$22.00	179	7.3	\$22.00	109	7.3	\$22.00
\$32.75 - \$39.99	574	8.7	\$37.27	184	8.6	\$36.69
\$40.00 - \$47.00	643	8.6	\$41.51	87	8.0	\$40.50
Over \$47.01	216	9.6	\$58.00	—	—	—
Total	3,618	7.4	\$21.42	1,929	6.7	\$11.77

The weighted average fair values of stock options at their grant date during 2000, 1999 and 1998, where the exercise price equaled the market price (estimated fair value) on the grant date were \$20.19, \$14.60 and \$8.86, respectively. In accordance with APB 25, no compensation expense was recognized. The table below reflects pro forma net income and L-3 Holdings EPS had the Company elected to adopt the fair value approach of SFAS 123.

	Year Ended December 31,		
	2000	1999	1998
Net income:			
As reported	\$82,727	\$58,689	\$32,551
Pro forma	75,064	54,625	31,246
Basic EPS:			
As reported	\$ 2.48	\$ 1.83	\$ 1.32
Pro forma	2.25	1.70	1.27
Diluted EPS:			
As reported	\$ 2.37	\$ 1.75	\$ 1.26
Pro forma	2.15	1.63	1.21

The estimated fair value of options granted was calculated using the Black-Scholes option-pricing valuation model. The weighted average assumptions used in the valuation models are presented in the table below.

	Year Ended December 31,	
	2000	1999
Expected option term	5.0	4.8
Expected volatility	35.8%	31.0%
Expected dividend yield	—	—
Risk-free interest rate	6.4%	4.7%

13. COMMITMENTS AND CONTINGENCIES

The Company leases certain facilities and equipment under agreements expiring at various dates through 2018. At December 31, 2000, future minimum payments under non-cancellable operating leases with initial or remaining terms in excess of one year are presented in the table below.

	Operating Leases		Total
	Real Estate	Equipment	
2001	\$ 26,612	\$2,754	\$ 29,366
2002	24,079	2,107	26,186
2003	19,207	1,111	20,318
2004	16,591	318	16,909
2005	19,812	34	19,846
Thereafter	160,427	—	160,427
Total	\$266,728	\$6,324	\$273,052

Real estate lease commitments have been reduced by minimum sublease rental income of \$15,434 due in the future under noncancellable subleases. Leases covering major items of real estate and equipment contain renewal and or purchase options. Rent expense, net of sublease income was \$34,123 for 2000, \$22,452 for 1999, and \$15,290 for 1998.

On March 30, 1998 and June 30, 1999, the Company entered into two separate real estate lease agreements, as lessee, with unrelated lessors which expire on March 30, 2001 and June 30, 2002, respectively, and are accounted for as operating leases. On or before each lease expiration date, the Company can exercise options under each lease agreement to either renew the lease, purchase the properties for \$12,500 and \$15,500, respectively, or sell the property on behalf of the lessor (the "Sale Option"). If the Company exercises the Sale Option, the Company must pay the lessor a residual guarantee amount of \$10,894 and \$13,524, respectively, on or before the lease expiration date, and at the time the property is sold, the Company must pay the lessor a supplemental rent in the amount of \$1,606 and \$1,976, respectively, to the extent that the sales proceeds exceed the respective residual guarantee amount by the supplemental rent amounts. In the event that the sales proceeds are less than the sum of the residual guarantee amount and the supplemental rent, the Company is required to pay a supplemental rent to the extent that the reduction in the fair value of the property is demonstrated by an independent appraisal to have been caused by the

Company's failure to properly maintain the property.

Accordingly, the aggregate residual guarantee amounts of \$24,418 have been included in the noncancellable real estate operating lease payments relating to the expiration of such leases.

On December 28, 2000, the Company entered into a sale-leaseback transaction on its facility located in Hauppauge, NY. The facility was sold for \$13,650. The lease agreement which is accounted for as an operating lease, has an initial term of 14 years with a fixed annual rent that increases 2.5% annually. The Company has the option to extend the lease term for an additional 3 terms of 5 years each. The gain of \$4,110 on the sale of the facility has been deferred and will be recognized ratably over the term of the lease.

The Company has a contract to provide and operate for the U.S. Air Force ("USAF") a full-service training facility including simulator systems near a USAF base. The Company expects to lease the simulator systems from unrelated third parties, and has entered into agreements with the owner-lessors of the simulator systems, under which the Company is acting as the construction agent on behalf of owner-lessors for procurement and construction for the simulator systems. The estimated project costs to construct the simulator systems is approximately \$48,360. During the construction period, if certain events occur that are caused by the Company's actions or failures to act, these agreements may obligate the Company to make payments to the owner-lessors which may be equal to 89.9% of the incurred project costs for the simulator systems at the time of such defaults. At December 30, 2002, the estimated completion date of the construction, pursuant to these agreements, the Company, as lessee, will enter into leases each with a term of 15 years with the owner-lessors for the use of the simulator systems. These leases are expected to be accounted for as operating leases and the aggregate noncancellable rental payments under such leases are estimated to be \$89,241.

The Company is engaged in providing products and services under contracts with the U.S. Government and to a lesser degree, under foreign government contracts, some of which are funded by the U.S. Government. All such contracts are subject to extensive legal and regulatory requirements, and, from time to time, agencies of the U.S. Government inves-

tigate whether such contracts were and are being conducted in accordance with these requirements. Under U.S. Government procurement regulations, an indictment of the Company by a federal grand jury could result in the Company being suspended for a period of time from eligibility for awards of new government contracts. A conviction could result in debarment from contracting with the federal government for a specified term. Additionally, in the event that U.S. Government expenditures for products and services of the type manufactured and provided by the Company are reduced, and not offset by greater commercial sales or other new programs or products, or acquisitions, there may be a reduction in the volume of contracts or subcontracts awarded to the Company.

The Company has been periodically subject to litigation, claims or assessments and various contingent liabilities incidental to its business. Management continually assesses the Company's obligations with respect to applicable environmental protection laws. While it is difficult to determine the timing and ultimate cost to be incurred by the Company in order to comply with these laws, based upon available internal and external assessments, with respect to those environmental loss contingencies of which management is aware, the Company believes that even without considering potential insurance recoveries, if any, there are no environmental loss contingencies that, individually or in the aggregate, would be material to the Company's consolidated results of operations. The Company accrues for these contingencies when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated.

With respect to those investigative actions, items of litigation, claims or assessments of which it is aware, management of the Company is of the opinion that the probability is remote that, after taking into account certain provisions that have been made with respect to these matters, the ultimate resolution of any such investigative actions, items of litigation, claims or assessments will have a material adverse effect on the financial position or results of operations of the Company.

On December 27, 2000, the Company filed a complaint against Raytheon and Raytheon Technical Services Company in the Court of Chancery for the State of Delaware in and for New Castle County, alleging that Raytheon failed to disclose material liabilities in connection with the sale of TDTS to the Company in February 2000. Specifically, the complaint alleges that Raytheon misrepresented the financial liabilities associated with the AVCATT contract which will cause the Company to incur damages of approximately \$100,000. The Company assumed the AVCATT contract as part of the acquisition of TDTS which was completed in February 2000. The complaint seeks rescission of the TDTS Asset Purchase and Sale Agreement and, alternatively, rescission of the AVCATT contract, rescissory damages and breach of contract.

14. PENSIONS AND OTHER EMPLOYEE BENEFITS

The Company maintains a number of pension plans, both contributory and noncontributory, covering employees at certain locations. Eligibility for participation in these plans varies and benefits are generally based on the participant's compensation and/or years of service. The Company's funding policy is generally to contribute in accordance with cost accounting standards that affect government contractors, subject to the Internal Revenue Code and regulations thereon. Plan assets are invested primarily in U.S. government and agency obligations and listed stocks and bonds.

The Company also provides postretirement medical and life insurance benefits for retired employees and dependents at certain locations. Participants are eligible for these benefits when they retire from active service and meet the eligibility requirements for the Company's pension plans. These benefits are funded primarily on a pay-as-you-go basis with the retiree generally paying a portion of the cost through contributions, deductibles and coinsurance provisions.

The table below summarizes the balance sheet impact, as well as the benefit obligations, assets, funded status and rate assumptions associated with the pension and postretirement benefit plans.

	Pension Plans		Postretirement Benefit Plans	
	2000	1999	2000	1999
Change in benefit obligation:				
Benefit obligation at beginning of year	\$328,541	\$340,483	\$ 65,554	\$ 75,262
Service cost	16,343	13,513	1,670	1,595
Interest cost	28,029	23,092	4,754	4,175
Participants' contributions	36	20	—	—
Amendments	853	3,564	—	(1,429)
Actuarial loss (gain)	8,867	(41,372)	(1,271)	(11,201)
Acquisitions	48,187	—	1,879	753
Benefits paid	(15,373)	(10,759)	(4,048)	(3,601)
Benefit obligation at end of year	\$415,483	\$328,541	\$ 68,538	\$ 65,554
Change in plan assets:				
Fair value of plan assets at beginning of year	\$367,451	\$288,502	\$ —	\$ —
Actual return on plan assets	(21,905)	81,800	—	—
Acquisitions	49,709	—	—	—
Employer contributions	11,345	7,888	4,048	3,601
Participants' contributions	36	20	—	—
Benefits paid	(15,373)	(10,759)	(4,048)	(3,601)
Fair value of plan assets at end of year	\$391,263	\$367,451	\$ —	\$ —
Funded status of the plans				
Unrecognized actuarial loss (gain)	(5,044)	(76,592)	(9,401)	(8,924)
Unrecognized prior service cost	3,777	3,275	(1,207)	(1,306)
Net amount recognized	\$ (25,487)	\$ (34,407)	\$ (79,146)	\$ (75,784)
Amounts recognized in the balance sheet consist of:				
Accrued benefit liability	\$ (26,377)	\$ (34,478)	\$ (79,146)	\$ (75,784)
Accumulated other comprehensive income	890	71	—	—
Net amount recognized	\$ (25,487)	\$ (34,407)	\$ (79,146)	\$ (75,784)
Rate assumptions:				
Discount rate	7.50%	7.75%	7.50%	7.75%
Rate of return on plan assets	9.50%	9.50%	n.a.	n.a.
Salary increases	4.50%	4.50%	4.50%	4.50%
Annual increase in cost of benefits	n.a.	n.a.	6.25%	6.50%

The annual increase in cost of benefits (“health care cost trend rate”) is assumed to be 5.0% in 2000 and decreases to a rate of 4.5% for 2001 and thereafter. Assumed health care cost trend rates have a significant effect on amounts reported for postretirement medical benefit plans. A one percentage point decrease in the assumed health care cost trend rates would have the effect of decreasing the aggregate service and interest cost components and the postretirement medical obligations by \$668 and \$7,392, respectively. A one percentage point increase in the assumed health care cost trend rate would have the effect of increasing the aggregate service and interest cost components and the postretirement medical obligations by \$736 and \$5,738, respectively.

The table below summarizes the components of net periodic pension and postretirement medical costs.

	Pension Plans		Postretirement Benefit Plans	
	2000	1999	2000	1999
Components of net periodic benefit cost:				
Service cost	\$ 16,343	\$ 13,513	\$ 1,670	\$ 1,595
Interest cost	28,029	23,092	4,754	4,175
Amortization of prior service cost	351	289	(99)	(123)
Expected return on plan assets	(39,109)	(26,251)	—	—
Recognized actuarial (gain) loss	(3,981)	(30)	(865)	(112)
Recognition due to settlement	307	—	—	—
Net periodic benefit cost	\$ 1,940	\$ 10,613	\$5,460	\$5,535

The accumulated benefit obligation, projected benefit obligation, and fair value of plan assets for pension plans with accumulated benefit obligations in excess of plan assets were \$86,426, \$92,180, and \$78,773 respectively, as of December 31, 2000 and \$4,459, \$5,307 and \$893 respectively, as of December 31, 1999.

In connection with the Company's assumption of certain plan obligations pursuant to the Company's acquisition of the predecessor company, Lockheed Martin has provided the Pension Benefit Guaranty Corporation (“PBGC”) with commitments to assume sponsorship or other forms of financial support under certain circumstances of the Company's pension plans for Communication Systems – West and Aviation Recorders (the “Subject Plans”). Upon the occurrence of certain events, Lockheed Martin, at its option, has the right to decide whether to cause the Company to transfer sponsorship of any or all of the Subject Plans to Lockheed Martin, even if

the PBGC has not sought to terminate the Subject Plans. Such a triggering event occurred in 1998, but reversed in 1999, relating to a decrease in the PBGC-mandated discount rate in 1998 that had resulted in an increase in the underlying liability. The Company notified Lockheed Martin of the 1998 triggering event, and in February 1999, Lockheed Martin informed the Company that it had no present intention to exercise its right to cause the Company to transfer sponsorship of the Subject Plans. If Lockheed Martin did assume sponsorship of these plans, it would be primarily liable for the costs associated with funding the Subject Plans or any costs associated with the termination of the Subject Plans but L-3 Communications would be required to reimburse Lockheed Martin for these costs. To date, the impact on pension expense and funding requirements resulting from this arrangement has not been significant. However, should Lockheed Martin assume sponsorship of the Subject Plans or if these plans were terminated, the impact of any increased pension expenses or funding requirements could be material to the Company. The Company has performed its obligations under the letter agreement with Lockheed Martin and the Lockheed Martin Commitment and has not received any communications from the PBGC concerning actions which the PBGC contemplates taking in respect of the Subject Plans.

Employee Savings Plans. Under its various employee savings plans, the Company matches the contributions of participating employees up to a designated level. The extent of the match, vesting terms and the form of the matching contributions vary among the plans. Under these plans, the Company's matching contributions in L-3 Holdings common stock and cash were \$15,201 for 2000, \$8,798 for 1999, and \$6,366 for 1998.

15. SUPPLEMENTAL CASH FLOW INFORMATION

	Year Ended December 31,		
	2000	1999	1998
Interest paid	\$81,390	\$50,532	\$42,908
Income taxes paid	10,052	6,317	496
Noncash transactions:			
Common stock issued related to acquisition	—	6,434	—
Contribution in common stock to savings plans	12,642	6,993	967

16. SEGMENT INFORMATION

The Company has two reportable segments, Secure Communication Systems and Specialized Communication Products, which are described in Note 1. The Company evaluates the performance of its operating divisions and reportable segments based on sales and operating income. All corporate expenses are allocated to the Company's divisions using an allocation methodology prescribed by U.S. Government regulations for government contractors. Accordingly, all costs and expenses are included in the Company's measure of segment profitability.

	Secure Communication Systems	Specialized Communication Products	Corporate	Elimination of Intersegment Sales	Consolidated Total
2000					
Sales	\$ 856,970	\$1,065,136		\$ (12,045)	\$1,910,061
Operating income	91,310	131,408			222,718
Total assets	792,949	1,480,790	\$189,805		2,463,544
Capital expenditures	10,750	22,830			33,580
Depreciation and amortization	26,417	47,837			74,254
1999					
Sales	\$ 544,418	\$ 867,495		\$ (6,451)	\$1,405,462
Operating income	46,955	103,531			150,486
Total assets	370,918	1,065,236	\$192,587		1,628,741
Capital expenditures	6,980	16,476			23,456
Depreciation and amortization	18,451	35,267			53,718
1998					
Sales	\$493,188	\$ 561,393		\$ (17,536)	\$1,037,045
Operating income	39,885	60,464			100,349
Total assets	368,891	797,469	\$119,036		1,285,396
Capital expenditures	5,755	17,674			23,429
Depreciation and amortization	17,325	23,030			40,355

Corporate assets not allocated to the reportable segments primarily include cash and cash equivalents, corporate office fixed assets, deferred income tax assets and deferred debt issuance costs.

Substantially all of the Company's operations are domestic. The Company's foreign operations are not material to the Company's results of operations, cash flows or financial position. Sales to principal customers are summarized in the table below.

	Year Ended December 31,		
	2000	1999	1998
U.S. Government agencies	\$1,284,379	\$ 924,006	\$ 716,234
Foreign governments	144,274	127,637	100,911
Commercial export	172,101	144,274	85,331
Other (principally U.S. commercial)	309,307	209,545	134,569
Consolidated sales	\$1,910,061	\$1,405,462	\$1,037,045

17. UNAUDITED QUARTERLY FINANCIAL DATA

Unaudited summarized financial data by quarter for the years ended December 31, 2000 and 1999 is presented in the table below.

	Mar 31	Jun 30	Sept 30	Dec 31
2000				
Sales	\$377,052	\$460,976	\$514,415	\$557,618
Operating income	34,669	49,653	62,815	75,581
Net income	10,929	16,459	24,110	31,229
Basic EPS	\$ 0.33	\$ 0.49	\$ 0.72	\$ 0.93
Diluted EPS	\$ 0.32	\$ 0.47	\$ 0.69	\$ 0.89
1999				
Sales	\$275,562	\$314,432	\$382,356	\$433,112
Operating income	26,167	31,149	42,840	50,330
Net income	7,199	11,086	17,349	23,055
Basic EPS	\$ 0.24	\$ 0.34	\$ 0.53	\$ 0.70
Diluted EPS	\$ 0.23	\$ 0.33	\$ 0.51	\$ 0.68

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Shareholders of L-3 Communications Holdings, Inc.

We have audited the accompanying consolidated balance sheets of L-3 Communications Holdings, Inc. and subsidiaries (the "Company") as of December 31, 2000 and 1999, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years ended December 31, 2000. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management,

as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2000 and 1999, their consolidated results of operations and cash flows for each of the three years ended December 31, 2000, in conformity with accounting principles generally accepted in the United States of America.



PricewaterhouseCoopers LLP

1177 Avenue of the Americas

New York, New York

February 6, 2001

Report of Management

The consolidated financial statements and other financial data contained in this annual report have been prepared in conformity with generally accepted accounting principles in the United States of America. The integrity and objectivity of this financial information is the responsibility of management. To this end, management maintains an adequate system of internal controls and supports an extensive program of internal reviews and audits to provide reasonable assurance that the Company's assets are protected and that transactions and events are recorded properly.

The consolidated financial statements have been audited by PricewaterhouseCoopers LLP, Independent Auditors. The Report of Independent Auditors, above, expresses an informed judgment as to whether management's financial statements, considered in their entirety, present fairly, in conformity with generally accepted accounting principles in the United States of America, the Company's financial position, results of operations and cash flows. This judgment is based on procedures described in the second paragraph of their report. These procedures include an assessment of the Company's internal control structure, and performing tests and other

auditing procedures sufficient to provide reasonable assurance that the financial statements are free of material misstatements.

To further assure objectivity, the financial information contained in this annual report is subject to review by the Audit Committee of the Board of Directors. The Audit Committee, composed of outside directors who are not employees, meets periodically with management, the internal auditors and the independent auditors to discuss auditing, internal control and financial reporting matters. The internal auditors and independent auditors periodically meet alone with the Audit Committee and have unlimited access to the Audit Committee at any time.

We believe that our policies and procedures provide reasonable assurance that operations are conducted in conformity with applicable laws and with our commitment to a high standard of business conduct.



Robert V. LaPenta

President and
Chief Financial Officer

Michael T. Strianese

Senior Vice President –
Finance

L-3 COMMUNICATIONS OFFICERS

Frank C. Lanza

Chairman and Chief Executive Officer

Robert V. LaPenta

President and Chief Financial Officer

Christopher C. Cambria

Senior Vice President, Secretary and General Counsel

Michael T. Strianese

Senior Vice President of Finance

General Jimmie V. Adams

(U.S.A.F. – Retired)

Vice President of Washington Operations

David T. Butler III

Vice President of Planning

Kenneth W. Manne

Vice President of Human Resources

Lawrence W. O'Brien

Vice President and Treasurer

General Robert W. RisCassi

(U.S. Army – Retired)

Vice President of Washington Operations

Charles J. Schafer

Vice President of Business Operations and
President of Products Group

Lawrence H. Schwartz

Vice President of Business Development

Cynthia A. Swain

Vice President of Corporate Communications

Joseph S. Paresi

Corporate Vice President of Product Development and
President of Security Systems Division

Curtis Brunson

Corporate Vice President and President of
Communication Systems – West Division

Alan R. Dietrich

Corporate Vice President and President of Telemetry Group

John Mega

Corporate Vice President and President of Microwave Group

Gregory B. Roberts

Corporate Vice President and President of
Communication Systems – East Division

Ralph G. D'Ambrosio

Controller

David M. Reilly

Assistant General Counsel and Assistant Secretary

SHAREHOLDER INFORMATION

Corporate Headquarters.

You can contact the corporate headquarters by writing to L-3 Communications, 600 Third Avenue, New York, NY 10016, or by calling 212-697-1111. To send a fax, dial 212-805-5353.

Corporate Information.

News media, analysts, shareholders and other investors seeking corporate information about L-3 Communications should contact Cynthia Swain, vice president of corporate communications at 212-697-1111.

Printed Materials.

Printed financial materials, including the 2000 Annual Report may be obtained, without charge, from L-3's Investor Relations firm, Morgen-Walke Associates by calling 212-850-5619.

Internet.

You can access quarterly and annual financial information, news releases and an overview of the company's products and services through the L-3 web site at <http://www.L-3com.com> on the Internet.

Auditors.

PricewaterhouseCoopers LLP, New York, NY.

Shareholder Assistance.

If you have questions concerning your shareholder account, please contact the stock transfer agent, First Chicago Trust Company of New York, a division of EquiServe, P.O. Box 2500, Jersey City, New Jersey 07303, or call 800-446-2617. For the hearing impaired, the phone number is TDD: 201-222-4955.

You can also contact the stock transfer agent at their web site at <http://www.equiserve.com> on the Internet.

Stock Exchange Listing.

The common stock of L-3 Communications is traded on the New York Stock Exchange under the symbol LLL.

Annual Meeting.

The annual meeting of shareholders will be held at 2:30 p.m. on Thursday April 26, 2001 at the JW Marriott New York Hotel, 151 West 54th Street, New York, NY.

Equal Opportunity Employer.

L-3 Communications Corporation is an equal opportunity employer. All matters regarding recruiting, hiring, training, compensation, benefits, promotions, transfers and all other personnel policies will continue to be free from discriminatory practices.

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communications

**600 Third Avenue
New York, NY 10016**