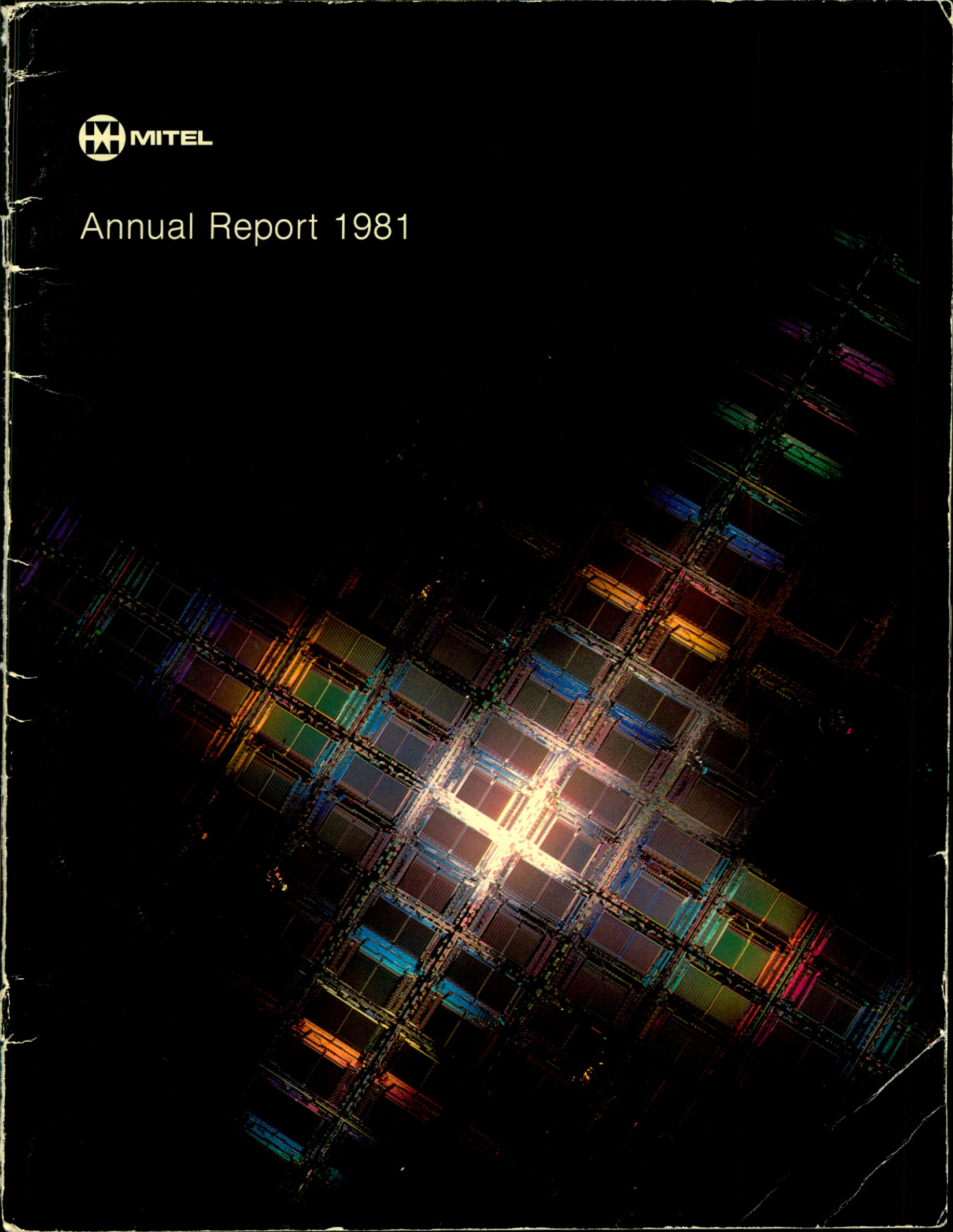
MITEL

Annual Report 1981



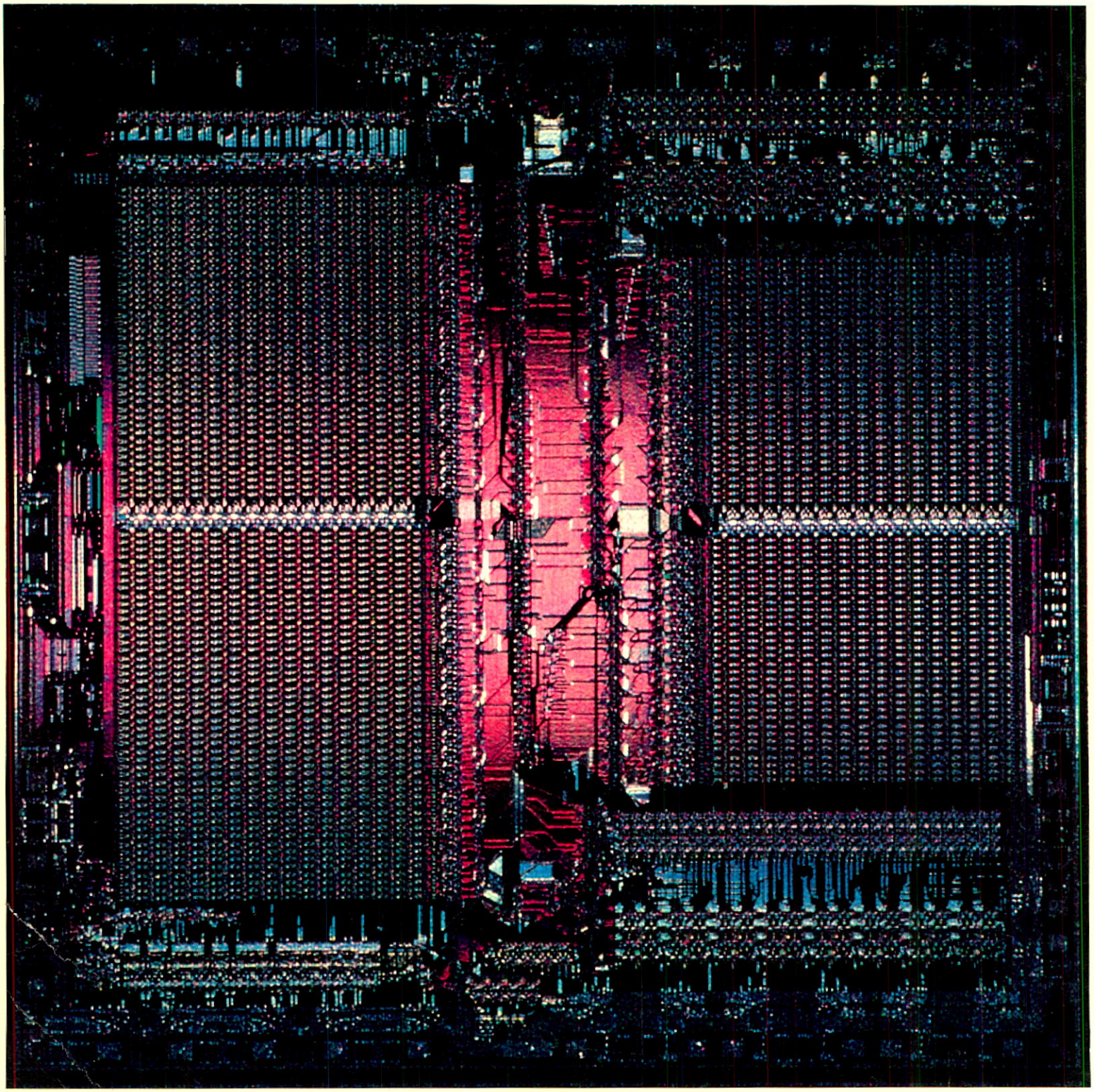


Table of Contents

Financial information herein is expressed in Canadian dollars, unless otherwise stated. For the exchange rate of the Canadian dollar please refer to the Financial Summary on page 40.

MT 8980, the DX chip is a powerful and versatile digital telecommunications switching chip (integrated circuit) which will accommodate data and voice traffic in the SX-2000 SUPERSWITCH, an office of the future business communications system to be introduced at the end of this year.

The chip is configured with a switching matrix which provides 65,356 switching cross-points or connection paths. Roughly .27 inches square, this chip is a critical component in the SX-2000, a digital switching system which will accommodate well over 10,000 lines with considerable flexibility.

The front cover is a study of light reflection and refraction on the surface of a silicon wafer of DX chips before the wafer has undergone its final fabrication process, the application of a protective coating.

The Company

Mitel started operations in 1973. The Company designs, develops, manufactures and markets electronic telecommunications equipment and integrated circuits. Since 1978, the primary product line of Mitel has been microprocessor-controlled telephone switch boards (private branch exchanges or "PBX's"), which connect commercial telephone users with public and private telephone networks.

The first Mitel product was the tone receiver, an electronic device for translating musical tones into electronic signals used to switch calls, control external equipment and interface with computers.

In 1975 Mitel combined tone receiver technology with integrated circuit technology to produce a tone-to-pulse converter, permitting telephone companies to offer modern touch tone phones in areas where central switching equipment can only receive rotary dial signals.

The Mitel telecommunications product line also includes devices to improve the service of existing telephone systems, such as intercoms, toll denial systems and call monitors.

Advanced integrated circuit technology developed by Mitel is the heart of the innovative features and performance of Mitel products.

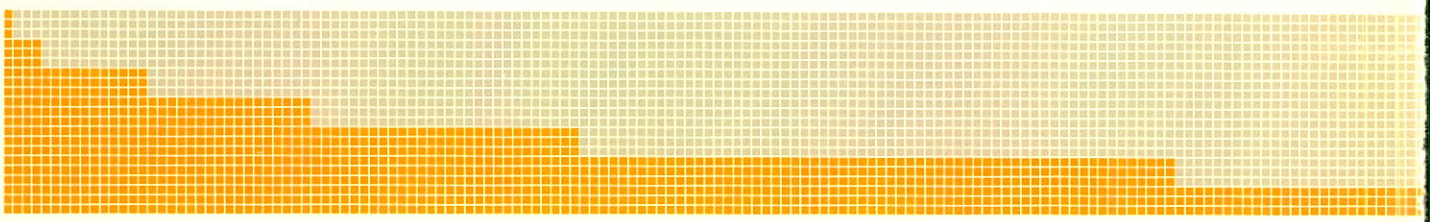
Annual Meeting

The Annual and Special Meeting of shareholders of the Company will take place at 4:30 p.m., Friday, July 24, 1981 at the Chateau Laurier Hotel in the city of Ottawa, Ontario.

Corporate Highlights

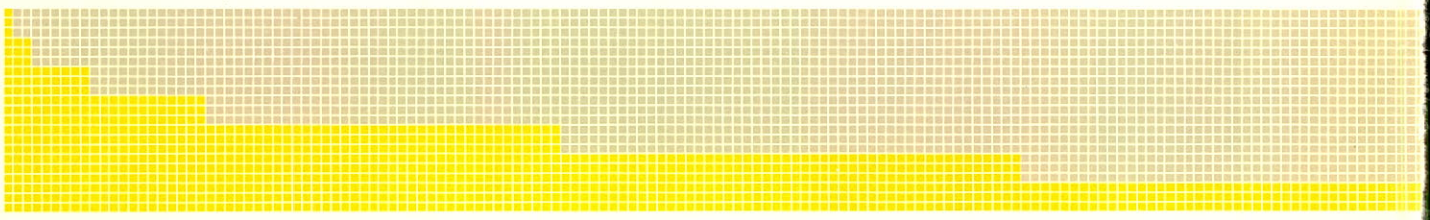
Total Sales × $1,000,000

75	.3
76	1.5
77	5.4
78	11.5
79	21.6
80	43.4
81	**111.2**



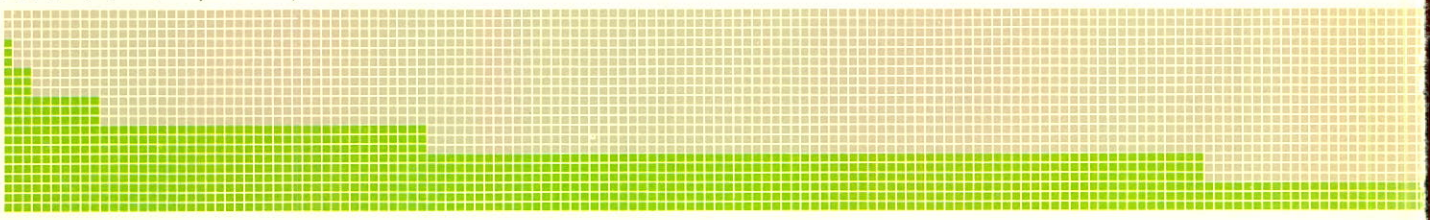
Net Income × $1,000,000

75	.03
76	.16
77	.5
78	1.1
79	3.1
80	5.6
81	**17.3**



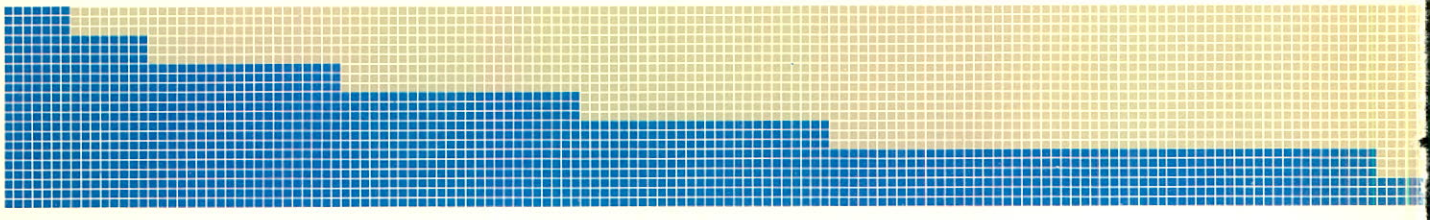
Net Worth × $1,000,000

75	(.01)
76	.14
77	.6
78	1.9
79	8.7
80	25.0
81	**60.2**



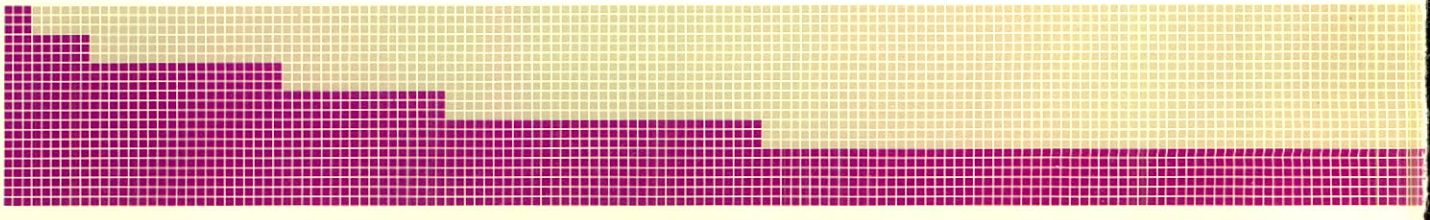
Total Plant Area × 1,000 ft^2

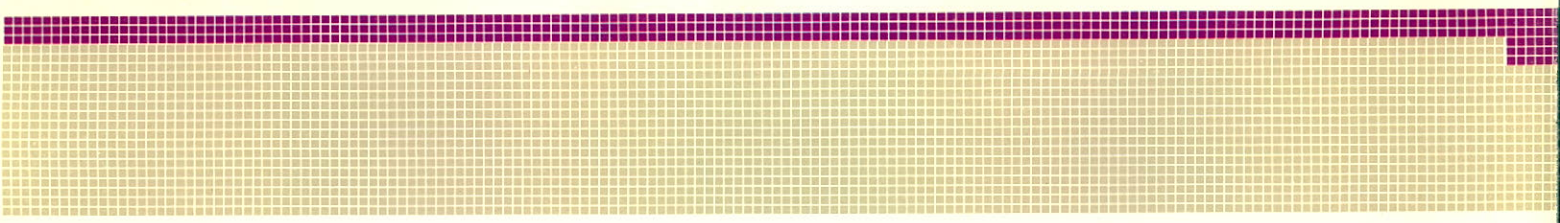
75	10
76	25
77	60
78	70
79	150
80	250
81	**550**

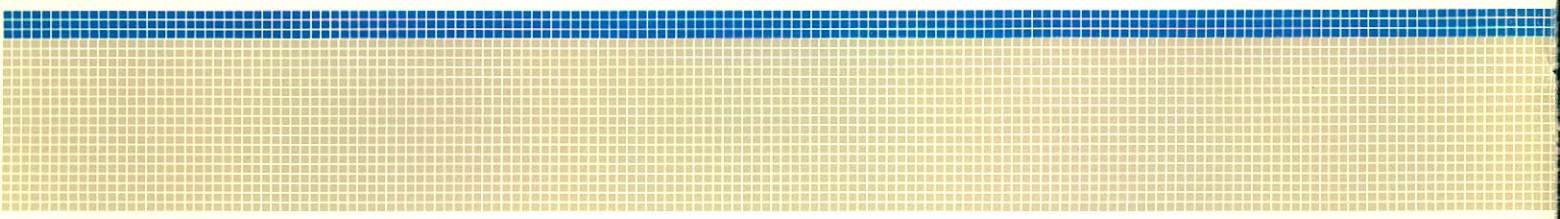


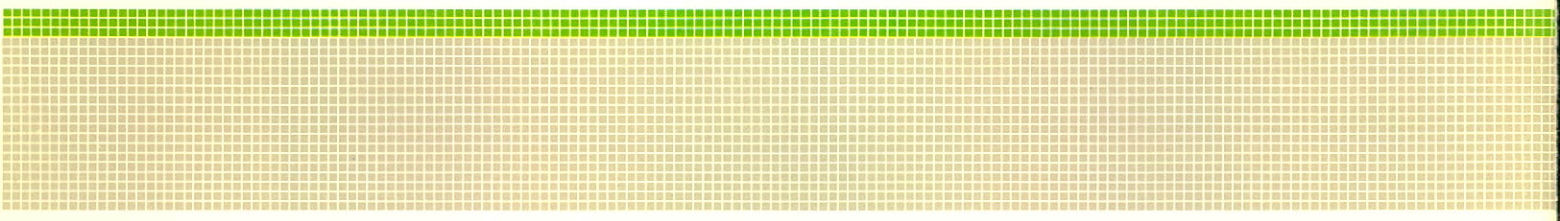
Total Employees

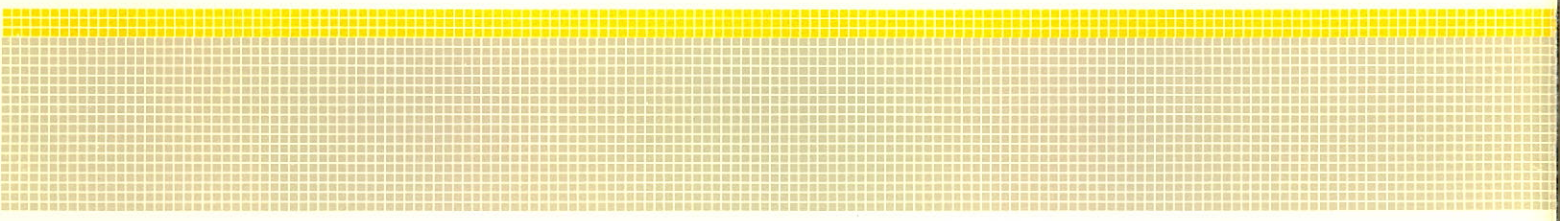
75	30
76	80
77	230
78	370
79	640
80	1240
81	**2500**

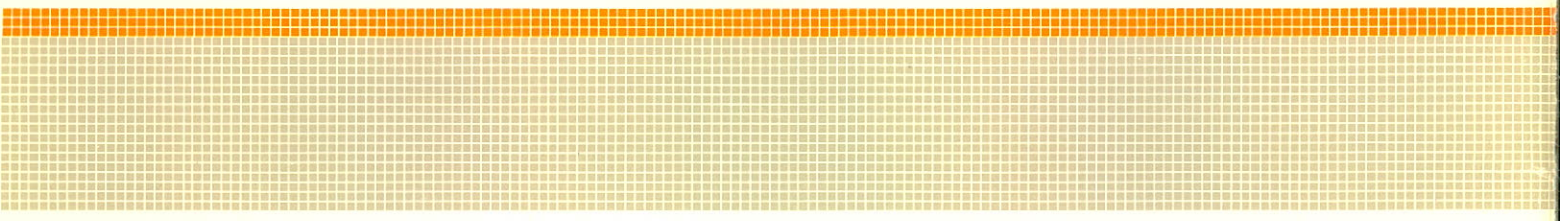




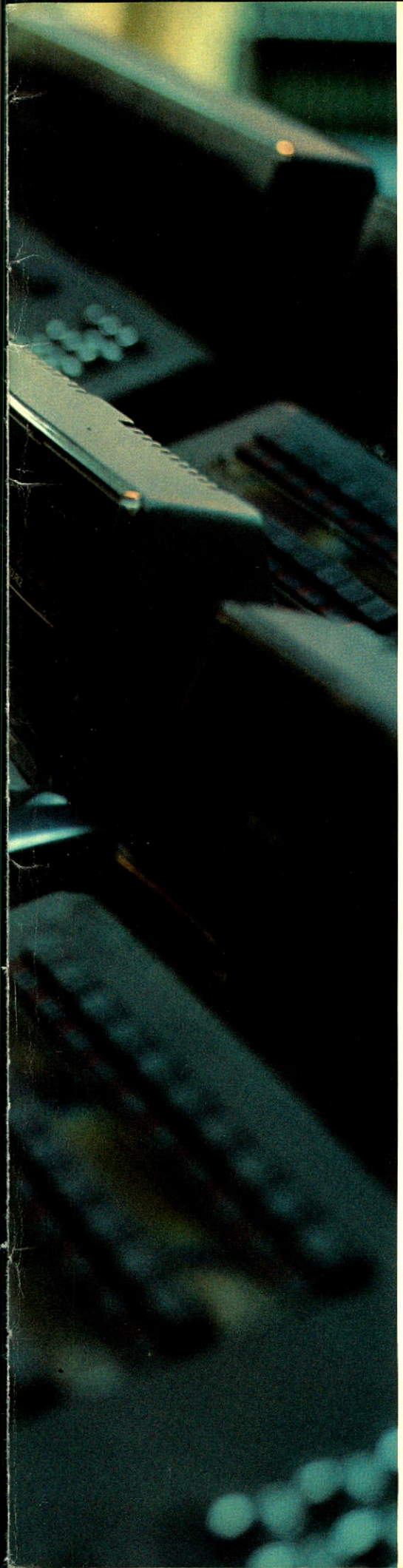








The President's Message



New SX-200/SX-100 Attendant Consoles awaiting shipment.

Fiscal 1981 was an excellent year for Mitel. Sales increased 156 percent to $111.2 million from $43.4 million last year, and profits rose 210 percent from $5.6 million to $17.3 million, the seventh consecutive year in which earnings virtually doubled. Given the enormous size of the telephone equipment marketplace and the opportunities which it presents, the company believes that the leading edge technology of Mitel will help to continue this smooth pattern of consistent growth.

Mitel is one of the world's leading suppliers of PBX equipment, and total market share more than tripled over the past year in North America by offering a flexible range of PBX products to appeal to a wide cross-section of telephone equipment users. The PBX line is currently expanding from five extension lines to well in excess of 10,000 extensions. Mitel is shipping at an annualized average rate of 100,000 telephone extension lines per month.

Mitel is a growth company in a growth industry. New opportunities are almost unlimited. The telecommunications marketplace offers three areas of growth potential for Mitel products: hotels-motels, businesses and homes. The process alone of upgrading existing switching systems to become more cost-effective and efficient represents a potential volume of business in a world market estimated to be about $6 billion. In many cases, existing equipment is 20 or even 30 years out of date.

North America has approximately 70 telephones per hundred people, Western Europe about 35 and the Third World less than one per hundred. The long-term potential of the Third World marketplace is enormous, both in the public and private switching areas. The small size and energy efficiency of Mitel equipment are characteristics very attractive for this market area.

One of the main ingredients in the success of Mitel has been the ability to design and manufacture specialized telecommunications chips.

In 1976, Mitel made the crucial decision to acquire an integrated circuit manufacturing facility.

In the past year, refinements to the ISO-CMOS™ technology pioneered by Mitel have improved the process which combines low-power operation with high-speed digital and voice transmission on the same chip. Also ISO-CMOS is now accepted as one of the optimal technologies for standard application in telecommunications integrated circuits world-wide.

Four major corporations in the telecommunications industry have licensed the Mitel ISO-CMOS technology and related products. Licensing agreements create valuable second, or alternative, sources for customers who integrate Mitel semiconductor devices into their products.

On May 18, 1981, Mitel common shares were listed on the New York Stock Exchange. Meeting the standards for listing enhances the financial prestige and the image of Mitel in the United States among large prospective customers and among a broader base of potential shareholders. In the past year, the Mitel ticker symbol also appeared for the first time on the Montreal and London Stock Exchanges.

Presence in the U.S. financial market assisted distribution of the recent public offering of 3.8 million common shares in the U.S. and Canada. Net proceeds from the offering will be used in part to repay interim short-term borrowings for financing an international expansion program. The remainder will be applied to finance working capital, further expansion and capital equipment.

The expansion program has facilitated growth in all operational areas. Approximately 500,000 square feet are under construction. A commitment to building for the future with Company-owned facilities gives Mitel the opportunity to invest in working environments which are both efficient and pleasing to employees.

A question frequently asked is how a bigger Mitel is going to avoid becoming slow-moving and sluggish. The answer is simple: a strong emphasis on office and plant automation, and a keen avoidance of bureaucratic obstructions.

An open door policy and team management at all levels is very much alive at Mitel; everyone is on a first name basis.

The overall aim is to achieve regularly established common goals and, in the process, make it fun to work. The spirit and dedication of Mitel employees, now over 2,500 strong, is the key to success. Mitel encourages all employees to recommend improvements for higher efficiency — contributions from all sources are impressive.

Universal profit-sharing and stock purchase programs, and outstanding achievement awards extend to employees throughout Mitel world-wide. The quality of this fast-moving team can only inspire confidence in the future of Mitel.

Dr. Michael C.J. Cowpland
President
May 29, 1981

Thick-film Hybrid
Facility expansion
under construction
in Kanata, Ont.

Marketing Overview

The Company's business grew significantly this year, with increased penetration worldwide, through growth in both product range and geographic market coverage.

The reputation that Mitel has established throughout the world for outstanding product value and functionality continues to spread. Accordingly, demand for the wide range of devices and systems which Mitel produces is increasing.

During the year, Mitel established new business offices in fifteen locations around the world — eleven in the United States, two in Canada, one in Europe and one in New Zealand.

Mitel telecommunications products are sold directly to private and government telephone companies. They are also sold indirectly through independent distributors who sell to telephone companies, private network users and installation companies. When products are purchased through distributors, Mitel provides servicing assistance and technical backup, and trains customers to install and maintain the equipment.

Thick-film Hybrid Laser Trimmers in Kanata, used in the trimming of ink resistors.

A central part of the Mitel marketing effort is mass producing manuals and brochures to educate distributors and purchasers about technology and equipment. During 1980, Mitel pioneered the world's first fully electronic system which publishes annually, millions of pages in English — and using computer-aided translation — French, Spanish and German.

Telecommunications product sales by any manufacturer largely depend on the ability to offer devices which can improve service or replace equipment telephone companies already have in use. Evaluation of a product for standardization throughout a network is a lengthy process because of the costs and long-term commitment involved. Once a customer tests and then approves, or accepts, a product, the device's standardization throughout the network becomes the foundation of its future with that purchaser.

The Mitel product line has been designed to accommodate different technical and feature standards for equipment throughout the world. Innovation in product design coupled with good product availability to meet delivery commitments has made Mitel a leader among PBX suppliers.

During the last year, important decisions to standardize on Mitel products included:

— Negotiations with British Telecom to supply a minimum $28 million in SX-200™ switching equipment, as well as a number of SX-20™ PBX systems.

— Approval, or acceptance, of the SX-200 by seven Bell Operating Companies in the United States for tariff filing with state regulatory authorities to establish rental rates for Bell System customers who use the equipment. This brings the number of Bell Operating Companies standardized on the SX-200 product family to 11.

— Acceptance of the SX-20 by two U.S. Bell Operating Companies.

— Standardization of the SX-200 by every major operating telephone company in Canada during 1980. Also most of the Canadian telephone companies are either in the process of evaluating the SX-20, or have already approved the product.

The Mitel line of interface products continues to provide specialized equipment for telephone company signaling systems. The growth in this product line, though not as dramatic as the PBX line, continues to be very encouraging.

Although most Mitel integrated circuits are for in-house use, they are also sold to other telecommunications and industrial electronic equipment manufacturers for incorporation into their products. Five percent of Mitel sales were derived this year from semiconductor products. The Mitel tone ringer and touch-tone receiver integrated circuits represented the largest volume of sales.

By establishing business offices in key world markets, by keeping accessible and visible in these areas through trade shows and by providing product support in major languages, Mitel is ideally positioned in the telecommunications marketplace.

Terence H. Matthews
Executive Vice President

54°C(130°F)Burn-in Room for Heat Testing SUPERSWITCH systems and sub-assemblies.


SUPERSWITCH
SUPERSWITCH

Telecom and Switching Divisions

The Telecom and Switching Divisions are proud of their achievement of meeting the targets and objectives for fiscal year 1981.

Today, most telephone switchboards are microprocessor-controlled systems which are far advanced from the older manually-operated "cordboards" and later automatic electro-mechanical systems. Mitel is in the forefront of PBX technology and manufactures state-of-the-art microprocessor-controlled systems using analog signal switching with a capability of handling from eight to 208 telephone extension lines.

Four new Superswitch™ systems are presently in various stages of design and development. Last year and this spring, Mitel introduced prototypes for the small-line-size market which represents about 60 percent of the total market. The new products are called SX-10™, Super 10™, SX-5™ and SX-2™.

Both the SX-10 and Super 10 are designed for small hotels and motels, small businesses and homes. They are intended to provide service for up to 16 extensions and up to eight outside lines or trunks. The SX-10 and Super 10 feature electronic voice synthesis to provide the user with certain audible information. The Super 10 is the world's first PBX system housed inside a receptionist's console. Full production of the SX-10 and Super 10 products is scheduled for the fall of 1981.

The SX-5 is a very small PBX which can be mounted on a wall and can handle up to six extensions and two trunks. It represents the most practical system in its size while retaining maximum feature flexibility for the user.

The SX-2 is a single-trunk device designed specifically for private homes. Its features include intercom and controls to govern, for example, door opening, thermostat override and outdoor lighting — just by using the telephone, even miles away from home.

SX-200/SX-100 Production Test area, Boca Raton, Florida.

During the decade of the Eighties, the Office of the Future is expected to create a hundred-billion-dollar market for PBX systems. The newest Mitel product, the SX-2000™ digital and data voice switch is expected to play a key role in this evolving marketplace.

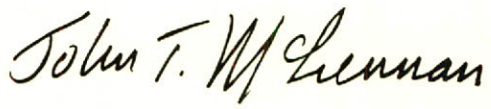
Our research indicates that when it goes into production next year, the SX-2000 promises to be one of the most advanced machines available because of its size, efficiency and additional features including the capability of routing data from one extension to another. It has a capacity well in excess of 10,000 lines. The modular design enables the SX-2000 to be adapted to more sophisticated markets when necessary because considerably greater capacity can be added.

Sales of PBX products, which had accounted for about 22 percent of total sales in fiscal 1979, now represent almost 80 percent of total sales. This rapid growth in volume would not have been possible without the commitment of Mitel to sophisticated management control systems. The major benefits of these systems have been in controlling inventory and providing timely, comprehensive management information. For example, automated planning for materials, handling and distribution has enabled production lead time to track the market demand for the Mitel product line to a manageable time frame within the production rate increases of Mitel.

Further automation in assembly and improved manufacturing procedures has helped to more than double production. Automatic testing equipment developed in-house has contributed in an indispensable way toward increasing levels of efficiency.

With plans to more than double overall production again in the coming fiscal year, Mitel will add about half-a-million square feet of manufacturing space. As part of this expansion, Kanata Switching Operations will move into two new plants (totalling 260,000 square feet) by July 1981; and Puerto Rican employees will move into a 130,000-square-foot facility in Bayamon by October 1981. In the United Kingdom, construction of a new 165,000 square-foot facility began at Caldicot, South Wales in April 1981 with completion scheduled for spring 1982.

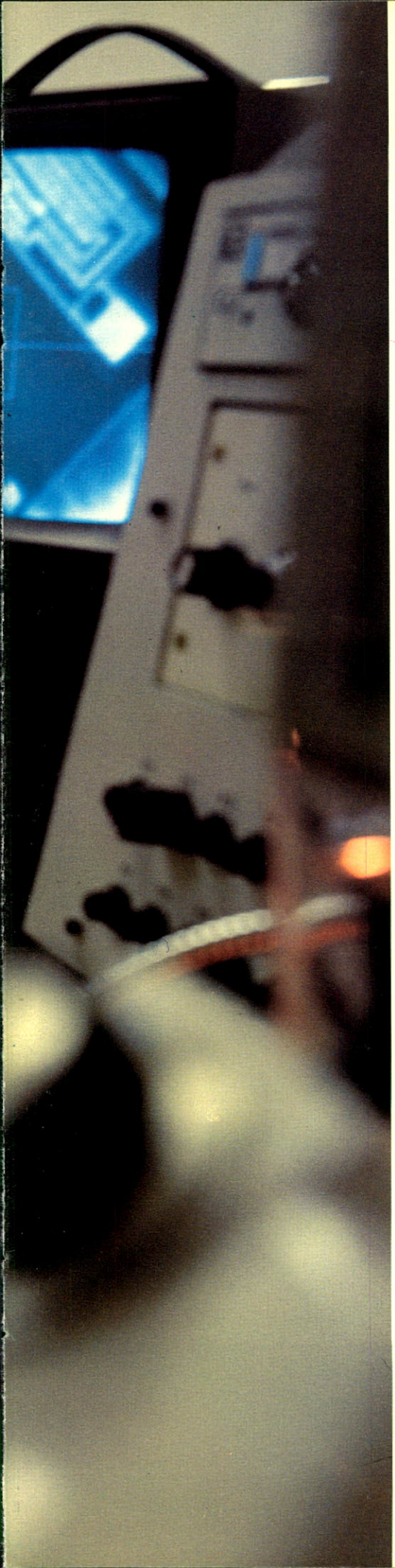
The Telecom and Switching Operations teams are confident that production targets can be met. The powerful combination of strategically designed products, automated manufacturing systems and motivated people promises outstanding success for the coming year.



John T. McLennan
Vice President, Operations

100,000 square foot Mitel, Boca Raton facility.

130,000 square foot Mitel, Puerto Rico facility.



Semiconductor Division

During the year the Semiconductor Division achieved significant progress in all fields of operations. Production output doubled, four cross-licensing technology agreements were signed, the semiconductor facilities were expanded, and new integrated circuit and thick-film hybrid products emerged from the Research and Development groups.

Integrated circuits are manufactured using silicon of extremely high purity in a rigorously controlled environment. Thick-film hybrids are miniature highly precise electronic circuits with excellent thermal stability which cuts the size and cost of electronic systems.

Licenses are reciprocal agreements to co-operate and share information about product development and technology improvements. Mitel has signed cross-licensing agreements in the United Kingdom for ISO-CMOS technology with British Telecom (formerly the British Post Office), The Marconi Electronic Company Ltd. and The Plessey Company Limited. Both Marconi and Plessey have licensed most of the Mitel integrated circuit products using ISO-CMOS with intentions to second source manufacture and sell these products to the general marketplace.

In January 1981, Mitel signed a similar licensing agreement with GTE (General Telephone and Electronics Corporation), the largest independent telephone company in the U.S. GTE plans to have its GTE Microcircuits Division located in Tempe, Arizona manufacture and sell the licensed products.

In June 1980, operations began in the Foreign Trade Zone of Burlington, Vermont where part of the manufacturing process takes place for integrated circuits and thick-film hybrids supplied mainly to Mitel Telecom and Switching Divisions. The foreign trade zone minimizes the costs of transferring components between our Canadian and U.S. plants. Plans are underway to add an additional plant with 60,000 square feet in the Burlington area. This facility will primarily assemble and test in-house integrated circuits and eventually fully produce thick-film hybrids.

High reliability assembly of ICs in Bromont, Quebec.

Manufacturing facilities are being expanded in both Kanata, Ontario and Bromont, Quebec. In Kanata, a 96,000-square-foot addition is under construction. This plant will house an expanded thick-film hybrid operation and a modularized, superclean manufacturing line for very large scale integrated (VLSI) circuit products. Automated process, assembly and test equipment will enable the high-volume manufacture of VLSI circuit products.

In Bromont, Quebec, 49,000 square feet of manufacturing space is being added. The Bromont plant is dedicated to the manufacture of both large scale integrated circuit (LSI) and VLSI products.

By mid-1981, the Semiconductor Division will have over 180,000 square feet of manufacturing space in operation. By early 1982, this area should grow to over 250,000 square feet.

The most important new VLSI product developed by Mitel is the DX integrated circuit, the digital switching chip to be used in the SX-2000. It permits the switching of 65,536 switch points digitally on a single chip approximately 1/4 inch square.

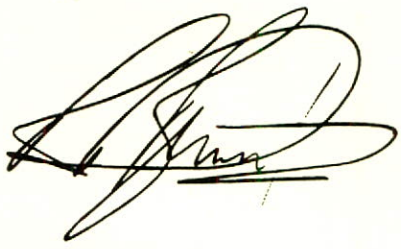
Also being developed for use in the SX-2000 is a codec (encode/decode) and filter chip, which uses an enhanced ISO-CMOS technology and switched-capacitor techniques. This chip combines two functions: 1) converting signals from analog to digital, and from digital back to analog (the codec function) and 2) receiving signals and filtering out extraneous frequencies (the filter function).

In 1980, Mitel successfully introduced 21 microprocessor interface ISO-CMOS products, designed to replace the industry's standard 54/74 LS Bipolar Octal (8-bit) products where low power is an advantage. Mitel is also manufacturing a high-speed, low-power ISO-CMOS 16K-bit read-only memory (ROM), a version of the standard NMOS 2316 ROM, which is a factory-programmed device for storing operating instructions or data.

Our research and development activities during the past fiscal year concentrated on three main areas: new technologies or improved manufacturing processes; LSI and VLSI products primarily for telecommunications applications; and thick-film hybrid technology to replace larger electronic circuits.

One example of the improvements which have been made through further developments in the Mitel ISO-CMOS process is the reduction of topological geometries to two microns on silicon wafers of five inches in diameter from the current industry standard of five microns on four-inch wafers. This improvement, which includes work in N-well CMOS and double-layer metallization, results in greater circuit density.

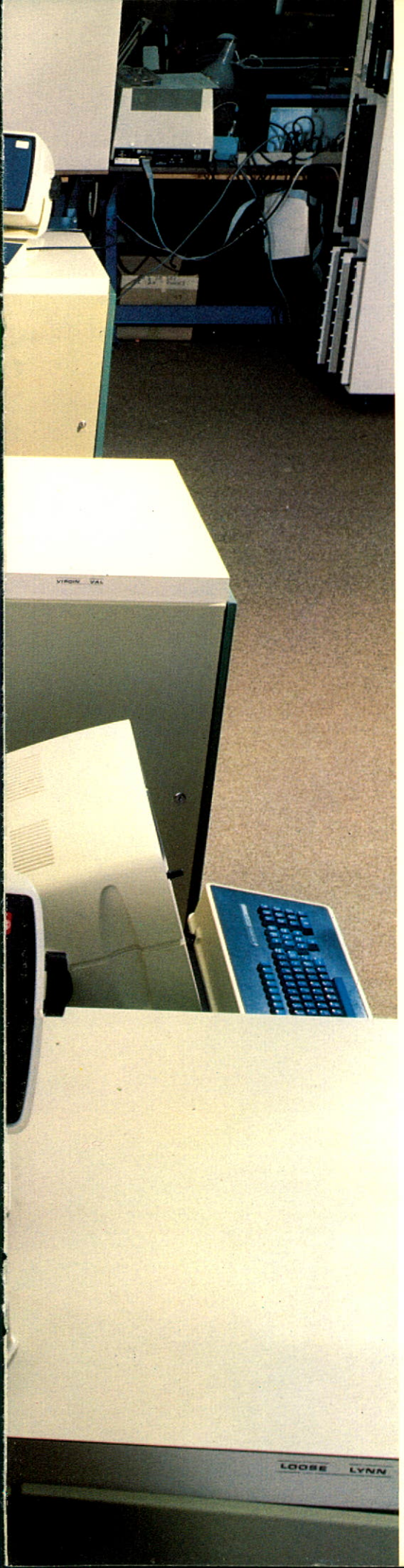
The Semiconductor Division is in the strongest position ever to carry out an energetic marketing, manufacturing and development program. The abilities and commitment to succeed are proven and we look forward to the coming year.



Ralph A. Bennett
Vice President and General Manager
Semiconductor Division

Fully automated IC bonders at Mitel Semiconductor.

Financial Review



High speed test systems for PABX sub-assemblies.

In fiscal 1981, Mitel met sales targets and exceeded earnings objectives which had called for $105 to $115 million in sales and $13 to $15 million in after-tax profits. Other sections of the Annual Report highlight success in meeting the operating targets. The financial results speak for themselves.

With earnings up 210 percent, net income as a percentage of sales was 15.5 percent. Earnings per share increased 179 percent over the prior year to $0.53, an increase moderated by a 7.3 percent dilution due to the public offering of June 1980.

The excellent public support of the Mitel stock offering in June 1980 raised approximately $16 million in working capital and helped fuel continued growth. Subsequent market activity and positive pressure on the share price prompted a 3-to-1 stock split effective October 27, 1980; all earnings per share calculations have been revised accordingly.

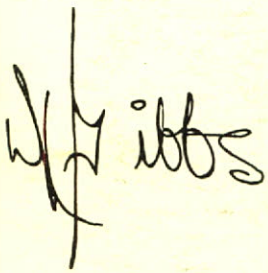
During fiscal 1981, $21 million was spent of a three-year $154-million expansion program to add new manufacturing facilities and capital equipment to meet anticipated demand for Mitel products. Of the remaining $133 million to be spent on the program, about $47 million is expected to be generated through low interest rate financing, as well as $13 million through government assistance grants. Part of the financing will also be provided by proceeds from the offering in May 1981 of 3.8 million common shares in North America and through internally generated funds.

During the last fiscal year, all the operating companies in the U.S. were merged into Mitel, Inc. Mitel established a new office in New Zealand and MITEL Mikroelektronik und Telefon GmbH was formed in West Germany. Mitel has progressively expanded manufacturing facilities to meet increasing product demand. By February 1981, Mitel was operating 12 plants in five countries.

The success of Mitel is directly attributable to the initiative, energy, and dedication of all employees. Locating, hiring, training and motivating people is a high priority, which is under the immediate direction of the President.

Mitel has instituted universal Stock Option and Stock Purchase Plans, Bonus Plans and a Profit-Sharing Plan to reward performance. In the last fiscal year, over $1.1 million was allocated for profit sharing to be paid to all employees, compared with $320,000 in the prior fiscal year.

Everyone at Mitel has moved into the new fiscal year with optimism. The coming year will bring many challenges, but we are confident that the consistent record of growth and financial stability will continue.



Donald R. Gibbs
Vice President, Finance

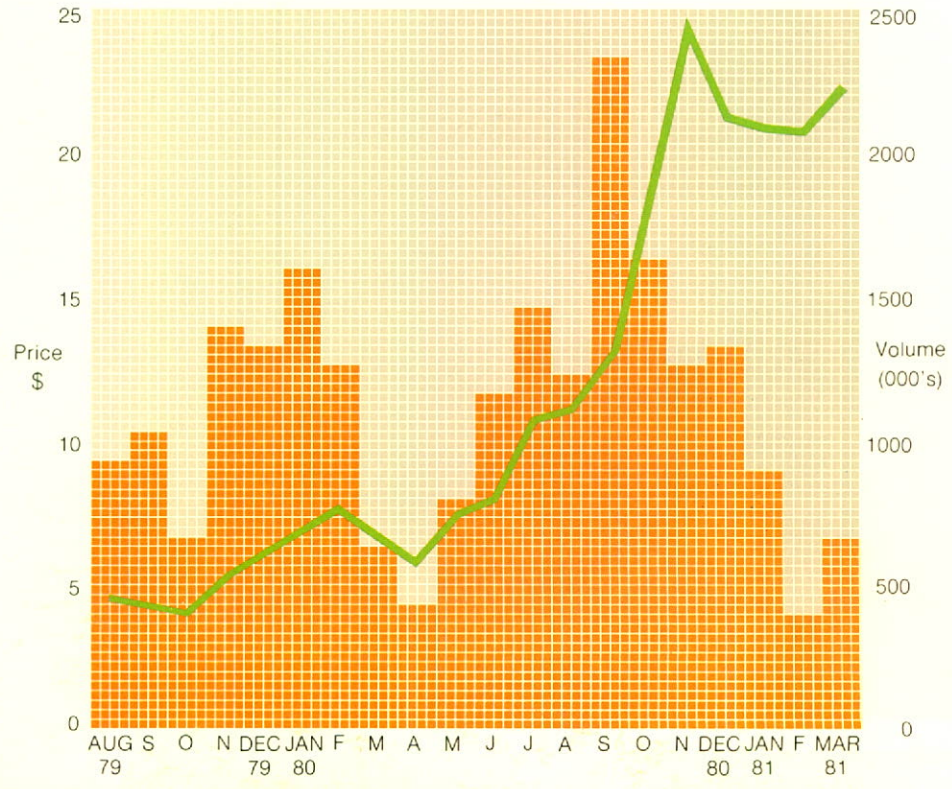
The Company's Common Shares are listed on the New York, Toronto, Montreal and London stock exchanges. The following table sets forth the high and low closing prices for the Common Shares and volume traded on The Toronto Stock Exchange, adjusted for the three-for-one split which was effective October 27, 1980 and on the New York Stock Exchange, where trading commenced on May 18, 1981.

The Company's first public offering of its Common Shares was made in Canada in July 1979 and trading of such shares on the Toronto Stock Exchange commenced on August 13, 1979. The closing price of the Common Shares on the New York Stock Exchange on May 28, 1981 was U.S. $35 1/2.

Price Range and Trading Volume of Shares

Period	Toronto High (Canadian Dollars)	Toronto Low (Canadian Dollars)	Toronto Volume
1979			
Third Quarter (from August 13)	$4 3/4	$4 1/8	1,955,718
Fourth Quarter	6 1/8	3 3/8	3,362,205
1980			
First Quarter	8 3/8	5	3,516,687
Second Quarter	8 7/8	5 3/4	2,415,156
Third Quarter	16	8 1/4	4,972,650
October	20	13 1/4	1,637,433
November	25 7/8	19 3/8	1,242,868
December	24 5/8	17 3/4	1,314,240
1981			
January	22 1/4	18 1/4	906,719
February	21 1/4	19 3/8	378,464
March	25 3/8	19 3/8	587,216
April	35 1/8	24 3/4	1,452,786
May 1 to 28	48 7/8	32 1/4	1,794,230

Period	New York High (U.S. Dollars)	New York Low (U.S. Dollars)	New York Volume
May 18 to 28	39 3/8	32 3/4	876,100



Computer Aided Design systems for the development of integrated circuits.

Financial Statements

Auditors' Report

To the Shareholders of
Mitel Corporation:

We have examined the consolidated balance sheet of Mitel Corporation as at February 27, 1981 and February 29, 1980 and the consolidated statements of income and retained earnings and changes in financial position for the five years ended February 27, 1981. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Company as at February 27, 1981 and February 29, 1980 and the results of its operations and the changes in its financial position for the five years ended February 27, 1981 in accordance with accounting principles generally accepted in Canada, applied, except as explained in Note 1(g) for the change in 1979 in accounting for development costs, with which change we concur, on a consistent basis.

Clarkson Gordon

Ottawa, Canada,
April 16, 1981.

Chartered Accountants

Consolidated Balance Sheets

Mitel Corporation
(Incorporated under the laws of Canada)

	February 27, 1981 (000's)	February 29, 1980 (000's)
Assets		
Current assets:		
Accounts receivable (notes 2 and 8)	$ 38,486	$ 13,128
Grants receivable (note 4)	1,106	1,334
Inventories (notes 3 and 8)	50,861	23,305
Prepaid expenses	432	244
Total current assets	90,885	38,011
Fixed assets (notes 4, 5, 8, 9 and 10)	49,390	12,913
Accumulated depreciation	(5,276)	(2,140)
	44,114	10,773
Deferred development costs (note 6)	6,232	2,698
Other assets (note 7)	1,650	518
Total assets	$142,881	$ 52,000
Liabilities and Shareholders' Equity		
Current liabilities:		
Bank indebtedness (note 8)	$ 35,826	$ 10,788
Accounts payable and accrued liabilities	24,145	9,392
Income and other taxes payable (note 15)	2,469	1,379
Current portion of long-term debt (note 9)	1,760	667
Total current liabilities	64,200	22,226
Long-term debt (note 9)	16,842	4,351
Deferred income taxes (note 15)	1,620	429
Total liabilities	82,662	27,006
Shareholders' equity:		
Capital stock (notes 11 and 12) —		
Issued: 1981, 33,286,473 shares; 1980, 30,901,473 shares	33,962	15,359
Retained earnings	26,257	9,635
Total shareholders' equity	60,219	24,994
Commitments (note 18)		
Total liabilities and shareholders' equity	$142,881	$ 52,000

On behalf of the Board:
(signed) M.C.J. Cowpland, Director
(signed) D. Cameron, Director

(See accompanying notes to the consolidated financial statements)

Consolidated Statements of Income and Retained Earnings

Mitel Corporation

	Years Ended				
	February 27, 1981 (000's)	February 29, 1980 (000's)	February 23, 1979 (000's)	February 24, 1978 (000's)	February 28, 1977 (000's)
INCOME					
Sales	$111,212	$ 43,411	$ 21,648	$ 11,528	$ 5,407
Expenses:					
Cost of sales (excluding depreciation)	53,443	21,381	10,195	5,351	3,777
Selling and administrative	24,772	11,256	5,340	2,934	99
Research and development	5,001	2,726	2,117	1,468	757
Less related government assistance	(766)	(1,055)	(1,003)	(427)	(208)
Depreciation	3,176	1,389	512	290	151
Interest—					
Long-term debt (note 9)	715	229	181	173	119
Other debt	2,875	378	254	92	3
Tender offer expense (note 14)	847	—	—	—	—
Income taxes (note 15)	3,887	1,545	1,031	441	193
Minority interest	—	—	(75)	60	15
	93,950	37,849	18,552	10,382	4,906
Net income for the year	$ 17,262	$ 5,562	$ 3,096	$ 1,146	$ 501
Earnings per share (note 13)	$ .53	$ .19	$ .12	$ .05	$ .02
RETAINED EARNINGS					
Retained earnings, beginning of year	$ 9,635	$ 4,887	$ 1,791	$ 645	$ 144
Net income for the year	17,262	5,562	3,096	1,146	501
	26,897	10,449	4,887	1,791	645
Stock issue expenses (net of tax recovery of $600,000 in 1981)	640	814	—	—	—
Retained earnings, end of year	$ 26,257	$ 9,635	$ 4,887	$ 1,791	$ 645

(See accompanying notes to the consolidated financial statements)

Consolidated Statements of Changes in Financial Position

Mitel Corporation

	Years Ended				
	February 27, 1981 (000's)	February 29, 1980 (000's)	February 23, 1979 (000's)	February 24, 1978 (000's)	February 28, 1977 (000's)
Working capital provided from:					
Operations—					
Net income for the year	$ 17,262	$ 5,562	$ 3,096	$ 1,146	$ 501
Items not requiring an outlay of working capital:					
Depreciation and amortization	3,764	1,593	554	290	151
Loss (gain) on disposal of fixed assets	34	(38)	(40)	—	(5)
Minority interest	—	—	(75)	60	15
Deferred income taxes	1,191	41	388	—	—
Total from operations	22,251	7,158	3,923	1,496	662
Increase in long-term debt	14,087	2,972	1,355	284	1,744
Minority interest investment in subsidiary	—	—	—	7	36
Proceeds from sale of fixed assets	38	90	939	—	27
Issue of shares (note 12)	18,603	11,550	3,710	98	—
Stock issue expenses	(640)	(814)	—	—	—
Miscellaneous	—	55	—	—	—
Total working capital provided	54,339	21,011	9,927	1,885	2,469
Working capital applied to:					
Additions to fixed assets	37,941	9,048	3,491	724	1,674
Less capital grants	(1,354)	(488)	(406)	(146)	(412)
Reduction of long-term debt	1,596	1,518	705	143	108
Investment	1,043	—	—	—	—
Acquisition of minority interest in subsidiary	—	—	44	—	—
Goodwill	—	—	307	—	—
Deferred development costs	4,081	2,290	606	—	—
Patents	116	130	65	—	—
Miscellaneous	16	—	44	56	77
Total working capital applied	43,439	12,498	4,856	777	1,447
Increase in working capital	10,900	8,513	5,071	1,108	1,022
Working capital, beginning of year	15,785	7,272	2,201	1,093	71
Working capital, end of year	$ 26,685	$ 15,785	$ 7,272	$ 2,201	$ 1,093
Working capital changes:					
Increase (decrease) in current assets—					
Accounts receivable	$ 25,358	$ 6,879	$ 4,027	$ 894	$ 1,026
Grants receivable	(228)	521	334	79	386
Inventories	27,556	16,490	4,641	784	1,032
Prepaid expenses	188	174	28	22	—
	52,874	24,064	9,030	1,779	2,444
Increase (decrease) in current liabilities—					
Bank indebtedness	25,038	9,047	1,454	(180)	369
Accounts payable and accrued liabilities	14,753	5,500	1,903	618	952
Income and other taxes payable	1,090	634	497	159	18
Current portion of long-term debt	1,093	370	105	74	83
	41,974	15,551	3,959	671	1,422
Increase in working capital	$ 10,900	$ 8,513	$ 5,071	$ 1,108	$ 1,022

(See accompanying notes to the consolidated financial statements)

Notes to the Consolidated Financial Statements

Mitel Corporation

1. Summary of Accounting Policies

These financial statements have been prepared by Management in accordance with accounting principles generally accepted in Canada. The more significant accounting policies are outlined below.

a) Basis of consolidation
The accompanying consolidated financial statements include the accounts of all subsidiary companies, all of which are wholly owned. The year-end for all companies in the group is the last Friday in February, which results in a 53-week year in 1980 and a 52-week year in 1977, 1978, 1979 and 1981.

b) Foreign currency translation
Foreign currencies have been translated into Canadian dollars as noted below:
- — Current monetary assets and liabilities and long-term debt — at the exchange rates prevailing on the balance sheet dates.
- — All other assets and liabilities and depreciation and amortization expense — at historical exchange rates.
- — Revenue and expenses (other than depreciation and amortization) — at the average exchange rates for the fiscal years.

Unrealized gains or losses arising from the translation of long-term debt are deferred and amortized over the remaining life of the debt. Other exchange gains and losses are included in income.

c) Revenue
Revenue from sales of products is recognized at the time goods are shipped to customers. Allowances for estimated warranty costs are provided at the time of sale. For sales of technology, revenue is recognized as milestones set out in the technical agreements and contracts are reached and approved.

d) Government assistance
Approved government grants are recorded as follows:
- — Capital grants — as a reduction of the cost of the related capital assets.
- — Operating grants — as a reduction of related current period expenses when incurred.

e) Inventories
Inventories are valued at the lower of cost, determined on an average cost basis, and:
- — Net realizable value for work-in-process and finished goods.
- — Current replacement cost for raw materials.

The cost of inventories on hand includes material, labour and manufacturing overhead where applicable.

f) Fixed assets
Buildings, machinery and equipment are recorded at cost, net of related specific government grants.
Depreciation and amortization are provided on the bases and at rates, generally, as set out below:

Assets	Bases	Rate
Buildings	Straight-line	4%
Equipment	Declining balance	20-30%
Leasehold improvements	Straight-line	over life of lease

The basis of depreciating buildings was changed on March 1, 1980 from 5% declining balance to 4% straight-line. The effect of this change on the financial statements for the five years ended February 27, 1981 was not material.

g) Research and development costs
Development costs (which include direct labour, materials and applicable overhead costs) relating to specific products that in Management's view have a clearly defined future market are deferred and amortized on a per unit basis against the first three years' estimated sales. Prior to 1979, such costs, which are not material to the financial statements, were expensed as incurred. See note 17 for the effect on net income. Research and other development costs (except for capital assets) are charged against income in the year of expenditure.

h) Other assets
Other assets include goodwill and product patents which are being amortized against income on a straight-line basis over 20 and 10 years respectively.

i) Income taxes
Included in income taxes for financial statement presentation are current and deferred income taxes. Deferred income taxes represent amounts not payable until future years because certain expenses, principally depreciation and amortization, have been expensed for tax purposes on an accelerated basis. Incentive tax credits are reflected as reductions in income tax expense in the year utilized.
Dividend payments from subsidiary companies in certain countries are subject to taxes at various rates. Of the balance of unremitted earnings of subsidiaries, included in consolidated retained earnings, a portion is not subject to tax; the remainder has been reinvested indefinitely and so no provision has been made for taxes.

j) Interest costs
Interest costs related to the construction of the Company's production facilities are capitalized. All other interest costs are charged to income as incurred.

k) Long-term lease arrangements
Long-term leases which are effectively purchases are capitalized in the accounts with the present value of the remaining lease payments shown as long-term lease obligations. Lease agreements where substantially all the benefits and risks of ownership do not accrue to the Company are expensed as lease payments are made.

2. Accounts Receivable

	1981 (000's)	1980 (000's)
Customers	$ 37,965	$ 11,858
Other receivables	800	1,383
	38,765	13,241
Less allowance for doubtful accounts	279	113
	$ 38,486	$ 13,128

3. Inventories

	1981 (000's)	1980 (000's)	1979 (000's)	1978 (000's)	1977 (000's)	1976 (000's)
Raw materials	$ 21,729	$ 13,305	$ 3,640	$ 1,295	$ 821	$ 359
Work-in-process	23,726	8,182	2,247	628	352	—
Finished goods	5,406	1,818	928	251	217	—
	$ 50,861	$ 23,305	$ 6,815	$ 2,174	$ 1,390	$ 359

4. Government Grants

a) Defence Industry Productivity Program (D.I.P.)
The Canadian Government financed the acquisition of specific equipment under the D.I.P. Program totalling $1,756,000. One half of such advances were forgiven and the balance is repayable without interest over five years to May, 1984 (note 9). The assets were recorded net of the 50% forgivable portion. Title to the assets passes to the Company when the final payment is made.

b) Microelectronics Development Program
The Company signed a ten-year agreement effective June 1, 1979 with the Canadian Government under which it will receive up to $20.93 million between June 1, 1979 and March 31, 1983 from the Special Electronics Program of the Department of Industry, Trade and Commerce.

The funding is allocated between two projects:

i) Capital Expansion Project under which the Government will contribute 50% of the direct costs of approved capital equipment to a maximum of $14.25 million.

ii) Product Development Project under which the Government will contribute 75% of the direct costs to a maximum of $6.68 million.

During the year, the Company recorded $677,000 (1980 — $403,000) as operating grants and $1,196,000 (1980 — $117,000) as capital grants under the program.
The programs are proceeding in accordance with their respective terms and no liability for repayment of such assistance under various contingency clauses is foreseen.

5. Fixed Assets

	1981 (000's)			1980 (000's)		
	Cost	Accumulated Depreciation	Net Book Value	Cost	Accumulated Depreciation	Net Book Value
Land	$ 1,252	$ —	$ 1,252	$ 561	$ —	$ 561
Buildings	17,856	480	17,376	1,850	162	1,688
Equipment and leasehold improvements	25,113	4,796	20,317	8,793	1,978	6,815
Construction-in-progress	5,169	—	5,169	1,709	—	1,709
	$ 49,390	$ 5,276	$ 44,114	$ 12,913	$ 2,140	$ 10,773

6. Deferred Development Costs

	1981 (000's)			1980 (000's)		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Deferred development costs	$ 6,978	$ 746	$ 6,232	$ 2,897	$ 199	$ 2,698

7. Other Assets

	1981 (000's)			1980 (000's)		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Investment	$ 1,043	$ —	$ 1,043	$ —	$ —	$ —
Goodwill	309	39	270	309	24	285
Patents	319	49	270	204	24	180
Other	67	—	67	53	—	53
	$ 1,738	$ 88	$ 1,650	$ 566	$ 48	$ 518

8. Bank Indebtedness

The Company has assigned certain of its accounts receivable, inventory and fixed assets to the bank as collateral for bank indebtedness and has issued to the bank a fixed and floating charge debenture on its remaining property and assets.
The Company has primary credit facilities with two Canadian banks aggregating $92,820,000 of which $32,100,000 is dedicated for capital acquisitions (bridge financing) and $60,720,000 is dedicated for general operating purposes in Canada and the United States. The operating lines of credit are subject to separate margin restrictions in each country related to accounts receivable and inventory. As at February 27, 1981, the unused bank credit available to the Company was $24,800,000 under the capital facility, $15,100,000 under the Canadian operating facility and $5,500,000 under the United States operating facility.
The Company also has a demand mortgage with a Canadian bank, bearing interest at 1/2% above the bank's prime rate. As at February 27, 1981, the principal amount of the mortgage was $3,150,000.

9. Long-term Debt

	1981 (000's)	1980 (000's)
Notes to shareholders, 10% due in 1981 with annual payments	$ 144	$ 306
Mortgages (secured by certain fixed assets), 9.6% to 13% due in 1988 to 2004 with monthly payments	1,972	1,521
Conditional sales contract, 11.5% due in 1981	213	240
Note payable (secured by certain fixed assets), 13.16% due in 1985 with monthly payments	1,952	—
Industrial revenue bonds, 9.4% (approximate — see below) due in 2000, with monthly payments	10,814	—
Capital leases, at interest rates varying from 6% to 17% (note 10)	1,965	1,276
Loans under government programs		
D.I.P., interest free, due in 1984-1985 with annual payments	578	770
Ontario Business Incentive Loan, interest free until 1984, subsequently 11.75% until due in 1989, with monthly payments, secured by fixed assets purchased under the program	750	679
Industrial Mortgage Term Loan, 11.75% due in 1985, with monthly payments	214	226
	18,602	5,018
Less current portion	1,760	667
	$ 16,842	$ 4,351

9. Long-term Debt (Cont'd)

A portion of the above debt is payable in U.S. dollars. Amounts outstanding in U.S. dollars are:

	1981 (000's)	1980 (000's)
Industrial revenue bonds —		
8.375% fixed, monthly payments	$ 4,000	$ —
8% to 12% floating, quarterly payments	5,000	—
Capital leases	1,007	362
Other	197	211
	$ 10,204	$ 573

Principal repayments in Canadian dollars, exluding capital leases (note 10), during the next five years are: 1982 — $1,653,000; 1983 — $1,461,000; 1984 — $1,553,000; 1985 — $1,585,000; 1986 — $1,471,000.
Included in interest expense in the consolidated statements of income is interest on long-term debt as follows:

	1981 (000's)	1980 (000's)	1979 (000's)	1978 (000's)	1977 (000's)
Capital leases	$ 189	$ 68	$ 27	$ 29	$ —
Other	1,196	285	154	144	119
Less interest capitalized	(670)	(124)	—	—	—
	$ 715	$ 229	$ 181	$ 173	$ 119

10. Capital Leases

Fixed assets under capital lease include:

	1981 (000's)			1980 (000's)		
	Cost	Accumulated Depreciation	Net Book Value	Cost	Accumulated Depreciation	Net Book Value
Building	$ 1,554	$ 100	$ 1,454	$ 415	$ 59	$ 356
Equipment	964	241	723	905	59	846
	$ 2,518	$ 341	$ 2,177	$ 1,320	$ 118	$ 1,202

Future minimum lease payments and the balance of the obligation under capital leases (in thousands of dollars) are:

1982	$ 400
1983	400
1984	400
1985	365
1986	199
Thereafter	1,733
	3,497
Less interest	(1,532)
Principal	$ 1,965

11. Stock Option and Stock Purchase Plans

a) Stock purchase plan — 1980

In fiscal 1980, the Board of Directors adopted a stock purchase plan effective February 15, 1980. The plan permitted employees to acquire shares at $6.55 per share. The plan terminated on February 12, 1981. The Company has issued 135,000 shares for an aggregate consideration of $884,700 to employees under the plan.

b) Stock option and stock purchase plans — 1981

During the year, the Board of Directors approved the introduction of a number of additional stock option and stock purchase plans. The Board allotted a total of 1,050,000 shares for distribution under the following plans:

		Outstanding Options			
	Shares Available for grant	Number	Aggregate Consideration (000's)	Price per Share	Exercise Period
Balance, February 29, 1980	—	—	—	—	
Additions for the year:					
Key employee option plan —					
— authorized	500,000				
— granted	(437,500)	437,500	$ 4,290	$ 9.53-$20.81	Feb. 21, 1983-Jan. 1, 1986
Basic employee option plan —					
— authorized	300,000				
— granted	(208,769)	208,769	$ 1,990	$ 9.53	Aug. 21, 1982-Nov. 20, 1982
Supplementary employee option plan —					
— authorized	50,000				
Employee stock option/ stock purchase plan —					
— authorized	200,000				
Balance, February 27, 1981	403,731	646,269	$ 6,280		

Under the stock option/stock purchase plan, the employees may either purchase the shares during the year or exercise the option during the six months following March 1, 1982.

No options were exercisable during the year.

12. Capital Stock

The Company's capital stock consists of an unlimited number of Common Shares.
Effective October 27, 1980, the shareholders of the Company approved the split of its Common Shares on a three-for-one basis. In these financial statements, numbers of shares and per share amounts reflect this split.
An analysis of the capital stock account for the five years ended February 27, 1981, expressed in terms of shares issued at that date, is as follows:

	Shares	Dollars
Balance, February, 1976 and 1977	24,000,000	$ 400
Employees' stock purchase plan — 1977	589,200	98,200
Balance, February, 1978	24,589,200	98,600
Investments in subsidiary companies	545,472	538,657
Issued for cash	2,466,861	3,171,574
Fractional shares not taken up	(66)	—
Balance, February, 1979	27,601,467	3,808,831
Public offering	3,300,000	11,550,000
Fractional shares taken up	6	—
Balance, February, 1980	30,901,473	15,358,831
Public offering	2,250,000	17,718,750
Employees' stock purchase plan (note 11)	135,000	884,700
Balance, February 27, 1981	33,286,473	$33,962,281

The Company may not declare or pay cash dividends until it has invested, in Canada, twice the amount contributed by the Canadian Government under the Capital Expansion Project portion of the program referred to in note 4(b)(i) in like or similar equipment.

13. Earnings per Share

The earnings per share figures are calculated using the weighted monthly average number of shares outstanding during the respective fiscal years, after giving retroactive effect to the three-for-one stock split in October, 1980. The weighted monthly average number of shares outstanding for each year was as follows: 1981 — 32,624,000; 1980 — 29,802,000; 1979 — 25,692,000; 1978 — 24,589,000; 1977 — 24,000,000.

14. Tender Offer Expense

During the year, the Company made a tender offer to acquire all of the outstanding shares of Applied Digital Data Systems, Inc. The offer was subsequently withdrawn and the related costs are included in tender offer expense in the statement of income.

15. Income Taxes

Details of income tax expense are as follows:

	1981 (000's)	1980 (000's)	1979 (000's)	1978 (000's)	1977 (000's)
Current—					
Canadian	**$ 1,214**	$ 784	$ 544	$ 274	$ 211
Foreign	**1,483**	720	99	167	(18)
Deferred—					
Canadian	**461**	8	9	—	—
Foreign	**729**	33	379	—	—
Total income tax expense	**$ 3,887**	$ 1,545	$ 1,031	$ 441	$ 193

Deferred taxes on income result primarily from timing differences in the recognition of depreciation and amortization for tax and financial reporting purposes.

The income tax expense reported differs from the amount computed by applying the Canadian rates to income before taxes. The reasons for these differences and their tax effects are as follows:

	1981 (000's)	1980 (000's)	1979 (000's)	1978 (000's)	1977 (000's)
Expected tax rate	51%	50%	49%	48%	48%
Expected tax expense	$ 10,786	$ 3,554	$ 1,517	$ 762	$ 333
Foreign tax exemptions	(3,379)	(1,519)	(737)	(481)	(201)
Foreign rate differentials	(205)	63	204	99	91
Research and investment incentives	(3,800)	(449)	(48)	—	(58)
Losses carried forward (utilized)	295	(61)	13	54	18
Unrealized currency translation loss	730	—	—	—	—
Other	(540)	(43)	82	7	10
	$ 3,887	$ 1,545	$ 1,031	$ 441	$ 193

Two subsidiaries receive exemptions from income taxes provided that they comply with certain conditions. One subsidiary is exempt from taxes until 1991; the other is exempt until 1988 after which it is subject to a reduced rate until 1998 on income from certain products.

Income before taxes attributable to all foreign operations is as follows:

1981 — $10,532,000; 1980 — $5,828,000; 1979 — $3,537,000; 1978 — $1,324,000; 1977 — $516,000.

As at February 27, 1981, the balance of unremitted earnings of subsidiaries which would be subject to Canadian tax on repatriation is $12,489,000 (1980 — $4,239,000). As explained in note 1(i), no provision has been made for Canadian taxes on such earnings.

16. Supplementary Expense Information to Consolidated Statements of Income

	1981 (000's)	1980 (000's)	1979 (000's)	1978 (000's)	1977 (000's)
Operating lease payments	$ 2,325	$ 1,168	$ 306	$ 111	$ 66
Maintenance and repairs	1,203	329	99	54	15
Royalties	245	67	63	94	56
Advertising	1,177	677	160	121	55
Taxes, other than income taxes	2,693	1,443	718	544	272
Amortization of:					
Deferred development costs	548	176	22	—	—
Other assets	40	28	20	—	—
Foreign exchange (gain) loss	321	(27)	(243)	(176)	(37)

17. United States Accounting Principles

The financial statements have been prepared in accordance with accounting principles generally accepted in Canada which, in the case of the Company, conform in all material respects with those in the United States except as follows:

a) Development costs relating to specific products that in Management's view have a clearly defined future market are deferred and amortized on a per unit basis against the first three years' estimated sales. In the United States, such costs would be charged to income in the period in which they were incurred.

b) Unrealized gains or losses on translation of long-term dollar liabilities repayable in foreign currencies are deferred and amortized over the remaining term of the liabilities. In the United States, such gains or losses would be included in income in the period in which they arise.

The following table reconciles net income as reported to the shareholders on the consolidated statements of income and retained earnings to the net income that would have been reported had the financial statements been prepared in accordance with United States accounting principles.

17. United States Accounting Principles (Cont'd)

	1981 (000's)	1980 (000's)	1979 (000's)	1978 (000's)	1977 (000's)
Net income as reported to shareholders	$ 17,262	$ 5,562	$ 3,096	$ 1,146	$ 501
Effect of expensing deferred development costs as incurred	(2,928)	(1,904)	(356)	—	—
Effect of deferring certain translation gains and losses	(14)	62	(63)	(46)	—
Net income in accordance with United States accounting principles	$ 14,320	$ 3,720	$ 2,677	$ 1,100	$ 501
Earnings per share in accordance with United States accounting principles (note 13)	$ 0.44	$ 0.12	$ 0.10	$ 0.04	$ 0.02
Shareholders' equity in accordance with United States accounting principles	$ 54,970	$22,687	$ 8,231	$ 1,844	$ 646

18. Commitments

a) Buildings and equipment
The Company is committed to spend approximately $35,000,000 for building and equipment additions in 1982.

b) Operating leases
The future minimum lease payments for operating leases for which the Company is committed are as follows: 1982 — $2,310,000; 1983 — $1,711,000; 1984 — $1,358,000; 1985 — $1,190,000; 1986 — $1,040,000; thereafter — $4,167,000.

19. Subsequent Events

a) Building purchase
The Company purchased a building in Ottawa, Canada in April, 1981 at a cost of $2,950,000. The facility is partially financed by a 9.25% mortgage of $716,000 due in April, 1997.

b) Public offering (unaudited)
The Company has announced an offering of additional Common Shares to be made in the United States and Canada.

20. Information on Geographic Segments

The Company operates exclusively as a vertically integrated manufacturer of a range of telecommunications products which is its only line of business.

Of the total sales by Canada to unaffiliated customers in 1981, $3,524,000 (1980 — $2,790,000 and 1979 — $1,719,000) were export sales, principally to Europe.

During the year ended February 27, 1981, the Company made sales of $23,963,000 and $12,628,000 to two major customers.

The following tables set forth information concerning the geographic segments for the years ended February 1981, 1980, and 1979.

	Canada (000's)	U.S. (000's)	Other (000's)	Eliminations (000's)	Total (000's)
Fiscal 1981					
Sales	$ 27,766	$ 70,325	$ 13,121	$ —	$ 111,212
Transfers between areas	45,991	44,703	8,567	(99,261)	—
Total sales	$ 73,757	$ 115,028	$ 21,688	$ (99,261)	$ 111,212
Segment operating profit	$ 16,616	$ 15,319	$ 3,337	$ (1,010)	$ 34,262
Deduct:					
Research and development expense					5,859
Less related government assistance					(766)
General corporate expense					4,430
Interest					3,590
Income taxes					3,887
Net income					$ 17,262
Identifiable Assets	$ 63,713	$ 57,746	$ 10,408	$ —	$ 131,867
Add:					
Corporate assets					4,782
Deferred development costs					6,232
Total assets					$ 142,881
Fiscal 1980					
Sales	$ 11,571	$ 28,612	$ 3,228	$ —	$ 43,411
Transfers between areas	15,794	16,512	3,441	(35,747)	—
Total sales	$ 27,365	$ 45,124	$ 6,669	$ (35,747)	$ 43,411
Segment operating profit	$ 4,041	$ 6,854	$ 2,032	$ (975)	$ 11,952
Deduct:					
Research and development expense					3,024
Less related government assistance					(1,055)
General corporate expense					2,269
Interest					607
Income taxes					1,545
Net income					$ 5,562
Identifiable Assets	$ 23,661	$ 19,302	$ 2,463	$ —	$ 45,426
Add:					
Corporate assets					3,876
Deferred development costs					2,698
Total assets					$ 52,000
Fiscal 1979					
Sales	$ 7,689	$ 12,618	$ 1,341	$ —	$ 21,648
Transfers between areas	7,873	7,441	2,576	(17,890)	—
Total sales	$ 15,562	$ 20,059	$ 3,917	$ (17,890)	$ 21,648
Segment operating profit	$ 1,698	$ 3,694	$ 1,734	$ 185	$ 7,311
Deduct:					
Research and development expense					2,236
Less related government assistance					(1,003)
General corporate expense					1,516
Interest					435
Income taxes					1,031
Net income					$ 3,096
Identifiable assets	$ 8,612	$ 7,225	$ 985	$ —	$ 16,822
Add:					
Corporate assets					1,250
Deferred development costs					584
Total assets					$ 18,656

Sales by Product and Geographic Area

(Unaudited)

The following table summarizes Mitel's sales of its products (and revenues derived by Mitel from licensing others to manufacture and sell integrated circuits and PBX's) in the geographic area indicated during the last five fiscal years:

	Fiscal year ended February									
	1977 (000's)		1978 (000's)		1979 (000's)		1980 (000's)		1981 (000's)	
	$	%	$	%	$	%	$	%	$	%
United States:										
SX-20	—		—		—		1,402		13,042	
SX-100	—		—		—		429		15,494	
SX-200	—		—		3,799		15,824		29,299	
Other telecommunications products	1,853		6,405		8,668		10,067		10,716	
Integrated circuits	—		217		684		975		1,841	
Licensing	—		—		—		—		600	
	1,853	34%	6,622	58%	13,151	61%	28,697	66%	70,992	64%
Canada:										
SX-20	—		—		—		46		5,245	
SX-100	—		—		—		508		1,890	
SX-200	—		—		625		4,353		10,330	
Other telecommunications products	2,525		2,913		3,953		3,684		4,238	
Integrated circuits	—		109		—		190		180	
Licensing	—		—		—		—		—	
	2,525	47%	3,022	26%	4,578	21%	8,781	20%	21,883	20%
Europe and Other Countries:										
SX-20	—		—		—		—		3,095	
SX-100	—		—		—		—		837	
SX-200	—		—		403		1,725		7,402	
Other telecommunications products	312		305		936		768		848	
Integrated circuits	237		939		1,188		1,524		3,762	
Licensing	480		640		1,392		1,916		2,393	
	1,029	19%	1,884	16%	3,919	18%	5,933	14%	18,337	16%
Total	$5,407	100%	$11,528	100%	$21,648	100%	$43,411	100%	$111,212	100%
Total:										
SX-20	—		—		—		1,448		21,382	
SX-100	—		—		—		937		18,221	
SX-200	—		—		4,827		21,902		47,031	
Other telecommunications products	4,690		9,623		13,557		14,519		15,802	
Total telecommunications products	4,690	87%	9,623	84%	18,384	85%	38,806	90%	102,436	92%
Integrated circuits	237	4%	1,265	11%	1,872	9%	2,689	6%	5,783	5%
Licensing	480	9%	640	5%	1,392	6%	1,916	4%	2,993	3%
Total	$5,407	100%	$11,528	100%	$21,648	100%	$43,411	100%	$111,212	100%

Management's Discussion and Analysis of Financial Condition and Results of Operations

Results of Operations

From the fiscal year ended February 1978 to the fiscal year ended February 1981, Mitel's sales have increased approximately 10 times from $11,528,000 to $111,212,000. During the same period, net income has increased approximately 15 times from $1,146,000 to $17,262,000. The Company's product mix has differed from year to year during this period; the Company's current sales are highly concentrated in mid-size PBX's sold in the North American markets; and the Company is currently developing both larger line-size PBX's and PBX's which will handle fewer telephone lines than its existing models.

The introduction of the PBX family of products plus their market penetration has been primarily responsible for Mitel's sales growth during this period. The primary reasons for the increase in sales were: in the fiscal year ended February 1979, the introduction of Mitel's first PBX, the SX-200 Superswitch, and further market penetration of Mitel's tone to pulse converters; in the fiscal year ended February 1980, further market penetration by the SX-200 and the introduction of new PBX products, the SX-100 Superswitch and the SX-20 Superswitch; and in the fiscal year ended February 1981, continuing market penetration of the SX-200, SX-100 and SX-20.

Net income as a percentage of sales improved to 14.3% in the fiscal year ended February 1979 from 9.9% in the prior fiscal year, primarily from the introduction of the SX-200, an increase in licensing fees and a change in accounting policy under which development costs relating to certain products were deferred and are being amortized on a per unit basis against future sales in accordance with the pronouncements of the Canadian Institute of Chartered Accountants. For the fiscal year ended February 1980, net income as a percentage of sales declined to 12.8% primarily as a result of costs associated with the introduction of the SX-100 and SX-20, the carrying costs of a build-up in inventories and a reduced effect of licensing fees on net income relative to sales. Net income as a percentage of sales increased to 15.5% in the fiscal year ended February 1981 mainly as a result of the considerable economies of scale which Mitel experienced in the production of its family of PBX products, particularly during the fourth quarter. The percentage of revenue associated with licensing arrangements is not expected to be significant in future years.

Sales and Net Income by Quarter
Fiscal year ended February

	1980					1981				
	1st Quarter (000's)	2nd Quarter (000's)	3rd Quarter (000's)	4th Quarter (000's)	Total (000's)	1st Quarter (000's)	2nd Quarter (000's)	3rd Quarter (000's)	4th Quarter (000's)	Total (000's)
Sales	$6,381	$7,646	$11,923	$17,461	$43,411	$20,336	$20,948	$26,909	$43,019	$111,212
% of Annual Sales	14.7%	17.6%	27.5%	40.2%	100.0%	18.3%	18.8%	24.2%	38.7%	100.0%
Net Income	$ 622	$ 624	$ 1,647	$ 2,669	$ 5,562	$ 2,013	$ 2,555	$ 3,537	$ 9,157	$ 17,262
Net Income as % of Sales	9.7%	8.2%	13.8%	15.3%	12.8%	9.9%	12.2%	13.1%	21.3%	15.5%

The quarterly variance in net income as a percentage of sales, as shown in the above table, can be primarily attributed to the following: volume efficiencies obtained in quarters with large increases in sales, particularly the fourth quarter of each fiscal year; the amount of development costs capitalized relative to total research and development costs in each quarter; the revenue from licensing agreements ($950,000 and $966,000 in the third and fourth quarters of the fiscal year ended February 1980, and $812,000, $561,000 and $1,620,000 in the second, third and fourth quarters of the fiscal year ended February 1981), which is recognized as contract milestones are met and for which only nominal costs, excluding income taxes, are incurred; and a build-up in the number of employees relative to sales in the first and second quarters of each year in anticipation of a higher level of sales in the third and fourth quarters. The rate of taxes applicable in determining net income from quarter to quarter also varies, depending upon the percentage of income derived during the quarter from foreign operations (see Note 15 to the Consolidated Financial Statements). In the fiscal year ended February 1981, the results of the second and fourth quarters were reduced by the costs related to the unsuccessful tender offer for Applied Digital Data Systems, Inc. in the pre-tax amounts of $500,000 and $347,000, respectively.

Sales in the second and third quarters of the fiscal year ended February 1981 were less than the Company had budgeted because of the deployment of personnel to correct system failures that developed in the summer of 1980 in the SX-20 and, to a lesser extent, in the SX-200 and SX-100. The failures, which occurred mainly in high humidity environments, were caused by malfunctioning integrated circuits. The Company's normal product testing procedures had not been able to detect the susceptibility of these integrated circuits to fail under certain climatic conditions. After diagnosis of the problems, steps were promptly taken to procure integrated circuits with higher reliability, to replace defective and potentially defective components, and to implement improved inspection and test procedures. The Company believes that these steps have resulted in elimination of the causes of the system failures. To a limited extent, order rates for the SX-20 are expected to continue to be adversely affected through the first half of fiscal year 1982 until customers regain confidence in the reliability of the product.

The Company establishes quarterly and yearly sales targets and has profit sharing, bonus and stock option programs for almost all employees as incentives to achieve its targets. As a result, the Company's sales in the last month of each quarter and the last quarter

of each fiscal year are typically significantly greater than the preceding months or quarters, respectively. Sales in the fourth quarter of fiscal years ended February 1980 and 1981, which were above the budgeted amounts, have permitted the Company to meet its annual sales target. However, the Company expects a decline in sales and earnings in the first quarter of the immediately succeeding fiscal year when its fourth quarter sales substantially exceed budget. Thus, the Company anticipates that sales in the first quarter of fiscal year 1982 (ending May 1981) will be lower and earnings significantly lower than in the fourth quarter of fiscal year 1981 (ending February 1981), although both sales and earnings should be substantially higher than in the first quarter of fiscal year 1981 (ending May 1980). Net income as a percentage of sales for the first quarter of fiscal year 1982 is expected to approximate the level of the first quarters of fiscal years 1981 and 1980. The Company does not believe that its higher than budgeted sales for the fourth quarter of fiscal 1981 will affect its sales for fiscal 1982 because the Company expects to operate at its production capacity during fiscal 1982.

The Company is experiencing its most rapid sales growth in markets outside Canada (see Note 20 to the Consolidated Financial Statements). However, the segmented profits in each of these markets have not grown as quickly as have Canadian profits. This is primarily because of the recognition of license revenue and income, which has higher profit margins, as Canadian revenue and income ; inefficiencies of start up operations in areas outside Canada; the initial manufacture of new products, which historically have higher profit margins, in Canada; and the manufacture of other telecommunication products, which have relatively lower profit margins, in the United States. In addition, in the fiscal year ended February, 1981, the U.S. segment incurred expenses relating to Mitel's unsuccessful tender offer for Applied Digital Data Systems, Inc.

The Company does not believe that inflation has had any significant impact on either costs or revenues during the last five fiscal years.

Liquidity

The Company's working capital has traditionally been below desired levels because cash generated by operations has not adequately financed accounts receivable and inventory growth resulting from an approximate doubling of revenues in each fiscal year. For the fiscal year ended February 1981, the Company's accounts receivable rose $25,358,000 and inventories rose $27,556,000 with an offsetting increase in accounts payable of $14,753,000. Bank indebtedness increased during the year $25,038,000, partly in response to these short term liquidity needs and partly to act as interim financing for certain capital projects. Average inventory as a percentage of cost of goods sold was 70% and 69% during the fiscal years ended February 1980 and 1981, respectively. The Company is implementing changes in its control systems intended to improve its inventory turnover rate. The use of external financing to satisfy a portion of short term liquidity requirements is expected to continue for the foreseeable future.

The Company is operating under commitment letters with Canadian chartered banks and their U.S. affiliates which make available to Mitel credit facilities totalling Can. $80,000,000 and U.S. $10,670,000. Borrowings under these facilities can be in the form of demand loans, Eurodollar loans, banker's acceptances or commercial letters of credit and are secured directly or indirectly by fixed and floating charge debentures and pledges with respect to substantially all of the assets of the Company. Included in the $80,000,000 described above is $50,000,000 of interim financing, of which $7,301,000 had been drawn down at February 27, 1981. See Note 8 to the Consolidated Financial Statements for additional information concerning the terms of the operating credit and financing facilities. Pursuant to these commitments, the interim financing will no longer be available following the issuance of the 3.8 million Common Shares offered under the company's recent public offering and borrowings thereunder must be repaid in full out of the proceeds of the sale of the Common Shares offered hereby.

The Company's long term liquidity needs have in the past been financed primarily through the issuance of Common Shares and as a result, the ratio of long term debt to shareholders' equity at 1981 fiscal year-end was 0.28 to 1.

Capital Expenditures and Resources

The following table sets forth the consolidated capital expenditures of the Company for the last five fiscal years:

	Fiscal year ended February				
	1977 (000's)	1978 (000's)	1979 (000's)	1980 (000's)	**1981 (000's)**
Capital expenditures	$1,674	$724	$3,491	$9,048	**$37,941**
Less: related government assistance	412	146	406	488	**1,354**
Net capital expenditures	$1,262	$578	$3,085	$8,560	**$36,587**

During the fiscal year ended February 1981, a major expansion program was initiated by the Company to ensure that adequate manufacturing facilities would be in place to meet anticipated future demand. However, present demand for the Company's PBX products exceeds existing production capacity and this situation is not expected to change in the first two quarters of the Company's current fiscal year. In the fiscal year ended February 1981, approximately $21,000,000 was spent on the expansion program of which $10,814,000 was financed by industrial revenue bonds (low interest financing through local government entities) and the remainder by the proceeds of the issue of Common Shares in June 1980, interim bank financing and working capital. The Company currently estimates that the remainder of the expansion program and capital equipment expenditures for the current and the next fiscal year will total approximately $133,000,000 and to date the Company has made firm commitments of $35,000,000. Of this amount, approximately $19,000,000 may be eligible for British Government assistance or for term loans at reduced rates of interest from the European Coal and Steel Community, or a combination of both; approximately $13,000,000 may be eligible for funding from the federal government of Canada under the Company's microelectronics development program and approximately $15,000,000 is expected to be financed by industrial revenue bonds. The remaining portion of anticipated expenditures under the expansion program will be financed from the proceeds of the company's recent public offering of 3.8 million Common Shares and internally generated funds.

Financial Summary

Selected Financial Data

The following table is derived from the Consolidated Financial Statements included elsewhere herein and which have been prepared in accordance with accounting principles generally accepted in Canada ("Can. GAAP"). These principles also conform, in all material respects, with accounting principles generally accepted in the United States ("U.S. GAAP"), except with respect to the deferral of unrealized foreign exchange gains and losses, as well as certain product development costs as more fully described in Note 17 to the Consolidated Financial Statements. The effect on Mitel's net income and earnings per share of the difference in accounting principles is reconciled below.

	Fiscal year ended February (at end of fiscal year for balance sheet data)				
	1977	1978	1979	1980	**1981**
	(Thousands of dollars except per share amounts)				
Income Statement Data:					
Sales	$5,407	$11,528	$21,648	$43,411	**$111,212**
Gross research and development expenses (including depreciation)	776	1,528	2,820	5,138	**9,392**
Net income	501	1,146	3,096	5,562	**17,262**
Earnings per share	0.02	0.05	0.12	0.19	**0.53**
Balance Sheet Data:					
Working capital	1,093	2,201	7,272	15,785	**26,685**
Total assets(1)	4,762	6,972	18,656	52,000	**142,881**
Short term debt	584	479	2,038	11,455	**37,586**
Long term debt	1,702	2,247	2,897	4,351	**16,842**
Shareholders' equity(2)	646	1,890	8,696	24,994	**60,219**
Reconciliation to U.S. GAAP:					
Net income—Can. GAAP	$ 501	$ 1,146	$ 3,096	$ 5,562	**$ 17,262**
Increased (decreased) by:					
Foreign exchange	—	(46)	(63)	62	**(14)**
Deferred development costs	—	—	(356)	(1,904)	**(2,928)**
Net income—U.S. GAAP	501	1,100	2,677	3,720	**14,320**
Earnings per share—U.S. GAAP	0.02	0.04	0.10	0.12	**0.44**

(1) Total assets determined under U.S. GAAP would be reduced by $46,000 in 1978, $692,000 in 1979, $2,745,000 in 1980 and $6,293,000 in 1981 from the amounts reported under Can. GAAP.

(2) Shareholders' equity determined under U.S. GAAP would be reduced by $46,000 in 1978, $465,000 in 1979, $2,307,000 in 1980 and $5,249,000 in 1981 from the amounts reported under Can. GAAP.

Exchange Rate of The Canadian Dollar

Financial information is expressed in Canadian dollars, unless otherwise stated. The high and low rates (i.e., the highest and lowest rates at which Canadian dollars were sold) of the Canadian dollar in exchange for U.S. currency from January 1, 1976 through May 27, 1981, as reported by the Bank of Canada, were as follows:

	U.S. Dollars					
	1976	1977	1978	1979	1980	**January 1, to May 27, 1981**
High	$1.0389	$0.9985	$0.9170	$0.8778	$0.8767	**$0.8487**
Low	0.9588	0.8963	0.8363	0.8320	0.8249	**0.8269**

On May 28, 1981 the noon buying rate in New York City, payable in Canadian dollars, as reported by the Federal Reserve Bank of New York, was U.S. $0.8321 = Can. $1.00.

Corporate Structure

Mitel Corporation
Canada

Stellar Holdings
(Nederland) B.V.
The Netherlands

- **Mitel Inc.** U.S.A.
- **Mitel Caribe Inc.** Puerto Rico
- **Mitel Telecom Ltd.** Great Britain
- **Mitel International Limited** Ireland
- **Mitel Telecommunications Ltd.** New Zealand
- **Mitel (Hong Kong) Ltd.** Hong Kong
- **Mitel Mikroelektronik und Telefon GmbH** West Germany

■ **Manufacturing Locations (Including Sales & Service):** CANADA — Kanata, Ont.; Bromont, Que. U.S.A. — Boca Raton, Fla.; Ogdensburg, N.Y.; Burlington, Vt. EUROPE — Slough, England; Shannon, Ireland; Newport, South Wales. CARIBBEAN — Catano, Puerto Rico. FAR EAST — Kowloon, Hong Kong. ■ **Sales and Service Locations:** CANADA — Burnaby, B.C.; Edmonton, Alta.; Toronto, Ont.; Halifax, N.S. U.S.A. — Washington, D.C.; Arlington, Va.; Mountainside, N.J.; Bellevue, Wash.; Bloomingdale, Ill.; Birmingham, Mi.; Lakewood, Co.; Havertown, Pa.; Dallas, Tx.; Birmingham, Al.; San Diego, and Costa Mesa, Ca.; Augusta, Ga.; Atlanta, Ga.; Branford, Ct.; Overland Park, Ks.; Emeryville, Ca. EUROPE — Slough, Berkshire, England; Maidenhead, Berkshire, England; Copenhagen, Denmark; Frankfurt, West Germany. OTHER — Wellington, New Zealand. NOTE — Dealer, Distributor and Agent Locations not included.

Corporate Directory

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Executive Vice President

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President
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Toronto, Ontario

* Robert J. Redmond
Partner
Gowling & Henderson
(barristers and solicitors)
Ottawa, Ontario

Kent H.E. Plumley
Partner
Gowling & Henderson
(barristers and solicitors)
Ottawa, Ontario

* Douglas I.C. Cameron
Vice President and Treasurer
Maclaren Power and Paper Company
(forest products company)
Buckingham, Quebec

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President

** Terence H. Matthews
Executive Vice President

** Donald R. Gibbs
Vice President, Finance

** John T. McLennan
Vice President, Operations

** Ralph A. Bennett
Vice President & General Manager
Semiconductor Division

Graham A. Neathway
Vice President, Telecom Division

Paul Wilker
Vice President, Product Marketing
Telecom Division

Raymond Whitbread
Vice President, R&D and Technology

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Vice President, European Operations
Mitel Telecom Ltd.

John Farmer
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Christopher Bailey
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Switching Division

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Semiconductor Division

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Vice President, Finance
Mitel Inc.

Theodore G. Nanz
Vice President, Operations
Mitel Inc.

Wil Riner
Vice President, Marketing
Mitel Inc.

Peter C. Madsen
Vice President, Market Development
Mitel Inc.

Auditors

Clarkson Gordon
Ottawa, Ontario

Legal Counsel

Gowling & Henderson
Ottawa, Ontario

Milbank, Tweed, Hadley & McCloy
New York. N.Y.

Bankers

Bank of Montreal
Royal Bank of Canada
Canadian Imperial Bank of Commerce

Transfer Agents

Montreal Trust Company
Morgan Guaranty Trust Company of New York
Bank of Montreal Trust Company

Stock Exchange Listings

Toronto Stock Exchange
Montreal Stock Exchange
London Stock Exchange
New York Stock Exchange

* Members — Audit Committee
** Members — Executive Committee

For further information about Mitel facilities, operations or products, please contact:

Public Relations Department
Mitel Corporation
P.O. Box 13089,
Kanata, Ontario
K2K 1X3
Canada
Telephone (613) 592-2122
Telex 053-4596
TWX 610-562-8529

A/R ORDER #: 9110-098-051NA

Prototype of the new SUPER 10, a complete communications system in a console which began production this spring.

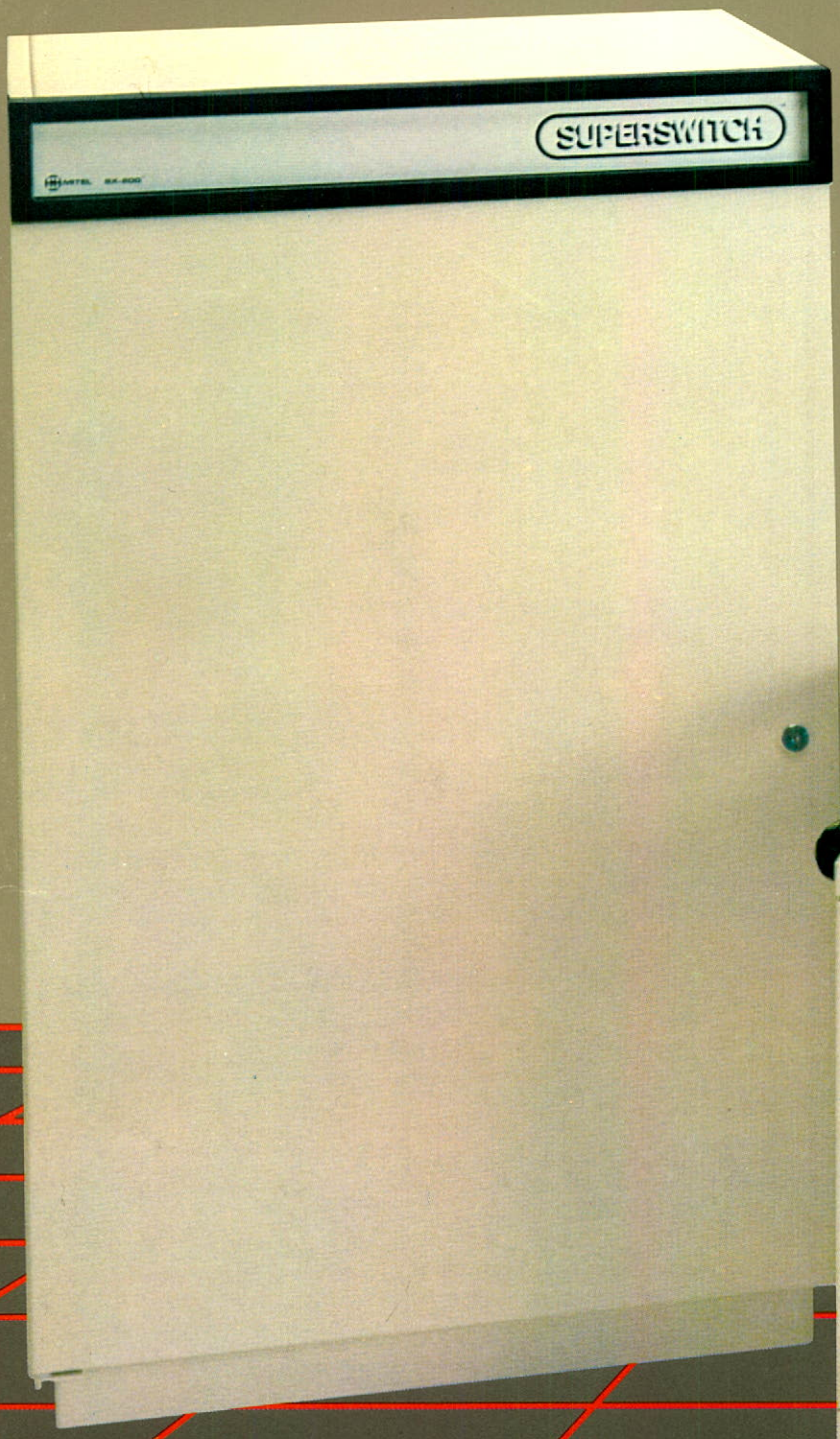
On the following pages is a sample of a typical advertisement used in the promotion of the Mitel SUPERSWITCH family of PBX systems.

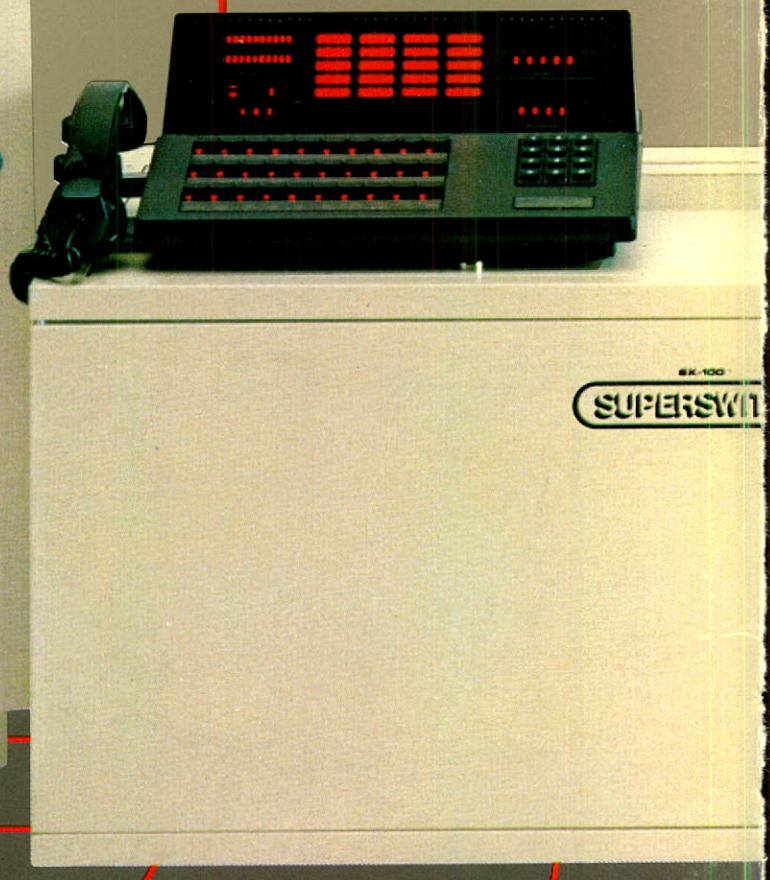
Powerful Performers!!!

Mitel makes more electronic PABX switchboards than any other manufacturer in the world.

Mitel systems offer powerful performance features in space-saving, energy-saving, money-saving packages.

SUPERSWITCH – The world standard for excellence!





SX-200™ Cabinet

SX-100™ Cabinet and Console

SX-200/SX-100

In commercial applications up to 176 extension lines, the SX-200/SX-100 consumes less energy than four standard electric typewriters and installs in less space than a standard filing cabinet. These products offer more features than any other in their line size.

SX-20

The SX-20 brings sophisticated electronic switchboard features to small business at less cost than any other system. In hotel/motel applications the SX-20 can improve service, build profits, and hold the line on costs.

More power to small businesses/ large homes

SX-10

During 1980, Mitel introduced the world's first talking communications system, the SX-10. An electronically synthesized voice makes the SX-10 user-friendly. It operates with standard telephones and provides the flexibility of up to 16 extensions for the smaller business or large home.

SX-5

PABX call-handling convenience comes to the small business or homeowner in the SX-5, in a cabinet slim enough to slip into a briefcase. The feature rich SX-5 accommodates 2 outside lines and 6 extensions. It uses standard telephones, consumes minimal energy, and is easily installed.

The performance continues

Next — a smaller system and a bigger system, the SX-2™ and the SX-2000™.

SUPERSWITCH™

PABXcellence™

MITEL

X-20™ and Remote Display

SX-10™

SX-5™

Produced by:

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Kanata

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