

# Message to the Shareholders and Employees of The Boeing Company



Lewis E. Platt  
Non-Executive Chairman

An intense focus on execution led to strongly improved results in 2004. Earnings were up 161 percent, and Boeing outperformed the S&P 500 Aerospace and Defense Index in total shareholder return for the year. Based on the numbers, the company is doing well. Even so, it was a distressing year for all who admire this company or feel privileged to be a part of it. Simply put, our reputation suffered as the company operated under a cloud of uncertainty throughout 2004 and into 2005.

While the U.S. Air Force lifted the suspension of our launch business in early 2005, we continue to bear the effects of events involving a very few people who are no longer part of the company. We did not conclude a long-sought contract with the U.S. Air Force for a new fleet of tankers. And sadly, the man who had started to turn the company around made a serious error in judgment. The board asked for Harry Stonecipher's resignation because it determined his actions surrounding a personal relationship were inconsistent with Boeing's code of conduct, reflected poor judgment and eroded his ability to lead this company.

As the senior leader of this company, I wish to make three main points from the outset.

One, no one should underestimate the strength of our business or the firmness of our resolve. It is harder to rebuild a reputation than it is to build one in the first place. We've taken decisive action to fix the problems identified and feel confident that we will succeed in that endeavor because we have attracted the right people, and we continue to do so. Our people are motivated by a fierce pride in what they do and what it means to be part of The Boeing Company.

Two, we understand the U.S. government's desire—and indeed its obligation—to leave no stone unturned in investigating lingering allegations of favoritism or abuse of the public trust. We are cooperating with the government in its investigations.

Three, as a result of our own internal reviews, I am more convinced than ever that the misdeeds are not systemic or characteristic of the overall behavior of the 159,000 people that make up this company. That said, we have spent an enormous amount of time and effort to ensure that the people throughout Boeing understand fully that integrity is a business fundamental. Our guiding principle is to exhibit the highest standards of business conduct at all times. We have drawn bright lines to define ethical decision making, and we have made it clear to all of our people that there will be zero tolerance for anyone who crosses the line into dishonest or unethical behavior.

## **Strategy and Execution**

Boeing is an aerospace company of unrivaled balance and breadth, and our strategy is well known. Most Boeing employees could recite the three main elements of our strategy in their sleep. First, we will run healthy core businesses. Next, we will leverage our strengths and move into adjacent businesses where we have a competitive advantage in technology or in customer knowledge and insight. Last, we will lead, not follow, in opening the new frontiers that are critical to long-term growth and competitiveness within the aerospace industry.

That is our strategy. It is working well, and it is not about to change. What has changed is a return to the fundamentals of executing the business. We

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took a good, hard look at the business case behind every one of our programs and businesses—re-examining targets, establishing new and more meaningful ones where needed, and really holding people accountable for their performance.

As a result of these thorough reviews, we took corrective action in several areas. We decided, for instance, that, even though our 717 brings tremendous value to the airlines that operate it, the overall market does not support continuing production beyond delivery on our current commitments. We also determined that Boeing Air Traffic Management simply isn't a business right now. So we scaled back the program and moved it into our Phantom Works research and development group. There, it will be nurtured as an extremely promising technology and business concept until customers are ready to make a financial commitment to radical improvement of the global air traffic control system.

But the biggest payoff came in the improved performance of our primary businesses—Integrated Defense Systems and Commercial Airplanes.

## Integrated Defense Systems

Boeing Integrated Defense Systems (IDS) performed extraordinarily well in 2004. Revenues grew by 11 percent; operating margins improved to 9.6 percent; and IDS continued to add to its backlog, already the highest in the defense industry.

IDS has established Boeing as the leading industry partner to the U.S. government in developing a “network-centric” view of the world and applying

that strategy to a wide array of conventional and nonconventional threats. It excels as the lead integrator of complex defense systems that involve different platforms (such as aircraft, tanks, ships and satellites) and has dramatically increased the sharing of information and capabilities among them.

During 2004, IDS captured more than \$30 billion in orders, including major contract awards from the U.S. Navy, Army and Air Force:

- A \$3.9 billion Navy contract to build the Multi-mission Maritime Aircraft that will replace the Navy's aging fleet of 223 P-3s with new aircraft based on the Boeing 737 airframe. This program represents \$44 billion in potential revenues.
- A \$6 billion extension of the Army's transformational Future Combat Systems program to expand the program's scope and accelerate delivery of key technologies and capabilities to current forces. This brings the total value for Boeing's part of the program to \$21 billion.
- A contract with a potential value of \$4.9 billion to provide maintenance and support work for the Air Force's C-17 fleet.

In addition to resolving issues from an earlier time period that affected the tanker procurement, the one remaining challenge for IDS is the commercial satellite business. This business continues to suffer from cost growth and technical problems. However, we have assigned good people to the business, and we expect to fix those problems in the coming year.

All in all, there is exceptional upside for Boeing in our defense businesses. Defense customers have

a high level of confidence in our company. They see Boeing as a clear leader in understanding the complex challenges of today's defense environment and in being able to marshal the resources (and especially the information and communications) that are needed to meet them.

## Commercial Airplanes

In the leanest of times, Boeing Commercial Airplanes (BCA) learned to excel at lean production and assembly. Since the collapse of the commercial airplane market in September 2001, BCA has exercised great ingenuity in finding new ways to reduce unit costs and speed cycle times. As a result, it has remained profitable despite a huge downturn in production, and it has continued to invest in the future. Now BCA is in an excellent position to grow and prosper in what promises to be a sustained upturn in the commercial airplane market.

Airline traffic finally pushed ahead of pre-9/11 levels in 2004. Outside the United States, many airlines have achieved strongly improved profitability. With load factors at record highs, airlines need more seats. Boeing is primed to meet that need with a full family of airplanes—including the most exciting new airplane since the dawn of the jet age.

We launched the Boeing 787 (formerly 7E7) Dreamliner on the biggest single order for a new airplane in Boeing history—a firm order for 50 787s from ANA (All Nippon Airways), with first deliveries scheduled in 2008. At the end of 2004, we reached 56 firm orders, with airline commitments for a total

of 126 new 787s. With announced sales in early 2005, that total reached 193.

Through the use of new materials and advances in aerodynamics, we've designed the sleek-looking 787 to open a new frontier in commercial flight. As the first widebody with high-strength, lightweight composite body, wings and tail, it is expected to outperform other midsize airplanes, delivering higher speed, more range, reduced fuel burn and emissions, greater interior comfort, reduced noise on landings and takeoffs, and superior economics. In opening nonstop service between scores of new city pairs, the 787 is designed to bring an unrivaled combination of convenience and comfort to long-distance travel. Even more compelling, with a 10 percent improvement in direct operating costs and 45 percent more cargo revenue capacity than competing aircraft, the 787 can accommodate both low ticket prices for the traveling public and high margins for airlines. That makes it a winner on all counts.

## Time to Level the Playing Field

While we continue to create value for our customers through Boeing products, we must also insist on a level competitive playing field in the marketplace. Four years ago, Airbus drew on substantial launch aid from four European governments to begin development of the A380 super jumbo jet, which is a direct competitor to our 747. Now it is asking for additional launch aid to support a competitor to the 787.

Enough is enough. Subsidized competition is unfair competition, and it is clearly forbidden by

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World Trade Organization rules. If Airbus wants to develop another airplane, it should pay for it out of cash from operations, or it should borrow the money at market rates—just as Boeing does.

Founded in 1970, Airbus is 35 years old. It has been treated as an “infant industry” for far too long. It’s time for Airbus to play by the rules that apply to large, mature enterprises.

## Connecting Global Travelers

With the launch of our in-flight Connexion by Boeing<sup>SM</sup> service in 2004, we continued to solidify our leadership in providing secure, high-speed Internet and e-mail connectivity to travelers worldwide. At year-end, the service was offered to passengers on four global airlines, on routes between Europe, Asia and the United States, with additional airlines planning to offer the in-flight service in 2005 and beyond. With in-flight service launched, Connexion by Boeing expanded its efforts to the open seas, conducting a successful three-month maritime demonstration of its real-time connectivity solution.

## Boeing's Future

Despite major distractions, people around the company kept their eyes on the ball throughout 2004. As a result, almost all parts of Boeing increased their

performance substantially. On a competitive basis, this company is better than ever, with great strength both in existing programs and in the leading-edge developments that will define the future.

Our defense systems business accounted for more than 58 percent of total revenues in 2004. This is a business that is broad and deep. And, as long as we execute, I am confident that it will continue to grow despite potential defense budget reductions. At the same time, we are on the cusp of what we believe will be a sustained recovery in the commercial airplane market, with an all-new airplane that will set whole new standards for operating performance and passenger comfort in long-distance travel.

In every way, we are executing the strategy. We are running healthy core businesses. We are experiencing strong growth in adjacent businesses such as aerospace services. Last, but not least, we have shown that Boeing is prepared to make the tough decisions to ensure real leadership in the aerospace industry for a long time to come.



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