1979 Annual Report

Hugh Russel Inc.

Since 1784

Hugh Russel Inc.

COMPANY DESCRIPTION

Hugh Russel Inc. is a diversified distributor of industrial goods with distribution outlets throughout Canada and the United States.

The original business was established in Montreal in 1784 as a general merchant firm, trading dry goods and hardware to agricultural settlements in eastern Canada and the New England states. With industrialization, Russel became a distributor of iron and steel products, setting the pattern for the modern business.

Today the primary business of Hugh Russel Inc. is the supply of a wide range of products and materials to manufacturing and construction industries; secondary operations involve sales to consumers through its retail customer outlets.

The function of the distributor is to buy products in bulk, to maintain regional and local distribution facilities throughout its market area and to deliver product on short notice to serve local demand. To ensure a constant availability of products Russel has developed sources of supply in many countries of the world.

Russel's distribution operations cover three main product groups:

- carbon and alloy steels;
- hardware and construction materials, plumbing and heating supplies and a range of home and leisure products;
- industrial bearings and other power transmission components used by industry.

A fourth group is engaged in the design, manufacture and sale of wire and cable making equipment from plants in Canada and the United States.

Cover Illustration:
The stylized depiction of Vulcan, the Roman god of fire and metalworking, on the company logo symbolizes Russel's close ties with industry. The logo used in the photograph was cut from mild steel in one of the Metals Group plants before being chrome plated.

HIGHLIGHTS

	1979	1978	Change
Sales	**$534,907,000**	$427,772,000	+25%
Earnings	**$14,072,000**	$9,168,000	+54%
Earnings per common share	**$4.84**	$3.15	+54%
Dividends paid per common share	**73 cents**	64 cents	+14%
Total assets	**$270,928,000**	$215,479,000	+26%
Equity per common share	**$23.16**	$19.19	+21%
Return on average common shareholders' equity	**23.1%**	17.6%	
Number of shareholders	**2,488**	2,555	
Total employees	**2,812**	2,704	
Ten-year compound rate of growth in:			
— Sales	**26.8%**		
— Earnings on common equity	**24.8%**		
— Common share dividends paid	**13.8%**		

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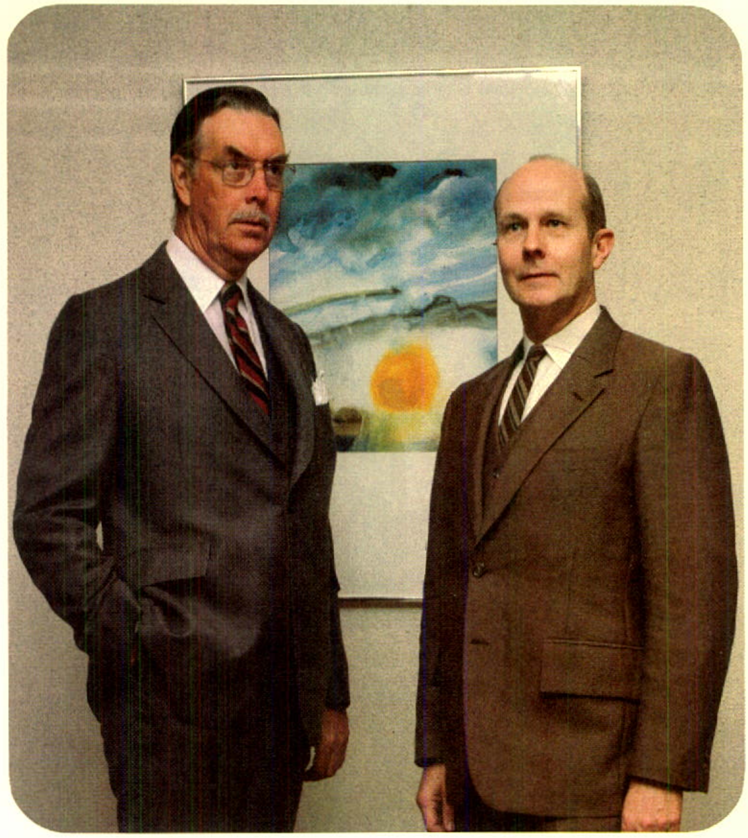
REPORT TO SHAREHOLDERS

In 1979 Russel achieved improved operating results in an economy of rising costs and considerable political uncertainty. Sales surpassed the $500,000,000 mark for the first time and the Corporation recorded the second highest earnings in its history.



A. D. Russel, Chairman, and J. P. Foster, President

Operating Performance Highlights

Net earnings for 1979, at $14,072,000, were up by 54% from the $9,168,000 reported in 1978. After providing for preferred dividends, earnings attributable to the common shares were $4.84 per share, compared to $3.15 per share last year.

As illustrated by Chart One, 1979 was the fourth consecutive year of increased earnings results. Over the ten-year period covered by the chart, earnings per share have increased at a compound rate of nearly 25% per year.

Net sales for the year of $534,907,000 were 25% higher than the $427,772,000 reported in 1978 and for the fourth consecutive year set a new record for the Corporation. (See Chart Two.)

Sales have grown at a compound rate of 27% over the past ten years; roughly one quarter of this growth is estimated to be the effect of increases in general price levels.

During 1979, the Metals Group produced record sales and profits in a buoyant steel market, contributing 53% of corporate sales and 86% of operating profits.

The Power Transmission Group showed improved operations in the Canadian division. A program of administrative reorganization in the United States prevented the Group as a whole from repeating last year's record results.

Costs of introducing a major new line of equipment depressed the earnings of the Engineering Group in 1979. This equipment, which is based upon patented technology, has been well received by the market and the Toronto plant is substantially sold out for 1980.

For the past several years the Home Products Group has been burdened with persistent difficulties flowing from a variety of factors. At last year's Annual Meeting of Shareholders a program designed to restore profits to acceptable levels was outlined. As a part of this program, a major warehouse near Montreal was closed in June 1979, resulting in one-time costs of $1,671,000. This action reflected in improved profit for the Group in 1979 compared to 1978.

Dividends

In December 1979, the Board of Directors increased the quarterly cash dividend to 21 cents, or an indicated annual dividend rate of 84 cents per common share. Total dividend payments on the common shares in 1979 were 73 cents, an increase of 14% over the previous year. The new dividend rate will provide an increase of 15% for the dividend payment in 1980 compared to 1979.

The Corporation also provides an optional stock dividend of substantially equivalent value to the cash dividend for shareholders who may wish to defer

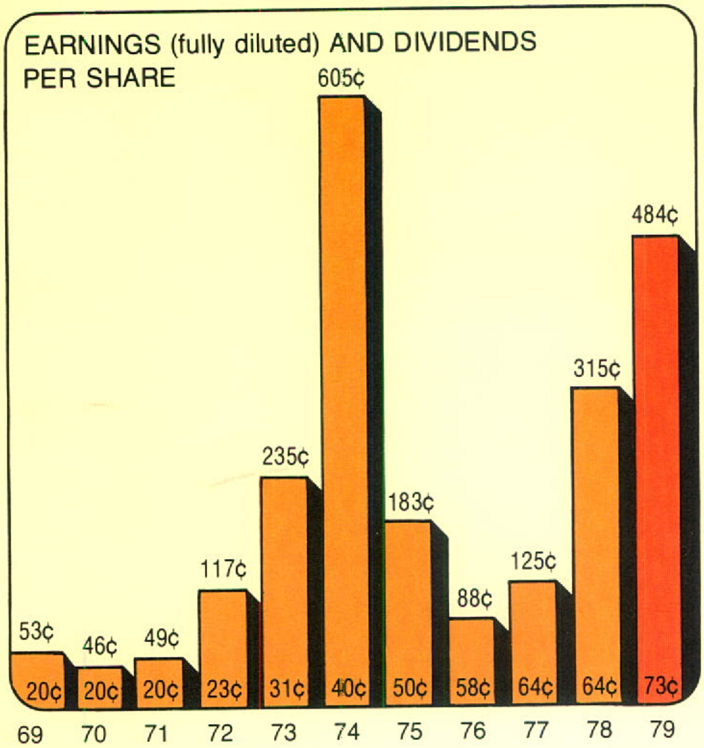


Chart One

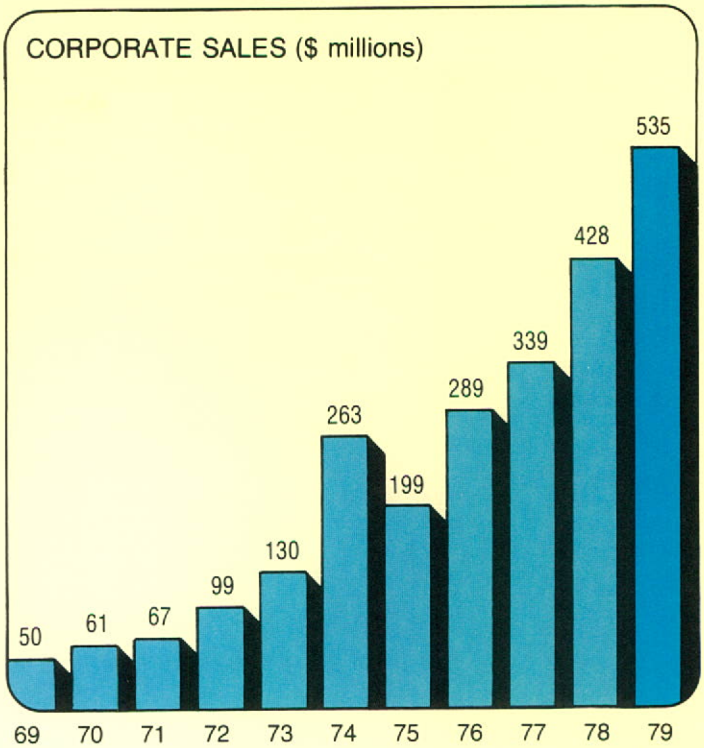


Chart Two

income taxes on their dividend income. The March 1980 stock dividend declared in December 1979 was for 1.5 Class B common shares on each 100 shares of Class B stock held.

Russel dividend policy is to pay a regular dividend based on the anticipated long term and sustainable earning power of the Corporation. This policy is designed to provide shareholders with a measure of confidence and certainty in existing and prospective dividend yield since payments are not geared to short term fluctuations in corporate profits.

Financial Position

In June the Corporation received the proceeds of an issue of $15,000,000 of Series C Preferred Shares. This new issue of Russel securities was well received by investors and the proceeds, together with cash flow from operations ($5.55 per common share in 1979, compared with $3.95 in 1978), have placed the Corporation in a strong financial position.

At the end of 1979 the Corporation had bank lines with Canadian chartered banks and financial institutions in the United States totalling $100 million, of which $14 million was unused at year end.

Working capital in the Corporation was $56,747,000 at the end of 1979, up 34% from the figure at the beginning of the year. Total assets rose by 26% to $270,928,000.

Shareholders' equity in the Corporation at year end was $84,046,000, an increase of 41% over 1978. Equity now constitutes 79% of the Corporation's capital employed; as shown in Chart Three, this figure is at the upper end of the range within which the Corporation has traditionally operated.

Expansion Projects

During the year both the Metals Group and the Power Transmission Group increased their penetration of United States distribution markets. In July the Metals Group acquired the Baldwin Steel Company, a Cleveland-based distributor of specialty steels used by industry for maintenance and repair work. Together with International Alloy Steel, also based in Cleveland, Baldwin provides the Metals Group with marketing activities in 25 states and a solid base on which to build further business in this important market segment.

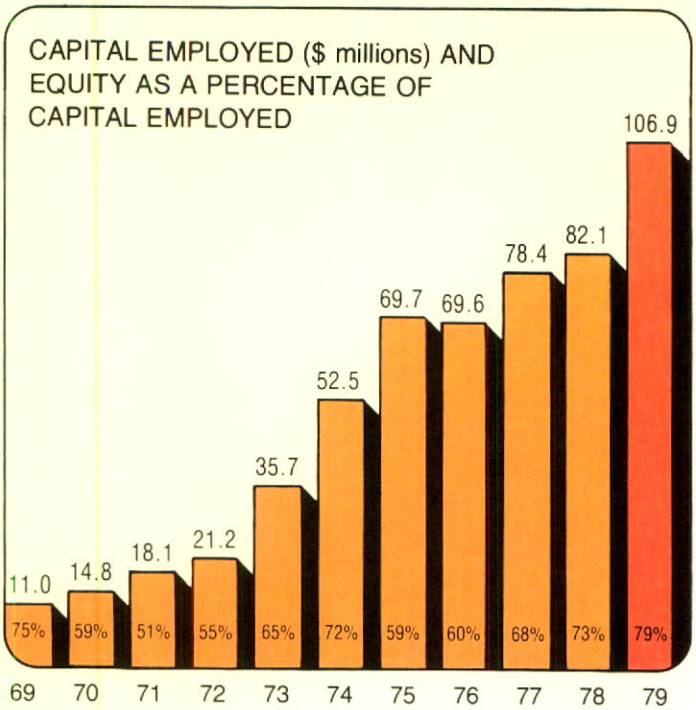


Chart Three

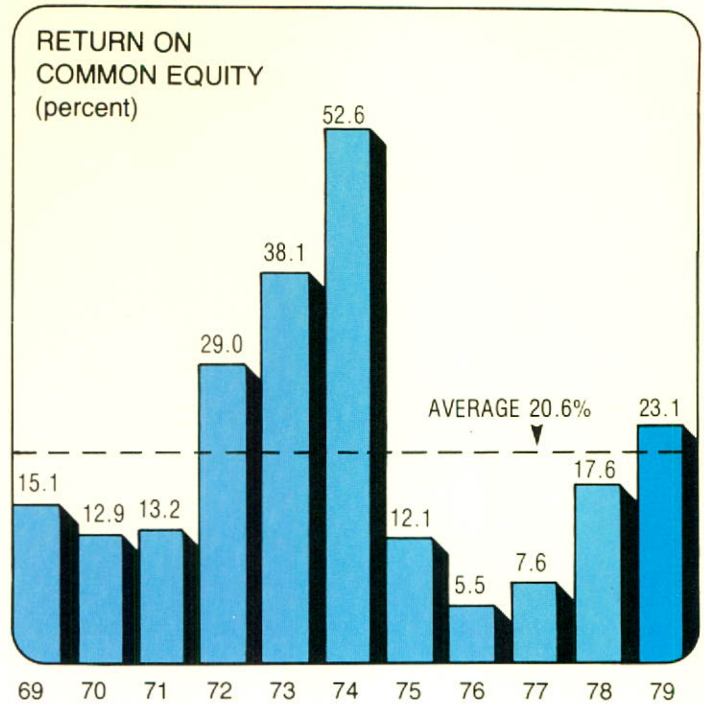


Chart Four

The Power Transmission Group made two moves during the year to strengthen its market position in the north-eastern United States. In June the Group acquired the Lindsay-Oberholzer companies of Philadelphia, and in December purchased the Precision Bearing & Supply Co., Inc., of New Bedford, Massachusetts. Both firms will operate as units of TEK Bearing Company, Inc., the Power Transmission Group operating arm in the United States.

Corporate Goals and Strategy

The corporate objective of Hugh Russel Inc. is to achieve an above-average return on the funds invested in the Corporation. Under present economic circumstances and rates of inflation the Corporation believes this goal will be achieved if the after-tax return on common equity exceeds 15% per year and the Corporation as a whole maintains a long-run growth rate of 15% a year or better.

Corporate strategy is to meet the return on equity goal through the profitable expansion of the Corporation's interests in the field of industrial distribution.

Chart Two illustrates the extent of the Corporation's growth over the past ten years. Net sales have increased ten-fold from $50,000,000 in 1969 to over $500,000,000 last year at a compound growth rate of some 27% — considerably in excess of the 15% annual growth target. Virtually all this growth has been in the distribution field; less than 5% of Russel's current business is in non-distribution activities. Businesses acquired since 1969 now contribute over half of the Corporation's sales.

Charts One and Four show the success achieved by the Corporation in meeting its financial goals. Over the ten-year period growth in earnings per common share has been well ahead of the 15% goal at nearly 25% per year (Chart One). As illustrated by Chart Four, return on common shareholders' equity over the past ten years has averaged 21% — significantly higher than the Corporation's objective of 15%.

Business Outlook

A general economic slowdown has been predicted for the North American economies for some time although to date the evidence for such a broad event is scanty. Nevertheless, it would be realistic to expect the level of business activity in 1980 to be below that of 1979. Interest rates are at historic highs and show little sign of coming down quickly and consumer spending on durables such as automobiles is clearly weaker.

We therefore expect to see a reduction in the operating profits of the Metals Group during 1980 and it is likely that such a reduction will overshadow the improvements expected from the other operating groups during the year.

Looking beyond 1980, any cyclical down-turn is expected to be of short duration, bottoming late this year or in early 1981. Economic conditions should then favour several years of pronounced growth for the Corporation. In short, the profitable growth of the Corporation is expected to continue over the coming five years.

Board of Director Changes

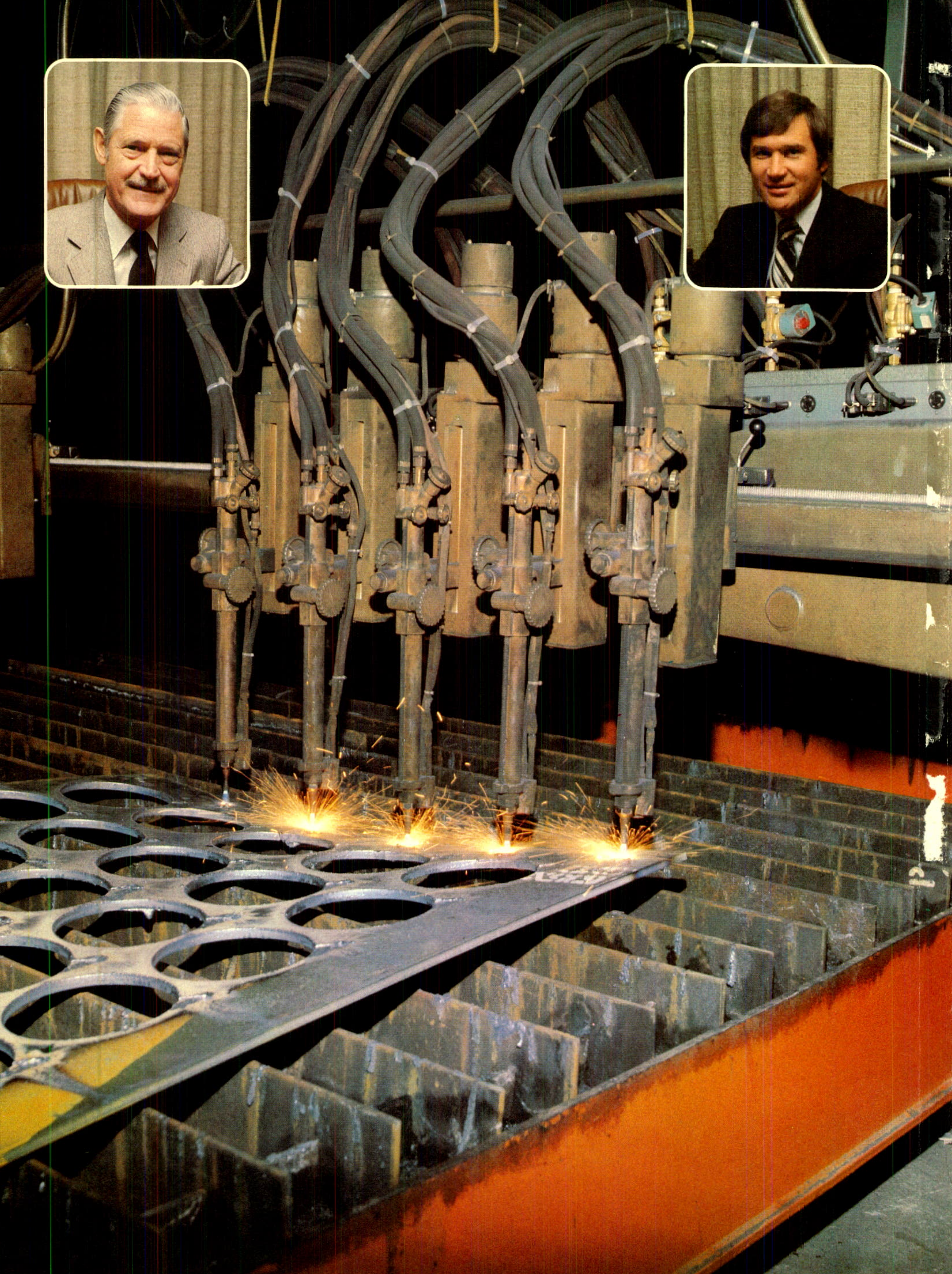
In December 1979, the Russel family agreed to sell its holdings in the Corporation to Bate Chemical Company Limited, a distribution firm owned by the family of G. H. Clifford Smith of Toronto. The transaction, which was essentially for Russel family estate planning purposes, makes Bate Chemical the Corporation's largest shareholder. Bate Chemical's interest is primarily of an investment nature, involving no changes in the Corporation's goals or management. In recognition of the significance of their investment, Mr. G. H. Clifford Smith and Mr. Stephen C. Smith, of Bate Chemical, were invited to join the Board of Directors effective January 21, 1980. Mr. A. D. Russel continues as Chairman of the Board.

Coincident with these changes, Mr. K. D. Mooney and Mr. R. Hartog relinquished their seats on the Russel Board. Mr. Mooney and Mr. Hartog have served as valued members of the Board for more than a decade; their counsel and experienced business judgement through a period of great growth for the Corporation made an important contribution to the success achieved. The Corporation has extended the sincere appreciation of all shareholders to Mr. Mooney and Mr. Hartog for their long and invaluable service.

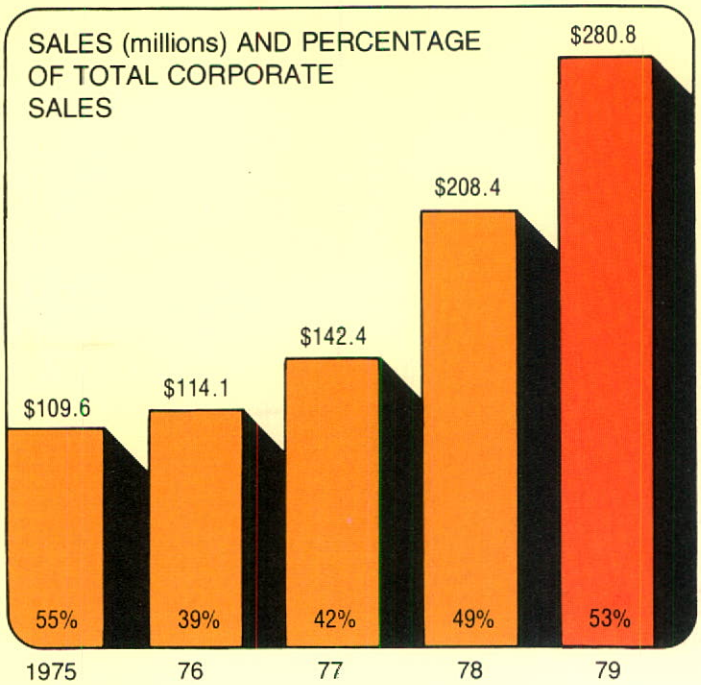
A. D. Russel
Chairman of the Board

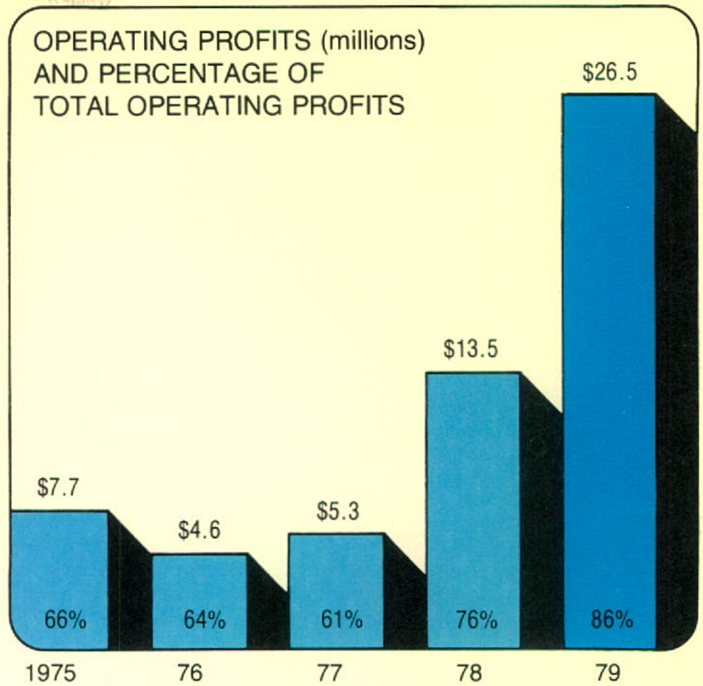
J. P. Foster
President and Chief Executive Officer

Toronto, Ontario
March 14, 1980.



METALS GROUP





The Metals Group is a leading distributor of carbon and alloy steels, operating from 17 steel service centres in Canada and the United States. Operations are conducted through five operating divisions — Russelsteel, Vincent Steel and St. Laurent Steel in Canada; International Alloy Steel and the Baldwin Steel Company in the United States.

The Metals Group serves customers ranging from major corporations to small, metal-working firms across a broad spectrum of industries, including manufacturing, construction, mining, forestry and petroleum exploration and production.

In 1979, the Metals Group recorded outstanding gains in both sales and earnings for the second year in a row. At $280,834,000, Group sales were the highest ever recorded. Operating profits for the Group of $26,477,000 were well ahead of the $13,504,000 earned in 1978. Operating profits were 9.4% of sales, compared to 6.5% last year.

The Metals Group maintained its position as the largest operating group in the Corporation, contributing 53% of total sales and 86% of operating profits.

During 1978, the Metals Group opened a new branch in Nova Scotia extending the Canadian plant network to a coast-to-coast coverage. The major emphasis in 1979 was placed on expanding operations in the United States, particularly in the specialty alloy steel business. In July, Russel acquired the Baldwin Steel Company, a specialty steel distributor with plants in Cleveland and Detroit and 18 sales agencies located in major centres in the United States. International Alloy Steel, acquired by Russel in 1978, also operates as a specialty steel distributor with 22 sales offices and plants in Cleveland and Clearfield, Utah.

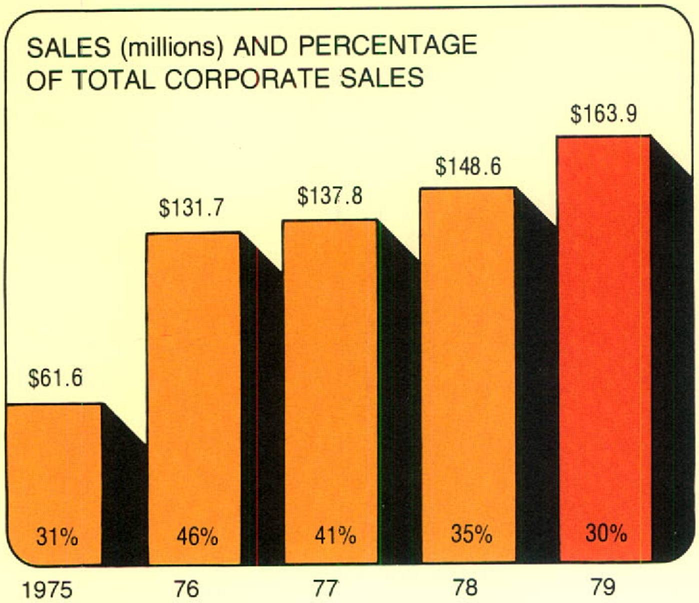
The Buffalo steel service centre, opened by Russelsteel in 1978 to serve markets in upper New York State and Pennsylvania, is already operating profitably.

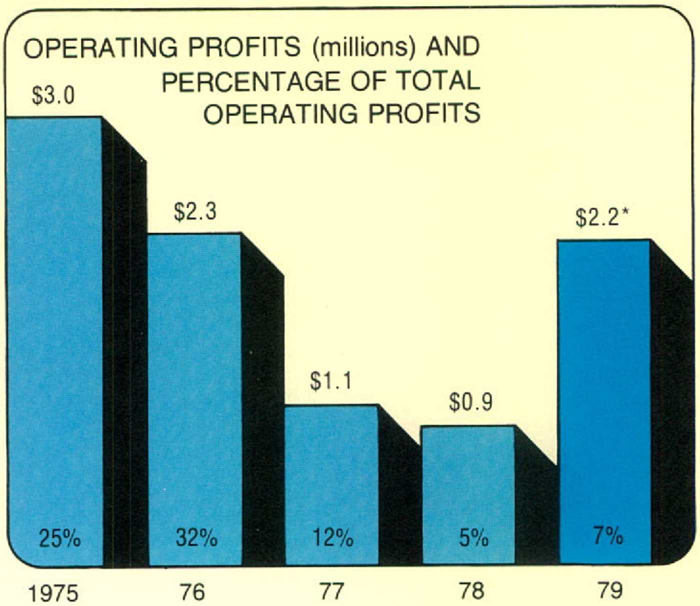
Although an anticipated slowdown in North American steel markets may lead to somewhat lower operating profit margins over the short term, the Metals Group is expected to consolidate and strengthen its position in both Canadian and United States markets in 1980.

Opposite Page:
Torch cutting equipment is used to pre-process steel plate to customer specifications. The intricate Russel logo on the front cover was cut from steel plate by this machine.
Inset Left:
M. D. Glenn, Chairman, Metals Group
Inset Right:
W. P. E. Mang, President, Metals Group


AJAX

HOME PRODUCTS GROUP





The Home Products Group is engaged in three distinct distribution activities:

- distribution to industrial customers;
- wholesaling to the retail trade; and
- retail merchandising.

Products distributed by the Group include hardware, electrical and sporting goods, plumbing, heating and air conditioning products, and building materials.

An important element of the business is the distribution of the Group's products and services to independent retail merchants and mass merchandisers serving the growing market for "Do-it-Yourself" home improvements.

As a result of rapid growth through the acquisition of a number of geographically and operationally diverse companies, the Group has been engaged in a continual process of consolidation and reorganization over the past few years. This has held profits to low levels.

Reorganization of acquired companies and facilities continued in 1979 with the closure of the 143,000 sq. ft. Boucherville warehouse in Quebec early in the year. This facility has operated at a substantial loss ever since the acquisition of the Lacroix business in 1976.

During 1979, sales at $162,854,000 were 10% ahead of those for 1978; operating profits at $2,240,000 were considerably ahead of the previous year. These operating profits are before a one-time charge of $1,671,000 arising from the closure of the Boucherville facility.

An outstanding feature of the 1979 Group results was the excellent performance of the Lytle Division. This firm specializes in the distribution of industrial and high technology valves through eight Canadian branches. In 1980, the Division will open its first U.S. branch in Philadelphia.

The outlook for the Home Products Group continues to be as outlined by the President at the April 12, 1979, Annual Meeting. The Group should make steady progress in 1980 but satisfactory profits will not be achieved before 1981.

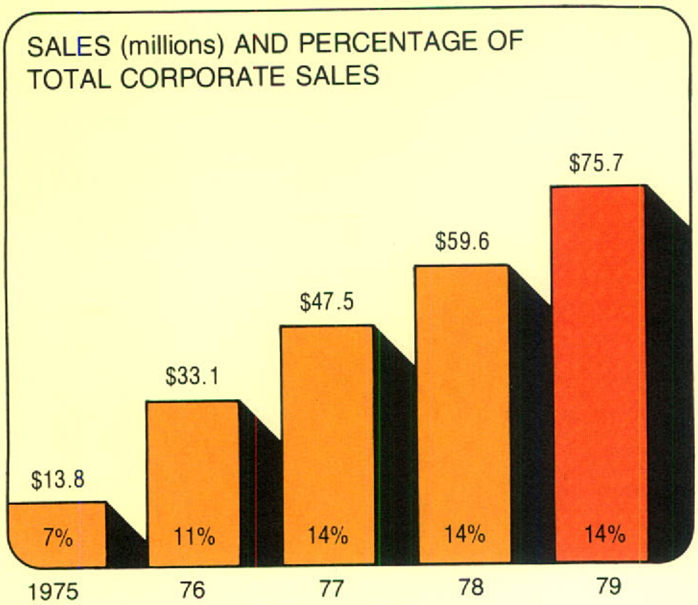
*Excludes one-time charge associated with Boucherville plant closure.

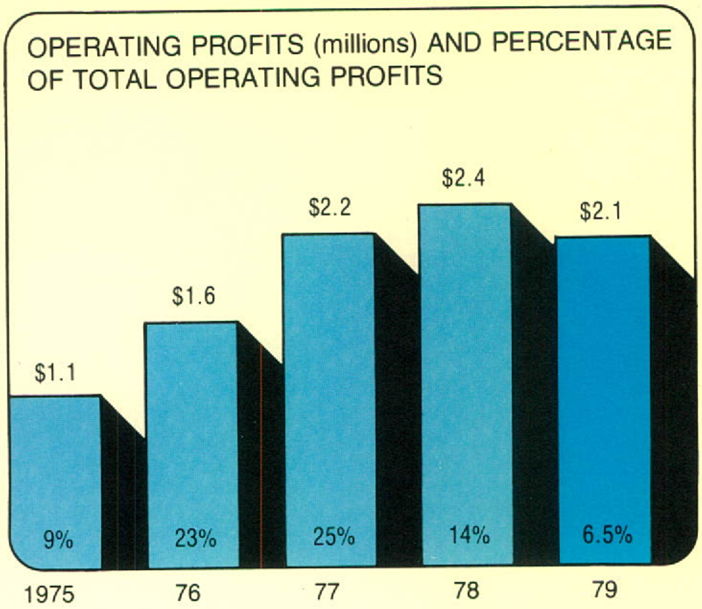
Opposite Page:
Large regional warehouses, with the movement of thousands of product items controlled by computer, are important factors in the service efficiency and competitiveness of the Home Products Group.
Inset Left:
J. M. O'Sullivan, Executive Vice-President, Home Products Group
Inset Right:
G. T. Urquhart, President, Home Products Group


ROW 4
ROW 3
TIMKEN
SKF
OIL SEALS
JOINTS D'ÉTANCHÉITÉ

Review of Business Operations

POWER TRANSMISSION GROUP





The Power Transmission Group is a supplier of over 100,000 industrial machinery parts and components, including ball, roller and other anti-friction bearings, gears, drives, bushings, mechanical power transmission components, lubricants and related accessories. The Group also supplies and services a comprehensive line of electrical, pneumatic and fluid power transmission components and products.

The Group operates from a network of 42 service branches in Canada and the United States — 17 branches of Canadian Bearings Co. Limited in Ontario and Quebec; and 25 service centres operated by the TEK Bearing Company, Inc., in the north-eastern United States.

The Power Transmission Group recorded a substantial increase in sales in 1979. Total sales were $75,665,000, up by 27% from the $59,576,000 reported last year. Markets in the New England states have been characterized by aggressive competition in recent months, bringing pressure on profit margins and operating costs. This, together with rising interest rates, precluded a repetition of last year's record profits. Operating profits for 1979 were $2,081,000, down by 13% from 1978.

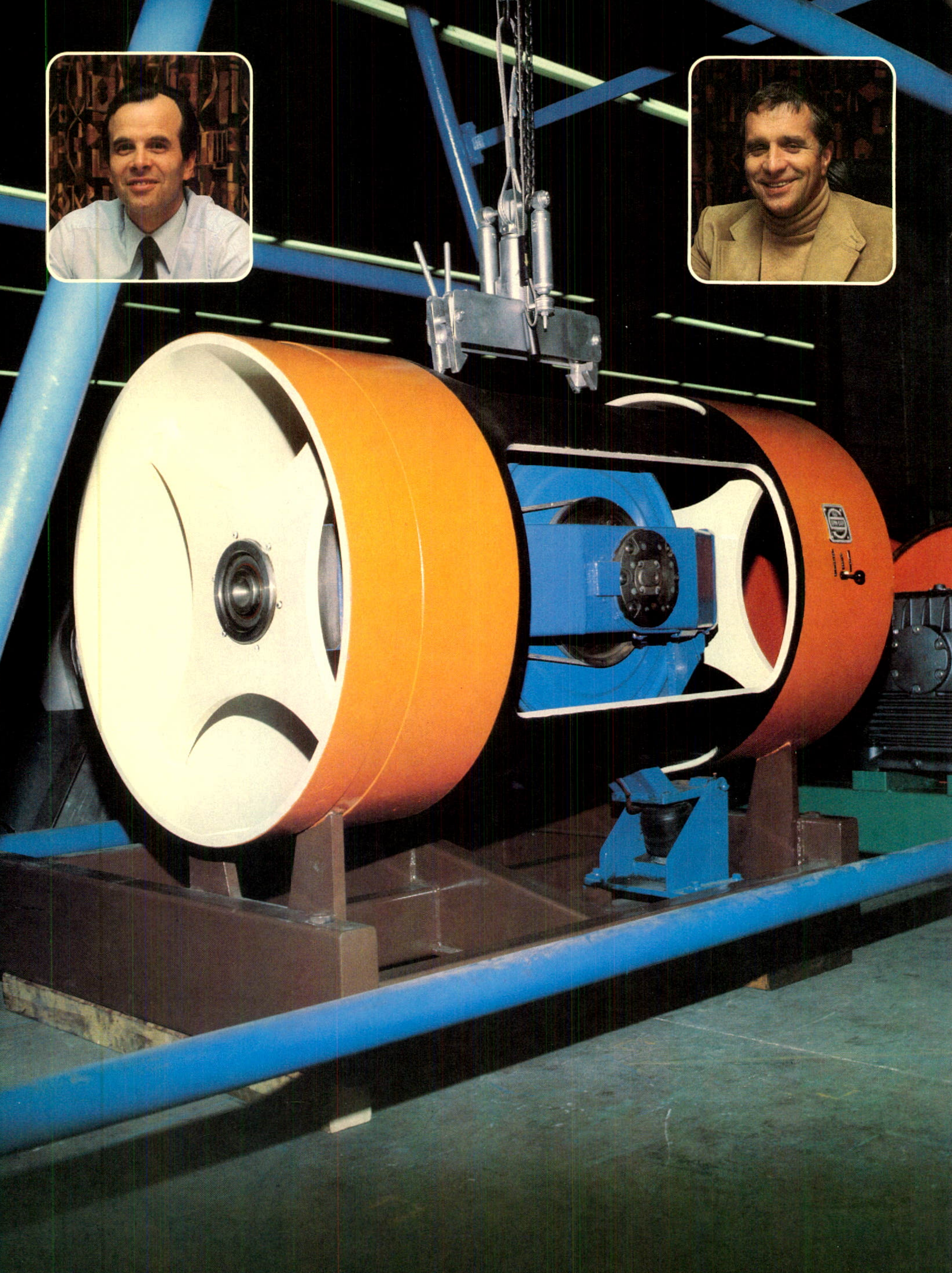
In June of 1979, the Lindsay-Oberholzer companies were acquired, providing the Group with new, established distribution operations in Philadelphia, Pennsylvania, and Wilmington, Delaware. In December, the Group purchased the Precision Bearing & Supply Co., Inc., of New Bedford, Massachusetts, strengthening the long-established base in the New England region.

The Group also extended its branch system, opening new outlets at Sault Ste. Marie, Ontario; Danbury, Connecticut; Nashua, New Hampshire; and Camden, New Jersey.

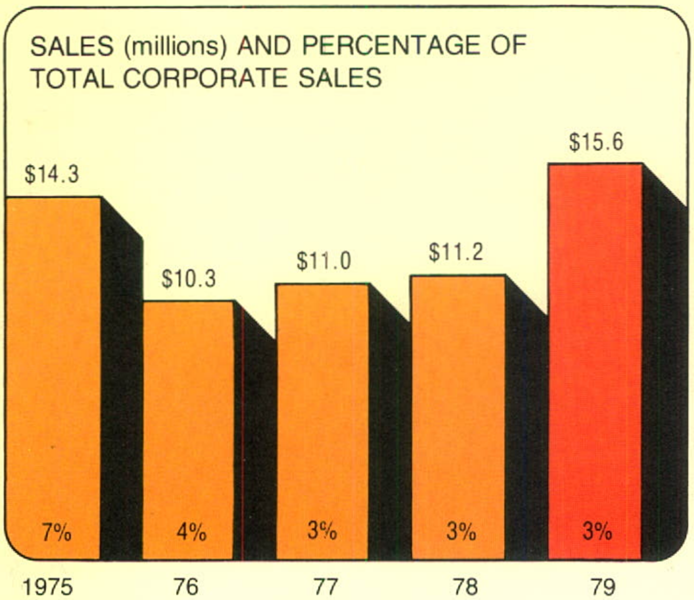
Despite less than buoyant markets and an increasingly competitive environment on both sides of the border, the Group expects increased sales with improved profitability during 1980.

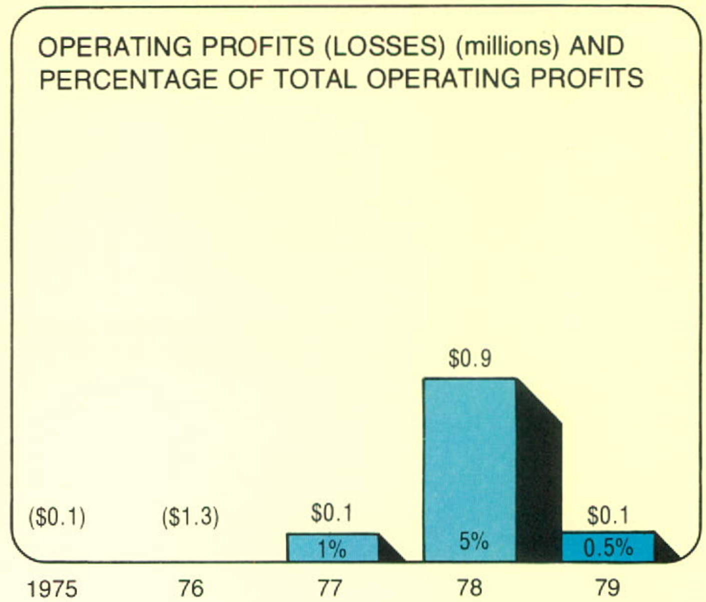
Further penetration of United States markets remains a high priority goal for the Power Transmission Group.

Opposite page:
Shelves of components in a typical Power Transmission branch warehouse. The thousands of items stocked in the Group's 42 branches are controlled by central computer: facilities and branches are restocked daily to keep inventory costs at a minimum.
Inset:
J. B. Adams, President, Power Transmission Group



ENGINEERING GROUP





Through its two principal operating divisions, Ceeco Machinery Manufacturing Limited in Toronto, and Syncro Machine Company in Perth Amboy, New Jersey, the Engineering Group designs and manufacturers wire and cable machinery used in the electrical cable, telecommunications and steel wire rope industries.

Ceeco Machinery produces wire stranding and processing equipment, while Syncro Machine manufactures wire drawing and related equipment. The Group has joint venture and licensing agreements in Brazil and Mexico through which its equipment is manufactured and sold.

International business continued to be a major area of activity for the Group and in 1979 over 80% of shipments were made to customers located outside of Canada. A subsidiary sales company, WICAMA Handels GmBH, in Germany, and the joint ventures and licensees were instrumental in securing this business.

Sales in 1979 were $15,554,000, up 40% over last year. Development costs associated with the new orbital strander and the introduction of other newly-designed equipment reduced operating profits sharply to $119,000.

During 1979, the Engineering Group obtained several important contracts for large steel wire rope equipment from North American producers. At the same time, the first commercial production models of the orbital strander system developed under a program sponsored by the Canadian government were delivered to customers in North America and Europe.

The success of the orbital strander system was a major factor in persuading the Canadian government to finance another major development program. This involves the design and manufacture of machines for handling reels weighing up to 100 metric tonnes. The first machine built under this latter program has already been sold to a major Mexican producer.

The increasing volume of business generated by these new product lines put a severe strain on the capacity of the Ceeco plant in Toronto during 1979. A move to new Toronto facilities built to the Engineering Group's specification will take place in the Spring of 1980. This new plant will provide one of the world's most modern facilities for the production of machinery for the wire industry.

The Engineering Group is a rapidly maturing manufacturing business with an established product line. This means a steadily lessening impact of the engineering and marketing costs associated with the design and introduction of new technology and steadily improving profitability for the Group.

Opposite Page:
The Ceeco patented orbital strander. This Canadian designed machinery has helped in bringing new efficiency and safety to the international cable industry.
Inset Left:
R. G. Rossi, Executive Vice-President, Engineering Group
Inset Right:
A. Varga, President, Engineering Group

Hugh Russel Inc.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT DECEMBER 31, 1979 (with comparative figures as at December 31, 1978)

	1979	1978
	(thousands of dollars)	
Current assets:		
Accounts receivable	$ 95,880	$ 79,153
Inventories	119,846	92,247
Prepaid expenses and other assets	5,074	4,364
	220,800	175,764
Current liabilities:		
Bank indebtedness (note 2)	86,027	77,184
Accounts payable and accrued charges	62,118	49,888
Income taxes payable	11,613	4,333
Contractual obligations due within one year (note 10)	3,075	1,586
Long term debt due within one year (note 6)	1,121	408
Capital lease obligations due within one year (note 10)	99	—
	164,053	133,399
Working capital	56,747	42,365
Other assets:		
Fixed assets (note 3)	25,855	23,719
Premiums on acquisition and other assets	20,961	14,281
Long term investments and advances	1,368	1,367
Deferred income taxes	1,944	348
	50,128	39,715
Capital employed	$106,875	$ 82,080
Represented by:		
Long term debt (note 6)	$ 19,207	$ 18,801
Deferred gains (note 11)	1,226	1,428
Obligations under capital leases (note 10)	1,835	—
Contractual obligations (note 10)	561	2,150
	22,829	22,379
Shareholders' equity —		
Share capital (note 7)	35,266	20,037
Contributed surplus	79	79
Retained earnings	48,701	39,585
	84,046	59,701
Capital employed	$106,875	$ 82,080
Total assets	$270,928	$215,479

(See accompanying notes)

On behalf of the Board:

A. D. Russel, Director
J. P. Foster, Director

CONSOLIDATED STATEMENTS OF EARNINGS AND RETAINED EARNINGS for the year ended December 31, 1979 (with comparative figures for 1978)

	1979		1978	
	(thousands of dollars except per share figures)			
Statement of Earnings		%		%
Sales	$534,907	100.0	$427,772	100.0
Cost of sales	412,878	77.2	336,525	78.6
Gross profit	122,029	22.8	91,247	21.4
Operating expenses other than depreciation and interest	78,775	14.7	64,075	15.0
Discontinued operations (note 5)	1,671	0.3	—	—
Earnings from operations before deducting the following:	41,583	7.8	27,172	6.4
Depreciation	2,523	0.5	2,079	0.5
Interest on short term borrowings	9,438	1.8	6,634	1.6
Interest on long term debt	2,474	0.4	2,281	0.5
Earnings before income taxes and amortization	27,148	5.1	16,178	3.8
Income taxes	12,035	2.3	6,766	1.6
Amortization of premiums on acquisition and other assets	1,041	0.2	244	0.1
Net earnings for the year	$ 14,072	2.6	$ 9,168	2.1
Earnings Per Common Share				
Net earnings for the year	$ 14,072		$ 9,168	
Preferred dividends	1,535		975	
Earnings attributable to common shares	$ 12,537		$ 8,193	
Earnings per common share	$ 4.84		$ 3.15	
Statement of Retained Earnings				
Retained earnings, beginning of year	$ 39,585		$ 33,258	
Net earnings for the year	14,072		9,168	
	53,657		42,426	
Deduct:				
Dividends paid on preferred shares	1,535		975	
Dividends paid on common shares (including value of stock dividends on Class B shares)	1,899		1,665	
Share repurchase	986		201	
Preferred share issue expenses	536		—	
Retained earnings, end of year	$ 48,701		$ 39,585	

(See accompanying notes)

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION for the year ended December 31, 1979 (with comparative figures for 1978)

		1979	1978
		(thousands of dollars)	
Working capital was obtained from:			
Operations —			
Net earnings for the year		$14,072	$ 9,168
Items not requiring working capital:			
Depreciation		2,523	2,079
Deferred income taxes		(1,596)	(145)
Amortization of premiums on acquisition and other assets		1,041	244
Amortization of deferred gain		(136)	(97)
		15,904	11,249
Disposal of fixed assets		1,621	588
Issue of preferred shares		15,000	—
Reduction in investments and advances		156	401
Deferred foreign exchange gain		(66)	180
Common shares issued under the employee share purchase plan		92	17
Common shares issued for stock dividend		521	—
Capital lease obligations assumed		2,171	—
Other long term debt issued		1,642	—
		37,041	12,435
Working capital was applied to:			
Acquire businesses		12,077	5,260
Less working capital obtained		5,827	4,046
		6,250	1,214
Consisting of —			
Fixed assets	$ 164		
Premiums on acquisition and other assets	6,156		
Long-term debt	(70)		
	$6,250		
Purchase fixed assets		3,945	1,465
Fixed assets acquired under capital leases		2,171	—
Increase premiums on previous acquisitions		1,565	510
Reduce contractual obligations		1,589	1,095
Reduce long term debt		1,306	1,566
Purchase common shares for cancellation		1,370	318
Pay dividends		3,434	2,640
Preferred share issue expenses		536	—
Long term advances		157	222
Reduce capital lease obligations		336	—
		22,659	9,030
Increase in working capital		14,382	3,405
Working capital, beginning of year		42,365	38,960
Working capital, end of year		$56,747	$42,365

(See accompanying notes)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1979

1. Accounting Policies

These financial statements have been prepared on the basis of information available up to January 28, 1980.

The following is a summary of the significant accounting policies followed by Hugh Russel Inc. in the preparation of the consolidated financial statements.

(a) Principles of consolidation —
The accompanying financial statements include the accounts of Hugh Russel Inc. and all subsidiaries.

(b) Foreign currency translation —
The accounts of foreign subsidiaries and foreign currency balances have been translated into Canadian dollars as follows:

(i) Current assets and current liabilities at exchange rates prevailing at year end;
(ii) Depreciation and non-current assets and liabilities at exchange rates prevailing on the dates of acquisition;
(iii) Revenues and expenses (other than depreciation) at average rates during the year.

Cumulative unrealized net gains on translation have been included in deferred gains in the Statement of Financial Position.

(c) Inventories —
Inventories are stated at the lower of cost and net realizable value. Canadian subsidiaries determine cost on a first-in, first-out (FIFO) or an average cost basis. United States subsidiaries determine cost on a last-in, first-out (LIFO) basis.

(d) Depreciation —
Depreciation is calculated on a straight line basis except in the Home Products Group where depreciation is calculated on a declining balance basis. The rates of depreciation are:

	Home Products Group	Other Groups
Buildings	5% and 10%	2½% to 10%
Machinery and equipment	15% and 20%	10% and 20%

(e) Premiums on acquisitions —
Premiums on acquisitions made prior to April, 1974 are carried at cost, without amortization. Premiums on acquisitions made subsequent to April, 1974 are being amortized over forty years. Irrespective of acquisition date, if a business is sold, is determined to have a limited life or suffers a decline in value that is other than temporary, the related premium is amortized over an appropriately shorter period.

(f) Other Assets —
Other assets, consisting mainly of patents, trademarks and contracts, are being amortized over the estimated life of the asset.

2. Bank Indebtedness

Accounts receivable and inventories have been pledged against bank indebtedness.

3. Fixed Assets

	1979			1978
	Cost	**Accumulated Depreciation**	**Net**	**Net**
Land	**$ 4,476,000**	**$ —**	**$ 4,476,000**	$ 4,550,000
Buildings	**19,553,000**	**5,915,000**	**13,638,000**	14,016,000
Machinery and equipment	**15,399,000**	**9,506,000**	**5,893,000**	5,153,000
	39,428,000	**15,421,000**	**24,007,000**	23,719,000
Assets Under Capital Leases:				
Land	**34,000**	**—**	**34,000**	—
Buildings	**851,000**	**30,000**	**821,000**	—
Machinery and equipment	**1,286,000**	**293,000**	**993,000**	—
	2,171,000	**323,000**	**1,848,000**	—
Total	**$41,599,000**	**$15,744,000**	**$25,855,000**	$23,719,000

4. Acquisitions

During 1979, subsidiaries of the Corporation made the following acquisitions:

(i) certain assets of the Baldwin Steel companies, privately held distributors of specialty steels, located in Cleveland and Detroit, U.S.A;

(ii) all the outstanding shares of the Lindsay-Oberholzer companies, privately held distributors of power transmission products, located in Philadelphia and Wilmington, U.S.A; and

(iii) certain assets of Precision Bearing & Supply Co., Inc., a privately held distributor of power transmission products located in New Bedford, Massachusetts, U.S.A.

The transactions have been accounted for by the purchase method.

The assets acquired were as follows:

	Baldwin Steel	**Lindsay-Oberholzer**	**Precision Bearing**
Tangible assets acquired	$ 4,844,000	$1,238,000	$378,000
Less liabilities assumed	—	539,000	—
	4,844,000	699,000	378,000
Other assets acquired	4,837,000	98,000	—
	9,681,000	797,000	378,000
Premium on acquisition	1,014,000	195,000	12,000
Cash consideration	$10,695,000	$ 992,000	$390,000
Effective date of acquisition	July 5	April 1	Nov. 30

5. Discontinued Operations

On July 1, 1979 a subsidiary, Lacroix (Quebec) Inc. closed its warehouse at Boucherville, Quebec. Costs resulting from this closure, including a write-down of the carrying value of the fixed assets, amounted to $1,671,000 before tax.

6. Long Term Debt

Hugh Russel Inc.	**1979**	1978
Secured sinking fund debentures		
$6\frac{1}{4}\%$ Series A, maturing 1985	**$ 1,328,000**	$ 1,336,000
10% Series B, maturing 1991	**2,390,000**	2,500,000
$8\frac{1}{2}\%$ Series C, maturing 1993	**4,100,000**	4,100,000
11% Series D, maturing 1995	**8,665,000**	9,030,000
	16,483,000	16,966,000
Subsidiary Companies		
Sumner Company Limited		
$6\frac{1}{2}\%$ general mortgage bonds, maturing 1984	**381,000**	446,000
Mortgages and other long term liabilities	**3,464,000**	1,797,000
	20,328,000	19,209,000
Less payments of principal due within one year, included in current liabilities	**1,121,000**	408,000
Total	**$19,207,000**	$18,801,000

Maturities and sinking fund requirements for the years 1980 through 1984 are:

1980	$1,121,000
1981	$ 901,000
1982	$ 960,000
1983	$1,176,000
1984	$1,203,000

The Series A, B, C and D debentures are secured by a first mortgage on the fixed assets and by a first floating charge on the remaining assets of the Corporation.

At December 31, 1979, the Corporation had satisfied all the requirements and general conditions of the debenture trust deeds, including those relating to payment of dividends.

7. Share Capital

Authorized:

The Corporation is authorized to issue:

(a) 1,750,000 First Preferred Shares of which 1,250,000 have been designated as follows:

(i) 500,000 9¾% Cumulative Redeemable First Preferred Shares Series B. These shares are entitled to a dividend of $1.95 per share per annum and are not redeemable before February 10, 1982, but will be redeemable thereafter at prices varying between $21.40 and $20.00. Prior to February 10, 1982, the shares may be purchased at a price not exceeding $21.95.

(ii) 750,000 $1.70 Cumulative Redeemable First Preferred Shares Series C. These shares are not redeemable before June 7, 1984, but will be redeemable thereafter at prices varying between $21.20 and $20.00. Prior to June 7, 1984, the shares may be purchased at a price not exceeding $21.70.

(b) An unlimited number of Class A and Class B common shares. These shares are interconvertible on a share for share basis at the holder's option.

Issued:

At December 31, 1979, the issued share capital comprised:

(a) First Preferred Shares:
500,000 First Preferred Shares Series B, issued for $10,000,000.
750,000 First Preferred Shares Series C, issued for $15,000,000.

(b) Common Shares:

Number of Shares			Issued For
Class A	Class B		
1,897,027	693,456	Outstanding at December 31, 1978	$10,037,000
17,123	—	Shares issued under provisions of the Employees' Share Purchase Plan	92,000
—	38,718	Common shares issued for stock dividend	521,000
(96,900)	—	Repurchased by the Corporation	(384,000)
(117,491)	117,491	Net transfers between classes	—
1,699,759	849,665	Outstanding at December 31, 1979	$10,266,000

During 1979, the Corporation purchased and cancelled 96,900 Class A common shares for $1,370,000 cash, of which $384,000 was deducted from share capital and $986,000 was charged to retained earnings.

8. Indebtedness to the Corporation and Subsidiaries

(a) The Corporation is authorized to provide loans to a trustee for the purchase of shares of the Corporation for the benefit of senior officers (who may be directors) specified by the Board of Directors. At December 31, 1979, the Corporation had advanced a total of $296,000 to the trustee pursuant to this plan.

(b) The Corporation has made non-interest bearing loans to eleven employees, two of whom are officers, to assist them upon relocation to purchase living accommodation for their occupation, while employed by the Corporation. The loans, amounting to $680,000 at December 31, 1979, are repayable over five or ten year terms and are secured by first mortgages.

9. Classes of Business

The Board of Directors has determined that the Corporation's classes of business, determined by reference to the Corporation's operating groups, are metals distribution, power transmission distribution, home products distribution and engineering and manufacturing and this has been recorded in the minutes.

10. Commitments

(a) Payments required on contractual obligations, primarily related to businesses previously acquired, are as follows:

1980	$3,075,000
1981	227,000
1982 and thereafter	334,000

(b) The Corporation has entered into operating lease agreements, primarily for warehouse and office space, which expire in various years between 1980 and 2000. Most have renewal options at rates to be negotiated. The Corporation also has a number of lease agreements that are required to be classified as capital leases, which expire in various years between 1987 and 1998.

Payments for the next five years for each type of lease commitment are:

	Operating Leases	Capital Leases
1980	$1,800,000	$ 99,000
1981	1,570,000	111,000
1982	1,205,000	125,000
1983	941,000	140,000
1984	802,000	157,000

11. Deferred Gains

Deferred gains comprise the unamortized balance of the gain resulting from the 1977 sale and leaseback by a subsidiary of its machinery and equipment, together with the gain resulting from the translation into Canadian funds of the Corporation's foreign operations.

AUDITORS' REPORT

Clarkson Gordon

To the Shareholders of
Hugh Russel Inc.:

We have examined the consolidated statement of financial position of Hugh Russel Inc. as at December 31, 1979 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. For Hugh Russel Inc. and those subsidiaries of which we are the auditors, 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. For those subsidiaries of which we are not the auditors, we have carried out such enquiries and examinations as we considered necessary in order to rely on the reports of the other auditors for purposes of consolidation.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1979 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Clarkson Gordon

Chartered Accountants

Toronto, Canada
January 28, 1980.

STATEMENT OF SEGMENTED INFORMATION

Year ended December 31, 1979

(Thousands of dollars)

	Metals	Power Transmission	Home Products	Engineering & Manufacturing	Consolidated
Sales to customers outside the corporation	$280,834	$75,665	$162,854	$15,554	$534,907
Inter-segment sales	2,903	97	—	418	3,418
Total sales	$283,737	$75,762	$162,854	$15,972	$538,325
Segment operating profit	$ 26,477	$ 2,081	$ 569	$ 119	$ 29,246
General corporate expenses					(2,098)
Income taxes					(12,035)
Amortization of other assets					(1,041)
Net income					$ 14,072
Capital expenditures	$ 2,173	$ 343	$ 1,287	$ 93	
Depreciation	$ 924	$ 217	$ 920	$ 303	

Notes:

(i) Details of the nature of the business conducted by each industry segment are disclosed fully elsewhere in this report.

(ii) Inter-segment sales are accounted for at market prices for similar products.

RESULTS BY QUARTER

Sales (Thousands of dollars)

Quarter	**1979**	1978	1977	1976	1975	1974
First	**$117,858**	$ 91,329	$ 72,659	$ 56,457	$ 48,088	$ 54,234
Second	**133,470**	111,254	88,288	73,660	47,763	66,723
Third	**141,686**	110,784	87,360	81,514	43,139	67,748
Fourth	**141,893**	114,405	90,432	77,533	60,308	74,094
TOTAL	**$534,907**	$427,772	$338,739	$289,164	$199,298	$262,800

Earnings per Common Share (Fully Diluted)

Quarter	**1979**	1978	1977	1976	1975	1974
First	**$0.73**	$0.22	$0.03	$0.21	$0.55	$1.61
Second	**1.32**	0.95	0.46	0.46	0.32	1.97
Third	**1.05**	0.96	0.36	0.26	0.43	1.57
Fourth	**1.74**	1.02	0.40	(.05)	0.53	0.90
TOTAL	**$4.84**	$3.15	$1.25	$0.88	$1.83	$6.05

Consolidated Financial Information

Ten Year Summary

Operating Results (thousands)	1979	1978
Sales	$534,907	$427,772
Earnings before deducting the following:	$ 33,816	$ 20,538
Depreciation	$ 2,523	$ 2,079
Interest on long term debt	$ 2,474	$ 2,281
Income taxes	$ 12,035	$ 6,766
Discontinued operations	$ 1,671	—
Amortization of premiums on acquisition and other assets	$ 1,041	$ 244
Earnings (1)	$ 14,072	$ 9,168
Per Share of Common Stock (1)		
Based on average common shares outstanding (thousands)	2,590	2,600
Earnings — fully diluted	$ 4.84	$ 3.15
Cash flow	$ 5.55	$ 3.95
Dividends paid	$ 0.73	$ 0.64
Book value	$ 23.16	$ 19.19
Market price — High	$ 16.00	$ 13.25
Market price — Low	$ 11.75	$ 8.50
Operating Statistics (1)		
Earnings to sales	2.6%	2.1%
Earnings to average common shareholders' equity	23.1%	17.6%
Earnings to average capital employed	14.9%	11.4%
Financial Ratios		
Total shareholders' equity to total assets	31.0%	27.7%
Current assets/total assets	81.5%	81.6%
Sales/working capital	9.4	10.1
Sales to total assets	2.0	2.0
Current assets/current liabilities	1.3	1.3
Long term debt interest coverage	11.6	8.0
Other Statistics		
Capital expenditures (thousands)	$ 3,945	$ 1,465
Total dividends paid (thousands)	$ 3,434	$ 2,640
Total dividends to earnings	24.4%	28.8%
Number of common shareholders	2,488	2,555
Number of shares traded (thousands)	1,235	670
Balance Sheet Data (thousands)		
Current assets	$220,800	$175,764
Current liabilities	$164,053	$133,399
Working capital	$ 56,747	$ 42,365
Fixed assets	$ 25,855	$ 23,719
Long term debt	$ 19,207	$ 18,801
Shareholders' equity	$ 84,046	$ 59,701
Capital employed	$106,875	$ 82,080
Total assets	$270,928	$215,479

(1) After adjusting for stock splits and before extraordinary items.

1977	1976	1975	1974	1973	1972	1971	1970	1969
$338,739	$289,164	$199,298	$262,800	$130,391	$99,106	$67,350	$61,113	$49,819
$ 11,879	$ 9,569	$ 13,418	$ 34,198	$ 13,887	$ 5,838	$ 2,933	$ 2,628	$ 2,373
$ 2,177	$ 1,835	$ 1,531	$ 1,228	$ 864	$ 738	$ 604	$ 513	$ 310
$ 2,613	$ 2,785	$ 1,889	$ 1,026	$ 986	$ 526	$ 359	$ 179	$ 148
$ 2,792	$ 2,587	$ 5,228	$ 16,281	$ 5,969	$ 2,182	$ 1,006	$ 1,052	$ 1,072
—	—	—	—	—	—	—	—	—
$ 212	$ 75	$ 16	—	—	—	—	—	—
$ 4,085	$ 2,287	$ 4,754	$ 15,663	$ 6,068	$ 2,392	$ 964	$ 884	$ 843
2,613	2,601	2,574	2,502	2,108	1,326	1,266	1,254	1,254
$ 1.25	$ 0.88	$ 1.83	$ 6.05	$ 2.35	$ 1.17	$ 0.49	$ 0.46	$ 0.53
$ 2.09	$ 1.35	$ 2.61	$ 6.76	$ 3.24	$ 2.36	$ 1.13	$ 0.98	$ 0.77
$ 0.64	$ 0.58	$ 0.50½	$ 0.40¼	$ 0.30¾	$ 0.22¾	$ 0.20	$ 0.20	$ 0.20
$ 16.64	$ 16.36	$ 15.92	$ 14.79	$ 9.29	$ 6.24	$ 4.70	$ 4.31	$ 3.98
$ 9.88	$ 13.00	$ 15.13	$ 21.00	$ 15.50	$ 13.00	$ 4.94	$ 5.56	$ 5.50
$ 7.50	$ 8.25	$ 9.75	$ 11.88	$ 10.00	$ 3.88	$ 3.25	$ 3.75	$ 3.94
1.2%	0.8%	2.4%	6.0%	4.7%	2.4%	1.4%	1.4%	1.7%
7.6%	5.5%	12.1%	52.6%	38.1%	29.0%	13.2%	12.9%	15.1%
5.3%	2.7%	7.8%	35.5%	18.3%	12.2%	5.9%	6.9%	9.1%
29.8%	25.5%	30.0%	32.7%	35.8%	23.7%	25.4%	25.6%	36.8%
78.0%	76.6%	76.2%	79.7%	78.0%	79.8%	75.6%	75.6%	78.4%
8.7	9.3	5.4	9.1	6.1	8.9	7.3	9.5	8.1
1.9	1.8	1.5	2.3	2.0	2.0	1.8	1.8	2.2
1.4	1.3	1.6	1.5	1.8	1.5	1.5	1.3	1.5
3.7	2.8	6.3	32.1	13.2	9.7	6.5	11.8	13.9
$ 1,617	$ 4,331	$ 2,107	$ 3,539	$ 1,094	$ 1,177	$ 825	$ 1,230	$ 437
$ 2,491	$ 1,509	$ 1,306	$ 1,036	$ 794	$ 505	$ 468	$ 465	$ 365
61.0%	66.0%	27.5%	6.6%	13.1%	21.1%	48.5%	52.6%	43.3%
2,425	2,372	2,481	2,209	1,975	1,204	837	798	760
289	440	428	976	1,024	1,083	184	354	392
$140,112	$126,300	$104,680	$ 91,997	$ 50,096	$39,480	$27,524	$25,728	$17,659
$101,152	$ 95,282	$ 67,733	$ 62,958	$ 28,545	$28,293	$18,339	$19,271	$11,523
$ 38,960	$ 31,018	$ 36,947	$ 29,039	$ 21,551	$11,187	$ 9,185	$ 6,457	$ 6,136
$ 24,773	$ 25,078	$ 20,330	$ 12,774	$ 9,869	$ 8,635	$ 6,875	$ 6,637	$ 3,584
$ 20,367	$ 21,063	$ 21,738	$ 11,665	$ 11,170	$ 6,515	$ 5,282	$ 2,541	$ 2,292
$ 53,474	$ 42,062	$ 41,257	$ 37,790	$ 23,027	$11,736	$ 9,268	$ 8,706	$ 8,287
$ 78,431	$ 69,642	$ 69,689	$ 52,513	$ 35,698	$21,205	$18,087	$14,780	$10,993
$179,583	$164,924	$137,422	$115,471	$ 64,243	$49,498	$36,426	$34,051	$22,516

Corporate Directory

Hugh Russel Inc.
Head Office:
2 St. Clair Avenue East
Suite 700,
Toronto, Ontario, M4T 2T5
Telephone: (416) 924-9104

Registrars and Transfer Agents
Common and Preferred shares:
Montreal Trust Company, Toronto, Montreal, Winnipeg, Regina, Calgary, Vancouver

General Counsel
J. D. Reilly, Q.C.

Auditors
Clarkson Gordon

Stock Exchanges
Common shares:
Montreal and Toronto:
Stock symbol: RUA

Preferred shares:
Toronto

Board of Directors

A. D. Russel*
Toronto, Ontario
Chairman of the Board
Hugh Russel Inc.

J. B. Adams
Oakville, Ontario
President, Power Transmission Group
Hugh Russel Inc.

J. P. Foster
Toronto, Ontario
President and Chief Executive Officer
Hugh Russel Inc.

M. D. Glenn
Thornhill, Ontario
Chairman, Metals Group
Hugh Russel Inc.

J. D. Reilly, Q.C.*
Toronto, Ontario
Partner, Hill, Friend & Reilly

G. D. Shearer, C.A.
Toronto, Ontario
Vice-President Finance, Russelsteel Division, Hugh Russel Inc.

G. H. C. Smith
Chairman
Bate Chemical Company Limited

S. C. Smith*
Toronto, Ontario
Partner, McCarthy & McCarthy

G. T. Urquhart
Moncton, New Brunswick
President, Home Products Group
Hugh Russel Inc.

J. W. Vingoe*
Weston, Ontario
President, Hauserman Ltd.

*A member of the Audit Committee

Corporate Officers

A. D. Russel
Chairman

J. P. Foster
President and Chief Executive Officer

M. D. Glenn
Vice-President

G. T. Urquhart
Vice-President

J. D. Reilly, Q.C.
Secretary

J. S. Smith, CGA
Treasurer

Operating Groups

Metals Group
535 Bowes Road,
Downsview, Ontario M3M 3B5
Telephone: (416) 669-4253

M. D. Glenn, Chairman
W. P. E. Mang, President

Marketing Divisions:
Russelsteel
Vincent Steel
St. Laurent Steel
International Alloy Steel
Baldwin Steel Company

Home Products Group
140 Baig Boulevard,
Moncton, New Brunswick E1E 1C8
Telephone: (504) 854-8086

G. T. Urquhart, President
J. M. O'Sullivan, Executive Vice-President

Marketing Divisions:
Sumner Company
Halliday Craftsmen
Boone Plumbing
Lytle
Lacroix
Boily & Cie.
Inland Distributors
Walter Woods
Pacific Sports
Alberta Caretakers
Inland Sports

Power Transmission Group
2 St. Clair Avenue East,
Toronto, Ontario M4V 1L5
Telephone: (416) 924-9104

J. B. Adams, President

Marketing Divisions:
Canadian Bearings
Motioneering
TEK Bearing
Lindsay-Oberholzer Companies
Precision Bearing & Supply

Engineering Group
2180 Highway #7
Concord, Ontario L4K 1B1
Telephone: (416) 669-2204

Andre Varga, President
R. G. Rossi, Executive Vice-President

Marketing Divisions:
Ceeco Machinery Manufacturing
Syncro Machine Company
Wicama Handels GmBH
Dicomasa (Mexico)
Ceeco do Brasil