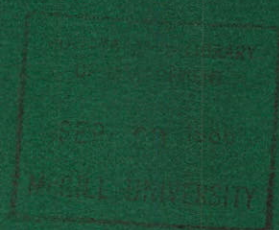


**The Hamilton
Group Limited**



**Annual
Report 1986**

CORPORATE INFORMATION

DIRECTORS:

Frederick W. Dakin*	Chairman, The G. W. Robinson Co. Limited
Graham R. Dawson*	Chairman, Dawson Construction Ltd.
Lincoln S. Magor**†	President, Mimik Inc.
Edward B. Priestner*†	President, Westinghouse Canada Inc.
John F. Schunk*	Retired, former Vice President, The Hamilton Group Limited
John G. Sheppard††*	Vice Chairman, Dofasco Inc.
Alan B. Young†	President, The Hamilton Group Limited
David M. Young	Chairman, Hamilton Rentals Limited — U.K.
William H. Young†	Chairman, The Hamilton Group Limited

††Chairman, Executive Committee of the Corporation

†Member, Executive Committee of the Corporation

**Chairman, Audit Committee of the Corporation

*Member, Audit Committee of the Corporation

HONORARY DIRECTOR:

James M. Young

OFFICERS:

William H. Young	Chairman
Alan B. Young	President
G. Duncan Shearer	Senior Vice President
William J. Young	Senior Vice President
Gordon Brown	Vice President
Mark W. Horsley	Vice President
Patricia L. Nielsen	Vice President
C. Leslie McCarthy	Vice President & Secretary

HEAD OFFICE:

Suite 300, Oakville Corporate Centre
700 Dorval Drive, Oakville, Ontario L6K 3V3

REGISTRAR AND TRANSFER AGENT:

National Trust Company, Toronto, Ontario

SOLICITORS:

Blake, Cassels & Graydon

AUDITORS:

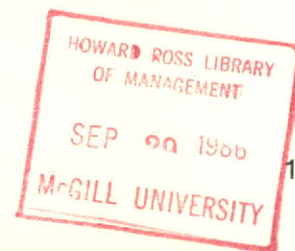
Peat, Marwick, Mitchell & Co.

HIGHLIGHTS

	1986	1985
Income (loss) before extraordinary items	\$(2,488,854)	\$ 3,251,684
Net income (loss)	\$(6,763,275)	\$ 3,474,794
Basic earnings (loss) per share		
Income (loss) before extraordinary items	\$ (1.02)	\$ 1.33
Net income (loss)	\$ (2.76)	\$ 1.42
Number of Class A and B shares outstanding	2,458,537	2,451,239
Class A and B shares registered in Canada	97.6%	95.6%

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ANNUAL REPORT OF DIRECTORS

TO THE SHAREHOLDERS

The fiscal year ended April 30, 1986 was disappointing. The poor operating results were due entirely to the performance of the computer rental and sales subsidiary in the United States. Further, a complete revaluation of the Mexican investments was necessary due to that country's foreign exchange problems, stemming largely from the major decrease in the price of oil and volume exported. This resulted in a major downward revision of the value of these assets.

Hamilton Group continued with its strategy of becoming a leader in the computer rental and sales business and the progress in this business is reported in the following section "Annual Report on Operations".

In line with the above strategy, Hamilton Group realized over \$20,000,000 in cash from disposal of non-computer business related assets during 1985 and 1986. Chief of these disposals was the sale of the company's interest in Citibank Leasing Canada Limited and Charter Credit Corporation.

Financial Results

The loss after tax but before extraordinary items was \$2,488,854 for fiscal 1986, compared to a profit of \$3,251,684 earned during the previous year. The loss in 1986 is equal to \$1.02 per common share outstanding, versus a profit of \$1.33 per share for 1985. The reason for this loss in 1986 is reported on in the following Annual Report on Operations.

The final loss for the year 1986 after tax and extraordinary items was \$6,763,275, or \$2.76 per share, compared to a 1985 profit of \$3,474,794, equal to \$1.42 per share. Extraordinary items total a loss of \$4,274,421 and represent basically the net difference between the added provision for losses on Mexican investments, and the gain on the sale of the Citibank Leasing Canada Limited investment. The detail of extraordinary items is given in Note 12 to Consolidated Financial Statements.

As reported in last years Annual Report, the company issued \$10,000,000 12% convertible subordinated debentures in May 1985. The funds realized from this issue, plus some of the proceeds from disposal of assets, were used to reduce short term bank debt by \$15,334,995 and term bank debt by a further \$7,213,739. Bank indebtedness at year end totalled \$14,351,015 compared to shareholders equity of \$9,066,014. The ratio of bank debt to borrowing base of equity plus \$10,000,000 subordinated debt was 0.75 to 1, and to operating assets was 0.39 to 1.

The number of common shares, Class A and B, outstanding during the year increased by the issue of 7,298 shares under the Employee Share Purchase Plan, to a total of 2,458,537 from 2,451,239. Book value per share decreased from \$6.45 per share to \$3.69 per share. However, with the Mexican investments carried at estimated realizable value and other assets carried at cost and well below market value, the book value appears understated.

The Class A shares of The Hamilton Group Limited which are listed on The Toronto Stock Exchange traded at a high of \$9.75 per share and a low of \$5.50 per share during the year. The price at the end of July 1986 was \$4.50 to \$4.75 per share.

Reorganization Programme

In keeping with the company's development as a computer sales and rental business, assets not relating directly to this business are for disposal. During the year the following disposals were completed.

On May 15, 1985 the sale of Hamilton Group's 40% interest in Citibank Leasing Canada Limited and Citibank Factoring Canada Limited was completed. This transaction produced a net gain of \$5,586,000 which was previously reported to shareholders.

On April 25, 1986 Hamilton Group sold its wholly-owned subsidiary, Charter Credit Corporation for its book value of \$1,400,000. The sale of Charter effectively takes Hamilton Group out of the mortgage and property rental business.

During the present fiscal year further sales are anticipated. The book value of the remaining real estate properties is now less than \$1,000,000, and the estimated market value of these assets is in the neighborhood of two times the book value.

IMPULSORA MEXICANA DE ARRENDAMIENTO, S.A. DE C.V. (IMEXA)

The investment situation in Mexico is very complex.

The actual business operations which are basically equipment leasing of office equipment and vehicles are doing very well. Financial margins are excellent, collection and bad debt experience favourable, and costs have been relatively well controlled within an economic environment where inflation exceeds 80% per year. New business volume has been restricted because IMEXA has been unable to borrow funds to pay for the acquisition of equipment for lease.

During the year the Bank of Mexico required that commercial banks place as a reserve with the central bank 90 pesos of every 100 peso deposit received. New loans were generally not available in Mexico. This restriction in new business volume has slowed IMEXA's growth and could endanger its future ability to service its debt to Hamilton Group through the government agency FICORCA.

Mexico is short of foreign exchange. Mexico's foreign debt of close to US\$100 billion was contracted during the period of high demand and high prices for oil. With the major drop in oil prices coupled with a reduction in export volume, Mexico does not have the foreign exchange available to service its foreign debt. It is involved in protracted and difficult negotiations with the International Monetary Fund for further loans in U.S. dollars, which will be followed by equally difficult negotiations with its foreign creditor banks.

The effect of the above is to make the timely payment of interest and capital to Hamilton Group on its loans very uncertain. Hamilton Group is owed US\$8 million via a Trust, with the acronym FICORCA, established by the Government of Mexico to eliminate foreign exchange exposure for Mexican corporations. It was formed in 1983 after the massive devaluation of the peso in the previous year. Under the terms of FICORCA, each loan has a "rescue" value which in effect is a contractual present cash value calculated on a very complex formula which considers foreign exchange rates, inflation rates, as well as interest rate variations.

If Hamilton Group accepts the "rescue" value IMEXA would then be left in a virtual debt free position with substantial leases receivable and excellent earnings, tax sheltered by previous foreign exchange losses. IMEXA would have a substantial value in pesos. The value in pesos is difficult to translate to U.S. dollars. From April 30, 1985 to 1986 the peso was devalued at the official controlled rate from \$215.30 pesos to \$502.90 pesos to US\$1.00, or 133%. Both the continuing rate of devaluation and the availability of dollars within Mexico is difficult to forecast.

The result of all the above noted uncertainty is to make the valuation of Hamilton Group's investments in Mexico difficult. The best estimate of net realizable funds as at April 30, 1986 was \$4,600,000 Canadian, and the provision has been increased to reflect this net book value.

Under Mexican law, auxiliary credit institutions, which include leasing companies such as IMEXA, must be Mexican controlled. Every effort is being made to comply with this law and for Hamilton Group to realize on its investment as much and as quickly as possible.

ASSETS IN COURSE OF REALIZATION

These assets with a book value of \$951,248, consist of real estate that Hamilton Group acquired during the operation of business either no longer owned or not in Hamilton Group's longer term plans. The four main groups of real estate are: the sites of former textile mills in Hamilton and Dundas; land in Burlington adjacent to Citibank Leasing Canada Limited, formerly an affiliate; three development sites near Bridgewater, Nova Scotia previously owned by Charter Credit Corporation; and the former head office building used by Hamilton Rentals Limited in London, England, when it was a wholly-owned subsidiary of Hamilton Group.

There are currently signed offers of sale and purchase outstanding on the building in London, England and on a parcel of land in Burlington, Ontario. An option has been granted on the 6.5 acre parcel in Dundas, Ontario. It is the continued intention to dispose of these assets in an orderly manner over a relatively short period of time.

AFFILIATED COMPANIES

INTERNATIONAL MERCANTILE FACTORS LTD. (IMF)

IMF continued its steady growth during Hamilton Group's fiscal 1986, and its earnings for the year established another record. Hamilton Group's book value of its investment in debt and equity of IMF increased to \$2,406,798 from \$2,144,520. Operating earnings attributable to Hamilton Group from this investment increased 7% to \$448,000 from \$420,000 in 1985. This represents a 20% return on the average investment in IMF during the year.

During the year, IMF wrote off all the unamortized goodwill on its balance sheet. This created an extraordinary item of which Hamilton Group's share was \$65,600.

Subsequent to April 30, 1986, management of IMF purchased 5% of the outstanding shares of the company. Hamilton Group and IMF's other equal shareholder each sold 2.5% or half of these shares. Hamilton Group's interest in IMF's equity now stands at 35.0%.

HAMILTON RENTALS LIMITED (EUROPE)

Hamilton Rentals Limited is owned 35.1% by Hamilton Group. The European operations encompass the United Kingdom, France, Germany and Holland in order of size. The results for 1986 were disappointing due largely to the poor performance of the German operations. Since the

April 30, 1986 year end, a letter of intent to purchase the German operations has been received from a group which includes the management of the operation. Hamilton Group's estimated share of \$250,000 of the loss on the disposal of the German operations has been provided for in extraordinary items. The disposal of the German operations will not only remove a "loss" from Hamilton Rentals on-going operations, but will allow management to concentrate their time on the profitable operations of the United Kingdom, France and Holland.

Hamilton Group's share of income from the European operations for 1986 was \$196,000 compared to \$499,000 in 1985. The 1986 income represents a return of approximately 5% on Hamilton Group's average investment in Hamilton Rentals Limited during 1986. However, with the closing of the German operations, the outlook is for a substantial improvement in 1987.

The book value of Hamilton Group's investment in Hamilton Rentals Limited is now \$3,569,168. The realizable value of this investment is estimated to be well in excess of the book value.

CANCORD

The rope, cordage and twine manufacturing division of The Hamilton Group Limited completed another successful year. Both sales and profits showed an increase over the previous year. However, Cancord is a relatively small operation.

Such products as awning and sash cords, rope and household twines can be found in your local hardware store under the Hercules brand name. Cords for drapes, vertical and Venetian blinds are other Cancord products often found in the home.

OUTLOOK

The outlook for the continued disposal of real estate assets and non-computer related business appears favourable under current market conditions.

The forecast for the next years growth in the computer business in Canada is modest due to the less than booming computer market place.

The outlook for the United States computer operations is far from clear. While the losses can be stopped, the future is clouded by the reorganization that is necessary at a time when the computer market in the United States is in recession.

Overall, the outlook is to return Hamilton Group to a profitable position in 1987.

EMPLOYEES

During the year W. J. Young was promoted to Senior Vice President in charge of computer sales and rental operations. P. L. Nielsen was appointed Vice President and General Manager of the Canadian computer operations.

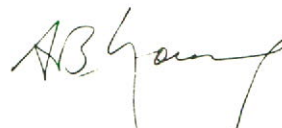
Our employees performed well during a busy and difficult year, and we must thank them for their continued support and dedication.

On behalf of the Board of Directors

August 15, 1986



W. H. Young, Chairman



A. B. Young, President

INTERIM REPORT TO SHAREHOLDERS - JULY 31, 1986

To the Shareholders:

The net loss after tax for the first quarter ended July 31, 1986 was \$178,504 (\$0.07 per share) compared to a net profit of \$139,093 (\$0.06 per share) for the same period of 1985. The net loss after an extraordinary gain of \$90,000 due to over-provision related to the disposal costs of the computer operations in Germany was \$88,504 (\$0.04 per share). In 1985 there was an extraordinary gain of \$5,586,573 from the sale of the Citibank Leasing Canada Limited shares so that net income a year ago was \$5,725,666 (\$2.34 per share).

The Company is continuing the implementation of its strategy of focusing on its core business of computer sales and rentals and the disposition of all non-related assets. This will lead to a much leaner management structure, tighter cost control, and an improved balance sheet.

A. B. Young has resigned as President of the Corporation. He will remain as a director and will be responsible for the disposition of non-operating assets. W. J. Young has been appointed President.

The annual report for 1986 and the information circular for the annual meeting are enclosed with this report. The annual meeting will be held at the Holiday Inn, Oakville at 4:30 p.m. on Thursday, October 16, 1986.

W. J. Young
President

THE HAMILTON GROUP LIMITED
CONSOLIDATED STATEMENT OF INCOME
THREE MONTHS ENDED JULY 31, 1986
(with comparative figures for 1985)

	<u>1986</u>	<u>1985</u>
Gross income	\$ 14,643,361	\$ 12,400,466
Income before the following	594,301	559,429
Investment income	218,706	241,678
Cost of borrowed money	813,007	801,107
	955,511	760,014
Income (loss) before income taxes and extraordinary items	(142,504)	41,093
Income taxes	(36,000)	98,000
Income (loss) before extraordinary items	(178,504)	139,093
Extraordinary items	90,000	5,586,573
Net income (loss)	\$(88,504)	\$ 5,725,666
Earnings per share (basic)		
Income (loss) before extraordinary items	\$ (0.07)	\$ 0.06
Net income (loss)	\$ (0.04)	\$ 2.34

THE HAMILTON GROUP LIMITED
CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
THREE MONTHS ENDED JULY 31, 1986
(with comparative figures for 1985)

	<u>1986</u>	<u>1985</u>
Funds provided from (used in) operations	\$(166,002)	\$ 2,512,769
Funds invested in operating assets		
Increase (decrease) in liabilities other than borrowings	(3,619,739)	2,546,499
Decrease (increase) in equipment for sale, rental or service	2,783,000	(3,219,263)
Decrease (increase) in accounts and notes receivable	3,242	(1,663,246)
Other assets	(58,308)	(273,165)
	<u>(891,805)</u>	<u>(2,609,175)</u>
Other assets and liabilities		
Assets in course of realization	(4,942)	45,321
Proceeds on sale of investments	101,560	14,500,000
Proceeds of debenture issue	-	10,000,000
Repayment of long-term debt	(209,062)	(5,542,284)
Decrease (increase) in investments and advances	-	(412,049)
Purchase of equipment and improvements	(20,744)	(111,169)
Other	-	(325,213)
	<u>(133,188)</u>	<u>18,154,606</u>
Decrease (increase) in short-term debt	\$(1,190,995)	\$ 18,058,200
Funds provided from (used in) operations per share, basic	\$ (0.07)	\$ 1.02

ANNUAL REPORT ON OPERATIONS

Gross income from computer sales and rentals increased from \$39,083,000 to \$58,218,000 — an increase of 49%. This increase was not reflected in operating profit due to problems with the business in the United States which are reported below. The operating profit before interest and taxes was reduced from \$3,488,000 for fiscal 1985 to \$627,000 for 1986. After interest, provision for taxes and extraordinary items, computer operations had a net loss of \$2,016,300. Assets employed in computer operations increased 11% to \$37,259,000 from \$33,541,000. In 1986 each dollar of assets generated \$1.56 of revenue compared to \$1.17 in 1985. This increasing efficiency in operations coupled with the steps taken to solve the problems with operations in the United States should mean much improved results for 1987.

The comprehensive data processing system continued its development and implementation on schedule. It is now a fully integrated system in Canada and is providing valuable timely and accurate information for both financial and control purposes. In the United States, the order entry, inventory and accounts receivable systems have been implemented successfully. By the mid-point of the present fiscal year the system will be fully integrated in the U.S. operations. As noted below, the implementation of this system defined many of the U.S. operations problems, and its success also provides optimism that the operations are now well controlled.

CANADA

HAMILTON COMPUTER SALES AND RENTALS (HCSR)

The Canadian operations enjoyed a very successful 1985/86. Revenue increased by 50% over the previous year while net operating income rose an even more impressive 70%. This was despite a year for the computer industry as a whole that was commonly referred to as a "slump".

A number of factors contributed to the success.

First of all, HCSR began to reap the benefits of all the work invested in the development of its management information system. Operating costs as a percentage of revenue were reduced significantly and the number of employees increased by only 10% despite the 50% increase in revenue. This trend of improved operating efficiencies is expected to continue throughout 1986/87.

Second, the geographic expansion into the Ottawa and Vancouver areas began to show profits in 1985/86. Most of the up front cost related to the start up of these branches was recognized in 1984/85, so both branches made significant contributions to the division's bottom line in the current year. Further geographic expansion is planned for late 1986/87.

Third, HCSR was able to take advantage of some of the new opportunities presenting themselves in the computer marketplace, particularly with respect to the sale of used equipment. There is an increasing demand for used microcomputer and related peripherals in Canadian corporations which HCSR is uniquely positioned to capitalize on because of its large pool of high quality rental equipment. This is another trend which can be expected to continue in 1986/87.

The outlook for HCSR remains positive despite the fact that the computer industry will likely be subject to increased pressure on margins and slower growth in 1986/87. HCSR's strategy of being a "one-stop shop" both in terms of its product line (i.e. anything from terminals to micros to minicomputers) and the financing alternatives offered (rent, purchase, or operating lease) has resulted in a loyal base of over 2,500 active customers. This, coupled with the efforts of the 115 highly motivated and dedicated employees, should result in a successful 1986/87.

U.S.A.

HGL SOFTWARE LIMITED

The results from HGL Software Limited have been very disappointing with substantial losses having been incurred in 1986. There were a number of reasons for this.

First, the company's principal business segment, minicomputers, was the hardest hit by the computer industry slump. As a result, sales remained flat for the year, while gross margins declined on all domestic business. Although the rental side of the business showed strong growth and solid gross margins, it was not enough to offset the decrease on the sales side.

Second, the implementation of the computerized management information system revealed serious control problems that existed under the previous manual system. As a result the company experienced significant write-offs of accounts receivable and inventory. The implementation of the new system, which has been successfully completed, will ensure that such losses will not recur.

Third, an infrastructure of costs was built based on the growth rates of previous years being maintained in 1986. Because of the industry slump, this growth did not occur. Operating costs, however, increased by 35% and as a result had a significant negative impact on the bottom line.

Management is working hard to correct the situation in the U.S. Personnel have been reduced by 35% in the last four months of 1986 which will reduce operating costs to fiscal 1985 levels. The successful implementation of the new management information system will allow HGL Software to benefit in 1987 from the same operating efficiencies Hamilton Computer Sales and Rentals experienced in 1986. A strong focus has been placed on asset control whereby inventory levels and accounts receivable have been significantly reduced. All these actions will dramatically improve the results in 1987.

Furthermore, in order to increase the focus on domestic operations, management has decided to withdraw from operating a China export company. China is a very difficult market to compete in, particularly at present with the uncertain foreign

exchange situation. The amount of time management had to devote to managing this operation detracted significantly from its ability to resolve its domestic problems. We will continue to participate in the China market by being a source of supply for equipment for any future sales.

Redwood Technology Inc. is the company that is developing and marketing the VOX office automation software in the United States that will operate on the Digital Equipment Corporation VAX series of minicomputers. Sales of the VOX software have not achieved the volume anticipated and therefore Hamilton Group has written off its investment in this company. Recent developments and the general increasing interest in office automation raise some hope that VOX products may prove moderately successful.

A plan has been implemented to restore the United States operations to at least break even level by October, failing which other measures will be taken to stop their negative impact on Hamilton Group's financial results.

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of The Hamilton Group Limited as at April 30, 1986 and the consolidated statements of income, retained earnings (deficit), contributed surplus 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 April 30, 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.

Hamilton, Canada
July 15, 1986

Peat, Marwick, Mitchell & Co.

Chartered Accountants

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEET

April 30, 1986

with comparative figures for 1985

	ASSETS	
	1986	1985
Operating assets:		
Cash and short-term deposits	\$ 65,000	419,000
Equipment for sale or rental (notes 2 & 15(a))	25,393,300	22,785,450
Accounts and notes receivable	10,226,463	10,290,845
Other	1,358,257	1,339,010
	<u>37,043,020</u>	<u>34,834,305</u>
Other assets:		
Assets in course of realization	951,248	1,046,287
Investments and advances, at equity (note 3)	5,989,071	15,460,172
Assets relating to Mexican subsidiaries (note 4)	4,600,000	10,479,560
Equipment and leasehold improvements (notes 5 & 15(a)) ..	2,566,226	1,396,959
Deferred income taxes	1,755,705	589,705
Other	162,043	207,318
	<u>16,024,293</u>	<u>29,180,001</u>
	<u><u>\$53,067,313</u></u>	<u><u>64,014,306</u></u>

LIABILITIES AND SHAREHOLDERS' EQUITY

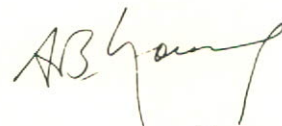
	1986	1985
Liabilities:		
Short-term bank debt (note 6)	\$13,359,005	28,694,000
Accounts payable and accrued liabilities	10,338,484	7,967,009
Income tax payable	2,062,000	—
Deferred revenue	1,808,000	1,053,300
Long-term bank debt (note 7)	992,010	8,205,749
Obligations under capital leases (note 15(a))	5,337,200	1,910,472
12% convertible subordinated debentures (note 8)	10,000,000	—
Deferred foreign exchange	104,600	353,600
	<u>44,001,299</u>	<u>48,184,130</u>
Shareholders' equity:		
Capital stock (note 9)	10,242,193	10,199,500
Retained earnings (deficit)	(1,337,179)	5,073,949
Foreign exchange translation adjustment	161,000	216,000
Contributed surplus	—	340,727
	<u>9,066,014</u>	<u>15,830,176</u>
Total shareholders' equity	9,066,014	15,830,176
Commitments and contingent liability (note 15)		
	<u>\$53,067,313</u>	<u>64,014,306</u>

See accompanying notes to consolidated financial statements.

On behalf of the Board:



Director



Director

CONSOLIDATED STATEMENT OF INCOME
Year ended April 30, 1986
with comparative figures for 1985

	1986	1985
Gross income (note 10)	\$61,136,522	41,628,170
Income before the following	\$ 1,095,630	3,063,725
Income from investments:		
Citibank companies (note 3(a))	—	2,700,000
Other	518,119	880,877
	518,119	3,580,877
	1,613,749	6,644,602
Cost of borrowed money including \$1,491,508 (1985; \$325,615) on indebtedness initially incurred for a term exceeding one year	3,100,603	3,632,918
Income (loss) before income taxes and extraordinary items	(1,486,854)	3,011,684
Income taxes (note 11)	(1,002,000)	240,000
Income (loss) before extraordinary items	(2,488,854)	3,251,684
Extraordinary items (note 12)	(4,274,421)	223,110
Net income (loss)	\$ (6,763,275)	3,474,794
Earnings (loss) per share (note 13):		
Income (loss) before extraordinary items	\$ (1.02)	1.33
Net income (loss)	\$ (2.76)	1.42

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF RETAINED EARNINGS (DEFICIT)
Year ended April 30, 1986
with comparative figures for 1985

	1986	1985
Retained earnings at beginning of year	\$ 5,073,949	1,849,838
Net income (loss)	(6,763,275)	3,474,794
Amortization and realization of excess of appraised value of property over cost	—	275,110
Transfer from contributed surplus	352,147	—
	(1,337,179)	5,599,742
Stock dividends	—	(525,793)
Retained earnings (deficit) at end of year	<u>\$ (1,337,179)</u>	<u>5,073,949</u>

CONSOLIDATED STATEMENT OF CONTRIBUTED SURPLUS
Year ended April 30, 1986
with comparative figures for 1985

	1986	1985
Amount at beginning of year	\$ 340,727	332,967
Discount on redemption of preferred shares of a subsidiary	11,420	7,760
Transfer to retained earnings	(352,147)	—
Amount at end of year	<u>\$ —</u>	<u>340,727</u>

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
Year ended April 30, 1986
with comparative figures for 1985

	1986	1985
Operations:		
Income (loss) before extraordinary items	\$ (2,488,854)	3,251,684
Add (deduct) items not affecting funds:		
Depreciation and amortization, net of recoveries on sales of \$2,927,087 (1985; \$1,760,545)	3,047,240	2,986,574
Equity income from investments, less cash dividends received	129,459	(1,628,393)
Deferred income taxes	1,002,000	(240,000)
Other	(136,512)	427,000
Funds provided from operations	1,553,333	4,796,865
Operating assets and liabilities:		
Increase in liabilities other than borrowings	6,504,779	1,669,148
Increase in equipment for sale or rental	(5,134,163)	(8,932,939)
Decrease (increase) in accounts and notes receivable	64,382	(4,473,237)
Other assets	(19,247)	(249,605)
Funds realized from (invested in) net operating assets	1,415,751	(11,986,633)
Other:		
Assets in course of realization	231,551	(664,247)
Proceeds of debenture issue	10,000,000	—
Proceeds on sale of investments	17,400,000	2,100,559
Decrease (increase) in investments and advances	(543,823)	2,474,375
Assets relating to Mexican subsidiaries	(6,204,852)	(16,125,960)
Purchases of equipment and leasehold improvements	(1,676,202)	(815,805)
Proceeds (repayment) of long-term bank debt	(7,213,739)	8,205,749
Other	18,976	182,966
	12,011,911	(4,642,363)
Decrease (increase) in short-term bank debt, net of change in cash and short-term deposits	\$14,980,995	(11,832,131)
Funds provided from operations, per share (basic)	\$ 0.63	1.96

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

April 30, 1986

The company, incorporated under the Canada Business Corporations Act, carries on the business of computer equipment sales and rental operations through its subsidiaries and associates in Canada, United States, Europe and Hong Kong.

1. Summary of significant accounting policies:

(a) Basis of presentation:

The consolidated financial statements include the accounts of the company and all subsidiaries except the Mexican subsidiaries (note 4). All material intercompany balances and transactions have been eliminated. Certain accounts of the previous year have been reclassified to conform with the current year's presentation.

Effective April 25, 1986, the company sold its investment in a wholly-owned subsidiary, Charter Credit Corporation, to a company in which it holds a 35% equity interest. Accordingly, income from investments includes a 100% equity interest in the results of operations of the former subsidiary to the date of sale and a 35% interest thereafter. For comparative purposes, the 1985 consolidated financial statements have been restated to account for the company's investment in its former subsidiary on the equity basis.

(b) Currency translation:

The consolidated financial statements are stated in Canadian dollars. Monetary items denominated in a foreign currency are translated at the rates of exchange in effect at the year-end. Non-monetary and operating items are translated at the rates of exchange in effect when the transactions occurred. Unrealized exchange gains or losses related to monetary items having a fixed or ascertainable life extending beyond the end of the subsequent fiscal year are included in the deferred foreign exchange account in the Consolidated Balance Sheet and amortized over the remaining life of the related monetary item. Other foreign currency translation gains or losses are included in the current year's income.

For purposes of preparing consolidated financial statements, accounts of foreign subsidiaries and affiliates are translated to Canadian dollars using the current rate method. Unrealized gains or losses on these translations are deferred until realized.

(c) Depreciation and amortization:

Depreciation is provided on equipment and rental property, and amortization on leasehold improvements, generally on a straight-line basis, at annual rates which are designed to write off the assets over their estimated useful life.

Depreciation is provided on equipment for rental at annual rates ranging from 16-2/3% to 33-1/3%. In addition, the carrying value of specific equipment, for which technological change or other factors reduce the originally estimated useful life, is written down to current estimated net realizable value.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
April 30, 1986

2. Equipment for sale or rental:	1986	1985
Equipment for rental, at cost.	\$29,023,600	23,418,410
Less accumulated depreciation.	9,997,800	7,471,487
	19,025,800	15,946,923
Equipment for sale, at cost.	6,367,500	6,838,527
	<u>\$25,393,300</u>	<u>22,785,450</u>
	1986	1985
3. Investments and advances, at equity:		
Hamilton Rentals Limited.	\$ 3,569,168	4,301,128
International Mercantile Factors Ltd.	2,406,798	2,144,520
Citibank Leasing Canada Limited and Citibank Factoring Canada Limited.	—	7,613,427
Charter Credit Corporation.	—	1,401,097
Other.	13,105	—
	<u>\$ 5,989,071</u>	<u>15,460,172</u>

- (a) Effective May 15, 1985, the company sold its 40% interest in the common shares of Citibank Leasing Canada Limited and Citibank Factoring Canada Limited under the terms of an agreement entered into on September 7, 1984. Cash proceeds amounted to \$17,000,000 resulting in a gain on disposal of \$5,586,573, after provision for income taxes of \$2,800,000 (note 12).
- (b) Effective April 25, 1986, the company sold its investment in its wholly-owned subsidiary, Charter Credit Corporation, for cash consideration of \$1,400,000, to a 35% owned affiliate. As a result of the sale, the company realized a gain of \$205,018, including recovery of income taxes of \$250,000 (note 12).

The company's share of the current year's net income (loss) of Charter Credit Corporation amounted to \$(15,659) (1985; \$157,158).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

April 30, 1986

4. Assets relating to Mexican subsidiaries:

Mexican regulations require the Company to sell a majority interest in Impulsora Mexicana de Arrendamiento, S.A. (IMEXA) to Mexican Nationals. The Company is proceeding with a plan to dispose of this subsidiary and is seeking a Mexican purchaser at this time.

Because of this requirement for disposal, the accounts of IMEXA are excluded from the consolidated financial statements and the Mexican assets are carried at \$4,600,000, which represents management's estimate of their net realizable value.

In recent months, the substantial fall in world oil prices has had a drastic impact on the Mexican economy, already weakened by its huge international debt. The inability of the Mexican authorities to reorganize their foreign debt commitments has caused further devaluation of the Mexican peso, and has heightened concern over the Bank of Mexico's ability to repay foreign debt. Tight money policies to control hyperinflation have caused further difficulties in obtaining operating credit lines to support growth of the Mexican subsidiary's operations.

These factors have increased the uncertainty as to the overall value of the company's assets in Mexico, and have led to management's decision to substantially increase the provision for losses on disposal of the Mexican assets.

The company's plan of disposal required completion of certain steps in order to strengthen IMEXA and improve its saleability:

- (a) During fiscal 1985, the company paid \$8,000,000 U.S. to acquire a Canadian bank's \$8,000,000 U.S. receivable, bearing interest at the London Interbank Offering Rate (LIBOR), from FICORCA, established to control payment of private sector foreign currency debt outside Mexico. This amount is repayable by the Trust to the company via the Canadian bank in installments from 1988 to 1992. Of the \$8,000,000 U.S., the repayment of \$5,300,000 U.S. is contingent on IMEXA fulfilling its obligation to make scheduled principal payments and pay interest at peso borrowing rates on a peso loan equivalent to \$5,300,000 U.S. at 1983 exchange rates. The repayment of the remaining \$2,700,000 U.S. is not subject to the fulfillment of any further obligations by the company or its subsidiaries.
- (b) In October 1985, IMEXA obtained final government approval to complete the merger, commenced in May 1983, with a subsidiary company and the company invested \$7,750,000 U.S. in the merged company to strengthen its capital base for purposes of disposal. IMEXA applied these funds to repay its remaining foreign debt, and to repay \$200,000 U.S. of its \$450,000 U.S. debt to the company. As the merged Mexican company is an auxiliary credit institution, the Banking Commission required it to divest certain assets which were sold to the company for \$250,000 U.S. These funds were then applied to retire its remaining debt to the company.

The assets and provision for losses relating to the company's Mexican subsidiaries are as follows:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
April 30, 1986

	1986	1985
Amounts bearing interest at LIBOR:		
Bank of Mexico trust (Ficorca plan) —		
\$8,000,000 U.S. repayable in the amount of		
\$500,000 U.S. in 1988; \$2,000,000 U.S. in each		
of 1989, 1990 and 1991; and \$1,500,000 U.S. in 1992 ...	\$10,679,000	10,928,000
\$450,000 U.S. repayable on demand.....	—	594,810
	10,679,000	11,522,810
Advances to Canadian banks on behalf of Mexican		
subsidiaries — \$3,750,000 U.S.	—	4,956,750
Share purchase — \$7,750,000 U.S.	10,423,565	—
Interest paid on behalf of IMEXA — \$528,000 U.S.	726,900	—
Other — \$430,000 U.S.	605,947	—
	22,435,412	16,479,560
Less provision for losses.....	17,835,412	6,000,000
	<u>\$ 4,600,000</u>	<u>10,479,560</u>
5. Equipment and leasehold improvements:	1986	1985
Equipment.....	\$ 3,074,643	1,577,039
Leasehold improvements	648,200	555,490
	3,722,843	2,132,529
Less accumulated depreciation and amortization	1,156,617	735,570
	<u>\$ 2,566,226</u>	<u>1,396,959</u>

6. Short-term bank debt:

As security for short-term bank debt, the company has pledged its shares of its subsidiaries and other investments and has given a demand debenture as collateral for a floating charge on all of the assets and undertakings of the company and its consolidated subsidiaries as well as a fixed charge on its real property in Canada. The company has also provided a general assignment of accounts receivable, an assignment of equipment for sale or rental, and a general security agreement of the company and its consolidated subsidiaries. Dividend payments are subject to bank approval.

At April 30, 1986, the company is not in compliance with some of the terms of the lending agreement with its bankers. The banks are in the process of conducting their normal annual review and management does not anticipate adverse results.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
April 30, 1986

7. Long-term bank debt:

The long-term bank debt bears interest at bank prime rate plus 1.5%, and is subject to the same security and other provisions as for the short-term debt (note 6).

The debt is repayable by monthly principal payments of \$35,833, a principal payment of \$360,000 on July 31, 1986 and periodic payments of proceeds of sale of assets in course of realization, and other non-operating assets.

8. 12% convertible subordinated debentures:

During the year, the company issued by private placement, \$10,000,000 principal amount of 12% convertible, redeemable, subordinated debentures, maturing May 16, 1995. The debentures are convertible into Class A shares of the company at \$9.50 per share, until maturity. Full conversion of these debentures would result in the issuance by the company of 1,052,631 additional Class A shares.

The debentures are redeemable by the company from May 16, 1988 to May 15, 1990 at a price of \$107.50 for each \$100 of principal, provided that the trading price of the company's Class A shares meets certain criteria. Thereafter, the debentures are redeemable at prices declining from \$104.50 for each \$100 of principal, to par at maturity. Commencing on May 16, 1988, the company is required to make all reasonable efforts to redeem \$50,000 of debentures per quarter, at the lesser of par and the current market price.

9. Capital stock:

(a) The capital stock is comprised of Class A and Class B shares without par value. The Class A and Class B shares are fully voting and are convertible into each other on a one-for-one basis. Class B shareholders receive a stock dividend equivalent to Class A cash dividends.

(b) Summary of changes in shares and stated value:

	Class A Shares	Class B Shares	Stated Value
Balance beginning of year	2,429,916	21,323	\$10,199,500
Shares converted during the year	1,413	(1,413)	—
Shares issued under 1985 employee share purchase plan	7,298	—	42,693
Balance end of year	<u>2,438,627</u>	<u>19,910</u>	<u>\$10,242,193</u>

An amount of \$92,087 is receivable from employees for shares issued under the company's previous Stock Purchase Plan.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
April 30, 1986

(c) 1985 Employee Share Purchase Plan:

In 1985, the company established an Employee Share Purchase Plan to provide eligible employees with the opportunity to purchase shares annually through a payroll deduction plan. The plan provides for employees to contribute up to 5% of their annual earnings to purchase stock from treasury.

A total of 50,000 Class A convertible shares were reserved for the Plan of which 7,298 shares have been issued to date.

(d) Stock Option Plan:

During the year, the Company established a Stock Option Plan to provide eligible employees with the option to purchase shares at a price equal to the current market price of the shares on the date of the grant.

A total of 190,000 Class A convertible shares were reserved for the Plan. On October 24, 1985, options for 38,000 shares were granted at a price of \$6.33 per share. The option expires October 23, 1990 and no shares have been issued to date under the Plan.

(e) Share exchange agreement:

Under a share exchange agreement entered into in 1984 between the company and the other shareholders of Hamilton Rentals Limited which acquired the company's former European subsidiaries, the other shareholders have the right, commencing July 31, 1986 through July 31, 1991, to exchange their shares for Class A shares of the company. The rate of exchange is 3.25 Hamilton Rentals Limited shares for one Class A share of the company or for equivalent cash at the date of exercise, at the company's option for certain shareholders. Full exercise of these options would result in the issuance by the company of 598,461 additional Class A shares.

10. Segmented information:

The directors have determined that the company is an investment holding company with the operations of its consolidated subsidiaries classified into one business segment of computer equipment sales and rental.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
April 30, 1986

A summary of the geographic segments of the company is as follows:

1986	Canada	United States	Other	Eliminations	Consolidated
Gross income, third parties.....	\$39,833,522	18,578,000	2,725,000	—	61,136,522
Transfers between geographic segments.....	372,109	—	—	(372,109)	—
Gross income.....	<u>\$40,205,631</u>	<u>18,578,000</u>	<u>2,725,000</u>	<u>(372,109)</u>	<u>61,136,522</u>
Segment income.....	<u>\$ 3,706,790</u>	<u>(2,903,000)</u>	<u>(14,000)</u>		789,790
Add net corporate expenses allocated to segments.....					305,840
Income before the following, per Consolidated Statement of Income.....					<u>\$ 1,095,630</u>
Identifiable assets.....	<u>\$44,208,206</u>	<u>14,307,000</u>	<u>2,265,000</u>	<u>(7,712,893)</u>	<u>\$53,067,313</u>

1985	Canada	United States		Eliminations	Consolidated
Gross income, third parties.....	\$27,156,170	14,472,000		—	41,628,170
Transfers between geographic segments.....	299,677	—		(299,677)	—
Gross income.....	<u>\$27,455,847</u>	<u>14,472,000</u>		<u>(299,677)</u>	<u>41,628,170</u>
Segment income.....	<u>\$ 2,790,745</u>	<u>870,000</u>			3,660,745
Less net corporate expenses not allocated to segments.....					(597,020)
Income before the following, per Consolidated Statement of Income.....					<u>\$ 3,063,725</u>
Identifiable assets.....	<u>\$58,490,849</u>	<u>12,101,000</u>		<u>(6,577,543)</u>	<u>\$64,014,306</u>

11. Income taxes:

A reconciliation comparing the expected income tax rate and the effective income tax rate is as follows:

	1986	1985
Basic Canadian Federal income tax rate.....	46.0%	46.0
Non-taxable investment income.....	16.4	(51.0)
Losses of U.S. subsidiary not tax effected.....	(113.1)	—
Provincial tax.....	(7.2)	—
Other.....	(9.5)	(3.0)
Effective income tax rate.....	<u>(67.4)%</u>	<u>(8.0)</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
April 30, 1986

The U.S. subsidiary has income tax losses for accounting purposes, aggregating approximately \$3,668,000, which are available to reduce income for tax in future years to 2001.

In addition, this subsidiary has investment tax credits aggregating approximately \$980,000 which are available to reduce income taxes payable for future years and expire in various years from 1997 to 2001.

12. Extraordinary items:	1986	1985
Gain on sale of Citibank Leasing Canada Limited and Citibank Factoring Canada Limited, net of provision for income taxes of \$2,800,000 (note 3(a))	\$ 5,586,573	—
Gain on sale of Charter Credit Corporation including recovery of deferred income taxes of \$250,000 (note 3(b))	205,018	—
Write down of assets relating to Mexican subsidiaries to estimated net realizable value, after recovery of deferred income taxes of \$2,656,000 (note 4)	(9,179,412)	—
Investment in Redwood Technology Inc. written off	(571,000)	—
Gain on sale of Torham Packaging Inc., after provision for deferred income taxes of \$250,000	—	129,110
Reduction of income taxes of Charter Credit Corporation due to application of prior years' losses	—	94,000
Proportionate share of provision by Hamilton Rentals Limited for estimated loss on disposal of subsidiary in Europe	(250,000)	—
Proportionate share of goodwill written off by International Mercantile Factors Ltd.	(65,600)	—
	<u>\$ (4,274,421)</u>	<u>223,110</u>

13. Earnings (loss) per share:
Earnings (loss) per share is calculated on the basis of the weighted average number of shares outstanding during the year. The shares under option referred to in notes 8 and 9 would have an anti-dilutive effect on the current year's loss per share.

14. Transactions with related parties:

The company entered into transactions with related parties in the normal course of business as follows:

	1986	1985
Management fees charged to associated companies	\$ 17,900	430,000
Interest charged to associated companies	\$ 120,000	120,000

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
April 30, 1986

15. Commitments and contingent liability:

(a) Lease commitments:

The following is a summary of assets acquired under capital leases:

	1986			1985
	Cost	Accumulated depreciation	Net book value	Net book value
Equipment for sale, rental or service.....	<u>\$ 4,246,300</u>	<u>620,400</u>	<u>3,625,900</u>	<u>1,240,862</u>
Equipment and leasehold improvements.....	<u>\$ 1,580,700</u>	<u>240,600</u>	<u>1,340,100</u>	<u>476,216</u>

The aggregate minimum capital lease payments are as follows:

1987	\$ 3,007,534
1988	1,241,967
1989	1,069,679
1990	863,167
1991	176,585
	<u>6,358,932</u>
Less amount representing interest, at annual rates from 11.5% to 13.75%	<u>1,021,732</u>
Balance of obligations under capital leases	<u>\$ 5,337,200</u>

In addition, the company has commitments under operating leases for premises and the aggregate minimum amount that will be incurred as annual rental is as follows:

1987	\$ 806,138
1988	748,449
1989	715,383
1990	565,294
1991	<u>93,142</u>

(b) Contingent liability:

Under the terms of the agreement for the sale of its investment in Charter Credit Corporation, to a 35% owned affiliate, the company has undertaken to absorb any shortfalls incurred to April 25, 1996 on the sale of specified assets at prices lower than stipulated amounts. The company has guaranteed minimum proceeds on assets having an agreed aggregate minimum value of \$2,796,000. This amount includes \$2,400,000 for one property on which the company participates in any net proceeds realized in excess of \$3,000,000.

PRINCIPAL COMPUTER OPERATING UNITS

HAMILTON COMPUTER SALES AND RENTALS

— Canada

Division of The Hamilton Group Limited

415 Horner Avenue, Toronto, Ontario

Branches: Montreal, Downtown Toronto, Ottawa, Calgary, Vancouver

P. L. Nielsen, General Manager of HAMILTON Computer Sales and Rentals and Vice President of The Hamilton Group Limited

G. Care, National Sales and Marketing Manager — Systems Products

R. Boulet, National Sales and Marketing Manager — Distribution Products

S. Meadley, Controller

Sells, rents and services computer hardware and software products. Operates retail computer sales store under the name HAMILTON Computer Business Center.

Principal suppliers — Calcomp, Compaq, Digital, Epson, Hewlett-Packard, IBM and Tektronix.

HGL SOFTWARE LIMITED — U.S.A.

100% owned subsidiary of The Hamilton Group Limited

6 Pearl Court, Allendale, New Jersey, U.S.A.

Branch: Dallas, Texas

G. Brown, President of HGL Software Limited and Vice President of The Hamilton Group Limited

H. Ungemach, Operations Manager

Sells, rents and services computer hardware and software products

Principal suppliers — Data General, Digital, Gould and Tektronix.

HAMILTON RENTALS LIMITED — Europe

35.1% owned affiliate of The Hamilton Group Limited. Under certain provisions for exchange of common shares, could become a 100% owned subsidiary.

Hamilton House, North Circular Road, London, England

Subsidiaries: France, Germany, Holland.

D. M. Young, Chairman

R. West, Managing Director

M. Bramley, Secretary and Finance Director

Sells, rents and services computer hardware and software products.

France in addition operates a division which sells, rents and services technical test and measurement equipment.

Principal suppliers — Digital, Hewlett-Packard, IBM, Satelcom and Tektronix.

REDWOOD TECHNOLOGY GROUP INC. — U.S.A.

20% owned affiliate of The Hamilton Group Limited

170 Aquidneck Avenue, Middletown, Rhode Island, U.S.A.

W. Reidy, President

Develops, sells and services VOX software products for office automation.

