HAWKER SIDDELEY

HAWKER SIDDELEY CANADA INC.

1989 ANNUAL REPORT

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HAWKER SIDDELEY
HAWKER SIDDELEY CANADA INC.

Operations Summary

		1989	1988	1987	1986	1985
Operating Data (millions of dollars)						
Sales	$	389.0	388.5	395.8	418.7	422.0
Income before taxes, minority and extraordinary items		39.7	36.0	39.9	34.3	32.2
Income taxes		15.1	14.5	15.2	14.2	14.5
Extraordinary items		(6.5)	(4.3)	6.3	(7.7)	(1.9)
Net income		13.7	13.5	27.6	9.5	13.4
Financial Data (millions of dollars)						
Working capital	$	102.3	127.8	157.6	122.9	127.8
Net fixed assets		241.8	224.6	178.7	184.7	186.3
Long term debt		45.3	53.8	28.6	34.5	40.3
Shareholders' equity		226.4	229.6	234.7	206.5	205.5
Funds provided by operations		32.3	60.9	37.6	25.0	23.1
Capital expenditures		35.1	71.9	9.2	16.1	10.8
Depreciation		15.7	14.9	13.9	15.0	14.2
Dividends						
– preferred shares		.8	.8	.8	.8	.8
– common shares		8.8	8.8	7.8	7.8	7.8
Aggregate remuneration of employees		115.2	115.1	119.5	116.7	121.6
Per Common Share (after Preferred dividends)						
Income before extraordinary items	$	2.38	2.08	2.52	2.01	1.78
Net income		1.58	1.56	3.29	1.06	1.54
Funds provided by operations		3.86	7.37	4.52	2.97	2.74
Dividends		1.08	1.08	.96	.96	.96
Year-end – Book Value		26.04	26.46	27.08	23.62	23.49
– Market Value (TSE)		25.63	22.00	20.88	26.25	23.00
Ratios						
Return on capital employed (Note 1)		14.1%	12.7%	15.2%	13.0%	12.5%
Return on shareholders' equity (Note 2)		6.0%	5.8%	13.0%	4.5%	6.9%
Debt/equity ratio		17:83	19:81	11:89	14:86	16:84
Working capital ratio		1.9	2.1	2.6	2.2	2.3
Other Data						
Shares issued and outstanding						
– preferred		140,000	140,000	140,000	140,000	140,000
– common		8,155,901	8,150,301	8,150,301	8,150,301	8,150,301
Number of shareholders						
– preferred		637	598	656	710	767
– common		2,689	2,961	3,184	3,550	4,271
Average number of employees		2,804	2,847	3,076	3,170	3,630

Notes:

1. Operating income as a percentage of the annual average of total assets less current liabilities (excluding funds).
2. Net income less preferred dividends as a percentage of the annual average shareholders' equity less preferred shares.

Report to the Shareholders

Your Directors submit herewith the audited accounts of Hawker Siddeley Canada Inc. and its subsidiary companies for the year ended December 31, 1989 and management's discussion and analysis of financial condition and results of operations.

FINANCIAL RESULTS

Sales

Sales were $389.0 million (1988 — $388.5 million). Improvement of $7.0 million realized in the Resource Industry segment was offset by reduced sales in the Transportation and Industrial segment principally caused by the strike at the Orenda Division. Sales by industry and geographic segments are shown in Note 12 to the financial statements.

Income

Income before extraordinary items in 1989 was $20.2 million (1988 — $17.7 million) equivalent to $2.38 per common share (1988 — $2.08 per common share). Net income was $13.7 million (1988 — $13.5 million) equivalent to $1.58 per common share (1988 — $1.56 per common share).

Extraordinary Items

Delay encountered in divesting Tree Farmer Equipment Company, Inc. required an additional provision of $4.2 million to cover a reduction in the estimated realizable value of assets and operating losses to January 18, 1990. Cost after tax of $4.7 million for a restructuring program at Canadian Steel Foundries Division, to be completed in 1990, was recorded in 1989. Explanations of extraordinary gains are provided in Note 3 to the financial statements.

DIVIDENDS

In 1989 the Corporation declared and paid the four quarterly preferred share dividends as they became due. A dividend of 27 cents was declared payable on January 11, 1990 to holders of common shares of record on December 21, 1989, following declarations and payments of 27 cents per common share in each of the previous three quarters.

Sir Peter Baxendell, Chairman of the Board (centre) with Board members Dr. A. K. Watkins, Managing Director and Chief Executive, Hawker Siddeley Group PLC (left), and R. D. Cole, President and Chief Executive Officer, Hawker Siddeley Canada Inc. (right).

DIRECTORS

On May 19, 1989, prior to the Annual General Meeting of Shareholders, Mr. B.R. Bensly retired from the Board after serving as a Director since 1985. Dr. A.K. Watkins, Mr. L. Hollander and Mrs. G. Saucier were new Directors elected at that meeting.

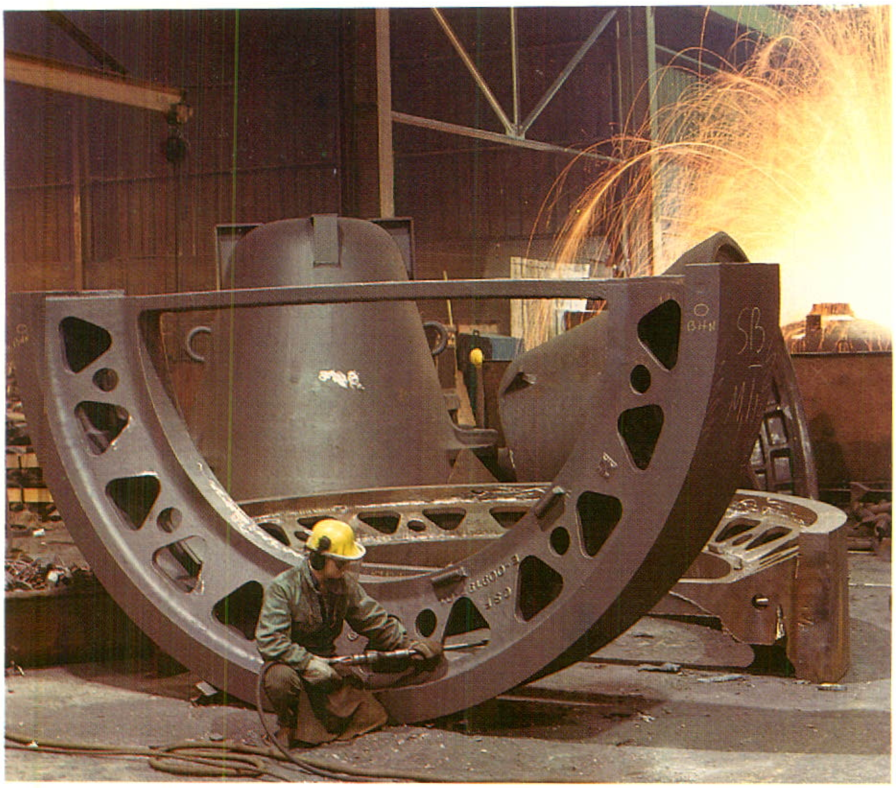
COMMENTS ON OPERATIONS

Transportation and Industrial Products Segment

The Orenda Division in Mississauga, Ontario has two principal operations, the manufacture of components for North America's leading aircraft jet engine builders and the Canadian and U.S. military aircraft spare parts markets, and the repair and overhaul of jet engines used in aircraft operated by the Canadian Armed Forces. Specialized engineering support is also provided to the Canadian Armed Forces together with technical manuals which are prepared and printed to military specifications.

Sales and profitability at Orenda were seriously affected by the prolonged strike of production shop employees from November 1988 until July 1989. The main issue was the introduction of greater job flexibility. This was considered essential by management to improve productivity and enhance prospects for the future viability of plant operations in an increasingly competitive industry. Changes in work practices were finally agreed to in the strike settlement and are being implemented. Other programs designed to reduce costs and improve quality have also been instituted.

Following the end of the dispute, efforts have been progressively directed at rebuilding the confidence of commercial and military customers, renegotiating disrupted delivery schedules and increasing bid activity, particularly in the sub-contract manufacturing sector of the business. A measure of the success achieved in these endeavours was the receipt towards year-end of contracts from



The Montreal, Quebec plant of Canadian Steel Foundries has the experience and facilities to produce large castings to meet virtually any requirement of a wide range of heavy industries.

the U.S. Air Force for the supply of jet engine turbine wheels. In the same period, the Canadian Department of National Defence renewed contracts for spare parts and jet engine and engine component repair and overhaul.

To increase Orenda's presence in the North American military and civil component markets and broaden the product range, the Corporation acquired in January 1990 the assets of two corporations supplying machined components to the aerospace industry, Middleton Aerospace Corporation, Middleton, Massachusetts, and Windsor Aerospace Limited, Windsor, Ontario. The operation of these units will be integrated under Orenda management as Windsor Aerospace Division and Middleton Aerospace Corporation.

Historically, the production of castings for the railway industry, including couplers, sideframes and bolsters, has been a major element in the business base of Canadian Steel Foundries Division, Montreal, Quebec. Such castings are used by railcar builders in the manufacture of new freight cars and by the railways in day-to-day operations as maintenance spare parts. The persistently low levels of railcar manufacturing in recent years and improvements in railroad maintenance practices have severely eroded the demand for these products. The foundry's other primary business lies in the supply of large custom-made castings to the electrical generating, manufacturing and mining industries. Improved demand for these items resulted in higher order intake beginning at the end of 1988 and continuing into 1989. These long lead-time orders, while producing a healthy order book, did not produce a sufficiently high level of deliveries in the year.

The combined impact of the above conditions at Canadian Steel Foundries resulted in a low level of casting production, inefficient operations and unsatisfactory profitability. A study of the alternatives open to this Division to improve the situation resulted in a decision being taken at year-end to concentrate entirely on the production of large custom-made industrial castings. For North American producers, the large castings market is expected to grow over the foreseeable future. The production of railroad castings was discontinued early in 1990.

Severe competitive conditions, which are expected to worsen as Canadian tariffs decline under the Canada-U.S. Free Trade Agreement, and reduced railcar manufacturing affected operations at Canadian Steel Wheel Division, Montreal, Quebec, where production of wrought steel wheels fell below the level of the previous year. The unit did, however, continue to contribute to profitability. Emphasis at the plant continues to be placed on reducing wheel manufacturing costs. Additionally, attention has been directed toward increased marketing of industrial circular products such as crane wheels and gear blanks to partially offset the reduced volume of railway wheel business available.

CGTX Inc., Montreal, Quebec, owns and operates a fleet of railway tank cars and hopper cars which are avail-

Although tank cars form the greater proportion of the CGTX railcar fleet, covered hopper cars such as these units at an Ontario polyethylene plant, are also available for full service lease.

Canadian Steel Wheel is a supplier of maintenance wheels to the United States railway passenger service operator, Amtrak.

able, on full service leases, to Canadian industry and railroads. New leases on railcars delivered from orders taken in the previous year, an increase in total fleet utilization compared to 1988 and higher rental rates, all contributed to improved results.

New orders for railcars custom built to meet specific needs of lessees were, however, very low. A proposed amendment to Canadian tax laws introduced by the Federal government in the 1989 budget, which would have raised the burden of taxation on leased railcars, brought business to a standstill and left CGTX with a minimal railcar order position for 1990 deliveries. After representations by the railcar leasing industry, we believe that the proposed measure may not be applied.

Railcar repair plants operated by CGTX in Montreal, Quebec; Moose Jaw, Saskatchewan; and Red Deer, Alberta had a busy year with the total volume of service work exceeding expectations.

Resource Industry Equipment Segment

The Corporation's sawmill and lumber processing capital equipment business is conducted by three units. The equipment is designed, manufactured and sold in Canada by Kockums CanCar Division, Surrey, British Columbia. In the United States, it is distributed by Kockums CanCar Corp., Atlanta, Georgia. Early in the year, a small sawmill equipment distribution business, now called Kockums CanCar Pty. Ltd., located in Campbellfield, Victoria, was acquired to distribute the Company's products in Australia and New Zealand.

Kockums CanCar sawmill machinery sales reached a record level in 1989, mainly as a result of increased exports of equipment to the United States. However, high cost overruns associated with the development, manufacture and start-up in the field of a new product line placed a heavy strain on the British Columbia-based unit and overall profitability was affected. The new machinery designs represent major advances in sawmilling technology and initial problems encountered are being addressed.

The unit's business potential was strengthened in European markets by the appointment of new distributors in Europe and important sales were made in Czechoslovakia and Sweden. The United States-based unit experienced improved sales and profitability as demand for capital equipment in that country remained high. These gains were partially offset by a lower volume of spare parts sales. Requirements for new capital equipment are expected to decline in the United States in 1990, and, as a result, spare parts sales are unlikely to improve as the lumber market slows in reaction to the declining volume of building renovations and new housing starts. The Australian sales unit was active and profitable during the year as it became fully integrated under Kockums CanCar management.

As indicated in the 1988 Annual Report, persistently poor market conditions in the United States forest industry for log skidder vehicles had given rise to a decision to divest ownership of Tree Farmer Equipment Company, Inc., Talladega, Alabama, in the year under review. The assets of this company were sold in January 1990 to another manufacturer of forestry equipment who will continue the business under the Tree Farmer name.

The principal business of Dosco Overseas Engineering Limited, Tuxford, Nottinghamshire, England, is the design and manufacture of a range of tunnelling and production machines for various types of mining. The company's main market is the United Kingdom's coal mining industry, but equipment is also sold for use in other coal producing countries, various mineral mining operations and civil engineering tunnelling projects. A range of associated equipment is also produced.

Changes in purchasing and product support policies by British Coal put downward pressure on Dosco's sales of new machinery and related spare parts and also on the level of repair and overhaul work available on existing machines. A program introduced in 1988 to provide mining machines to British Coal on long-term leases continued to be favourably received by the customer and additional machines were delivered under this plan. This activity, combined with improvement in plant efficiency, enabled profitability to rise above that of the previous year.

Efforts continued to be made to diversify the product range and, to this end, a line of crushers and sizers for the quarrying industry was developed. In addition, agreements were concluded to enable pipe conveyor systems and additional types of tunnelling machines to be manufactured and distributed under license. Export sales promotion was active in 1989 and opportunities which were pursued for machine placements in coal and other types of mining in several countries should result in a high level of deliveries in 1990.

Hollybank Engineering Company Limited operates a facility adjacent to the Dosco factory in the United Kingdom where it produces roof support systems for use in mine roadways. Strong activity in the first half of the year slowed later to more sustainable levels. The increased sales volume resulted in improved profitability over the previous year despite continuing pressure on margins. The contract mining business acquired in 1988 prospered and order intake was very satisfactory. The use of contractors to carry out certain phases of mining activity appears to be gaining increasing acceptance within the United Kingdom coal industry. Hollybank's experience and success in this growing market should prove beneficial in future years.

The Dosco Corporation, a subsidiary based in Abingdon, Virginia, had a good year. The unit supplies Dosco-built machines to mining and construction customers in the U.S., provides after sales service and overhauls, and also manufactures arch supports for tunnels. Sales of support systems rose with much of the increase coming from civil engineering contractors although the traditional mining customers showed steady demand. Requirements for spare parts for mining machines also remained at a satisfactory level.

A TB3000 twin-boom mining machine at work in a Spanish potash mine in conditions typical of those in which Dosco mining equipment is designed to operate.

COMMENTS ON FINANCIAL CONDITION

At December 31, 1989 the Corporation's financial condition remained strong in spite of the strike during the year at Orenda Division.

The Corporation has extensive credit facilities with a number of Canadian banks.

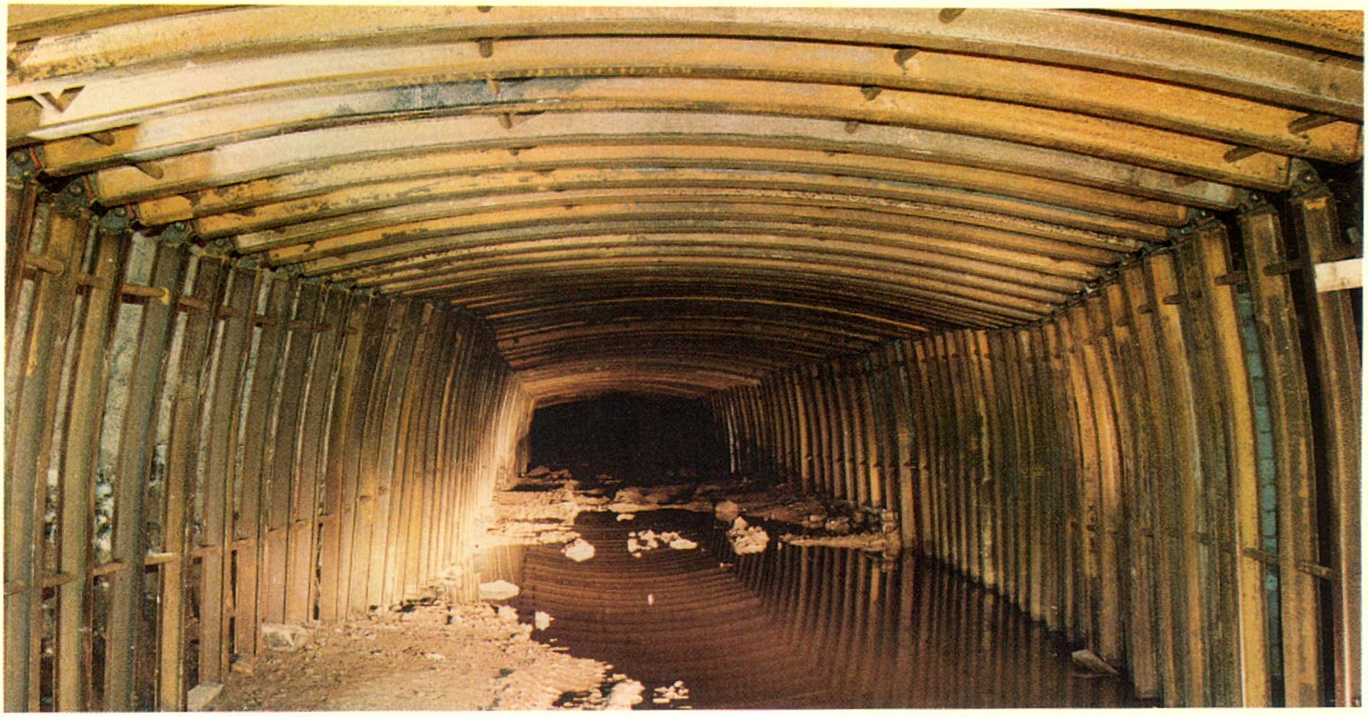
The exceptional capital expenditure growth at CGTX Inc. in 1988 and 1989 resulted from expenditures on railway rolling stock over the 2 years of $90.5 million. $60.5 million was financed internally and 30.0 million long-term debt was issued in 1988. CGTX Inc. rolling stock with a net book value of $97.7 million is pledged against long-term debt.

Changes in Financial Condition

The change in working capital items indicates an absorption of funds of $11.2 million in 1989 as compared with a generation of $26.7 million in 1988. The main reason for an unfavourable absorption in 1989 was the prolonged strike at Orenda Division.

Income tax payments were $11.0 million and $16.4 million in 1989 and 1988 respectively. The reduction in tax payments reflect the effect on current income taxes payable by CGTX Inc., because of the capital expenditure program, and the operating loss sustained at Orenda Division. As a result of tax losses carried forward, no income tax payments were required in the United States.

In the transportation and industrial products segment, sales were down 4% from the previous year reflecting the lengthy stike at Orenda. Partially offsetting this decline was higher rail car leasing revenue associated with the previous year's increase in



Widely used in coalmine roadways, roof arch supports manufactured by Hollybank Engineering also serve several sectors of the mining industry. These supports line a tunnel in a gypsum mine.

CGTX's fleet size and improved hydro-electric custom casting shipments at Canadian Steel Foundries Division. Although sales were lower, operating income exceeded that in 1988 by 23% with the improved earnings at CGTX more than compensating for lower results by other units in this segment.

In the resource industry equipment segment, revenues exceeded those of last year by 3% due largely to the achievements of the Kockums CanCar operations in the United States, Hollybank Engineering Company Limited's continued expansion in the contract mining area, and the strong surge in demand for Dosco Corporation's supports from the civil engineering sector in the United States. However, Dosco Oversea's domestic sales were down as British Coal continued rationalizing its colliery operations and prospects in the export market especially for China and India did not materialize.

In this segment, operating income was 9% higher than in 1988 mainly reflecting the elimination of Tree Farmer Equipment operating losses which were charged to the divestiture provision set up in 1988. Productivity gains at Dosco Overseas improved profitability despite reduced sales. Dosco Corporation enjoyed its most profitable year ever as a result of the delivery of supports for a large tunnel project in Houston, Texas. Hollybank's reduced operating margins reflected prevailing market conditions, but were offset by increased shipments of supports and growing contract mining sales. Kockums CanCar's cost overruns incurred in the development and start-up of a new product line eliminated the profits realized on the sales of standard capital equipment and spare parts.

CORPORATE INTENT

During the 1980s, the Corporation gradually reduced its presence in the highly cyclical railway supply industry. The entry into export markets for sawmill products, the expansion into contract mining and the recent acquisition of two manufacturing facilities supplying components to the aerospace industry have largely replaced the revenues foregone from the former rail products manufacturing operations. Efforts are continuing to develop and acquire new business activities that will provide increased revenues and return to shareholders.

Submitted on behalf of the Board

Peter Baxendell

Peter Baxendell
Chairman

R.D. Cole

R.D. Cole
President and Chief Executive Officer

Mississauga, Ontario
March 1, 1990

Consolidated Statement of Income and Retained Earnings

	Year ended December 31 1989	1988
	(in thousands)	
Sales (Note 12)	$ 389,019	$ 388,508
Cost of sales, selling, general and administrative expenses	332,900	339,420
Depreciation	15,652	14,937
	348,552	354,357
Operating income (Note 12)	40,467	34,151
Interest (expense) (Note 2)	(803)	1,820
Income before income taxes, minority interest and extraordinary items	39,664	35,971
Income taxes (Note 9)	15,089	14,499
	24,575	21,472
Minority interest	4,391	3,728
Income before extraordinary items	20,184	17,744
Extraordinary items (Note 3)	(6,472)	(4,251)
Net income for the year	13,712	13,493
Retained earnings, beginning of year	161,149	157,263
	174,861	170,756
Dividends		
Preferred shares	805	805
Common shares	8,806	8,802
	9,611	9,607
Retained earnings, end of year	$ 165,250	$ 161,149
Income per common share after preferred dividends		
Before extraordinary items	$ 2.38	$ 2.08
After extraordinary items	$ 1.58	$ 1.56

Consolidated Statement of Changes in Financial Position

	Year ended December 31 1989	1988
	(in thousands)	
Funds (net cash and short-term investments), beginning of year	$ 72,804	$ 79,156
Operating activities		
Income before income taxes, minority interest and extraordinary items	39,664	35,971
Items not affecting funds		
Depreciation	15,652	14,937
Other	(894)	(321)
	54,422	50,587
Change in working capital items (excluding funds and income taxes) related to operations	(11,153)	26,703
Income tax payments	(11,009)	(16,421)
Funds provided by operations	32,260	60,869
Investing activities		
Proceeds on disposal of fixed assets	2,837	4,971
Additions to fixed assets		
Railway rolling stock leasing fleet	(26,684)	(63,777)
Plant and equipment	(8,421)	(8,077)
Miscellaneous	—	(85)
Funds used in investing activities	(32,268)	(66,968)
Financing activities		
Common shares issued (Note 10)	118	—
(Reduction) increase in long-term debt	(4,562)	24,370
Purchase of minority interest in Kockums companies	—	(4,250)
Dividends paid to		
Shareholders of Hawker Siddeley Canada Inc.	(9,609)	(9,364)
Minority shareholder of a subsidiary	(1,613)	(1,612)
Funds (used in) provided by financing activities	(15,666)	9,144
Unrealized foreign currency translation loss on net current assets of foreign subsidiaries	(7,574)	(9,397)
Net funds used in the year	(23,248)	(6,352)
Funds (net cash and short-term investments), end of year	$ 49,556	$ 72,804

Consolidated Balance Sheet

ASSETS	December 31 1989	1988
	(in thousands)	
Current assets		
Cash and short-term investments	$ 58,452	$ 83,805
Accounts receivable	72,245	73,335
Due from affiliated companies (Note 5)	1,451	—
Income taxes recoverable	3,845	3,038
Inventories	71,674	80,843
Prepaid expenses	2,729	3,482
	210,396	244,503
Fixed assets (Note 6)	439,481	411,268
Less: Accumulated depreciation	197,719	186,677
	241,762	224,591
	$ 452,158	$ 469,094

Approved by the Board:
Peter Baxendell, Director
R.D. Cole, Director

LIABILITIES AND SHAREHOLDERS' EQUITY	December 31 1989	1988
	(in thousands)	
Current liabilities		
Bank advances	$ 8,896	$ 11,001
Accounts payable and accrued liabilities	73,600	80,020
Dividends payable	2,403	2,402
Income and other taxes	12,835	14,143
Advances on sales contracts	2,095	1,152
Owing to affiliated companies (Note 5)	—	4,446
Long-term debt due within one year (Note 7)	8,293	3,572
	108,122	116,736
Long-term debt (Note 7)	45,300	53,840
Deferred income taxes (Note 9)	38,558	37,853
Minority interest	33,811	31,033
Shareholders' equity		
Preferred and common shares (Note 10)	68,501	68,383
Retained earnings	165,250	161,149
Unrealized foreign currency translation adjustments (Note 11)	(7,384)	100
	226,367	229,632
	$ 452,158	$ 469,094

Notes to Consolidated Financial Statements for the year ended December 31, 1989

1. Summary of principal accounting policies

Principles of consolidation
The consolidated financial statements include the accounts of Hawker Siddeley Canada Inc. and all subsidiary companies.

Foreign currency translation
Assets and liabilities of foreign subsidiaries and other assets and liabilities in foreign currencies are translated at year-end rates of exchange. Revenue and expense items are translated at average rates of exchange during the year.

Net unrealized exchange adjustments arising from translation of the financial statements of foreign subsidiaries are included in a separate translation adjustments account in shareholders' equity. Other exchange gains and losses, including amortization of such amounts related to long-term debt over its remaining life, are included in income.

Recognition of revenue, profits and losses
Revenue and profits are recorded at the time the product is shipped or the service performed. Provision is made for any losses, including possible losses arising from claims and suits, in the year in which they are first foreseen.

Short-term investments
Short-term investments are recorded at the lower of cost and market value.

Inventories
Inventories are carried at the lower of cost and net realizable value, less progress payments.

Fixed assets
Fixed assets are carried at cost. Depreciation on these assets is provided over their estimated useful lives on the straight-line method, generally at annual rates of 2½% on buildings, 10% on equipment and 3⅓% to 5% on railway rolling stock.

2. Interest (expense)

Interest reported in the consolidated statement of income is as follows:

	1989	1988
	(in thousands)	
Interest income		
Short-term deposits and investments	$ 6,657	$ 7,088
Interest expense		
Bank advances	888	594
Loans from affiliated companies (Note 5)	478	758
Long-term debt	6,094	3,916
	7,460	5,268
Net interest (expense)	$ (803)	$ 1,820

3. Extraordinary items

	1989	1988
	(in thousands)	
Provision for estimated costs and losses relating to the divestiture of the Tree Farmer Equipment operations, less related income taxes of $400,000 (1988 — $800,000) (see Note 13)	$ (4,200)	$ (7,700)
Provision for estimated costs and losses relating to the restructuring program at Canadian Steel Foundries, less related income taxes of $3,100,000	(4,700)	—
Minority interest in Kockums companies in excess of purchase price of shares formerly held by minority shareholders	—	1,972
Reversal of a prior year's provision which is no longer required, less related income taxes of $126,000 (1988 — $749,000)	174	1,035
Effect of tax losses in prior years not previously recorded	1,154	442
Proceeds from an insurance claim respecting damaged property, less related income taxes of $440,000	1,100	—
	$ (6,472)	$ (4,251)

4. Research and development costs

Research and development costs charged to income amounted to $3,398,000 (1988 – $4,706,000).

5. Related party transactions

Hawker Siddeley Group Public Limited Company, a United Kingdom based company, which operates through subsidiaries in many countries, is the beneficial owner of 59.1% of the outstanding common shares and 41.8% of the outstanding preferred shares of the company.

During 1989, the company and its subsidiaries had no significant sales to or purchases from related parties.

Loans to or from affiliated companies are based on commercial bank lending rates.

6. Fixed assets

	1989 (in thousands)		1988 (in thousands)	
	Cost	Accumulated depreciation	Cost	Accumulated depreciation
Land and land improvements	$ 5,775	$ 1,358	$ 5,652	$ 1,285
Buildings	42,828	27,789	42,693	27,063
Equipment	93,532	66,565	89,109	63,295
Railway rolling stock leasing fleet	297,346	102,007	273,814	95,034
	$439,481	$197,719	$411,268	$186,677

7. Long-term debt

	1989	1988
	(in thousands)	
CGTX Inc. (55% owned)		
First Mortgage Sinking Fund Equipment Notes		
10¼%, due 1990 – 2000		
(U.S. $2,750,000; 1988 – U.S. $3,250,000)	$ 3,190	$ 4,032
8⅞% – 11⅛%, due 1990 – 1999	20,403	23,380
	23,593	27,412
First Mortgage Equipment Notes		
11¼%, due 1990 – 1992	15,000	15,000
11%, due 1993	15,000	15,000
	53,593	57,412
Promissory Note owing to an affiliated company		
¾% below Canadian bank prime rate, due 1989	—	1,000
	53,593	58,412
Due within one year included in current liabilities ($1,000,000 included in owing to affiliated companies in 1988)	(8,293)	(4,572)
	$ 45,300	$ 53,840

Principal payments on long-term debt will be as follows for the years indicated:

Year ending December 31	Amount (in thousands)
1991	$ 8,002
1992	7,802
1993	17,803
1994	2,602
1995 – 2000	9,091
	$ 45,300

Railway rolling stock with a net book value of $97,667,000 is pledged by CGTX Inc. as security for its long-term debt.

8. Pensions

The estimated actuarial present value of defined pension benefits accrued to December 31, 1989 was $114,000,000 (1988 – $116,000,000) and the value of the pension fund assets (based on average market) at that date was approximately $162,000,000 (1988 – $156,000,000).

9. Income taxes

The consolidated provision for income taxes, which includes deferred income taxes of $4,077,000 (1988 – $753,000), has been determined as follows:

	1989	1988
	(in thousands)	
Consolidated provision at statutory rates of taxation	$ 15,795	$ 15,354
Decrease in provision resulting from		
Manufacturing and processing tax credit	(179)	(314)
Other	(527)	(541)
Consolidated provision for income taxes	$ 15,089	$ 14,499

At December 31, 1989, the U.S. subsidiaries had accumulated losses for income tax purposes of approximately U.S. $22,200,000 which are available to reduce their taxable income of future years and expire during the years 1996 to 2004. Also, expenses of approximately U.S. $7,700,000 at December 31, 1989 have been charged to net income but not yet allowed for tax purposes.

At December 31, 1989, the company had a loss for income tax purposes of approximately $495,000, which is available to reduce its taxable income of future years and expires in 1992. Also, expenses of approximately $3,500,000 at December 31, 1989 have been charged to net income but not yet allowed for tax purposes.

The potential future tax benefits of approximately U.S. $10,200,000 for the U.S. subsidiaries and $1,500,000 for the company, based on 1989 income tax rates, have not been recorded in the accounts.

10. Preferred and common shares

	Shares	1989
		(in thousands)
Preferred shares		
5¾% cumulative preferred shares, redeemable at the option of the company at $105 per share		
Authorized and issued	140,000	$ 14,000
Common shares		
Issued	8,155,901	54,501
		$ 68,501

The company is authorized to issue an unlimited number of preferred shares junior to the 5¾% cumulative preferred shares and an unlimited number of common shares.

At December 31, 1989, options granted to officers of the company were outstanding for the purchase of 45,600 common shares at $19.63, 12,400 common shares at $22.00, 43,900 common shares at $24.00 (granted during 1989) and 5,750 common shares at $29.00. All options will expire at various dates during the next ten years if not exercised.

During the year, options for 5,600 common shares were exercised for a total consideration of $118,000.

11. Foreign exchange translation adjustments

Movements in the unrealized foreign currency translation adjustments account are as follows:

	1989	1988
	(in thousands)	
Balance, beginning of year	$ 100	$ 9,089
Adjustments for the year	(7,484)	(8,989)
Balance, end of year	$ (7,384)	$ 100

12. Segmented information

INDUSTRY

	Transportation and industrial 1989	Transportation and industrial 1988
Sales to customers*	$ 143,724	$ 150,175
Inter-segment sales**	—	9
Sales	$ 143,724	$ 150,184
Segment operating income	$ 27,351	$ 22,166
General corporate expenses		
Operating income		
Identifiable assets	$ 280,054	$ 261,405
Corporate assets		
Total assets		
Capital expenditures	$ 29,896	$ 66,597
Depreciation	$ 13,239	$ 12,138

GEOGRAPHIC

	Canada 1989	Canada 1988	Europe 1989	Europe 1988
Sales to customers	$ 183,634	$ 192,440	$ 153,422	$ 153,416
Sales between geographic segments**	16,087	8,344	222	—
Sales	$ 199,721	$ 200,784	$ 153,644	$ 153,416
Segment operating income	$ 26,700	$ 24,122	$ 12,527	$ 12,242
General corporate expenses				
Operating income				
Identifiable assets	$ 309,159	$ 286,348	$ 76,579	$ 92,438
Corporate assets				
Total assets				

The company provides products and services in two major segments:

Transportation and industrial – includes manufacture of steel castings and forgings for the railway and manufacturing industry, revenue from leases of railway tank and hopper cars, repair and overhaul of jet engines and of industrial turbines and miscellaneous other products.

Resource industry equipment – includes mining equipment, tunnelling machines, parts and roof support systems for mine roadways and tunnels, lumber processing and logging equipment for the forestry and forest products industries.

Canadian sales to customers include export sales of $20,904,000 in 1989 and $25,181,000 in 1988, primarily to customers in the United States.

* Transportation and industrial sales to customers include $52,055,000 (1988 — 43,304,000) relating to leasing operations.

** Intersegment sales are accounted for at prices comparable to market prices.

SEGMENTS (in thousands)

Resource industry equipment		Eliminations		Consolidated	
1989	1988	1989	1988	1989	1988
$ 245,295	$ 238,333	$ —	$ —	$ 389,019	$ 388,508
—	—	—	(9)	—	—
$ 245,295	$ 238,333	$ —	$ (9)	$ 389,019	$ 388,508
$ 14,204	$ 13,066	$ —	$ —	$ 41,555	$ 35,232
				(1,088)	(1,081)
				$ 40,467	$ 34,151
$ 126,863	$ 145,414	$ (43)	$ (53)	$ 406,874	$ 406,766
				45,284	62,328
				$ 452,158	$ 469,094
$ 4,887	$ 4,809				
$ 2,357	$ 2,751				

SEGMENTS (in thousands)

United States		Eliminations		Consolidated	
1989	1988	1989	1988	1989	1988
$ 51,963	$ 42,652	$ —	$ —	$ 389,019	$ 388,508
5,932	(299)	(22,241)	(8,045)	—	—
$ 57,895	$ 42,353	$ (22,241)	$ (8,045)	$ 389,019	$ 388,508
$ 2,328	$ (1,132)	$ —	$ —	$ 41,555	$ 35,232
				(1,088)	(1,081)
				$ 40,467	$ 34,151
$ 22,936	$ 30,588	$ (1,800)	$ (2,608)	$ 406,874	$ 406,766
				45,284	62,328
				$ 452,158	$ 469,094

13. Subsequent events

On January 5, 1990, the company purchased the assets of Windsor Aerospace Limited and a wholly-owned U.S. subsidiary purchased the assets of Middleton Aerospace Corporation for a total consideration of U.S. $23,300,000 subject to adjustments on closing.

On January 19, 1990, the company sold the Tree Farmer Equipment business and certain assets for a cash consideration of U.S. $1,600,000.

Auditors' Report

Chartered Accountants

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Price Waterhouse

March 1, 1990

AUDITORS' REPORT

To the Shareholders of
Hawker Siddeley Canada Inc.

We have examined the consolidated balance sheets of Hawker Siddeley Canada Inc. as at December 31, 1989 and 1988 and the consolidated statements of income and retained earnings and changes in financial position for the years then ended. Our examinations were 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 December 31, 1989 and 1988 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles applied on a consistent basis.

Price Waterhouse

Chartered Accountants

Divisions & Subsidiaries, Products & Services

Divisions

Canadian Steel Foundries Division, Montreal, Que.
Canadian Steel Wheel Division, Montreal, Que.
Kockums CanCar Division, Surrey, B.C.
Orenda Division, Mississauga, Ont.
Windsor Aerospace Division, Windsor, Ont.

Subsidiaries (Note)

Can-Car, Inc., Wilmington, Delaware, U.S.A.
  Kockums CanCar Corp., Atlanta, Ga., Vancouver, Wash., U.S.A.
  Middleton Aerospace Corporation, Middleton, Mass., U.S.A.
  The Dosco Corporation, Abingdon, Va., U.S.A.
Dosco Overseas Engineering Limited, Tuxford, England
  Hollybank Engineering Company Limited, Tuxford, England
CGTX Inc., Montreal, Que., Mississauga, Ont., Moose Jaw, Sask., Red Deer and Calgary, Alta.
Kockums CanCar Pty. Ltd., Campbellfield, Victoria, Australia

Note: With the exception of CGTX Inc. (55% owned), all subsidiaries are 100% owned, directly or indirectly, by Hawker Siddeley Canada Inc.

Products and Services

Divisions

Canadian Steel Foundries Division
  Steel castings for the electrical generating, mining, and manufacturing industries
Canadian Steel Wheel Division
  Forged wheels for railway passenger and freight cars and locomotives; industrial wheels
Kockums CanCar Division
  Sawmill and lumber processing equipment; sales and service
Orenda Division
  Aircraft jet engine repair and overhaul; jet engine components; engineering design and laboratory testing services; graphics services
Windsor Aerospace Division
  Precision machined parts for the aerospace and related industries

Subsidiaries

Kockums CanCar Corp.
Kockums CanCar Pty. Ltd.
  Sawmill and lumber processing equipment sales and service
The Dosco Corporation
  Sales and service of mining and tunnelling machines; roof support systems for mine roadways and civil engineering tunnels
Dosco Overseas Engineering Limited
  Production and tunnelling machines for coal, mineral and ore mining; dust suppression equipment; pipeline conveyor systems
Hollybank Engineering Company Limited
  Roof support systems for mine roadways and civil engineering tunnels; contract mining
Middleton Aerospace Corporation
  Precision machined parts for the aerospace industry
CGTX Inc.
  Full-service leasing and repair of railway tank cars and hopper cars

Hawker Siddeley Canada Inc.

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Directors

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R. D. Cole, Oakville, Ontario
A. H. Crockett, Toronto, Ontario
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G. Saucier, Montreal, Quebec
T. K. Shoyama, Victoria, British Columbia
R. F. Tanner, Mississauga, Ontario
Dr. A. K. Watkins, Buckinghamshire, England

Executive Management

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J. F. Howard, Q.C., Vice-Chairman
R. D. Cole, President and Chief Executive Officer
Dr. A. K. Watkins, Managing Director and Chief Executive, Hawker Siddeley Group PLC
W. G. Broley, Comptroller
B. M. Budd, Secretary and General Counsel
M. J. Colman, Vice-President (Canadian Steel Foundries and Canadian Steel Wheel Divisions)
L. Francoeur, Vice-President, Finance
W. C. Griffiths, Vice-President (Kockums CanCar Division) (President, Kockums CanCar Corp.)
A. D. Johnson, Managing Director, Dosco Overseas Engineering Limited
J. C. Léger, President and Chief Executive Officer, CGTX Inc.
R. J. Munro, Vice-President (Orenda Division) (President, Middleton Aerospace Corporation)
F. J. Sandford, Treasurer
Dr. K. T. Sisson, Managing Director, Hollybank Engineering Company Limited

Auditors

Price Waterhouse, Toronto, Ontario

Registrar and Transfer Agent

National Trust Company, Toronto, Montreal, Winnipeg and Vancouver

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