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iscal year 2004. This is due to the increase in our orders received in the second half of the fiscal year and demonstrating the return of confidence from our customers following the implementation of our refinancing package.

The decrease of customer cash deposits at the end of fiscal year 2003 as compared to fiscal year 2002 was mainly due to translation effects.

Provisions for risks and charges

At 31 March 2004, the provisions for risks and charges were 3,489 million compared with 3,738 million at 31 March 2003.

This net decrease was accounted for mainly by the following movements:

a decrease in provisions on contracts for 601 million, mainly resulting from application of the GT24/GT26 gas turbines and to the disposal of activities;

an increase in restructuring provisions of 247 million due to the numerous restructuring plans announced, for which we have recorded a high level of provisions in fiscal year 2004 that will be applied during the fiscal year 2005; and

a decrease in foreign currency translation effects.

At 31 March 2003, the provisions for risks and charges were 3,738 million compared with 3,849 million at 31 March 2002. The decrease was due to a decrease in provisions on contracts, restructuring and other provisions, foreign currency translation effects which more than offset the net increase in provisions for the GT24/GT26 gas turbines.

Shareholders equity and minority interests

Shareholders equity at 31 March 2004 was 97 million, including minority interests, compared with 802 million at 31 March 2003 and 1,843 million at 31 March 2002. This decrease at 31 March 2004 was mainly due to the net loss for the period of 1,788 million, offset by the capital increase of 300 million, the issuance of convertible bonds for 733 million net of related costs and the positive impact of cumulative translation adjustments for 77 million. The decrease at 31 March 2003 was mainly due to the net loss and translation adjustments, partially offset by a capital increase of 622 million.

As at 31 March 2004, 152 million of bonds, out of the 901 million issued, have not yet been converted into capital.

Securitisation of existing receivables

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In order to fund our activity, we sell selected existing trade receivables to a third party on an irrevocable, without recourse basis. The net cash proceeds from securitisation of existing trade receivables at 31 March 2004 was 94 million compared with 357 million at 31 March 2003 and 1,036 million at 31 March 2002.

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⁽¹⁾ 31 March 2003 and 2004 adjusted figures for the purpose of the filing of this Annual Report on Form 20-F. See Note 1(c) to the Consolidated Financial Statements.

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Securitisation of future receivables

In order to finance working capital and to mitigate the cash-negative profiles of some contracts, we have sold to third parties selected future receivables due from our customers. This securitisation of future receivables has the benefit of reducing our exposure to customers (since some future receivables are sold without recourse to us should the obligor under the receivable default for reasons other than our failure to meet our obligations under the relevant contract) and applies principally to Marine and Transport. The total securitisation of future receivables at 31 March 2004 was 265 million compared with 1,292 million at 31 March 2003 and 1,735 million at 31 March 2002. The decrease in fiscal year 2004 compared with fiscal year 2003 was mainly due to the delivery of two cruise-ships by our Marine Sector. During fiscal year 2004, we did not enter into any new securitisation of future receivables. The decrease in fiscal year 2003 compared with fiscal year 2002 was mainly due to the lower level of orders received in Marine.

Financial debt

Our financial debt was 4,372 million at 31 March 2004, compared with 6,331 million at 31 March 2003 and 6,035 million at 31 March 2002.

Net debt

We define net debt as financial debt less short-term investments, cash and cash equivalents. Net debt was 2,906 million at 31 March 2004, compared with 4,561 million at 31 March 2003 and 3,799 million at 31 March 2002. Our net debt decreased due to the capital increase, the issuance of bonds mandatorily reimbursable with shares and proceeds on disposal of investments partly offset by net cash used in operating activities. The increase in fiscal year 2003 was due to a decrease in cash and cash equivalents and the reclassification of our preference shares and undated subordinated notes.

LIQUIDITY AND CAPITAL RESOURCES**CONSOLIDATED STATEMENT OF CASH FLOWS**

The following table sets out selected figures concerning our consolidated statement of cash flows:

| | Year ended 31 March | | |
|---|----------------------------|-------------|-------------|
| | 2002 | 2003 | 2004 |
| | <i>(in million)</i> | | |
| <i>Total Group Actual Figures</i> | | | |
| Net income after elimination of non-cash items ⁽¹⁾ | 341 | (1,181) | (973) |

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| | | | |
|--|--------------|--------------|----------------|
| Change in net working capital ⁽¹⁾ | (920) | 644 | (85) |
| Net cash provided by (used in) operating activities | (579) | (537) | (1,058) |
| Net cash provided by (used in) investing activities | 123 | (341) | 1,561 |
| Net cash provided by (used in) financing activities | (136) | 621 | 1,173 |
| | (592) | (257) | 1,676 |
| Net effect of exchange rate | (12) | (41) | (7) |
| Other changes and reclassifications | 16 | (464) | (14) |
| Decrease (increase) in net debt | (588) | (762) | 1,655 |

Net cash provided by (used in) operating activities

Net cash provided by operating activities is defined as the net income after elimination of non-cash items plus working capital movements. Net cash provided by (used in) operating activities was (1,058) million in fiscal year 2004 compared to (537) million in fiscal year 2003 and (579) million in the fiscal year 2002.

⁽¹⁾ 31 March 2003 and 2004 adjusted figures for the purpose of the filing of this Annual Report on Form 20-F. See Note 1(c) to the Consolidated Financial Statements.

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Net income after elimination of non-cash items was (973³) million in fiscal year 2004. This amount represented the cash generated by net income before working capital movements. As provisions are included in the definition of our working capital, provisions are not part of the elimination of non-cash items. This negative amount was mainly due high levels of restructuring and financial expenditures.

Change in net working capital was (85³) million. The principal movements in working capital were due to:

a decrease of 267 million in sale of trade receivables (securitisation of existing receivables);

a decrease of 332² million in contract-related provisions due to the application of GT24/GT26 provisions partially offset by new provisions recorded on other contracts and for restructuring not yet applied;

stable customer deposits and advances; and

a decrease of 1,005⁴ million in trade payables and other payables, a decrease by 389 million of inventories and contracts in progress and a decrease of trade and other receivables by 747⁷ million, these movements are mainly due to the decrease in sales by 10% on a comparable basis and a high level of delivery in the fiscal year 2004. The positive cash flow of 131 million triggered by this net decrease in working capital resulted from the application of accrued contract costs for the GT24/GT26, a positive change for Marine following deliveries and the combined effect of a decrease in activity and a better working capital management (mainly reduction of overdue receivables from customers).

The net cash used in operating activities of (537) million in fiscal year 2003 was mainly due to the net loss for the fiscal year, partly offset by positive change in working capital. The net cash used in operating activities of (579) million in fiscal year 2002 was mainly affected by the net outflow from change in working capital.

Net cash provided by (used in) investing activities

Net cash provided by investing activities was 1,561 million in fiscal year 2004. This amount comprised:

proceeds of 244 million from disposals of property, plant and equipment (including 206 million from the disposal of real estate);

capital expenditures for 254 million;

decrease in other fixed assets of 125 million mainly due to the proceeds from the early reimbursement of receivables due to us by two special purpose entities in connection with Marine vendor financing; and

cash proceeds from the sale of investments, net of net cash sold for 1,454 million, comprising of mainly the proceeds from the sale of our Industrial Turbine businesses for 784 million and our T&D activities for 632 million.

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Net cash provided by (used in) investing activities was (341) million in fiscal year 2003 and 123 million in fiscal year 2002. The net cash outflow in fiscal year 2003 was mainly due to 410 million of capital expenditures and 154 million of cash expenditures for the acquisition of the remaining 49% in Fiat Ferroviaria Spa.

The net cash inflow in fiscal year 2002 was mainly due to sale of investments (Contracting and GTRM).

Net cash provided by (used in) financing activities

Net cash provided by financing activities in fiscal year 2004 was 1,173 million, including a capital increase for 300 million and ORA issuance for 901 million, compared with 621 million of net proceeds in fiscal year 2003, including primarily proceeds from a capital increase completed in July 2002.

The net cash used in financing activities in fiscal year 2002 of 136 million was due to dividends paid.

Decrease (increase) in net debt

As a result of the above, our net debt decreased by 1,655 million in fiscal year 2004, compared with an increase of 762 million in fiscal year 2003 and of 588 million in fiscal year 2002.

(1) 31 March 2003 and 2004 adjusted figures for the purpose of the filing of this Annual Report on Form 20-F. See Note 1(c) to the Consolidated Financial Statements.

Table of Contents**MATURITY AND LIQUIDITY**

We rely on a variety of sources of liquidity in order to finance our operations, including principally borrowings under revolving credit facilities, the issuance of commercial paper and asset disposals. Additional sources include customer deposits and advances and proceeds from the sale of trade receivables, including future trade receivables. In the past, we have also used the issuance of securities, including debt securities and preferred shares, as a source of liquidity.

In August 2003, we entered into a new financing package with more than 30 of our commercial lenders and the French State, and in September 2003 we amended this financial package, as described above under Status of Our Action Plan and Main Events of Fiscal Year 2004 2003 Financing Package . Implementation of this financing package has reduced and substantially changed the maturity profile of our debt.

The following table sets forth our outstanding financial debt obligations (including future receivables securitised) and available credit lines as of 31 March 2004:

| Outstanding lines as of 31 March 04 | 1st quarter FY2005 | 2nd quarter FY2005 | 3rd quarter FY2005 | 4th quarter FY2005 | Fiscal Year 2005 | Fiscal Year 2006 | Fiscal Year 2007 | Fiscal Year 2008 | Fiscal Year 2009 | After Fiscal Year 2009 | |
|---|--|--|--|--|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|---------------------------------------|--------------|
| Redeemable preference shares | 205 | | | | | (205) | | | | | |
| Subordinated notes | 250 | | | | | | (250) | | | | |
| Subordinated loans (PSDD) | 1,563 | | | | | | | | (1,563) | | |
| Subordinated long-term bond (TSDD) | 200 | | | | | | | | | (200) | |
| Subordinated bonds reimbursable with shares TSDD R ^A) | 300 | | | | | | | | | (300) | |
| Bonds | 650 | | | | | | (650) | | | | |
| Syndicated loans | 722 | | | | | | (722) | | | | |
| Bilateral loans | 260 | | | | | (27) | (33) | (200) | | | |
| Commercial paper | 420 | | | (420) | (420) | | | | | | |
| Bank overdrafts/other facilities/accrued interests ⁽²⁾ | 320 | (278) | | | (278) | (14) | (6) | (3) | (3) | (16) | |
| Sub-total | 4,890 | (278) | 0 | 0 | (420) | (698) | (246) | (1,661) | (203) | (1,566) | (516) |
| Future receivables ⁽³⁾ | 265 | (68) | (69) | (68) | (60) | (265) | | | | | |
| Total⁽⁴⁾ | 5,155 | (346) | (69) | (68) | (480) | (963) | (246) | (1,661) | (203) | (1,566) | (516) |
| Financial debt | 4,372 | | | | | | | | | | |
| Available lines | 783 | | | | | | | | | | |

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- (1) Subordinated bonds reimbursable with shares (TSDD RA) will only be reimbursed in cash in the event the European Commission does not approve their reimbursement with shares. See Status of Our Action Plan and Main Events of Fiscal Year 2004-2003 Financing Package .
- (2) Facilities entered into by subsidiaries have been classified as being immediately due because such facilities are generally uncommitted.
- (3) Excluding the reimbursement of which will come directly from the direct payment of the customer to the investor to whom we sold the right to receive the payment.
- (4) Under US GAAP, as our covenants have been suspended until 30 September 2004, all outstanding debt has been classified as short term. See Note 33(D)(g) to our Consolidated Financial Statements.

Total available unused credit lines, together with cash available in the Group, amounted to 2,249 million at 31 March 2004, compared with 2,370 million at 31 March 2003. The amounts consisted of:

Available credit lines at Group level, which were constituted of 420 million of commercial paper and 363 million of the tranche B of the Subordinated loans (PSDD), for 783 million at 31 March 2004, compared with a bridge facility of 600 million at 31 March 2003;

Cash available at Group level was 532 million at 31 March 2004, compared with 610 million at 31 March 2003; and

Cash available at subsidiary level of 934 million at 31 March 2004, compared with 1,160 million at 31 March 2003.

ALSTOM, the Group parent company, may readily access some cash held by wholly owned subsidiaries through the payment of dividends or pursuant to intercompany lending arrangements. Local constraints can delay or

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restrict this access, however. Furthermore, while we have the power to control decisions of subsidiaries of which we are the majority owner, our subsidiaries are distinct legal entities and the payment of dividends and the making of loans, advances and other payments to us by them may be subject to legal or contractual restrictions, be contingent upon their earnings or be subject to business or other constraints. These limitations include local financial assistance rules, corporate benefit laws and other legal restrictions. Our policy is to centralise liquidity of subsidiaries at the parent company level when possible, and to continue to progress towards this goal. The cash available at subsidiary level was 2,069 million, 1,160 million and 934 million, respectively, in March 2002, 2003 and 2004.

PENSION ACCOUNTING

We provide various types of retirement, termination and post-retirement benefits (including healthcare and medical) to our employees. The type of benefits offered to an individual employee is related to local legal requirements as well as the historical operating practices of the specific subsidiaries and involves us in the operation of, or participation in, various retirement plans.

These plans are either defined-contribution, defined-benefit or multi-employer plans.

Defined contribution plans

For the defined-contribution plans, we pay contributions to independently administered funds at a fixed percentage of employees' pay. The pension costs in respect of defined-contribution plans are charged in the income statement as operating expenses and represent the contributions paid by the Company to these funds.

Defined-benefit plans

These plans mainly cover retirement and termination benefits and post-retirement medical benefits.

For the defined benefit plans, which we operate, benefits are normally based on an employee's pensionable remuneration and length of service. These plans are either funded through independently administered pension funds or unfunded. Pension liabilities are assessed annually by external professionally qualified actuaries. These actuarial assessments are carried out for each plan using the Projected Unit Credit method with a measurement date of 31 December. The financial and demographic assumptions used are determined at the measurement date as being appropriate for the plan and the country in which it is situated.

The most important assumptions made are listed below:

discount rate;

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inflation rate;

rate of salary increases;

long-term rate of return on plan assets;

mortality rates; and

employee turnover rates.

Certain assumptions used are discussed in Note 21 to the Consolidated Financial Statements.

The assets of externally administered defined-benefit plans are invested mainly in equity and debt securities. The components of these assets are disclosed in Note 21 to the Consolidated Financial Statements.

The expected costs of providing retirement pensions under defined-benefit plans, as well as the costs of other post-retirement benefit plans, are charged to the profit and loss account over the periods benefiting from the employees' services.

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Valuation of the Projected Benefit Obligation

The actuarial value of the future obligations of the employer estimated with the Projected Unit Credit method (Projected Benefit Obligation - PBO) fluctuates annually, depending upon the following:

increases related to the acquisition by the employees of one additional year of rights (service cost);

increase in the present value of the PBO which arises because the benefits are one year closer to their payment dates (interest cost);

decreases related to the benefits paid during the year;

changes related to modifications of the actuarial assumptions (actuarial gains and losses : discount rate, inflation rate, rate of salary increases etc);

changes in obligations related to plan amendments;

changes due to curtailments or settlements applied on the plans; and

changes in scope (business combinations / disposals).

The change in the PBO is disclosed in Note 21 to the Consolidated Financial Statements.

Valuation of plan assets

The fair value of the assets held by each plan is the amount that the plan could reasonably expect to receive in a current sale of the assets between a willing buyer and a willing seller. This is compared with the PBO and the difference is referred to as the funded status of the plan.

The changes in the fair value of assets and the funded status are disclosed in Note 21 to the Consolidated Financial Statements.

Actuarial gains and losses, prior year service costs and transition obligations

A number of factors can trigger actuarial gains and losses:

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differences between the assumptions used and the actual experience (for instance, an actual return on assets differing from the expected rate of return at the beginning of the year);

changes in the long-term actuarial assumptions (inflation rate, discount rate, rate of salary escalation, mortality table etc);

changes due to plan amendments; and

impact of the first application of the actuarial methodology (Projected Unit Credit method).

The impact of these factors is shown in the table entitled "Change in plan assets" in Note 21 to the Consolidated Financial Statements:

unrecognised actuarial loss (gain);

unrecognised prior service cost (due to plan amendments); and

unrecognised transition.

The unrecognised actuarial loss (gain) at the year-end is compared on a plan-by-plan basis with the higher of the PBO and the fair value of the assets held. If the unrecognised actuarial loss (gain) exceeds 10% of this amount the excess above the 10% level is spread across the remaining working lives of the employees of the respective plan.

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As of 31 March 2004, the actuarial losses unrecognised in the balance sheet were 918 million, a decrease of 49 million since March 2003. Recognition of these liabilities under French GAAP is allowed over the average remaining working lives of the relevant participants. Thus, starting with fiscal year 2005, the portion above 10% calculated scheme by scheme, is spread across the average residual working period of these plans, being 10-15 years.

The unrecognised gains on prior service costs and on transition amounted to 33 million at 31 March 2004. The total amount is amortised on a straight-line basis over the remaining working lives of the plans participants.

Pension cost

The total pension cost related to defined benefit is defined annually by qualified actuaries and is detailed in Note 21 to the Consolidated Financial Statements as follows:

service cost, which corresponds to the acquisition of one additional year of rights;

interest cost, which is due to the increase in the present value of the PBO which arises because the benefits are one period closer to their payment dates;

expected return on plan assets (profit);

cost (or potentially profit) corresponding to the amortisation of prior service cost;

cost (or potentially profit) corresponding to the amortisation of actuarial gains and losses; and

profit (or potentially cost) of Curtailments/Settlements corresponding to the impact of a reduction/cancellation of the obligation mainly due to a modification of the plan's scope (downsizing, business disposals, closing of a defined-benefits plan, etc).

Multi-employer plans in the United States and Canada

We employ workers from US and Canada Trade Unions mainly in our Customer Service activity related to the boiler after-market.

The pension costs charged in the income statement as Other expenses Pension costs represent contributions payable by us to these dedicated funds.

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During the year ended 31 March 2004, pension and other post retirement benefit costs recorded totaled of 263 million. Of this amount 191 million related to defined benefit schemes, 32 million to defined contribution schemes, 28 million to multi-employer schemes and 12 million to other post retirement benefits. The total cash spend in the year was 199 million.

The fair value of defined benefit scheme assets totaled 2,263 million at 31 March 2004 and the benefit obligations, pension and other benefits, totaled 3,633 million leaving an underfunding in the plans of 1,370 million. We have recorded accrued benefits costs of 485 million in our Consolidated Financial Statements. This leaves 885 million to be recorded, taking into account changes in actuarial assumptions and plan assets and provisions, over the average future service period of employees.

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The following table sets forth our off-balance sheet commitments, which are discussed further at Note 27 to the Consolidated Financial Statements:

| | At 31 March | | |
|--|---------------------|---------------|--------------|
| | 2002 | 2003 | 2004 |
| | <i>(in million)</i> | | |
| <i>Total Group Actual figures</i> | | | |
| Guarantees related to contracts | 11,451 | 9,465 | 8,169 |
| Guarantees related to vendor financing | 932 | 749 | 640 |
| Discounted notes receivables | 18 | 11 | 6 |
| Commitments to purchase fixed assets | 8 | 7 | 0 |
| Other guarantees | 58 | 94 | 43 |
| Off balance sheet commitments | 12,467 | 10,326 | 8,858 |

Guarantees related to contracts

The overall amount given as guarantees on contracts decreased from 9,465 million in March 2003 to 8,169 million in March 2004, a decrease by 14% mainly due the disposal of our Industrial Turbine businesses and our T&D activities, and to exchange rate variations.

Vendor Financing Exposure

In some instances, we have provided financial support to institutions which finance some of our customers and also, in some cases, directly to our customers for their purchases of our products. We refer to this financial support as vendor financing. We have not committed to provide any vendor financing guarantees to our customers since fiscal year 1999.

Vendor financing totalled 969 million at 31 March 2004 (of which 640 million was off balance sheet) compared to 1,259 million at 31 March 2003 (of which 749 million was off balance sheet). This decrease was mainly due to the early reimbursement to us of 180 million due to us from two special purpose entities following the agreement with our lenders under our new financing package.

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For addition information please refer to the Notes 25 and 27(a)(2) of the Consolidated Financial Statements.

Contractual Obligations

The following table sets forth, as of 31 March 2004, our financial debt, long-term rental, capital and operating lease obligations and pensions obligations, broken down by the periods in which the relevant payments are due.

| | At 31 March 2004 | Less than 1 year | 1-3 years | 3-5 years | More than 5 years |
|---|------------------------|---------------------|---------------------|--------------|----------------------|
| | | | | | |
| | | | <i>(in million)</i> | | |
| Financial Debt Obligations (Exclusive of Capital lease Obligations) | 4,372 | 543 | 1,907 | 1,406 | 516 |
| Long term rental | 683 | 11 | 31 | 44 | 597 |
| Capital Lease Obligations | 237 | 37 | 55 | 39 | 106 |
| Operating Lease Obligations | 430 | 62 | 106 | 75 | 187 |
| Pensions and retirement obligations, net | 485 | 63 | 120 | 120 | 182 |
| Total | 6,207 | 716 | 2,219 | 1,684 | 1,588 |

See Notes 27(b), Note 22 and Note 21 of the Consolidated Financial Statements.

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CRITICAL ACCOUNTING POLICIES

The preparation of our Consolidated Financial Statements requires us to make estimates and judgements that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of commitments and contingencies, including financing arrangements. On a regular ongoing basis, we evaluate our estimates, including those relating to projects, products, parts and other after-market operations, and included in accrued contract costs, provisions for risks and charges, bad debts, inventories, investments, intangible assets, including goodwill and other acquired intangibles, taxation including deferred tax assets and liabilities, warranty obligations, restructuring, long-term service contracts, pensions and other post-retirement benefits, commitments, contingencies and litigation. Estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgements about the carrying value of assets and liabilities. Actual results may differ from those estimates under different circumstances, assumptions or conditions.

Accounting policies important to an understanding of the financial statements include those related to business combinations, consolidation methods, goodwill, other acquired intangible assets and restructuring that may be subject to the application of differing accounting principles. We believe the following critical accounting policies are most affected by our judgements and estimates in preparing our Consolidated Financial Statements.

Revenue recognition on long-term contracts

We recognise revenue and profit as work progresses on long-term, fixed-price contracts using the percentage of completion method, based on contract milestones or costs incurred (See Note 2(c) to the Consolidated Financial Statements), which relies on estimates of total expected contract revenue and cost. We follow this method because we believe we can make reasonably dependable estimates of the revenue and costs applicable to various defined stages, or milestones, of a contract. Recognised revenues and profit taken are subject to revisions as the contract progresses to completion. Revisions to profit estimates are charged to income in the period in which the facts that give rise to the revision become known. When we book revenue, we also book certain contract costs (including direct materials and labour costs and indirect costs related to the contract) so that the contract margin, on a cumulative basis, equals the total contract gross margin determined in the latest project review. We generally account for long-term service contracts using the percentage of completion method, recognising revenue as performance of the contract's progress using estimated contract profit rates. Selling and administrative expenses are charged to expenses as incurred.

Contract accruals

Significant estimates are involved in the determination of provisions related to contract losses and warranty costs. If a project review indicates a negative gross margin, we recognise the entire expected loss on the contract when we identify the negative gross margin. Estimates of future costs reflect our current best estimate of the probable outflow of financial resources that will be required to settle contractual obligations. These estimates are assessed on a contract-by-contract basis. Such estimates are subject to change based on new information as projects progress toward completion.

We provide for the estimated cost of product warranties at the time revenue is recognised. Our warranty obligations are affected by product failure rates, material usage and service delivery costs incurred in correcting any failures. Should actual failure rates, material usage or service delivery cost of the products differ from current estimates, revisions to the estimated warranty liability would be required. The introduction of technologically advanced products exposes us to risk of product failure significantly beyond the terms of standard contractual warranties applying to suppliers of equipment only. Should adverse changes to product failure rates occur, additional cost to complete may be required and

result in actual financial consequences different from our estimates.

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Inventories

We write down our inventories for estimated obsolescence or unmarketability in an amount equal to the difference between the cost of the inventory and the estimated market value based on a assumptions about future demand and market conditions. If actual market conditions are less favourable than those we project, additional inventory write-downs may be required.

Doubtful accounts

We maintain allowances for doubtful accounts, for estimated losses resulting from the inability of our customers to make required payments. If the financial conditions of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances could be required.

Impairment of long term assets

We review our long term assets, both tangible and intangible, on an annual basis and record an impairment charge when we believe an asset has experienced a decline in value that is other than temporary. Future adverse changes in market conditions or poor operating results from underlying assets could result in losses or an inability to recover the carrying value of the assets that may not be reflected in the current carrying value. This could require us to record an impairment charge in the future.

In respect of goodwill and other intangible assets, we base our impairment testing by Sector on the Group's internal three-year Business Plan and extrapolate over ten years together with a terminal value. These are discounted at the Group's Weighted Average Cost of Capital (WACC).

Valuation of deferred tax assets

We record a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realised. We take into account future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance. When we determine that we are able to realise our deferred tax assets in the future in excess of our net recorded amount, we make an adjustment to the deferred tax asset, to increase income in the period that such determination is made. Likewise, when we determine that we are not able to realise all or part of our net deferred tax assets, an adjustment to the deferred tax asset is charged to income.

Pension benefits

We sponsor pension and other retirement plans in various forms covering substantially all employees who meet eligibility requirements. Several statistical and other factors that attempt to anticipate future events are used in calculating the expense and liability related to the plans. These factors include assumptions about the discount rate, expected return on plan assets and rate of future compensation increases as determined by

us, within certain guidelines.

In addition, our actuarial consultants also use subjective factors such as withdrawal and mortality rates to estimate these factors. The actuarial assumptions we use may differ materially from actual results due to changing market and economic conditions, higher or lower withdrawal rates or longer or shorter life spans of participants. These differences could result in a significant change to the amount of pension expense recorded and on the assessment of the benefit obligations.

Capital leases

Under French GAAP the Group can elect to capitalise finance leases (benchmark treatment) or not to capitalise.

The Group has chosen the latter option.

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Operating income

The Group does not include within its Income Statement line item operating Income, restructuring costs, employee profit sharing and pension costs. These are included within the line item Earnings before Interest and Tax.

Other significant accounting policies

Other significant accounting policies are important to an understanding of the financial statements. Policies related to purchase accounting, consolidation policies, provisions and financial instruments and debt require difficult judgements on complex matters that are often subject to multiple sources of authoritative guidance.

TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

Following the coming into force of European Regulation n° 1606/2002, European-listed companies are required to adopt International Financial Reporting Standards (IFRS/IAS) in the preparation of their Consolidated Financial Statements covering periods beginning on or after 1 January 2005. Consequently, ALSTOM Consolidated Financial Statements covering the period beginning 1 April 2005 will be presented according to IFRS, together with comparative information related to the previous period converted to the same standards. In order to present those comparative data, an opening balance sheet at 1 April 2004 (transition date) converted to IFRS will have to be prepared.

The group has set up an IFRS implementation program aiming at the following objectives:

identification of differences between the accounting principles currently followed by the Group and the applicable provisions of IFRS, with respect to recognition, measurement and presentation,

estimation of main impacts,

analysis of required adaptations of corporate processes and information systems, and

organisation of training action plans.

The project is supervised by a Management Committee, chaired by the Group Chief Financial Officer and composed of representatives of Sectors and Corporate. Working groups have been set up in order to address the main issues potentially impacting the Group's financial statements and the existing information systems. A central team is in charge of co-ordinating the project.

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The adoption of the new body of accounting standards is still subject to the approval by the European Commission of the standards related to financial instruments and of the new standards, amendments or interpretations issued since June 2003.

Accordingly, the forecast impacts of the conversion to IFRS are based on a platform which is not yet fully finalised by the International Accounting Standard Board and have to be considered only as the conclusion of a preliminary diagnosis.

On the date of publication of this report, the Group is of the opinion that the main differences in accounting treatments due to the conversion to IFRS already identified are the following:

Pension and long-term benefits

According to IFRS 1 which governs the preparation of the balance sheet at the transition date, two alternative treatments of unrecognised actuarial gains or losses can be considered:

immediate recognition in the balance sheet of all actuarial gains or losses related to pension benefits existing at the date of transition, measured according to IAS 19 (Employee Benefits); or

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complete retrospective application of IAS 19 since inception of all plans with cumulative amortisation of actuarial gains and losses, as if the standard had been applied in the previous years.

Recognition of development costs as assets

Development costs which meet the conditions set out in IAS 38 (Intangible assets) must be recognised as assets, whereas they are presently expensed as incurred.

The Group is currently reviewing its information systems in order to assess if they are able to provide the necessary data for identification of costs eligible as assets, both in future years and retrospectively with respect to the technology internally developed and used at the date of first-time adoption of the standard.

The counterpart of any recognition of development assets would be an increase in assets and opening equity at the transition date.

Leases

The main impact of the conversion to IFRS will relate to assets financed through capital leases and sales type leases.

Those assets, as well as corresponding liabilities, will have to be recognised in the balance sheet, while they are presently disclosed as off balance sheet commitments. This change of accounting method will significantly increase both fixed assets and financial debt. Opening equity and future earnings will be marginally affected.

Revenue and cost recognition

Revenue and cost recognition on construction and long term service contracts is currently under review. The Group will assess if any material impact can derive from the adoption of IFRS when an interpretation about the combination or segmentation of contracts currently considered by the IFRS Interpretation Committee is released.

Reclassification of penalties and claims as reduction of sales instead of increase in costs will reduce future revenues on contracts subject to such penalties, if any.

Some other reclassifications in the presentation of construction contracts in the balance sheet are likely to occur.

Financial instruments

Derivative instruments will have to be recorded at their fair value in the balance sheet, whatever the nature of the underlying asset or liability.

The new standards will mainly affect foreign currency hedges: currency derivative financial instruments which will not meet the documentation and effectiveness criteria required by the standard will be recorded without any corresponding offset by the recognition of the fair value of hedged items. Such a situation will generate volatility in income from operations.

There will be major implications for accounting systems, as hedging instruments are required to be reviewed with the underlying assets or liabilities to which they relate.

Due to the complexity of processes to be implemented to satisfy the IFRS requirements on financial derivatives, the group has decided, as authorised by IFRS1 First time application of IFRS, not to apply IAS 32-39 (Financial instruments) in the comparative data to be prepared for the fiscal year 2005.

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Consolidation scope

IFRS requires a controlled special purpose entity to be consolidated, even in cases where the group owns no shares in this entity.

The French Standard, presently in force and applied by the group, demands consolidation, only if the group owns a share in the entity.

Starting from financial years beginning after 31 March 2004, the requirement of the French Law will be the same as IFRS.

This modification will result in an increase of assets and financial debt.

Business combinations

As permitted by IFRS1, the group has elected not to restate past business combinations according to IFRS.

Under the new standard, goodwill will no longer be amortised. Impairment tests will have to be performed at transition date and at regular intervals, at least, yearly.

Presentation of financial statements

The aggregation in the profit and loss account of items of income and expense as non-operating income or expense is prohibited by the IFRS. These items will have to be included in the income from operations. Income and expenses from discontinued operations will be presented on a single line as soon as the sale is highly probable, while they are presently part of the group's operations until the effective date of disposal.

Changes in the presentation of the balance sheet will mainly result from the distinction between current and non-current items and from some reclassifications in working capital items. Assets and liabilities included within a disposal group classified as held for sale will be presented separately.

SIGNIFICANT DIFFERENCES BETWEEN ACCOUNTING PRINCIPLES GENERALLY ACCEPTED IN FRANCE AND IN THE US

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As a foreign registrant on the New York Stock Exchange, we prepare a reconciling table of net income and shareholders' equity from French GAAP to US GAAP for inclusion in our Annual Report on Form 20-F filed with the Securities and Exchange Commission (SEC).

The main differences related to net income, liabilities and shareholders' equity are as follows:

Accounting for restructuring costs The conditions under which a liability can be recorded are different than those that prevail under French GAAP. We record a liability related to a restructuring plan whenever the plan is finalised, approved by management and announced before the closing of the financial statements. In US GAAP, exit costs are accrued as a liability when an announcement is made to employees prior to the closing date. In addition, some costs that are recorded as restructuring costs under French GAAP are classified under cost of goods sold in US GAAP (inventory write offs which result from restructuring plans). Finally, the Group applied since the 1 January 2003 the SFAS 146. This statement requires that a liability for costs associated with exit or disposal activities be recognised at fair value when the liability is incurred rather than at the date an entity commits to a plan of restructuring.

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Valuation and accounting of financial instruments Under French GAAP, profit and losses on financial instruments considered as hedges of our interest rate and forward exchange rate risks are recorded in the same period as the hedged item. The US standard SFAS 133, which is applicable to us since 1 April 2001, requires that all derivatives are recorded at their fair values in the balance sheet. The change in fair value of these derivatives is recorded in the income statement. If, under certain criteria, the derivative is qualified as a hedge, the effect in the income statement resulting from the change in fair values is compensated by the income or loss generated by the change of the value of the underlying item.

Business combination The allocation of purchase price to assets and liabilities acquired or assumed following an acquisition can be revised under French GAAP until the end of the fiscal year following the fiscal year of an acquisition, whereas, according to US GAAP, such revision can only be made within the 12-month period following the acquisition. This difference in principles has reduced the goodwill recognised at the time of the acquisition, on 11 May 2000 of the 50% remaining stakeholding of ABB in the joint venture ABB ALSTOM POWER, renamed Power.

Pension, termination and post-retirement benefits-defined benefit plan The Group determines its costs and accruals in accordance with actuarial techniques compliant with the methodology stated by SFAS 87, *Employers Accounting for Pensions*, and SFAS 106, *Employers Accounting for Post Retirement Benefits Other Than Pensions*. Minimum liability adjustments (MLA) are not recognised in the Group's financial statements as under French GAAP the recognition of these adjustments is not required. Under US GAAP the Minimum Liability Adjustment is recognised through the net equity.

Financial debt Certain items which are not necessarily recorded as financial debt under French GAAP, such as capital leases, are recorded as financial debt under US GAAP. Financial debt is also increased under US GAAP with the consolidation of special purpose entities which are not consolidated under French GAAP.

Valuation of Goodwill Beginning 1 April 2002, the Group adopted SFAS 142, *Goodwill and Other Intangible Assets*. As a result, goodwill is no longer amortised. Instead the Group periodically evaluate goodwill for recoverability. The Group has determined that no potential goodwill impairment existed as at 31 March 2003 and 31 March 2004, the annual testing date, following the adoption of SFAS 142.

Valuation of deferred tax assets In certain circumstances there can be differences arising between French GAAP and US GAAP as a result of interpretation of US accounting rules. In the year ended 31 March 2004, the Group in interpreting US accounting rules concluded that full valuation allowance for deferred tax assets is required under SFAS 109 *Accounting for Income Taxes*.

Net deferred tax assets accordingly were subject of a full valuation allowance in the US GAAP accounts for the year ended 31 March 2004 but not in the French GAAP accounts. This interpretive judgement under US GAAP reflected the uncertainty surrounding the implementation of the financing package and the resultant issues concerning the financial condition of the Group and produced an uncertainty which led to the requirement to take a valuation allowance against all the net deferred tax assets of the Group.

Other than in these circumstances, differences in deferred tax accounting between French and US GAAP should not be material.

In addition to the matters described above that impact net income, liabilities and shareholders' equity, there are other differences in accounting principles between French GAAP and US GAAP that may materially affect the presentation of the balance sheet and income statement.

IMPACT OF EXCHANGE RATE AND INTEREST RATE FLUCTUATIONS

Our policy is to use derivatives, such as forward foreign exchange contracts, in order to hedge exchange rate fluctuations and, to a much lesser extent, interest rate fluctuations. Our policy does not permit any speculative market position.

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We have implemented a centralised treasury policy in order to better control the company's financial risks and to optimise cash management by pooling our available cash, thereby reducing the amount of external debt required and permitting us to obtain better terms under our various financing arrangements.

The Corporate Treasurer reports directly to the CFO and has global responsibility for foreign exchange risk, interest rate management, intra-group financing and cash management. He managed a team of about 27 people in fiscal year 2004 located in the Paris Headquarters. Corporate Treasury is organised in a Front-Office or Dealing Room, a Middle-Office and a Back-Office to ensure segregation of duties. In addition to this, a small team operates the netting of intercompany payments and prepares a weekly cash forecast. A network of Country Treasurers supports Corporate Treasury in the countries where we have a significant presence.

Corporate Treasury acts as an in-house bank for subsidiaries by providing hedging and funding and maintaining internal current accounts. We have implemented cash pooling structures to centralise cash on a daily basis in the countries where local regulations permit it.

Corporate Treasury uses the Reuters CashFlow Treasury Management System for straight-through processing of treasury transactions from dealing to settlement and management of in-house banking activity. Our Treasury Management System is interfaced with SAP for automatic generation of accounting entries. The Dealing Room is equipped with a Reuters Information System for real-time market data and uses a professional telephone dealing system provided by Etrali to tape all exchanges with banks' dealing rooms. A dedicated Information Technology team administers Treasury systems and guarantees back-up and contingency plans.

The Middle Office monitors the Dealing Room activity, guarantees that no open positions are maintained, and produces regular risk reporting.

Exchange rate risks

In the course of our operations, we are exposed to currency risk arising from tenders for business remitted in foreign currency, and from awarded contracts or firm commitments under which revenues are denominated in foreign currency. The principal currencies to which we had significant exposure in fiscal year 2004 were the US dollar, British Pound and Swiss Franc. We hedge risks related to firm commitments and tenders as follows:

by using forward contracts for firm commitments;

by using foreign exchange derivative instruments, for tenders, usually pursuant to strategies involving combinations of purchased and written options; or

by entering into specific insurance policies, such as with Coface in France or Hermes in Germany.

The purpose of these hedging activities is to protect us against any adverse currency movements which may affect contract revenues should the tender be successful, and to minimise the cost of having to unwind the strategy in the event of an unsuccessful tender. The decision whether to hedge tender volumes is based on the probability of the transaction being awarded to us, expected payment terms and our assessment of market

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conditions. Under our policy, only senior management may make such decisions.

When a tender results in the award of a contract, we hedge the resulting net cash flows mainly in the forward markets or, in some exceptional cases, keep them covered under insurance policies. Due to the long-term nature of our business, the average duration of these forward contracts is approximately 12-14 months. We may, in some circumstances, enter into forward foreign exchange contracts of a shorter maturity than the expected underlying currency flow. Such contracts are rolled over until the occurrence of the underlying flow. Although this provides adequate protection against exchange rate fluctuations, we remain exposed to variations in the differential between the interest rates of the two currencies involved. The impact of such variations remains, however, relatively minor.

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We do not hedge our net assets invested in foreign operations. We monitor our market positions closely and regularly analyse market valuations. We also have in place counter-party risk management guidelines. All derivative transactions, including forward exchange contracts, are designed and executed by our central corporate treasury department, except in some specific countries where restrictive regulations prevent a centralised execution.

Interest rate risks

See Note 29(b) to the Consolidated Financial Statements for discussion of our interest rate risks and of sensitivity to interest rate variation.

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| | Nominal values | | | | Fair market values | | | |
|--|------------------------------|--------------|------------|-----------|------------------------------|--------------|------------|-----------|
| | Maturity as at 31 March 2004 | | | | Maturity as at 31 March 2004 | | | |
| | Total | < 1 year | 1-5 years | > 5 years | Total | < 1 year | 1-5 years | > 5 years |
| | <i>(in million)</i> | | | | | | | |
| BALANCE SHEET ITEMS | | | | | | | | |
| Assets | | | | | | | | |
| Loans, deposits and retentions | 798 | 282 | 102 | 414 | 782 | 282 | 102 | 398 |
| Other financial assets | 62 | | | 62 | 62 | | | 62 |
| Short-term investments | 39 | 35 | 4 | | 39 | 35 | 4 | |
| Cash and cash equivalents | 1,427 | 1,427 | | | 1,427 | 1,427 | | |
| Liabilities | | | | | | | | |
| Financial debt | 4,372 | 543 | 3,313 | 516 | 4,310 | 543 | 3,251 | 516 |
| OFF BALANCE SHEET ITEMS | | | | | | | | |
| Interest rate instruments | | | | | | | | |
| Interest rate swaps : receive fixed | 374 | 21 | 353 | | 18 | 1 | 17 | |
| Euro | 320 | | 320 | | 17 | | 17 | |
| US Dollar | 54 | 21 | 33 | | 1 | 1 | | |
| Foreign exchange instruments | | | | | | | | |
| Currency swaps Currency purchased | 2,728 | 2,705 | 23 | | (127) | (126) | (1) | |
| Australian Dollar | 89 | 89 | | | 2 | 2 | | |
| Swiss Franc | 716 | 706 | 10 | | (3) | (2) | (1) | |
| Czech Koruna | 55 | 55 | | | 1 | 1 | | |
| British Pound | 233 | 232 | 1 | | | | | |
| Polish New Zloty | 72 | 65 | 7 | | | | | |
| Swedish Krona | 78 | 73 | 5 | | | | | |
| US Dollar | 1,401 | 1,401 | | | (128) | (128) | | |
| Other Currencies | 84 | 84 | | | 1 | 1 | | |