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## DESCRIPTION OF THE BUSINESS

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**H**arris, through its subsidiaries, is engaged in the manufacture of concrete reinforcing steel and merchant steel; the fabrication and placing of concrete reinforcing steel; the production and marketing of epoxy-coated reinforcing steel; the design and installation of concrete post-tensioning systems; the manufacture and distribution of wire and wire products, welded wire mesh and cold finished bar; the manufacture and distribution of heavy industrial steel and aluminum grating; and the fabrication and erection of structural steel.

The company serves all of Canada, the north eastern and central United States and participates in international projects.

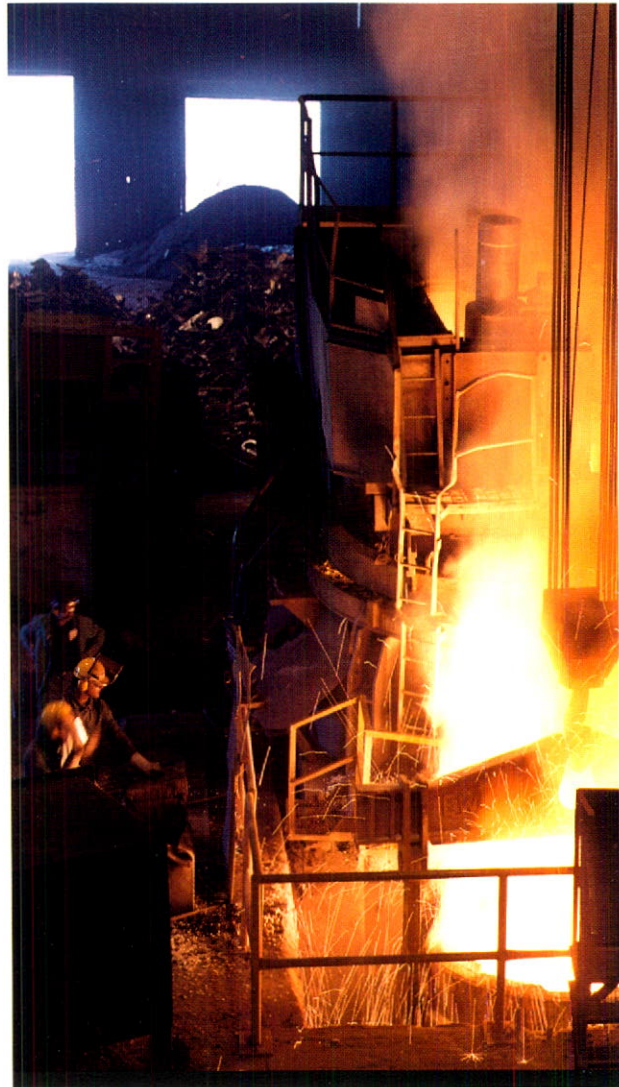
Harris became a public company in 1967 and has paid dividends since 1972.

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### Annual Meeting

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All shareholders are cordially invited to attend the annual meeting on Wednesday, June 24, 1987, 3:00 p.m. in the Essex Room of the Sheraton Centre, 123 Queen Street West, Toronto.



Molten steel being poured into an automated continuous caster at Courtice Steel's meltshop in Cambridge, Ontario.

Cover photo: Courtice Steel caster operator controlling the flow of molten steel from the tundish into the moulds during the continuous casting of billets.

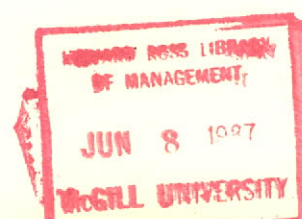
# FINANCIAL HIGHLIGHTS



Years ending December 31

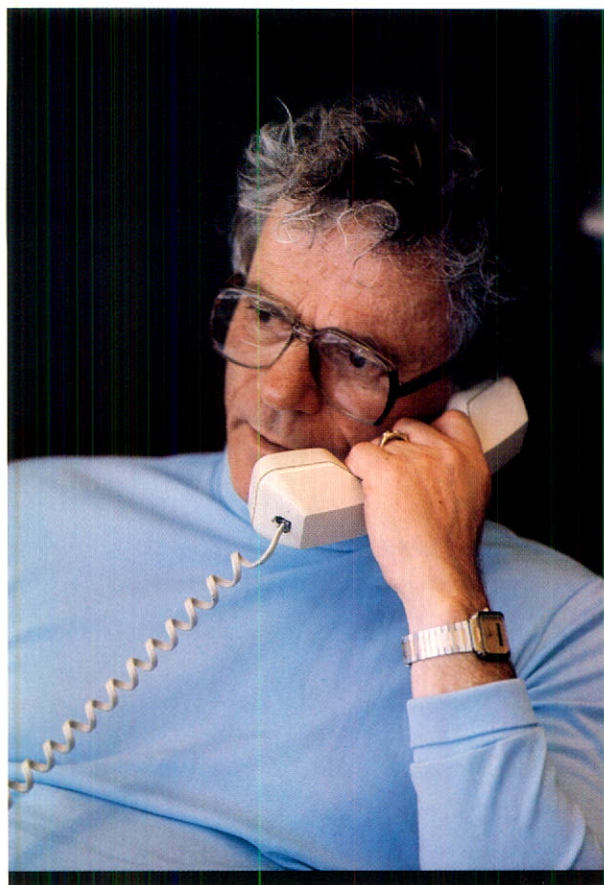
(Dollars in thousands except per share amounts)

	1986	1985
<b>Operating results</b>		
Sales from continuing operations	\$ 312,368	\$ 273,077
Earnings from continuing operations	4,411	9,461
Return on sales	1.4%	3.5%
Earnings (loss) from discontinued operations	210	(81)
Earnings before extraordinary item	4,621	9,380
Return on average equity	7.4%	20.8%
<b>Per Share</b>		
Earnings from continuing operations	\$ .36	\$ .92
Earnings (loss) from discontinued operations	.02	(.01)
Earnings before extraordinary item	.38	.91
Dividends	.24	.185
Shareholders' equity	5.42	5.63
Average shares outstanding	12,271,489	10,310,393
<b>At year end</b>		
Total assets	\$ 183,780	\$ 141,197
Long-term debt	15,149	6,345
Shareholders' equity	66,451	58,042
Long-term debt/Total capital	18.6%	9.9%
Current ratio	1.2:1	1.5:1
Number of employees	2,109	1,732
Number of shareholders – Class A	606	602
– Class B	314	263





## REPORT TO SHAREHOLDERS



I would like to begin this Report to our Shareholders by paying tribute to Geoffrey Jackson and Ed Lee who passed away in 1986.

Geoff had been President of the Frankel Structural Steel Group since 1975 and a Director of our Company since 1976. His outstanding personal qualities had made Geoff a leader in Canada's structural steel industry for three decades. All of Geoff's colleagues and friends will miss him greatly.

Ed, who died after a long illness during which he continued as Vice President of Manufacturing at Laurel Steel, was a highly-creative member of Laurel's management team. Ed was extremely well-liked by everyone with whom he worked and an inspiration to all who knew him.

### 1986 Commentary

1986 earnings were far below our Profit Plan for the year. This disappointing result stems from a loss in our Structural Steel Division.

Our Balance Sheet, and future prospects, have been strengthened by the acquisition in early 1986 of

Courtice Steel for \$2,558,605 and 600,000 Class A Shares at \$11.75 per share. This has added \$7,050,000 to our Shareholders' Equity.

We have committed approximately \$27 million for a new steel bar rolling mill at the site of our melt shop in Cambridge, Ontario. Although a term loan for up to \$30 million has been arranged and is available to fund the project, we have not yet drawn against this new facility. To date approximately \$14 million of rolling mill expenditures have been financed by utilizing existing operating lines of credit, which has temporarily reduced working capital.

All of our Divisions performed well in 1986 except for Structural Steel.

Laurel Steel achieved very good results again despite the tight competitive market for most of their products. Volumes were up but margins were lower.

During the year Laurel purchased a much larger building outside of Detroit, Michigan and has now converted this facility to a cold finished bar plant. The move to the new location was completed in January 1987 and Laurel is now serving a large part of its steadily-growing American market from this new plant.

Harris Rebar faced a highly competitive marketplace for most of 1986, but bookings greatly increased in the fourth quarter. Harris Rebar's profit performance exceeded Plan.

In 1986, as in every year since its acquisition in 1977, Fisher & Ludlow performed better than Plan. F & L's new "Deck Span" grating has made excellent market penetration.

The Frankel Structural Steel Companies fell \$9,000,000 pre-tax short of their Profit Plan. This was almost entirely attributable to a job in Philadelphia that was estimated and managed by the Steel Structures Group in the U.S. Appropriate management changes have been made and Steel Structures is now operating much more effectively.

We sold our Second Manufacturing Division in November 1986 and have since been able to sublet our total future lease obligations. The sale of Secord will release about \$4 million of investment. A provision of 2.5¢ per share has been made for potential losses on the sale.

Courtice Steel performed very well by all measures in 1986 — profit results, production of raw steel and productivity in the rolling mill. Courtice sold out their total rolling capacity by continuing to sell very successfully into their market niche of small merchant bar sections, and by supplying Harris with all the rebar that could not be sold to other fabricators.



## Strategic Developments

Our Management and Board are convinced that we have an outstanding opportunity to greatly increase the earnings per share of the Harris Steel Group when we view it as a number of manufacturing divisions around a highly-flexible and efficient steel mill that would be their primary source of supply.

Within the Harris Steel Group, after the sale of Secord, all of the present divisions will be significant downstream processors of product from the new mill we are building in Cambridge, Ontario, except for Frankel. The Frankel Structural Steel Companies do not use steel products that can be rolled in a bar mill.

We believe we can achieve maximum earnings potential for our shareholders much more rapidly by redirecting our investment in Frankel into facilities that will consume large quantities of product from our new mill.

## Market Opportunities in 1987

Although the market for epoxy-coated rebar has become much more competitive and margins are falling, the total rebar market in the Ontario marketplace has shown a spectacular increase in volume so far in 1987 and a supply shortage has become evident in the last several weeks. Our fabricator, Harris Rebar, as well as most of the other fabricators in Ontario and Quebec, have considerably increased their order backlogs and future business prospects look very positive well into 1988. A growing shortage of rebar in Ontario and Quebec is giving us the opportunity to substantially improve margins on new sales of rebar.

We intend to maintain, but not increase, our historic share of this key market.

Laurel Steel are now on stream in their new cold finished bar plant in Michigan. The volume of incoming orders has increased in the Laurel companies, but a combination of surplus capacity and a higher value for the Canadian dollar is significantly reducing margins in cold finished bar and carbon wire.

The markets for Laurel's concrete accessories and construction mesh are very strong and we expect to be able to achieve better margins in these products.

Fisher & Ludlow continue to operate very well in their grating markets. Their new "Deck Span" line is being enlarged and market penetration has been excellent. Margins in "Deck Span" are improving.

Courtice Steel will have no trouble selling out their Bowmanville plant's production in the first half of the year, or the second half when we continue to operate

Bowmanville, but will also be phasing in the new Cambridge mill. We will be charging operating results with the total interest, and part of the depreciation, on the Cambridge project, as soon as we begin to break in the new mill, which is scheduled to start up in July.

Courtice Steel's markets, both for the present product lines and for those from the new mill, have strengthened considerably in the last few months. We anticipate only a small profit increase in Courtice in 1987, however, due to our careful projection of the time required to phase-in the new mill.

## The Outlook for 1988 and Beyond

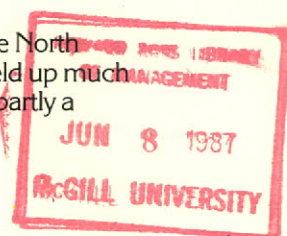
In the first half of 1988 Courtice will be bringing on new steelmaking capacity and will gradually build up production in the rolling mill. They will begin rolling special sections for Harris companies and for others. Our management teams are presently examining various products that can be manufactured from steel produced by Courtice. We expect to start reaping the benefits of higher margin production in 1988 when we will begin to show a large increase in Return on Sales, Return on Equity, and Earnings Per Share.

In 1989 Courtice will reach our initial planned levels for the mill. We expect another large earnings increase in 1989 over 1988. Any higher margin products that can be further manufactured in the Group, or sold to other companies, will enhance planned profit levels, and the utilization of more of the mill's ultimate capacity will bring additional increases.

Although present economic conditions and the direction of interest rates appear uncertain, considerable strength has developed in many steel product areas in both Canada and the United States. Many of these are products that will be rolled by Courtice.

Several factors seem to be combining to give the present strength:

- 1) Considerable steel capacity has been removed from the market.
- 2) The Import Restraint Program in the U.S. has created some product shortages.
- 3) The plummeting American dollar has made American steel much more competitive at home as well as in export markets. Relative to European and Far Eastern currencies the Canadian dollar has also been dropping.
- 4) Industrial demand, particularly in the North American automotive sector, has held up much better than anticipated. This is also partly a function of the lower dollar.





- 5) The long strike at the largest American producer, U.S. Steel, created the expectation that their return to production would depress prices. Everyone allowed inventories to run down. Now that U.S. steel is back prices in most product lines are going up, not down, and everyone is scrambling to build inventories. What the steel buyer has not understood is the change in philosophy at most steel mills today. The past concentration on volume has now been replaced by a new emphasis on margins. The steel mills have learned in the last four years that their losses have come less from lack of capacity utilization than from depressed margins.

Most of the foregoing factors are fundamental and long-term and give strong reasons for optimism for our future steel markets.

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### **Trade Negotiations with the U.S.**

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I am firmly convinced that a successful conclusion to the Government's initiative on Free Trade with the Americans would be a boon to all of Canada, but especially to the industrial heartland of Ontario. The Harris Steel Group would eagerly welcome the challenge of operating in a North American marketplace that assured a "level playing field" to every participant.

Our steel trade with the United States has reached a new phase.

Although Canadian steel shipments to the United States have been rising at the same time that shipments from other major exporting countries have been falling, there is a growing awareness amongst U.S. politicians that Canadians are excellent and fair-trade suppliers of steel to much of American industry.

A large part of the increase in steel shipments to the U.S. has come from new players who did not export three years ago, and have little long-term investment in the industry. In order to assure the Americans that Canada intends to exercise prudence in our steel exports to the U.S., the Canadian Government has begun to implement a Steel Export Licensing System that will monitor shipments of all steel exported to the United States from Canada. If abuses are identified under this licensing program, those of us who have large investments in Canadian steel will expect our Government to step in to control exports by these new players. This will be necessary in order to protect our free access to the American market.

Of course, a Comprehensive Free Trade Agreement that created a free North American Market for steel, and which would have to include country of origin rules, would go a long way to resolve the whole steel trade issue.

As always, our management teams and all of our employees have given their entrepreneurial skills and dedication to our joint enterprise and, on behalf of all of the shareholders and the Board, I thank them.

Our management are exceedingly optimistic about the opportunities for earnings for our shareholders. The future looks very bright!



Milton E. Harris, O.C.  
Chairman of the Board and President

Toronto, Ontario, May 4, 1987



## CORPORATE OVERVIEW



**H**arris Steel Group Inc. operates an electric arc furnace and produces merchant bar products and reinforcing steel rods ("rebar"). It further processes and markets the products manufactured by its own steel mill through independent operating divisions – fabricators, suppliers and subcontractors of construction steel and related products, and manufacturers of low carbon wire and cold finished bars.

Though each division operates autonomously, the combined activities of the division are mutually enhanced by:

1. Exploring new markets for downstream manufactured products that use steel from a bar mill; and
2. Developing steel mill products to exploit specific marketing opportunities identified by operating divisions.

The Harris Group intends to maximize the utilization of its steel making capacity and increase its return on capital by developing markets for specially-designed products within its own operating divisions, and outside companies.



Adjustable gauge for the cold shearing of finished bars, in lengths from 10 feet to 65 feet, on Courtice Steel's new rolling mill in Cambridge, Ontario.



# BUSINESS OPERATIONS REVIEW

## STEEL MANUFACTURING

### Courtice Steel Limited

Courtice Steel was acquired effective February 12, 1986.

Courtice operates a melt shop in Cambridge, Ontario. Billets are produced from scrap steel using an electric arc furnace and automated continuous casting of molten steel. The billets are shipped to the company's rolling mill in Bowmanville, Ontario (a distance of 100 miles) to be processed into reinforcing steel bars and merchant bars.

The Cambridge melt shop commenced production in 1981 at a site strategically located near abundant sources of scrap steel and hydro electric power. Prior to 1981 Courtice operated strictly as a re-rolling mill at its Bowmanville location purchasing raw material from other steel producers.

Courtice Steel attained its maximum rolling capacity of more than 80,000 tons in 1986 by continuing to sell very successfully into its market niche of small merchant bar shapes and by supplying Harris' Concrete Reinforcing Group with all the reinforcing steel that could not be sold to other fabricator customers. Profitability would have

improved during the year had it not been for a 2¢ per share charge against operations resulting from the decision to abandon plans to produce reinforcing steel directly from scrap railroad rail at the Bowmanville rolling mill.

Major investments in facilities were committed shortly after the acquisition of Courtice. A new \$27 million "fast change" mill, being built at the site of the melt shop in Cambridge, will start production in the second half of 1987.

Courtice Steel's markets, both for the present product lines and for those from the new mill, have strengthened considerably in recent months. The company will have no trouble selling out higher production levels in 1987. The Bowmanville rolling mill will continue to operate while the new mill in Cambridge is being phased in.

Operating costs will be charged with all of the interest and part of the depreciation related to the new mill as soon as it is ready for production. Due to the foregoing accounting policy and our conservative projection of the time required to break in the new mill, we are forecasting only a small improvement in Courtice's profit in 1987.



Concrete foundations for Courtice Steel's "state-of-the-art" rolling mill. Production at the new mill is scheduled to commence in July 1987.



## WIRE PRODUCTS AND COLD FINISHED BARS



### Laurel Steel Products Limited

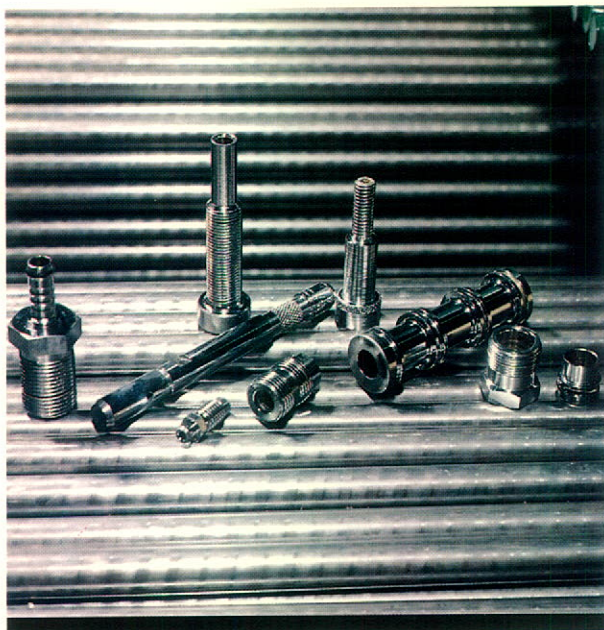
Laurel Steel manufactures wire, wire products and cold finished bars which are sold to a wide range of customers including automotive and appliance manufacturers, defence contractors and steel distributors. Laurel also makes welded mesh and other wire products used by the construction industry for the reinforcing of concrete.

On July 3, 1986 the employees of Laurel Steel were saddened by the loss of Ed Lee, Vice President of Manufacturing, who passed away after a lengthy illness. Ed's outstanding leadership qualities were a major factor in the growth and success of Laurel Steel. His dedication to his responsibilities at Laurel, and to his family, while suffering from a debilitating health problem was an inspiration to everyone.

Although shipments were up 25% over 1985, earnings increased by only 7% due to higher cost of raw materials and import price competition. Laurel gained market share by widening the range and sizes of products offered — while continuing to satisfy customer needs for shortened delivery times.

In 1986 major investments were made as part of Laurel's commitment to expand its presence in the key U.S. cold finished bar market. After considering a site in Connecticut, the company decided to relocate its American manufacturing facilities from Novi, Michigan to a 56,000 square foot building in New Hudson (also on the outskirts of Detroit). "State-of-the-art" cold finished bar drawing equipment has been installed and a significant portion of Laurel's U.S. sales is now being supplied from New Hudson. The new plant is being managed by DeLane Pate, previously in charge of the Nebraska cold finish operations of Nucor Corporation.

In the first quarter of 1987 order volume has increased in the Laurel companies as a result of stronger than expected industrial demand, particularly in the automotive sector, and booming construction activity. Canadian markets and prices have strengthened for concrete accessories and construction mesh making the outlook very good for an improvement in the margins on these products. A reduction in Laurel's overall earnings is likely in 1987, however, because of the negative effect of rising material costs on wire and cold finished bar margins, and the higher value of the Canadian dollar.



Hydraulic hose couplings, fluctuating valves and other machined fittings are among the many manufacturing applications of Laurel Steel's cold finished bar.



A service feature welcomed by customers is Laurel's ability to deliver — and unload — with its own trucks.



## CONCRETE REINFORCING

### Harris Rebar/VSL/G & H Steel

Harris Rebar Inc., VSL Canada Ltd. and VSL Ltée fabricate and erect reinforcing steel bars, post-tensioning systems and epoxy-coated reinforcing steel bars under the trade name "Epoxicote". Harris' epoxy-coating process, which has gained wide acceptance, prevents deterioration caused by salt and extends the life of concrete bridge decks and parking slabs from an average of 3-18 years to 50 years or more.

G & H Steel Industries, operating as a division of Harris Rebar Inc. supplies, fabricates and erects reinforcing steel bars and post-tensioning systems and manufactures "Epoxicote" in British Columbia.

The Harris Concrete Reinforcing Group offers steel reinforcing service from 11 manufacturing plants

located across Canada. Harris may be the only company in the world with the full range of proprietary reinforcing steel products — fabricated supply, erection, post-tension, mesh, splices and epoxy-coating.

Despite the downturn in construction activity in western Canada in 1986, increased demand in the Concrete Reinforcing Group's remaining market areas caused earnings to surpass 1985's results.

Prospects for the current year are very encouraging. The concrete construction market in Ontario and Quebec has strengthened and our order backlog, as well as the backlogs of other fabricators, has increased dramatically. We are forecasting that 1987 will see a substantial improvement in the profitability of Harris' reinforcing operations.



Harris Rebar/VSL have a contract to supply, fabricate and place 700 metric tons of reinforcing steel for a sewage treatment facility in Halton County, Ontario. This project consists of 8 reinforced concrete tanks, each of which is 43 meters (141 feet) in diameter.



## STRUCTURAL STEEL

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### **Frankel Steel/Central Fabricators/ Steel Structures Holding Corp.**

Frankel Steel, Central Fabricators and Steel Structures Holding Corp. supply, fabricate and erect structural steel for large scale construction projects such as high rise office buildings, bridges and manufacturing facilities throughout North America and in international markets.

Geoffrey Jackson, the President of Frankel Steel Limited since 1975, passed away suddenly in September 1986. Memories of his warm personality, intelligence and humour will remain with Frankel's employees, Geoff's colleagues and his many friends, as well as his family.

Maurice Charlebois, a long-time Vice President of Frankel Steel, has succeeded Geoff as Chief Operating Officer of the structural steel group of companies.

The Structural Steel Group accounted for half of the 1986 revenues of Harris Steel Group Inc. overall. A year ago structural steel generated over 50% of consolidated earnings. In 1986, however, a pre-tax loss was incurred on structural steel operations due to poor performance on a large project in Philadelphia, estimated and managed by Steel Structures, the American arm of the Structural Steel Group.

Appropriate management changes have been made and Steel Structures is now operating much more effectively.

In early 1987 a strategic decision was reached to focus future developments within the Harris Steel Group on products that can be supplied by the new mill we are building in Cambridge, Ontario.

All of the present divisions within the Harris Steel Group, except for Frankel, will be significant downstream processors of product from the new mill. Because the structural steel group of companies do not consume steel products that can be rolled in a bar mill, they must be seen as a stand-alone operation.

Accordingly, Frankel and the remaining companies comprising the Structural Steel Group have been offered for sale. With the exception of Steel Structures, all of the individual companies in the group were profitable in 1986. Frankel's excellent reputation, management, facilities and position in the marketplace should be attractive to a purchaser.

## STEEL AND ALUMINUM GRATING

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### **Fisher & Ludlow Inc.**

Fisher & Ludlow manufactures and fabricates heavy steel and aluminum grating for various industrial applications such as walkways, landings, working platforms and stairways. With three steel grating machines in service, Fisher & Ludlow is the only grating manufacturer capable of responding immediately to customer requirements for special sizes.

Fisher & Ludlow also produces "Deck Span", a lighter plank grating or "safety grating". Introduced in the second half of 1985, "Deck Span" is now stocked and marketed to Fisher & Ludlow's customers by the company's sales offices in Montreal, Edmonton and Vancouver, as well as its main plant in Burlington, Ontario.

1986 was another very successful year for Fisher & Ludlow. Sales volumes were up 16% over 1985 while earnings rose 28%.

During the past decade, Fisher & Ludlow's excellent management has steadily improved service capability and cut costs, winning an ever increasing share of the Canadian grating market along with a growing amount of American business.

## OVERHEAD CRANES AND DOORS

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### **Secord Manufacturing Limited**

After assessing Secord's crane and door manufacturing business in relation to the overall strategic plan of the Harris Steel Group, the decision was taken to offer the company for sale.

On November 14, 1986 Secord's business and some of its assets were sold to Canada Machinery Corporation.

The sale of Secord will free approximately \$4 million for investment in areas more directly related to Harris' strategic objectives.

Secord entered the year with a large order backlog and its 1986 operations were profitable. Provision has been made for possible losses on disposal and the costs of discontinuance resulting in an extraordinary charge against earnings of 2.5¢ per share.

As a division of CMC, Secord Manufacturing will continue to custom design, manufacture, install and service doors and overhead cranes for Canada's major heavy industries and utilities.

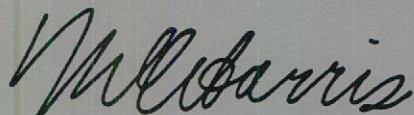


# CONSOLIDATED BALANCE SHEET

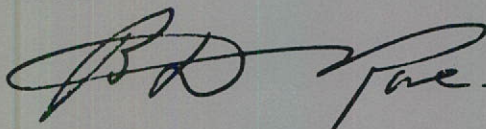
As at December 31, 1986

Assets	1986	1985
<b>Current Assets</b>		
Accounts receivable . . . . .	\$ 70,982,987	\$ 53,424,146
Inventories (note 5). . . . .	37,209,302	30,167,007
Unbilled contract costs . . . . .	7,301,485	18,111,017
Prepaid expenses and deposits. . . . .	879,616	954,933
	116,373,390	102,657,103
<b>Fixed Assets</b> (note 6). . . . .	62,613,535	36,861,512
<b>Goodwill</b> — at amortized cost. . . . .	4,793,349	1,678,449
	\$ 183,780,274	\$ 141,197,064
<b>Liabilities</b>		
<b>Current Liabilities</b>		
Bank indebtedness (note 7) . . . . .	\$ 39,968,446	\$ 21,120,804
Accounts payable and accrued liabilities. . . . .	39,113,150	32,679,285
Income and other taxes payable . . . . .	5,918,855	5,710,932
Deferred income taxes . . . . .	7,140,000	6,990,000
Current portion of long-term debt (note 7) . . . . .	959,420	878,134
	93,099,871	67,379,155
<b>Long-Term Debt</b> — less current portion (note 7). . . . .	15,148,993	6,345,464
<b>Deferred Income Taxes.</b> . . . .	9,080,000	9,430,000
	117,328,864	83,154,619
<b>Shareholders' Equity</b>		
<b>Capital Stock</b> (note 8) . . . . .	28,935,374	21,885,374
<b>Retained Earnings</b> . . . . .	37,516,036	36,157,071
	66,451,410	58,042,445
	\$ 183,780,274	\$ 141,197,064

SIGNED ON BEHALF OF THE BOARD



Director



Director



# CONSOLIDATED STATEMENT OF EARNINGS

For the Year Ended December 31, 1986



	1986	1985
<b>Continuing operations</b>		
Sales and Construction Revenue . . . . .	\$312,368,489	\$273,077,414
Cost of Sales and Contract Costs . . . . .	273,799,126	233,667,235
Gross Operating Profit . . . . .	38,569,363	39,410,179
<b>Expenses</b>		
Selling and administrative . . . . .	22,297,962	17,852,282
Interest (note 7). . . . .	3,383,887	1,934,202
Depreciation . . . . .	4,331,461	2,930,369
Amortization of goodwill . . . . .	114,839	48,214
	30,128,149	22,765,067
Earnings From Continuing Operations Before Income Taxes . . . . .	8,441,214	16,645,112
Provision For Income Taxes (note 10). . . . .	4,029,880	7,183,758
Earnings From Continuing Operations . . . . .	4,411,334	9,461,354
Earnings (Loss) From Discontinued Operations (note 2) . . . . .	209,866	(81,123)
Earnings Before Extraordinary Item . . . . .	4,621,200	9,380,231
Extraordinary Loss on Discontinuance of Operations (note 2). . . . .	300,509	—
Net Earnings For The Year . . . . .	\$ 4,320,691	\$ 9,380,231
<b>Earnings Per Share (note 1(h))</b>		
Continuing operations . . . . .	.36	.92
Discontinued operations. . . . .	.02	(.01)
Before extraordinary item . . . . .	.38	.91
After extraordinary item . . . . .	.35	.91

# CONSOLIDATED STATEMENT OF RETAINED EARNINGS

For the Year Ended December 31, 1986

	1986	1985
Balance — Beginning of Year . . . . .	\$ 36,157,071	\$ 28,703,874
Cost of issuance of Class A non-voting shares. . . . .	—	25,068
	36,157,071	28,678,806
Net earnings for the year . . . . .	4,320,691	9,380,231
	40,477,762	38,059,037
Dividends (note 8). . . . .	2,961,726	1,901,966
Balance — End of Year . . . . .	\$ 37,516,036	\$ 36,157,071



# CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

For the Year Ended December 31, 1986

	1986	1985
<b>Operating Activities</b>		
Cash provided from (used in) continuing operations —		
Earnings from continuing operations . . . . .	\$ 4,411,334	\$ 9,461,354
Depreciation and amortization . . . . .	4,446,300	2,978,583
Deferred income taxes — long-term . . . . .	(1,144,108)	2,740,000
Loss (gain) on sale of fixed assets . . . . .	252,815	(60,065)
Imputed interest on acquisition of Courtice Steel Limited . . . . .	25,043	—
(Increase) in operating working capital . . . . .	(5,284,152)	(22,608,127)
	2,707,232	(7,488,255)
Cash provided from (used in) discontinued operations . . . . .	(518,121)	173,415
Cash provided from discontinuance of operations . . . . .	76,000	—
	(442,121)	173,415
<b>Investing Activities</b>		
Acquisition of Courtice Steel Limited . . . . .	(9,608,605)	—
Less: Value of Class A non-voting shares issued . . . . .	7,050,000	—
	(2,558,605)	—
Additions to fixed assets (net of unpaid amounts) . . . . .	(15,880,057)	(12,039,451)
Proceeds from sale of fixed assets . . . . .	1,019,430	162,886
	(17,419,232)	(11,876,565)
<b>Financing Activities</b>		
Proceeds from issuance of Class A non-voting shares . . . . .	—	18,365,000
Less: Cost of issuance of Class A non-voting shares . . . . .	—	(25,068)
	—	18,339,932
Proceeds from long-term debt . . . . .	4,302,136	5,015,009
Reduction of long-term debt . . . . .	(977,936)	(8,935,734)
	3,324,200	14,419,207
<b>Dividends</b> . . . . .	(2,961,726)	(1,901,966)
<b>Increase in Bank Indebtedness</b> . . . . .	(14,791,647)	(6,674,164)
<b>Bank Indebtedness — Beginning of Year</b> . . . . .	(21,120,804)	(14,446,640)
<b>Bank Indebtedness of Courtice Steel Limited at Date of Acquisition</b> . . . . .	(4,055,995)	—
<b>Bank Indebtedness — End of Year (note 7)</b> . . . . .	\$ (39,968,446)	\$ (21,120,804)

## AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of Harris Steel Group Inc. as at December 31, 1986 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1986 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.

Coopers & Lybrand  
Chartered Accountants

Toronto, Ontario, April 9, 1987



# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS



For the Year Ended December 31, 1986

## 1. Accounting Policies

### (a) Basis of consolidation

The consolidated financial statements include the accounts of the company and all its subsidiaries at their respective year-ends.

Joint ventures, both incorporated and unincorporated, are accounted for under the proportionate consolidation method. This method reflects the company's share of the joint ventures' assets, liabilities, revenues and expenses in the financial statements as indicated in note 3.

### (b) Foreign exchange

The company applies the temporal method of accounting for the translation into Canadian dollars of foreign currency amounts and the accounts of its U.S. subsidiaries, all of which are integrated operations. Monetary assets and liabilities are translated at the exchange rate in effect at the balance sheet date and non-monetary assets and related depreciation expense are translated at historic exchange rates. Revenues and expenses, other than depreciation, are translated at the average exchange rate for the year.

Foreign exchange gains and losses on transactions during the year and on the year-end translation of the accounts are reflected in earnings.

### (c) Inventories

The company values its inventory at the lower of cost and market. Cost is determined on a weighted average basis for structural steel inventories and on a first-in, first-out basis for all other inventories. Market is defined as replacement cost for raw materials and net realizable value for work-in-process and finished goods.

### (d) Unbilled contract costs

Unbilled contract costs represent contracts in progress valued on the percentage-of-completion basis. Under the percentage-of-completion method, profit is accrued as the work is performed, and provision is made for anticipated losses to the completion of the contract. Although the company uses its best engineering estimates, the final results of jobs in progress will necessarily be dependent upon future costs and revenues. Claims for additional compensation are included in income only when approved by the owner.

### (e) Fixed assets and depreciation

Fixed assets are recorded at historical cost less applicable investment tax credits. The company depreciates its buildings, steel making facilities and equipment and machinery and equipment on a straight-line basis and its mobile equipment on a declining balance basis at the following rates:

Buildings	— 2½%
Steel making facilities and equipment	— 5%
Machinery and equipment	— 7½%
Mobile equipment	— 30%

Gain or loss on disposal of individual assets is recognized in income in the year of disposal.

### (f) Goodwill

Goodwill represents the excess of the cost of each investment in shares of a subsidiary over the fair value of its underlying net assets at the date of acquisition and is currently being amortized on a straight-line basis over forty years.

### (g) Income taxes

The company follows the income tax allocation method of accounting for income taxes. Under this method, income taxes in the consolidated statement of earnings are based upon the revenues and expenses recorded in the accounts, which may differ from income taxes actually paid or payable. The cumulative effect of these differences is shown in the consolidated balance sheet as "deferred income taxes".

### (h) Earnings per share

Earnings per share are calculated on 12,271,489 shares (1985 — 10,310,393 shares), being the weighted average number of shares outstanding during the year.

## 2. Discontinued Operations

The operations of Secord Manufacturing Limited were discontinued effective from November 14, 1986 and its remaining assets were written down to estimated realizable value. Net assets of the discontinued operations included in the balance sheet consist of the following:

	\$
Current assets	3,533,963
Fixed assets and goodwill	883,591
Liabilities	(3,750,897)
	<u>666,657</u>

The company incurred and/or provided for costs on the discontinuance of \$367,909 in 1986.

These amounts, less tax recoveries, are reported as an extraordinary item in 1986 as follows:

	\$
Asset disposals	155,175
Other costs	154,000
Write-off of goodwill — net	58,734
	<u>367,909</u>
Income tax recovery	(67,400)
Extraordinary item	<u>300,509</u>



The results of the discontinued operations were as follows:

	1986	1985
	\$	\$
Sales	14,567,231	11,309,862
Cost of sales	12,977,676	9,966,536
Gross profit	1,589,555	1,343,326
Expenses	1,177,689	1,503,653
	411,866	(160,327)
Income tax expense (recovery)	202,000	(79,204)
Earnings (loss) from discontinued operations	209,866	(81,123)

### 3. Accounting for Joint Ventures

A summary of the company's pro-rata share of joint venture operations is set out below:

	1986	1985
	\$	\$
Assets	41,200	384,861
Liabilities	70,027	76,408
Revenues	48,298	17,448
Expenses	31,133	13,116

### 4. Acquisition of Subsidiary Company

Effective February 12, 1986, the company acquired all the outstanding shares of Courtice Steel Limited, a manufacturer of concrete reinforcing steel and merchant steel, for cash of \$2,558,605 and 600,000 Class A non-voting shares valued at \$11.75 per share. The acquisition was accounted for as a purchase with the acquired company's operating results being included in the consolidated results of the company from the effective acquisition date.

Net assets acquired:	\$
Operating working capital	4,286,078
Fixed assets	11,974,650
Bank indebtedness	(4,055,995)
Long-term debt	(5,451,955)
Deferred income taxes	(769,124)
Goodwill	3,624,951
Purchase Price	9,608,605

### 5. Inventories

	1986	1985
	\$	\$
Raw materials and work-in-process	29,886,651	25,147,660
Finished goods	7,322,651	5,019,347
	37,209,302	30,167,007

### 6. Fixed Assets - at cost

	1986	1985
	\$	\$
Land	3,758,939	3,129,121
Buildings	14,832,157	13,363,768
Steel making facilities and equipment	12,469,264	—
Machinery and equipment	44,208,976	35,939,740
Mobile equipment	4,696,524	4,974,498
Facilities under construction	10,373,226	—
	90,339,086	57,407,127
Less: Accumulated depreciation	27,725,551	20,545,615
	62,613,535	36,861,512

The company plans to invest approximately \$27 million in a new steel rolling mill. Approximately \$9.5 million of this amount is included above as "facilities under construction".

### 7. Long-Term Debt and Bank Indebtedness

	1986	1985
	\$	\$
Term bank loan, due June 1, 2000, with principal repayments amortized over 15 years, callable at the lender's option in 1992, net of unamortized deferred finance charges of \$123,714 (1985 - \$151,223). Effective January 1, 1987 and January 1, 1988, the interest rate will increase from 70% to 77.78% and 85.56%, respectively, of U.S. bank prime lending rate	4,784,725	4,954,373
Loan payable at 13.25%, repayable in blended monthly instalments of principal and interest of \$67,112 with the balance due November 1, 1988	1,361,179	1,948,256
Term bank loans	9,712,409	—
Other	250,100	320,969
	16,108,413	7,223,598
Less: Current portion	959,420	878,134
	15,148,993	6,345,464

The revolving term bank loans of \$9,712,409 are subject to call on demand and bear interest at the bank prime lending rate. The company has opted to have the loans remain a revolving credit facility at least until the next annual review in 1987. Should the company opt to convert the loans to a term facility, principal repayments of \$2,500,000



in annual instalments would commence on July 1, 1988, and the interest rate would rise to prime plus ½%.

Specific fixed assets, with a carrying value of approximately \$16,300,000, are pledged against the above loans. In addition, inventories and accounts receivable are pledged as security for the company's bank indebtedness.

Interest incurred on long-term debt for the year amounted to \$1,049,790 (1985 – \$826,621).

Principal repayments during the next five fiscal years (not including the possible term loan repayments) are as follows:

	\$
1987	959,420
1988	985,278
1989	278,897
1990	297,505
1991	308,536

Subsequent to December 31, 1986, the company arranged a term loan of up to \$30 million at the bank prime lending rate to finance its investment in a new steel rolling mill (see note 6). If the full facility of \$30 million is utilized, the foregoing principal repayments will be increased by \$5 million in 1988, \$10 million in 1989 and \$15 million in 1990. As at March 31, 1987, the company had expended approximately \$14 million on this project. None of the term loan facility has yet been drawn.

## 8. Capital Stock and Dividends

	1986 \$	1985 \$
Capital stock (without par value) –		
Authorized –		
An unlimited number of Class A non-voting shares		
An unlimited number of Class B shares		
100 common shares		
Issued and fully paid –		
9,234,998 Class A non-voting shares (1985 – 8,634,998 shares)	28,143,631	21,093,631
3,105,532 Class B shares	791,743	791,743
	<u>28,935,374</u>	<u>21,885,374</u>

### Share issue

During the year the company issued 600,000 Class A non-voting shares for \$7,050,000 as partial consideration for the purchase of Courtice Steel Limited.

## Voting rights

Class A non-voting shares are not entitled to vote unless the company has failed to pay dividends totalling 2½¢ per Class A non-voting share for eight consecutive fiscal quarters. Thereafter, each Class A non-voting share is entitled to one vote until, in any fiscal quarter, a dividend of 2½¢ per Class A non-voting share has been paid or declared and set aside for payment.

Each Class B share is entitled to one vote at all meetings of the shareholders.

## Take-over protection

The Class A non-voting shares become convertible into Class B voting shares on a share-for-share basis after a bona fide offer, which must, by reason of applicable securities laws or stock exchange by-laws, regulations or policies, be made to each holder of Class B voting shares whose last recorded address is in the jurisdiction to which the relevant requirement applies, is accepted by the holders of a majority of the outstanding Class B voting shares.

## Dividends

Class A non-voting shares are eligible to receive a preferential, non-cumulative, quarterly dividend of 2½¢ per share.

Class B shares are not eligible to receive a dividend in any quarter until a dividend of 2½¢ per share has been paid on the Class A non-voting shares. Thereafter, Class B shares are eligible for a dividend of up to 2½¢ per share in any quarter.

Dividends in excess of 2½¢ per share in any quarter will be paid equally on the Class A non-voting shares and Class B shares.

During 1986, the company paid dividends of 24¢ per issued Class A non-voting and Class B share.

## 9. Lease Commitments

The company is required to make aggregate future minimum lease payments of \$6,885,000 under operating leases that have non-cancellable lease terms in excess of one year at December 31, 1986. Annual lease payments during the next five fiscal years are as follows:

	\$
1987	1,834,000
1988	1,540,000
1989	1,307,000
1990	1,092,000
1991	753,000



## 10. Income Taxes

The provision for income taxes reflects an effective tax rate which differs from the statutory tax rate. A reconciliation of the two rates is as follows:

	1986 %	1985 %
Canadian and U.S. basic federal income tax rates	46.0	46.0
Provincial and state taxes net of federal deductions	4.5	4.5
Statutory tax rate	50.5	50.5
Add (deduct) the tax effect of –		
Investment and other tax credits	–	(0.5)
Inventory allowance	(0.8)	(2.4)
Manufacturing and processing profits deduction	(7.5)	(4.9)
Non-taxable foreign exchange losses (gains)	0.2	(0.3)
Non-deductible portion of purchase price of subsidiaries	3.8	0.4
Federal surtax	2.1	0.7
Other	0.8	(0.3)
Effective tax rate	49.1	43.2

## 11. Contingent Liabilities

The company's subsidiaries have operations throughout the United States and Canada and in the normal course, the company and its subsidiaries are named as defendants in various legal actions. Based on the advice of its counsel, the company is of the opinion that the actions outstanding, in the aggregate, will not result in material detriment to the company.

## 12. Segmented Information and Export Sales

### a) Geographic segmented information

1986	Canada \$	United States \$	Total \$
<b>Revenues</b>			
Sales and construction revenue	251,743,007	147,992,292	399,735,299
Intersegment revenue	(71,927,765)	(15,439,045)	(87,366,810)
	<u>179,815,242</u>	<u>132,553,247</u>	<u>312,368,489</u>
<b>Net Earnings</b>			
Operating profit	<u>34,612,428</u>	<u>3,956,935</u>	<u>38,569,363</u>
Selling and administrative expenses			(22,297,962)
Depreciation			(4,331,461)
Interest expense			(3,383,887)
Amortization of goodwill			(114,839)
Income taxes			(4,029,880)
Earnings from discontinued operations			209,866
Extraordinary loss on discontinuance of operations			(300,509)
			<u>4,320,691</u>
<b>Identifiable Assets</b>	<u>128,606,669</u>	<u>55,173,605</u>	<u>183,780,274</u>

## 1985

	Canada \$	United States \$	Total \$
<b>Revenues</b>			
Sales and construction revenue	222,057,460	99,036,970	321,094,430
Intersegment revenue	(34,628,141)	(13,388,875)	(48,017,016)
	<u>187,429,319</u>	<u>85,648,095</u>	<u>273,077,414</u>
<b>Net Earnings</b>			
Operating profit	<u>30,747,025</u>	<u>8,663,154</u>	<u>39,410,179</u>
Selling and administrative expenses			(17,852,282)
Depreciation			(2,930,369)
Interest expense			(1,934,202)
Amortization of goodwill			(48,214)
Income taxes			(7,183,758)
Loss from discontinued operations			(81,123)
			<u>9,380,231</u>
<b>Identifiable Assets</b>	<u>105,170,988</u>	<u>36,026,076</u>	<u>141,197,064</u>

### b) Industry segmented information

In 1985 and prior years, the company operated within the steel industry in general. As a result of corporate strategies developed in 1986, management has determined the company's structural steel operations to be a reportable industry segment in 1986.

1986	Steel Operations Other Than Structural Steel \$	Structural Steel Operations \$	Total \$
<b>Revenues</b>			
Sales and construction revenue	156,338,344	156,299,952	312,638,296
Intersegment revenue	(267,061)	(2,746)	(269,807)
	<u>156,071,283</u>	<u>156,297,206</u>	<u>312,368,489</u>
<b>Net Earnings</b>			
Operating profit	27,126,751	11,442,612	38,569,363
Depreciation	(2,699,285)	(1,632,176)	(4,331,461)
	<u>24,427,466</u>	<u>9,810,436</u>	<u>34,237,902</u>
Selling and administrative expenses			(22,297,962)
Interest expense			(3,383,887)
Amortization of goodwill			(114,839)
Income taxes			(4,029,880)
Earnings from discontinued operations			209,866
Extraordinary loss on discontinuance of operations			(300,509)
			<u>4,320,691</u>
<b>Identifiable Assets</b>	<u>108,304,014</u>	<u>75,476,260</u>	<u>183,780,274</u>
<b>Capital Expenditures</b>	<u>12,995,135</u>	<u>5,122,720</u>	<u>18,117,855</u>

c) In 1986, the company's Canadian segment had direct sales to customers in foreign countries, primarily the United States, of approximately Cdn. \$43 million (1985 – Cdn. \$75 million). Aggregate direct sales to U.S. customers amounted to approximately Cdn. \$176 million (1985 – Cdn. \$160 million).

d) Intersegment revenues above have been determined on the same basis as similar transactions with unrelated parties.

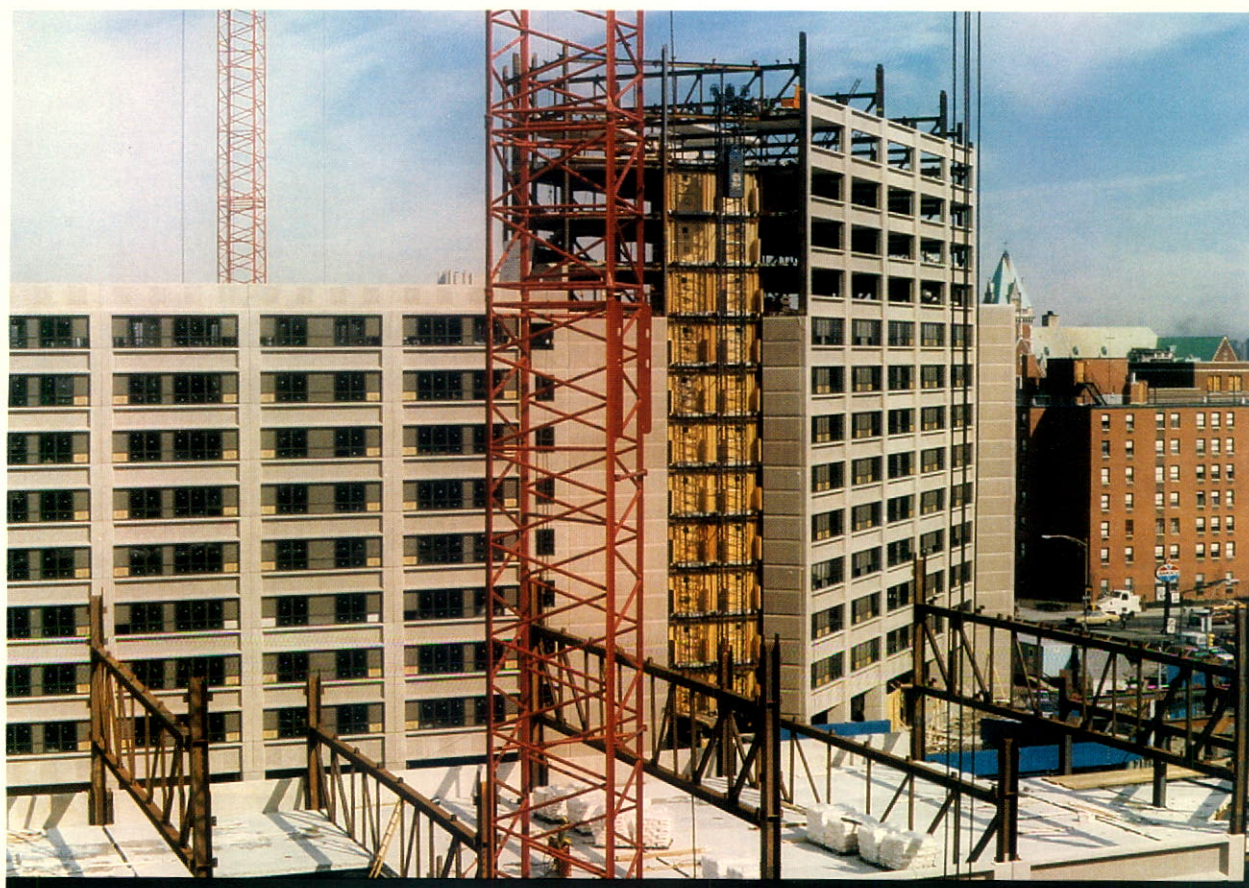


## QUARTERLY FINANCIAL DATA (unaudited)



(Dollars in thousands except per share amounts)

	First quarter	Second quarter	Third quarter	Fourth quarter	Year
<b>1986</b>					
Sales from continuing operations	\$67,819	\$81,166	\$85,683	\$77,700	\$312,368
Earnings from continuing operations	1,009	1,660	308	1,434	4,411
Earnings (loss) from discontinued operations	(76)	(29)	(69)	384	210
Earnings before extraordinary item	933	1,631	239	1,818	4,621
Earnings per share:					
Continuing operations	.08	.13	.03	.12	.36
Discontinued operations	—	—	(.01)	.03	.02
Before extraordinary item	.08	.13	.02	.15	.38
<b>1985</b>					
Sales from continuing operations	\$53,939	\$70,695	\$75,101	\$73,342	\$273,077
Earnings from continuing operations	1,219	2,368	1,959	3,915	9,461
Earnings (loss) from discontinued operations	(141)	(176)	58	178	(81)
Earnings before extraordinary item	1,078	2,192	2,017	4,093	9,380
Earnings per share:					
Continuing operations	.12	.24	.20	.36	.92
Discontinued operations	(.01)	(.01)	—	.01	(.01)
Before extraordinary item	.11	.23	.20	.37	.91



Three building "Towers on the Park" apartment complex in New York City. This residential project utilizes Steel Structures' Staggered Truss Building System, which enables "fast track" construction at a lower cost than traditional buildings.



# FINANCIAL SUMMARY

	1986	1985	(Dollars in thousands except per share amounts)		
	1984	1983	1982		
<b>Operating results</b>					
Sales from continuing operations	\$ 312,368	\$ 273,077	\$ 166,244	\$ 167,126	\$ 146,484
Earnings from continuing operations	4,411	9,461	3,463	5,315	4,552
Return on sales	1.4%	3.5%	2.1%	3.2%	3.1%
Earnings (loss) from discontinued operations	\$ 210	\$ (81)	\$ (481)	\$ (1,814)	\$ (340)
Earnings before extraordinary items	4,621	9,380	2,982	3,501	4,212
Return on average equity	7.4%	20.8%	9.5%	11.7%	15.1%
<b>Per Share</b>					
Earnings from continuing operations	\$ .36	\$ .92	\$ .36	\$ .55	\$ .47
Earnings (loss) from discontinued operations	.02	(.01)	(.05)	(.19)	(.03)
Earnings before extraordinary items	.38	.91	.31	.36	.44
Dividends	.24	.185	.14	.14	.14
Shareholders' equity	5.42	5.63	3.31	3.14	3.02
Average shares outstanding	12,271,489	10,310,393	9,740,530	9,740,530	9,692,880
<b>At year end</b>					
Total assets	\$ 183,780	\$ 141,197	\$ 104,102	\$ 97,545	\$ 97,768
Working capital	23,274	35,278	19,439	17,049	14,172
Current ratio	1.2:1	1.5:1	1.4:1	1.3:1	1.3:1
Fixed assets, less depreciation	\$ 62,614	\$ 36,862	\$ 28,002	\$ 27,288	\$ 25,840
Goodwill	4,793	1,678	1,727	1,532	1,572
Deferred income taxes	9,080	9,430	6,690	4,680	3,428
Long-term debt	15,149	6,345	10,254	10,583	8,851
Shareholders' equity	66,451	58,042	32,224	30,606	29,305
Long-term debt/Total capital	18.6%	9.9%	24.1%	25.7%	23.2%



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**Frankel Steel Limited**  
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**Central Fabricators Ltd.**  
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**Steel Structures Holding Corp.**  
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 Telephone: (215) 865-3032

**Laurel Steel Products Limited**  
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 Telephone: (416) 632-5141

**Laurel Steel of New England Inc.**  
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 Telephone: (617) 588-2118

**Laurel Steel Inc.**  
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 New Hudson, Michigan 48165  
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**Fisher & Ludlow Inc.**  
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**Courtice Steel Limited**  
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 Telex: 06-981390

## Investor information

**Registrar and transfer agent**  
 National Trust Company,  
 4 King Street West,  
 Toronto, Ontario M5H 3W7

**Counsel**  
 Goodman & Goodman

**Auditors**  
 Coopers & Lybrand

**Bankers**  
 Royal Bank of Canada  
 Toronto Dominion Bank

## Corporate officers

**Milton E. Harris, O.C.**  
 Chairman of the Board and President

**Bruce Timmerman, C.A.**  
 Vice President - Finance

**Lorie Waisberg, Q.C.**  
 Secretary

## Operating executives

**Maurice Charlebois**  
 President  
 Frankel Steel Limited

**John Harris**  
 President  
 Harris Rebar Inc.

**James B. Kelly**  
 President  
 Courtice Steel Limited

**Derek Price**  
 General Manager  
 Fisher & Ludlow Inc.

**Glenn Riddell**  
 President  
 Laurel Steel Products Limited

## Board of directors

**Milton E. Harris, O.C.**  
 Chairman of the Board and  
 President  
 Harris Steel Group Inc.  
 Director since 1953

**Cecil H. Franklin**  
 Chairman  
 Algonquin Mercantile Corporation  
 Director since 1973

**Neil B. Ivory**  
 President of Pembroke  
 Management Ltd.  
 President and Chief Executive  
 Officer of GBC Capital Ltd.  
 Director since 1977

**James W. Leech**  
 President  
 Unicorp Canada Corporation  
 Director since 1982

**Barrie D. Rose, F.C.A.**  
 Chairman and Chief Executive  
 Officer  
 Androcan Inc.  
 Director since 1973

**Alexander Kerney**  
 Chairman of the Board  
 Courtice Steel Limited  
 Appointed Director in 1986

## Audit Committee

Milton E. Harris, O.C.  
 Cecil H. Franklin  
 Neil B. Ivory  
 Barrie D. Rose, F.C.A.



## STOCK MARKET TRADING INFORMATION

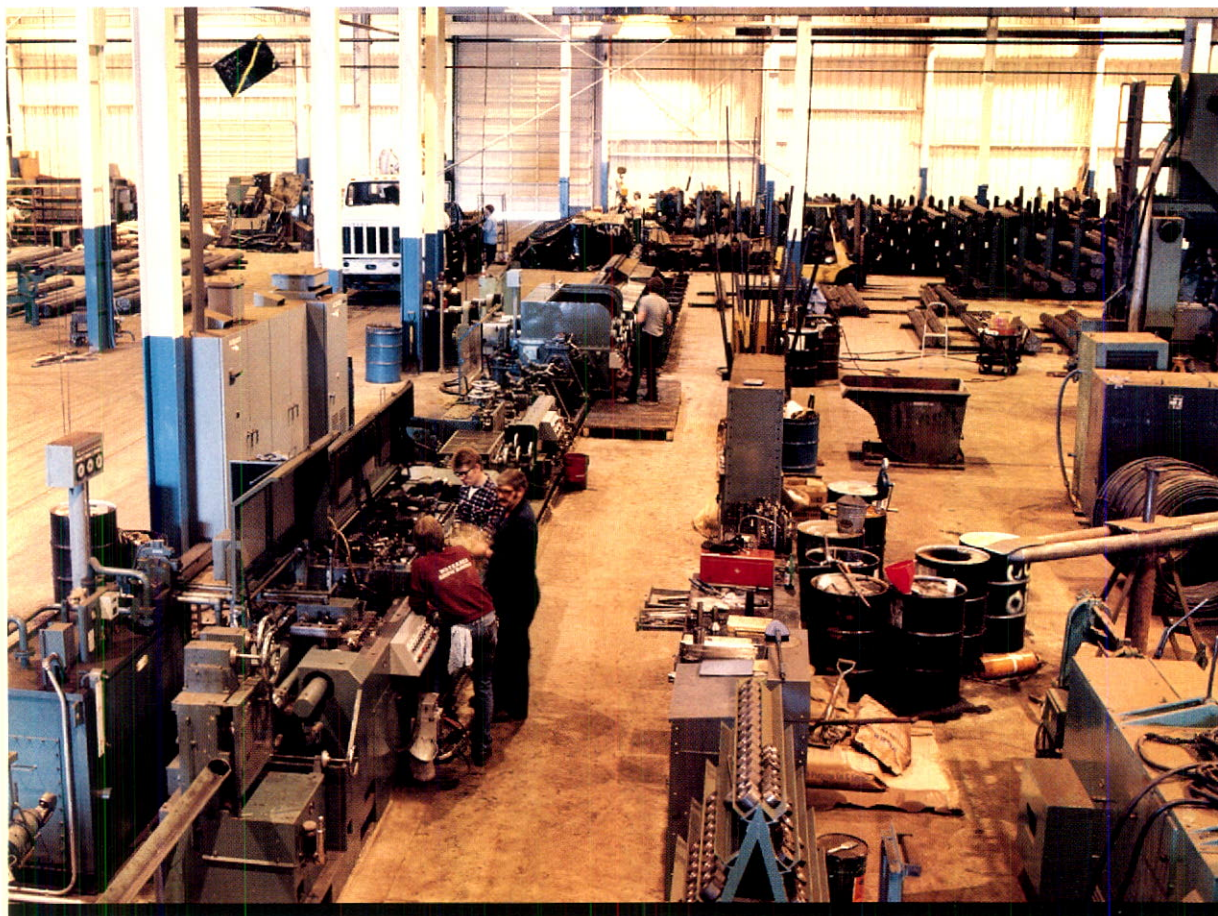
The company's shares are listed on The Toronto Stock Exchange as Harris A (HSG.A) and Harris B (HSG.B).

### Class A shares 1986

	High	Low	Close	Shares traded	Dividend
First quarter	14.75	9.87	14.00	2,310,621	\$.06
Second quarter	16.25	12.25	12.87	1,290,035	.06
Third quarter	13.00	10.25	10.62	723,960	.06
Fourth quarter	11.25	8.12	8.75	448,651	.06
Year	16.25	8.12	8.75	4,773,267	.24
Year 1985	11.00	4.37	10.25	4,248,465	.185

### Class B shares 1986

	High	Low	Close	Shares traded	Dividend
First quarter	14.75	9.50	14.00	254,830	\$.06
Second quarter	15.87	12.62	12.62	131,940	.06
Third quarter	12.50	9.87	10.25	65,500	.06
Fourth quarter	11.50	9.50	9.50	17,600	.06
Year	15.87	9.50	9.50	469,870	.24
Year 1985	10.37	4.50	10.00	402,367	.185



A significant portion of Laurel Steel Inc.'s U.S. sales are being supplied from this recently acquired 56,000 square foot plant on the outskirts of Detroit, Michigan.







