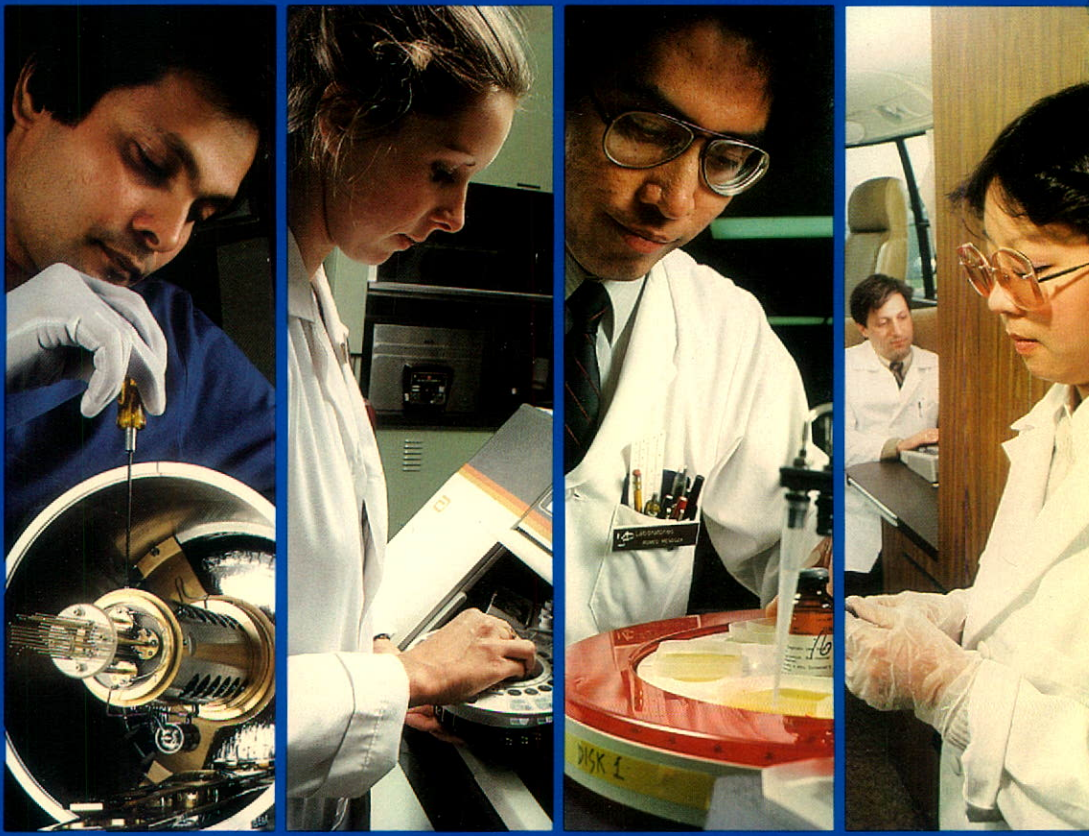
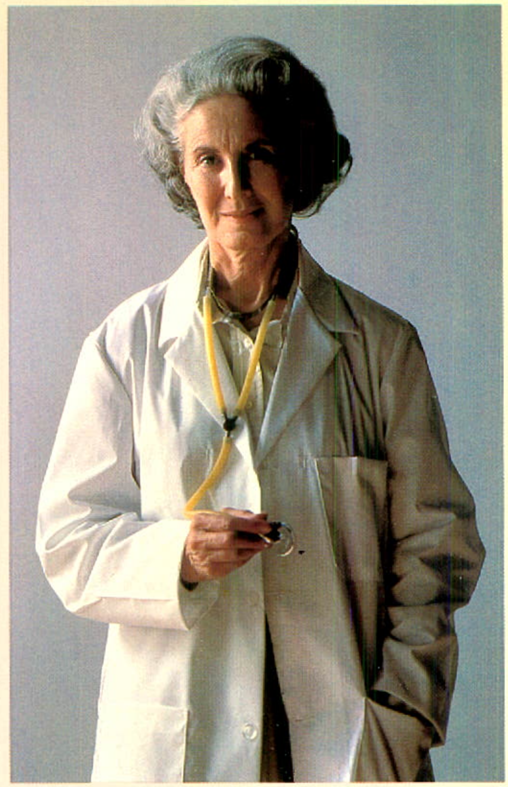
MDS Health Group Limited

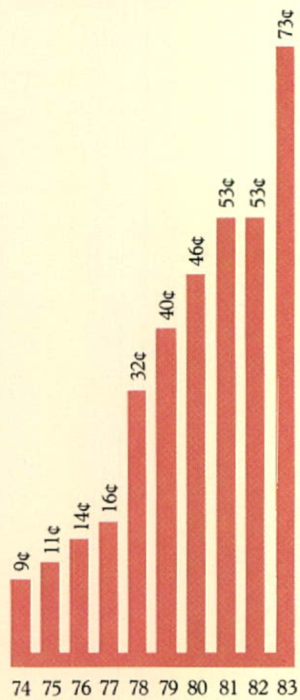
Annual Report 1983



MDS
Dedicated to excellence in quality and service.

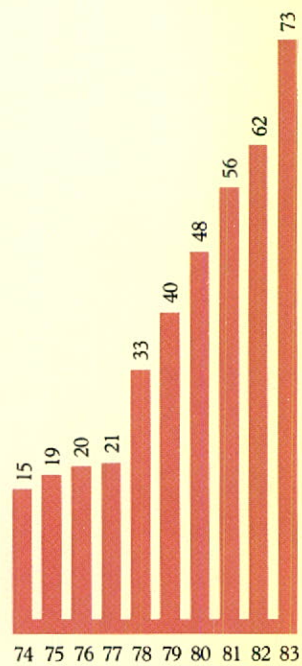


Earnings per share*
(Class A Common and
Class B Non-Voting shares)



*Reflects share split in
July, 1983 and September, 1980

Revenues in millions



MDS Health Group Limited

Profile

MDS is a professionally directed technology-based company providing health related testing and measurement services and systems for physicians, hospitals, nursing homes, industry and government. MDS activities are organized into four operating divisions: Clinical Laboratories, SCIEX, Health Care Services and Tomatis. A network of 135 laboratories and specimen collection centres in Canada and the United States is the principal contributor to the company's revenues and profits.

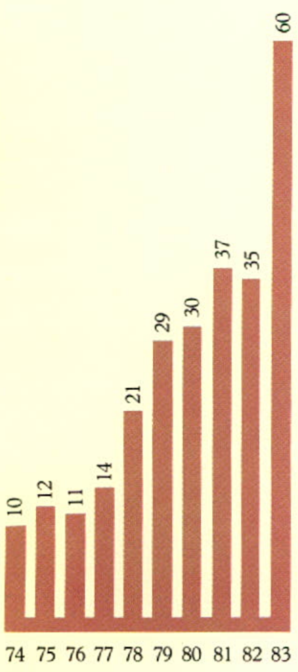
The Class A Common and Class B Non-Voting shares trade on The Toronto Stock Exchange under the symbols MHG.A and MHG.B. Employees, through the Deferred Profit Sharing Plan, represent the largest shareholder in MDS Health Group Limited with a voting interest represented by approximately 26% of the outstanding Class A Common shares.

Strategy for the mid-eighties

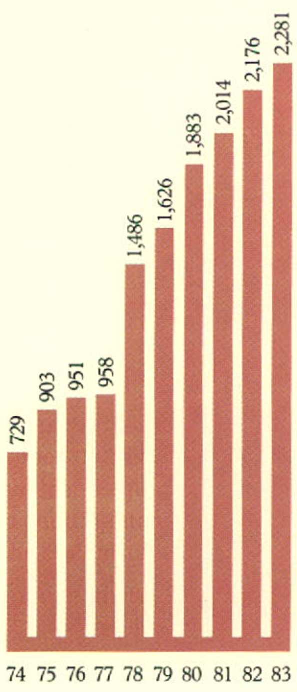
MDS is a customer driven company whose objective is to be a leader in any market segment in which it is active. Fundamental to its overall strategy is a commitment to excellence in quality and service. The company believes this can only be achieved by hiring and retaining good people and by providing a participative working climate that fosters teamwork, rewards innovation and encourages exceptional performance.

Overall growth is based primarily on internal business development activities, but is complemented with strategic acquisitions. MDS will continue to seek out and develop new products and services which fit with its existing businesses and are responsive to its existing markets.

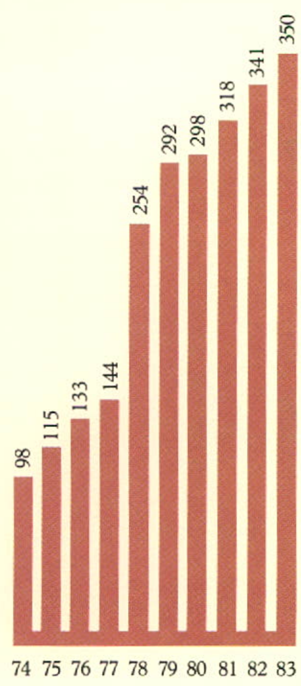
Total assets in millions



Total employees
(includes part-time employees)



Total square footage of facilities occupied
(thousands of square feet)



Research and development
(expenditures in $ thousands*)

*estimated

**SCIEX acquired in 1982

HOWARD ROSS LIBRARY
OF MANAGEMENT
JUL 29 1986
McGILL UNIVERSITY

Report to Shareholders

The year ended October 31, 1983 was a rewarding one for MDS, as record levels in revenues and earnings were reached for the thirteenth consecutive year.

Revenues increased by 18% to $73 million and generated net after-tax earnings of $5.1 million. Earnings per share for the year were 73¢ versus 53¢ in the previous year. The earnings per share figure reflects the issue of 600,000 Class B Non-Voting shares in March, 1983 and the split of the outstanding Class A Common and Class B Non-Voting shares on a 2 for 1 basis in July, 1983.

The improvement in earnings is attributed to higher revenues in the principal service–clinical laboratory testing–and improved operating margins in the other divisions.

Financial Condition

During the year the company's working capital position increased to $27 million (including cash and marketable securities of $23 million) as compared with $13 million at the end of the previous fiscal period. A significant part of the increase results from the $12.3 million of equity raised through the private placement of the Class B Non-Voting shares.

The purpose of this financing was to provide funds for continuing growth through internal development and acquisitions. Subsequent to year end, the company acquired a small mobile diagnostic X-ray company in Ontario and the operations of two clinical laboratory companies in Michigan, with combined revenues of $8 million. Negotiations are proceeding with several additional strategic acquisition prospects and it is hoped that one or more of these negotiations will be completed in fiscal 1984.

Operating Highlights

Clinical Laboratories

The Ontario laboratory operation continued its volume growth during fiscal 1983. Testing volumes increased at a rate higher than the previous year

Financial Highlights

Year ending October 31	**1983**	1982
Net revenues	**$72,699,000**	$61,722,000
Net earnings	**5,142,000**	3,405,000
Shareholders' equity	**34,557,000**	17,814,000
Total assets employed	**60,133,000**	35,094,000
Debt as a percentage of capital employed	**24%**	37%
Current ratio	**2.9:1**	3.0:1

and demand was strong in all regions. A particularly disappointing development during the year was the application of the Ontario Government's Inflation Restraint Act to all licensed laboratories. The agreed upon 6% fee increase to be effective April 1, 1983 was rescinded. Negotiations are proceeding with the government for a mutually acceptable fee increase under the Act which could be retroactive to April 1, 1983.

In anticipation of continued strong growth in demand for its laboratory testing services and as part of its commitment to high quality, the company commenced construction of a new Toronto regional laboratory facility. The new building located close to the company's current head office ultimately will provide MDS with a fully computerized reference facility capable of handling greatly expanded reference testing for the company's laboratory network and other private laboratories and hospital laboratories. Completion is scheduled for March, 1984.

United States laboratory revenues increased 15% over the previous period and though pre-tax profits were better than the previous period, they were still less than planned. Next year this group will continue to focus on improving profit margins. The acquisition in December, 1983 of Genessee Clinical Laboratories in Flint, Michigan and the signing of a management contract with Chelsea Medical Laboratories will provide the division with a strong base for growth in a new geographical area. Strategically, through the Chelsea agreement, the company enters the business of managing U.S. hospital laboratories—a significant new area of growth under the recently introduced medicare reimbursement system which encourages hospitals to use outside services to reduce costs.

SCIEX

Fiscal 1983 represented a year of significant progress for SCIEX which is involved in the design, manufacture and marketing of equipment for trace chemical analysis. Revenues for the year were 45% higher than the previous fiscal period and gross operating profit exceeded plan. In fiscal 1983 SCIEX introduced the ELAN, a new product concept for the detection and identification of minute traces of elements and their isotopes in a wide variety of substances. This new product has significant advantages over existing elemental analyzers and has generated considerable interest in the international scientific and service communities. First deliveries of the ELAN will take place in the Spring of 1984. The estimated market potential for the ELAN type of analyzer is projected to exceed $60 million by 1988 and SCIEX expects to be a leader in this market segment. Subsequent to year-end the Federal Government signed a $1.6 million contract for the development and supply of ELAN systems to various government departments.

During the year the TAGA 6000 trace organic analyzer was enhanced with an extension of its analysis range and with the incorporation of a higher proportion of SCIEX exclusive components (85%). The impressive list of TAGA purchasers continued to grow and more significantly, some customers ordered a second system. In July, 1983, a new company, in which MDS has a beneficial interest, acquired two mobile TAGA systems from SCIEX and is using these systems to provide analytical testing services to industry and government both in Canada and the United States. The exposure of TAGA's capabilities through this new association should play an important role in producing future orders for TAGA systems.

Health Care Services

MDS Health Care Services achieved record revenues and earnings for the third consecutive year. Paramedical services for the insurance industry were extended with the opening of an Eastern Ontario regional office in Ottawa and services were also expanded to include physician and ECG services on a mobile basis. The occupational health activities of the division were also extended with the inauguration of in-plant, mobile physician and paramedical services.

Tomatis Division

The Tomatis Division continued to experience less than acceptable financial results during the last fiscal period. This was particularly disappointing in light of the continued demonstration of the value of the program. This division provides Listening Training Programs for individuals who have an auditory processing problem—a learning disability. Several school boards implemented pilot projects for the Listening Training Program during the last fiscal period and achieved positive results. Hopefully this further confirmation of the program's effectiveness will broaden acceptance which is necessary for the program to become financially viable.

Future Outlook

MDS is positioned for a new period of substantial growth which should be reflected in fiscal 1984. Emphasis will continue on the building of its base laboratory business in Canada and the United States. New internal growth opportunities in providing mobile testing services to the clinical, environmental and occupational health markets should materialize before the end of the next fiscal period. Significant increases are also expected in the demand for SCIEX products and analytical testing services.

Appreciation

On behalf of the Board of Directors, I thank all our employees and professional consultants for their efforts during the last year. We are proud of our MDS team of people and their dedication to excellence. Their efforts made possible the high quality of MDS services and products and the successful results of the last year. A special note of appreciation to our clients for their continued support and for their commitment to working with us to build a better and healthier world.

W. G. Lewitt
President
January 12, 1984

Divisional Overview

MDS Today

Approximately 2,300 people including full-time and part-time employees and consultants were employed by MDS as of October 31, 1983.

MDS offices, laboratories and facilities are located in 76 Canadian and U.S. communities and these facilities occupy a total of 350,000 square feet of space.

MDS services and products are represented by four divisions and a brief overview of these divisions follows.

Clinical Laboratories

MDS Laboratories provide clinical diagnostic services to approximately 2.7 million people each year through a network of 135 laboratories and specimen collection centres located in Ontario and in the tri-state area of New York, New Jersey, and Pennsylvania. More than 500 individual laboratory tests are offered by the MDS laboratory network, as well as supportive ECG, X-ray and pulmonary function diagnostic procedures. These services—more than 40,000 procedures per day—are provided to a client base of 7,000 physicians, 300 hospitals and 400 nursing homes and in some cases are provided on a mobile basis for house-bound or bedridden patients. The laboratories are the largest division of MDS, constituting a major portion of the company's revenues.

The carefully controlled environment of a fixed site laboratory is a familiar setting for many health related biomeasurements. A laboratory analyst and industrial hygienist are shown discussing findings which could impact on the well-being of people and the management of manufacturing processes many hundreds of miles away.

In contrast, the situations depicted in the remaining photographs show that when it is more useful and appropriate, the technology can be taken directly into the plant, the office, the home, or in the case of the Tomatis Electronic Ear—the schoolroom.

SCIEX

SCIEX* is involved in the design, manufacture and marketing of mass spectrometer systems for the detection of trace amounts of organic and inorganic substances.

TAGA* systems have a wide range of applications for the identification of trace amounts of organic contaminants in the environment, in the workplace or in industrial processes and products. The rugged and flexible nature of these systems allows them to be used either in a fixed laboratory facility or in the field in a mobile van.

The ELAN* system is a new product for the measurement of trace quantities of elements. The superior detection levels of the ELAN combined with its capability to measure the stable isotopes of the elements provides a significant advantage over existing elemental analyzers.

*"Trademarks of MDS Health Group Limited"

Health Care Services

MDS, through its Health Care Services Division, provides a variety of health assessment and testing services to industry.

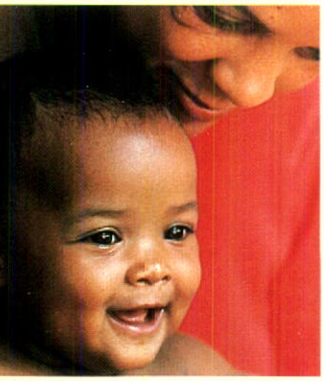
As an approved examiner for more than 100 Canadian life insurance companies, MDS conducts mobile paramedical assessments from Chicoutimi, Quebec to Victoria, B.C. MDS Executive Health Clinics in Toronto, Montreal and Ottawa provide a wide range of pre-employment, periodic, third party and overseas placement health assessments for several hundred large Canadian companies.

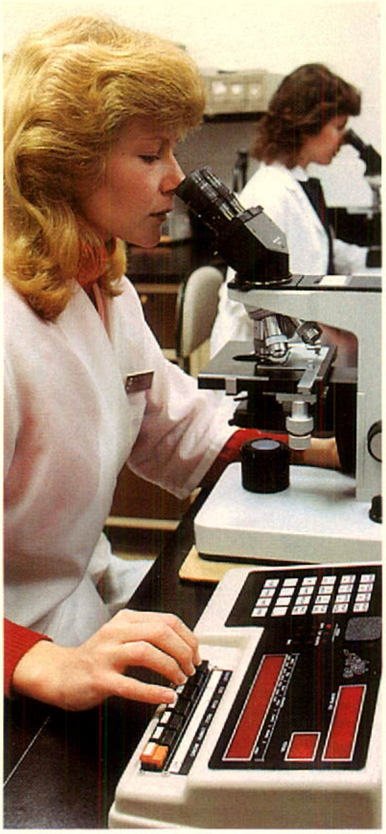
The Evans Medical Industrial Clinic provides specialized occupational health services to some 700 small and medium-sized companies in Ontario.

Tomatis

The Tomatis Division provides Listening Training Programs for children and adults who have an auditory processing deficit. A standard version of the program is available for implementation by school boards and private teaching facilities. More severe cases are treated at the Tomatis Centre in Toronto.

Auditory processing problems are increasingly being recognized as a significant obstacle to proper academic development and a contributor to associated problems in emotional and behavioural areas. It is estimated that in North America and Europe 10-12% of children are affected to some degree by this disability.

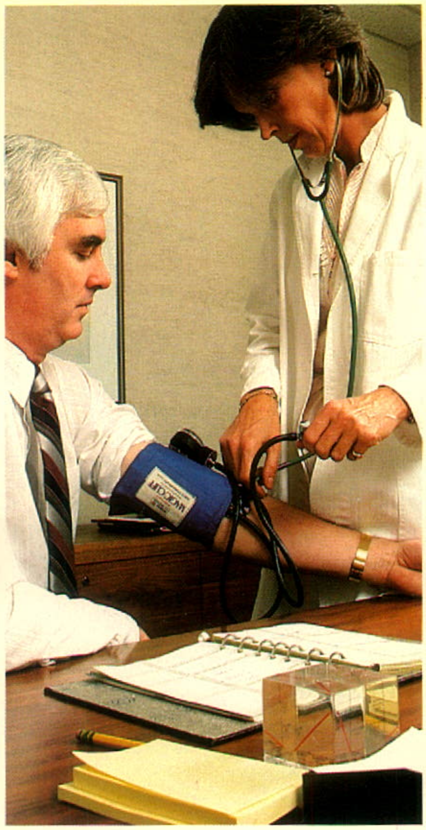




Divisional Highlights 1983

MDS Laboratories

- Achieved record revenues and earnings for combined U.S. and Canadian laboratory operations.
- Signed agreements to take over the operations of two clinical laboratories and a mobile X-ray service with aggregate annual revenues of $8 million. These acquisitions, completed subsequent to the year end, will provide geographical expansion into the State of Michigan, an extension of services to the Ontario nursing home market and entry into the management of U.S. hospital laboratories.
- Established a pilot project to introduce pulmonary function testing services to communities in which this service is not readily available.
- Initiated major expansion of Ontario testing capacity with commencement of construction of a new reference facility in Toronto and completion of new laboratories in Sudbury and Richmond Hill.
- Installed a new on-line laboratory computer at its regional laboratory in Reading, Pennsylvania.
- Introduced new quality control and method audit systems to further enhance MDS quality control procedures.
- Established an Employee Stock Ownership Plan for its employees in the United States.



SCIEX

- Achieved 1983 target for sales of TAGA 6000.
- Signed a $1.4 million contract with the National Research Council for further research and development on the TAGA product line.
- Entered into two business arrangements to provide TAGA based analytical testing services to industry and governments.
- Completed development on the ELAN —a new product concept introduced in 1983 for the measurement of trace quantities of elements.
- Signed (subsequent to year end) a $1.6 million Source Development Fund contract for the supply and development of ELAN systems for various departments within the Federal Government (pictured above).

MDS Health Care Services

- Achieved record revenues and earnings for the third consecutive year.
- Inaugurated physician and diagnostic ECG services on a mobile basis for the life insurance industry in Toronto, Mississauga, Montreal, Ottawa and Vancouver.
- Opened Eastern Ontario regional office for mobile paramedical services in Ottawa.
- Expanded occupational health services to include in-plant physician and nurse health assessments and audiometric testing.

Tomatis

- Implemented pilot projects with three school boards and four private centres to use the standard version of the Tomatis Listening Program.
- Provided listening training to more than 300 children and adolescents through the combined Tomatis Centre and standardized school programs.
- Initiated additional external research studies at North Shore University Hospital, a teaching facility of Cornell University Medical Center, Long Island, N.Y.
- Obtained Canadian, U.S., French and Mexican patents for the electronic equipment used in the Tomatis Listening Program.

MDS Dedication to excellence in quality

In a highly technical service and product oriented organization quality depends upon the calibre and motivation of the people involved. MDS believes it can attract and keep the best people by providing a business climate that encourages employee development and provides the opportunity to participate in the ownership of the company. Indicative of the company's success is the fact that 38% of the full-time employees who worked for MDS ten years ago are still with the company.

The company generally allocates 10% of pre-tax profits to a Deferred Profit Sharing Plan, the proceeds of which have been used to purchase shares of MDS on behalf of employees. More than 87,000 Class A Common shares were purchased on behalf of approximately 1,050 employee participants in 1983. The plan continues to be the largest shareholder in MDS Health Group Limited with 26% of the outstanding Class A Common shares.

Dedication to excellence in quality is a key component of the MDS value system. It is reflected in each of the businesses, through the active involvement of Professional Advisory Boards, the implementation and participation in extensive quality assurance and proficiency testing programs and the commitment to continuing training and education of all employees. It is further reflected in the extra measures taken to preserve the integrity of specimens tested, the reagents used and the components purchased for manufactured products.

This dedication is exemplified in many ways in daily operations:

- In the clinical laboratory, precision, reproducibility, sensitivity and specificity measurements are applied thousands of times a day to confirm the reliability of analytical results required by physicians to effectively treat their patients.
- On the SCIEX production floor, precision machined assemblies are

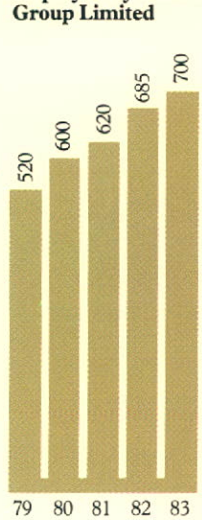
subjected to rigorous testing to assure zero defects performance under unusually severe operating conditions.

- In the SCIEX R & D Laboratory, colour graphics software and state-of-the-art digital design are creatively integrated to provide unparalleled ease of operation in highly complex measuring systems.
- On the road, MDS couriers drive six million miles per year to preserve the integrity of biological specimens in transit to the testing laboratory.
- In the community, there are 360 nurses who are alumni of a training program that builds on their professional skills to provide the insurance industry with the highest quality mobile paramedical health assessments.

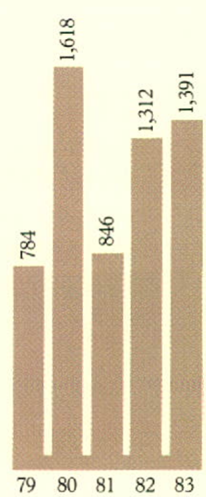
The 2,300 employees of the committed MDS team all adhere to the same high standards and share this concept of and genuine concern for quality.

Expenditures	**1983**	1982	1981	1980	1979
Research and development (gross)	**$2,248,000**	2,689,000	185,000	87,000	79,000
Leasehold improvements and building additions	**$1,644,000**	469,000	120,000	369,000	585,000

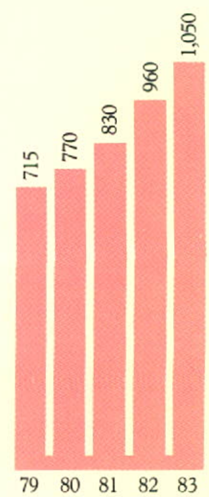
Consultants, scientists and technologists employed by MDS Health Group Limited

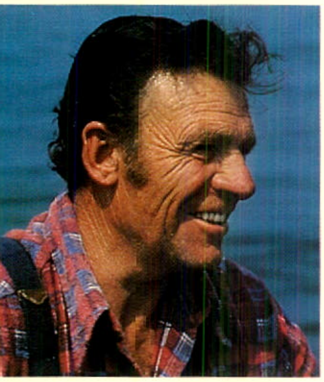


Equipment purchases
in $ thousands



Employees in Deferred Profit Sharing Plan





MDS Dedication to excellence in service

MDS is dedicated to providing its clients—physicians, hospitals, governments, and industrial concerns—with the highest calibre of professional service. The attitude and commitment of everyone in the company to this goal is the key to MDS success.

Over the years MDS has endeavoured to maintain close contact with its clients and to be responsive to their needs. This is evident from the structure of its business operations which favours decentralized regional delivery of services backed by strong central support and control.

The MDS laboratory network exemplifies this approach in 69 communities in Canada and the U.S.A. In each community, a small local team applies the total MDS network resources to meet the particular and evolving needs for diagnostic laboratory services.

The network facilitates access to nationally recognized experts in all aspects of laboratory medicine and occupational health assessment. It makes available a complete spectrum of highly standardized occupational, environmental and clinical laboratory procedures together with their associated data bases. Through this network, the company is able to develop educational tools to enrich knowledge in its fields and to devise aids to optimize the utilization of its services. The network also supplies logistical support to transport people, equipment and supplies and facilitates the rapid transfer of specimens and information from location to location.

The local team is jointly headed by a pathologist, physician or laboratory scientist, and a business manager. Both are active in and sensitive to the needs of their community. Together they undertake the delivery of services for the benefit of individual clients and provide essential feedback to the network about changing needs and trends.

They are joined in these endeavours by nurses, laboratory and radiological technologists, data management personnel, couriers and laboratory services representatives.

Through its decentralized operations, MDS is further able to reach out into the community and provide services on a mobile basis when they are required. Such services include mobile paramedical examinations for insurance applicants, diagnostic X-ray, ECG and specimen collection for nursing home residents, in-plant physician and testing services for industrial workers, mobile environmental testing for industry and government and specialized testing programs sponsored for rural communities.

Local team members enjoy face to face contact with many of the 2.7 million people who are directly served by MDS each year. This gives a personal importance and meaning to their striving for excellence in service.

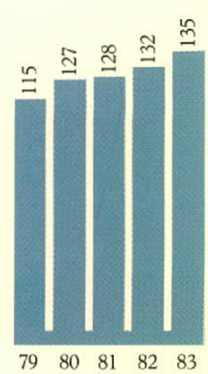
Divisions of MDS Health Group

Markets served:	MDS Laboratories	SCIEX	Health Care Services	Tomatis
Clinical Doctors, Hospitals, Nursing Homes	●	●		
Worker Health Industry, Government	●	●	●	
Community Health Municipal Authorities, Consumer Associations	●	●	●	●
Insurance	●	●	●	

Patients served annually by MDS Laboratories

Tests performed daily by MDS Laboratories

Number of laboratory locations (as of October 31)



A Ten Year Financial Summary

Years ended October 31

Figures in thousands of dollars	**1983**	1982	1981	1980	1979	1978	1977	1976	1975	1974
Operating Results										
Net revenues	**72,699**	61,722	55,971	47,702	39,698	32,820	20,494	19,870	18,645	14,576
Earnings before extraordinary items	**5,142**	3,405	3,297	2,812	2,240	2,085	1,089	957	938	784
Net earnings	**5,142**	3,405	3,297	2,812	2,126	2,085	1,089	995	938	382
Financial Position										
Working capital	**27,096**	12,677	10,865	9,277	8,702	4,904	2,835	912	1,514	1,208
Fixed assets (net)	**9,563**	7,311	6,901	6,109	5,044	3,470	2,053	2,144	2,139	1,728
Other assets (including goodwill)	**9,072**	8,838	8,709	6,749	6,415	5,561	5,063	3,895	3,646	3,618
Total assets	**60,133**	35,094	36,526	30,426	28,660	21,415	13,632	10,576	11,469	9,769
Long term debt	**11,062**	10,792	11,149	10,552	10,880	6,673	3,756	1,660	1,702	1,846
Shareholders' equity	**34,557**	17,814	15,021	11,404	9,120	6,677	6,186	5,269	5,527	4,600
Source of Funds										
Working capital from operations	**7,589**	5,346	5,061	4,411	3,354	2,741	1,365	1,305	1,253	1,069
Long term debt	**701**				4,198	1,000	2,540	600		425
Share capital	**12,380**		937		766	567	1	4	6	1
Application of Funds										
Fixed assets	**5,287**	2,786	1,968	2,677	2,580	1,940	386	480	854	987
Acquisitions	**424**	276	1,009	598	225	(92)	227	(8)		351
Dividends on Class A Common and Class B Non-Voting shares	**779**	612	580	471	392	192	156	167		
Dividends on Preferred shares			37	57	57	20	17	17	17	17
Reduction in long term debt	**431**	357	298	328	402	829	443	792	144	204
Purchase of shares for cancellation						1,949		1,073		
Per Share Data*										
Adjusted basic earnings for Class A Common and Class B Non-Voting (fully diluted and before extraordinary items) shares	**.73**	.53	.53	.46	.40	.32	.16	.14	.11	.09
Dividends										
Common				.15	.30	.15	.10	.10		
Class A Common	**.088**	.075	.075	.038						
Class B Non-Voting	**.138**	.125	.125	.063						
Book Value of Class A Common and Class B Non-Voting (at year end)	**4.74**	2.93	2.47	1.92	1.54	1.19	.90	.77	.63	.53
Price Range										
Common				15½-7¾	13-7¼	8⅝-2⅞	2⅞-2⅜	3-2	2½-1⅜	3¼-1½
Class A Common	**17½-6¾**	6⅞-4⅜	7½-5	6¼-4						
Class B Non-Voting	**16⅞-6¾**	6¾-4⅜	6¼-4¾	5-3½						
Number outstanding										
Common					1,344	1,269	1,674	1,673	2,152	2,147
Class A Common	**2,949**	2,991	3,008	2,678						
Class B Non-Voting	**4,346**	3,103	3,086	2,732						
Ratios										
Current	**2.9**	3.0	2.1	2.1	2.1	1.7	1.9	1.3	1.4	1.4
Long term debt/capital employed	**.24**	.37	.42	.48	.52	.47	.37	.23	.23	.28

*In September, 1980 each common share outstanding was split into one Class A Common share and one Class B Non-Voting share. In July, 1983 each Class A Common and Class B Non-Voting share was split on a two for one basis. Earnings and book value per share figures have been retroactively adjusted to reflect both these share splits. In addition, only dividend, price range and number of shares outstanding figures have been restated for the two for one Class A Common and Class B Non-Voting share split.

Responsibility for Financial Statements

Management

The accompanying consolidated financial statements of MDS Health Group Limited have been prepared by management in accordance with generally accepted accounting principles consistently applied. The most significant of these accounting principles have been set out in note 1 to the financial statements. These statements are presented on the accrual basis of accounting and accordingly, a precise determination of many assets and liabilities is dependent upon future events which necessarily involves the use of estimates and approximations which have been made using careful judgement. In recognizing that the corporation is responsible for both the integrity and objectivity of the financial statements, management is satisfied that these financial statements have been prepared with this in mind and within reasonable limits of materiality.

The Board of Directors has appointed an Audit Committee consisting of three non-management directors. The committee meets periodically during the year to review with management and the auditors any significant accounting and auditing matters and to review and finalize the annual financial statements of the corporation along with the independent auditors' report prior to the submission of the financial statements to the Board of Directors for final approval. The Audit Committee also reviews any major weaknesses in the corporation's systems of internal control reported by the auditors.

The financial information throughout the text of this Annual Report is consistent with the information presented in the financial statements.

The corporation's accounting procedures and related systems of internal control are designed to provide reasonable assurance that its assets are safeguarded and its financial records are reliable.

External Auditors

The auditors' opinion is based upon an independent and objective examination of the corporation's financial results for the year conducted in accordance with generally accepted auditing standards. This examination includes an understanding and evaluation by the auditors of the corporation's accounting systems and internal control procedures as well as obtaining a sound understanding of the corporation's business. The external auditors conduct appropriate tests of the corporation's transactions and obtain sufficient audit evidence in order to provide them with reasonable assurance that the financial statements are presented fairly in accordance with generally accepted accounting principles thus enabling them to issue their report to the shareholders.

Clarkson Gordon, Chartered Accountants, having been appointed by the shareholders of the corporation to serve as the corporation's external auditors, have examined the consolidated financial statements of the corporation for the year ended October 31, 1983 and have reported thereon in their report set out below which is dated January 12, 1984.

Auditors' Report

To the Shareholders of MDS Health Group Limited:

We have examined the consolidated statement of financial position of MDS Health Group Limited as at October 31, 1983 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 corporation as at October 31, 1983 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Clarkson Gordon
Chartered Accountants.

Mississauga, Canada,
January 12, 1984.

Consolidated Statement of Earnings

Year ended October 31, 1983 (with comparative figures for 1982)

(thousands of dollars)	**1983**	1982
Net revenues	**$72,699**	$61,722
Operating costs before the following:	**59,998**	51,988
Depreciation and amortization	**2,555**	2,026
Interest expense–long term	**1,491**	1,561
–other	**187**	333
	64,231	55,908
Operating earnings	**8,468**	5,814
Dividend and interest income	**1,149**	516
Earnings before income taxes	**9,617**	6,330
Income taxes–current	**4,625**	1,600
–deferred	**(150)**	1,325
	4,475	2,925
Net earnings	**$ 5,142**	$ 3,405

Earnings per Class A Common and Class B Non-Voting share	**$ .73**	$ .53

Note: Class B Non-Voting shareholders are entitled to an additional 5¢ per share by means of a non-cumulative dividend which was paid in both 1983 and 1982.

Consolidated Statement of Retained Earnings

Year ended October 31, 1983 (with comparative figures for 1982)

(thousands of dollars)	**1983**	1982
Retained earnings, beginning of year	**$13,227**	$10,434
Net earnings	**5,142**	3,405
Dividends	**(779)**	(612)
Retained earnings, end of year	**$17,590**	$13,227

(See accompanying notes)

Consolidated Statement of Financial Position

as at October 31, 1983
(with comparative figures as at October 31, 1982)

(thousands of dollars)	1983	1982
Current assets:		
Cash and short term deposits	**$11,613**	$ 1,654
Marketable securities at cost (market values 1983–$11,619; 1982–$1,122)	**11,339**	1,122
Accounts receivable	**13,615**	11,407
Inventory	**3,754**	3,929
Prepaid expenses	**946**	644
Current deferred income taxes	**231**	189
	41,498	18,945
Current liabilities:		
Bank indebtedness	**2,035**	649
Accounts payable and accrued liabilities	**7,263**	4,571
Current portion of long term debt	**638**	791
Income and other taxes payable	**3,702**	244
Deposits	**764**	13
	14,402	6,268
Working capital	**27,096**	12,677
Fixed assets	**9,563**	7,311
Other assets	**648**	685
Excess of amounts paid over the fair value of net tangible assets acquired on the purchases of shares and assets, less amortization and write-off	**8,424**	8,153
Capital employed	**$45,731**	$28,826
Represented by:		
Long term debt	**$11,062**	$10,792
Deferred income taxes	**112**	220
Shareholders' equity:		
Share capital	**16,967**	4,587
Retained earnings	**17,590**	13,227
	34,557	17,814
	$45,731	$28,826
Total assets	**$60,133**	$35,094

On behalf of the Board:

Director

R H Yamada

Director

(See accompanying notes)

Consolidated Statement of Changes in Financial Position

Year ended October 31, 1983 (with comparative figures for 1982)

(thousands of dollars)	**1983**	1982
Funds were provided from:		
Operations–		
Net earnings	**$ 5,142**	$ 3,405
Add (deduct) items not affecting working capital:		
Depreciation and amortization	**2,413**	1,894
Amortization of goodwill	**142**	132
Deferred income taxes	**(108)**	(85)
Funds provided from operations	**7,589**	5,346
Issue of shares	**12,380**	
Proceeds on disposal of fixed assets	**633**	482
Reduction in other assets	**37**	15
Total funds provided	**20,639**	5,843
Funds were applied to:		
Acquisitions		
Goodwill	**413**	276
Fixed assets	**11**	
	424	276
Purchase of fixed assets (less long term debt assumed of $701 in 1983)	**4,586**	2,786
Reduction in long term debt	**431**	357
Payment of dividends	**779**	612
Total funds applied	**6,220**	4,031
Increase in working capital	**$14,419**	$ 1,812
Changes in components of working capital:		
Increase (decrease) in current assets–		
Cash and short term deposits	**$ 9,959**	$ (1,633)
Marketable securities	**10,217**	1,122
Accounts receivable	**2,208**	113
Inventory	**(175)**	(200)
Prepaid expenses	**302**	24
Current deferred income taxes	**42**	(70)
Future income tax reductions		(1,327)
	22,553	(1,971)
Increase (decrease) in current liabilities–		
Bank indebtedness	**1,386**	(386)
Accounts payable and accrued liabilities	**2,692**	(928)
Current portion of long term debt	**(153)**	(2)
Income and other taxes payable	**3,458**	(1,459)
Deposits	**751**	(1,008)
	8,134	(3,783)
Increase in working capital	**$14,419**	$ 1,812

(See accompanying notes)

1. Accounting policies

These financial statements are prepared in accordance with generally accepted accounting principles, the most significant of which are as follows:

(a) Basis of consolidation–
The accounts of all subsidiaries are consolidated on a purchase basis from the date of acquisition.

(b) Fixed assets–
Fixed assets are carried in the accounts at cost. Gains and losses arising on the disposal of individual assets are recognized in earnings in the year of disposal.

Assets leased by the corporation under agreements which transfer substantially all of the benefits and risk of ownership of the assets to the corporation are accounted for as capital leases.

Depreciation is provided on a straight-line basis at rates based on the estimated useful lives of the assets. Estimated useful lives range from twenty-five to thirty years for buildings, five to ten years for equipment, furniture and fixtures, three to five years for computer equipment and one to three years for motor vehicles. Leasehold improvements are amortized over the lesser of 10 years or the term of the lease plus one renewal period. No depreciation is provided on assets under construction.

(c) Inventories–
Inventories are valued at the lower of direct cost and net realizable value on the first-in, first-out basis. Work in process and finished goods include materials, direct labour and overhead.

(d) Interest and dividend income–
Interest income and expense is recorded on an accrual basis. Dividend income is recorded as received.

(e) Research and start-up costs–
Certain costs associated with new products and start-up of new businesses are expensed as incurred. Research and development funding is recorded on a billed basis as approved under the terms of individual agreements.

(f) Amortization of intangibles–
For acquisitions after March 31, 1974, the excess of amounts paid over the fair value of the net tangible assets (also referred to as goodwill in these financial statements) acquired on the purchase of shares and assets is capitalized and is being amortized over periods not exceeding forty years. For acquisitions prior to April 1, 1974, the excess has been capitalized and no amounts are being amortized.

(g) Debt issue expense–
Debt issue expense is amortized over the term of the debt.

(h) Investments in and advances to other companies–
Investments in and advances to other companies are recorded at cost less allowance for doubtful realization.

(i) Income taxes–
The corporation follows the deferral method of income tax allocation. Deferred income taxes result from differences between amounts claimed for tax purposes and amounts charged in the accounts. Where the corporation is virtually certain of realizing a future income tax reduction from a loss for tax purposes incurred in the reporting period, such future income tax reduction is recognized in the accounts in the current year.

Federal and provincial investment tax credits are applied as a reduction of income taxes on the flow-through method.

(j) Exchange translation–
The statements of companies whose accounts are maintained in U.S. dollars have been translated into Canadian dollars substantially as follows: inventories, fixed assets, goodwill, deferred income taxes and related expenses, at historic rates of exchange; all other assets and liabilities, at exchange rates prevailing at the end of the year; income and expenses (other than those related to assets and liabilities translated at historic rates) at average rates for the year. Translation gains and losses are included in earnings except for unrealized gains and losses on long term debt which are deferred and charged to earnings over the unexpired term of the debt.

(k) Earnings per share–
Basic earnings per share, which approximate fully diluted earnings per share, have been calculated using the weighted monthly average number of Class A Common and Class B Non-Voting shares outstanding during the year after deducting the extra dividends paid on the Class B Non-Voting shares.

2. Long term debt

			Total	
	Maturity	Current portion	1983	1982
Canadian operations:				
1979 debentures	1999	$207,000	$ 9,413,000	$ 9,597,000
Mortgage at 10%	1985		701,000	
Obligations under capital leases at an average rate approximating 15%	1984-1986	254,000	569,000	649,000
Other debt	1985-1998	50,000	600,000	1,096,000
		511,000	11,283,000	11,342,000
U.S. operations:				
6% Note and other debt	1984-1987	69,000	97,000	241,000
Obligation under capital lease at 13%	1988	58,000	320,000	
		$638,000	11,700,000	11,583,000
Less current portion			638,000	791,000
			$11,062,000	$10,792,000

The 1979 debentures bear interest at a rate of 1⅜% over the prime rate (with a minimum rate of 10% and a maximum rate of 13¼% for the ten years ended October 31, 1991) and have been collateralized by a fixed and floating charge issued by the parent corporation and its U.S. subsidiary. Under the terms of the trust indenture, the corporation may pledge its accounts receivable and inventory as collateral for short term bank borrowings provided total bank borrowings are at least $1,000,000 less than the book value of current assets.

The mortgage loan is collateralized by land with a book value of approximately $950,000. The other debt consists of a $100,000 8% unsecured debenture, a $100,000 8% unsecured note and a $400,000 non-interest bearing loan which is forgivable subject to certain conditions. Since some of the conditions relating to the $400,000 loan have not been fulfilled, the corporation is renegotiating the terms.

If these negotiations are not successful, the cash outlay to the corporation, net of income taxes, will be $200,000.

The corporation has an operating line of credit of $10,000,000 ($6,000,000 in 1982) with a Canadian chartered bank for which a specific charge on accounts receivable and inventory has been given. At October 31, 1983, $2,035,000 ($649,000 in 1982) has been advanced to the corporation as a demand loan in connection with this line of credit.

Principal repayments of long term debt required in the next five fiscal years are:

1984 – $ 638,000	1987 – $ 390,000
1985 – 1,339,000	1988 – 351,000
1986 – 406,000	

At October 31, 1983, the corporation has satisfied all covenants under the trust deed relating to the debentures.

3. Share capital

(a) Summary of issued share capital–

	Balance October 31, 1982	Conversions during year	Issued during year	Balance October 31, 1983
(i) **Voting shares**				
Class A Common shares				
Number	2,991,214	(42,382)		2,948,832
Amount	$2,394,000	$(34,000)		$ 2,360,000
(ii) **Non-Voting shares**				
Class B Non-Voting shares				
Number	3,103,126	42,382	1,200,000	4,345,508
Amount	$2,192,000	$ 34,000	$12,354,000	$14,580,000
Class C Series 1 shares				
Number	89,250			89,250
Amount	$ 1,000			$ 1,000
Class C Series 2 shares				
Number	11,900			11,900
Amount	–			–
Class C Series 3 shares				
Number	–		24,255	24,255
Amount	–		$ 24,000	$ 24,000
Class C Series 4 shares				
Number	–		3,234	3,234
Amount	–		$ 2,000	$ 2,000
Total amount of issued share capital	$4,587,000	$ –	$12,380,000	$16,967,000

(b) Private placement–

On March 31, 1983, the corporation, through a private placement, issued 600,000 Class B Non-Voting shares for a total consideration of $12,600,000 less issuance costs of $246,000 (after-tax). The net proceeds were applied to working capital.

(c) Share split–

At a Special Meeting of the Shareholders on June 29, 1983, approval was given to sub-divide the corporation's Class A Common and Class B Non-Voting shares on a two for one basis. The above share summarization reflects this sub-division, which took place for shareholders of record on July 13, 1983.

(d) Authorized share capital–

The authorized share capital of each class consists of an unlimited number of shares without par value except for Class D shares of which 100,000 were authorized during the year.

(i) Class A Common shares are convertible on a one for one basis into Class B Non-Voting shares and participate equally in dividends with the Class B Non-Voting shares after the declaration of a 2½¢ per share non-cumulative dividend on the Class B Non-Voting shares in each fiscal half year of the corporation. Class B Non-Voting shares are not convertible into Class A Common shares.

(ii) Class C shares are non-voting and non-dividend bearing. The ultimate value of the Class C shares is dependent upon the after-tax earnings of the SCIEX® division.

Under a specific formula, the conversion of the Class C Series 1 shares into Class A Common and Class B Non-Voting shares will commence when the SCIEX® division attains cumulative after-tax earnings of $2,450,000 in the period June 1, 1981 to May 31, 1986. After all Class C Series 1 shares have been converted, Series 2 shares shall become redeemable at the rate of $100 per share or the equivalent number of Class A Common and/or Class B Non-Voting shares at the then market value of those shares, at the option of the corporation. If the maximum after-tax earnings level of $8,050,000 in aggregate is achieved for the five year period ending May 31, 1986, 80,325 Class A Common and 98,175 Class B Non-Voting shares will have been issued and either a cash payment of $1,190,000 or the equivalent value by way of Class A Common and Class B Non-Voting shares will have been issued. For the period June 1, 1981 to October 31, 1983, the SCIEX® division has not attained the base period earnings of $2,450,000; accordingly no Class C Series 1 and Series 2 shares are as yet convertible.

The Series 3 and Series 4 shares, which are reserved for certain SCIEX® employees under a Key Employee Trust Plan, are similar to the Series 1 and Series 2 shares respectively except that the earnings period for conversion purposes is November 1, 1982 to October 31, 1987, the after-tax earnings formula is not subject to a base earnings level and maximum convertibility arises when SCIEX® after-tax earnings reach $5,600,000 in aggregate for the five year period. If the maximum earnings level is achieved, 21,830 Class A Common shares and 26,680 Class B Non-Voting shares will have been issued and either a cash payment of $323,000 or the equivalent value by way of Class A Common and Class B Non-Voting shares will have been issued, based on the outstanding number of Series 3 and Series 4 shares issued to date.

All Series 1 and Series 2 shares not converted at May 31, 1986, and all Series 3 and Series 4 shares not converted at October 31, 1987, will be redeemed by the corporation at their paid-in value.

(iii) Class D shares, which were created for the Employee Stock Purchase Plan, are non-voting, non-dividend bearing, and are convertible into Class A Common shares on a one for one basis in the third, fourth and fifth year from date of issue. Five years from the date of issue the shares are redeemable at issue price.

If ratified at the corporation's annual meeting on March 6, 1984, the Class D shares will bear a variable dividend, equal to two-thirds of the Bank prime rate, payable quarterly.

(e) Employee Stock Option Plan–
During the year, the Board of Directors authorized the creation of an Employee Stock Option Plan and reservation of 100,000 Class B Non-Voting shares of the corporation. During the year, options to purchase 60,000 Class B Non-Voting shares at $12.15 per share were issued and were outstanding at year end. These options are exercisable at various dates up to January 2, 1989.

(f) SCIEX®Key Employee Trust Plan–
31,500 Class C Series 3 and 4,200 Class C Series 4 shares have been authorized for issue under a Key Employee Trust Plan for certain SCIEX®employees. During the year, 24,255 Class C Series 3 and 3,234 Class C Series 4 shares were issued.

(g) Employee Stock Purchase Plan–
During the year, the Board of Directors authorized the creation of an Employee Stock Purchase Plan and 30,000 Class D shares were allotted at $13.63 per share but not issued.

4. Inventory

Inventory consists of:

	1983	1982
Laboratory and other supplies	$2,739,000	$2,615,000
Work in process	748,000	148,000
Finished goods	267,000	1,166,000
	$3,754,000	$3,929,000

5. Fixed assets

	1983			1982
	Cost	Accumulated depreciation and amortization	Net	Net
Land	$ 982,000	$	$ 982,000	$ 37,000
Buildings	359,000	112,000	247,000	266,000
Equipment and furniture	12,234,000	6,408,000	5,826,000	5,743,000
Leasehold improvements	3,428,000	2,143,000	1,285,000	1,265,000
Asset under construction	1,223,000		1,223,000	
	$18,226,000	$8,663,000	$9,563,000	$7,311,000

6. Other assets

Other assets are carried at cost less applicable amortization and allowances and consist of:

	1983	1982
Investment in and advances to other companies	$378,000	$361,000
Debt issue expense	183,000	201,000
Other	87,000	123,000
	$648,000	$685,000

7. Acquisitions

During the year, the corporation acquired two medical laboratories for a total consideration of $318,000. Of the total purchase price, $11,000 was ascribed to fixed assets and $307,000 to goodwill.

In addition, payments of $106,000 were made in connection with certain previous acquisition agreements and have been ascribed to goodwill.

8. Research and development costs

During the year, the corporation incurred research and development costs of $2,248,000 ($2,689,000 in 1982) and received Government funding and related revenues of $1,489,000 ($1,990,000 in 1982) with respect to these expenditures. The net amount of $759,000 ($699,000 in 1982) has been charged to earnings.

9. Other information

During the year, the corporation entered into agreements (one of which closed in November, 1983) whereby Sciex®equipment was acquired by two companies which, in turn, contracted for a fee with the corporation to develop software applications for the corporation for time periods approximating one year. These agreements allow the corporation to acquire partial equity interests in these companies subject to varying conditions as set out in the agreements. Any costs directly attributable to these options are nominal in value and have been reflected in the accounts at cost.

In connection with one of these transactions, the corporation has guaranteed a capital lease in the amount of $720,000.

10. Segmented information

The Directors have determined that the corporation operated within one dominant segment, the provision of testing, measurement and related services and products for health care and associated markets.

The corporation also carries on operations in the United States. The following summary presents key information by geographic segment. During the year inter-segment revenues from Canada to the United States amounted to $2,200,000 (nil in 1982) which represented cost plus an appropriate mark-up.

	Canada		United States		Total	
(thousands of dollars)	1983	1982	1983	1982	1983	1982
Net segment revenues	$52,816	$46,228	$19,883	$15,494	$72,699	$61,722
Operating earnings (before the following):	$11,689	$ 9,041	$ 1,012	$ 693	$12,701	$ 9,734
Depreciation and amortization	1,652	1,328	903	698	2,555	2,026
Interest and dividends*	848	1,663	(319)	(285)	529	1,378
Earnings before income taxes	9,189	6,050	428	280	9,617	6,330
Income taxes	4,428	2,925	47		4,475	2,925
Net earnings	$ 4,761	$ 3,125	$ 381	$ 280	$ 5,142	$ 3,405
Identifiable assets	$40,400	$23,600	$19,700	$11,500	$60,100	$35,100

*Interest expense (income) and dividend income are directly attributable to debt or investment existing in the geographic segment indicated above.

11. Income taxes

Certain of the corporation's United States subsidiaries have loss carryforwards (for which no future tax benefit has been recorded in the accounts), many of which arose prior to acquisitions, which amount to $1,491,000 and expire as follows: 1990–$169,000; 1991–$131,000; 1992–$194,000; 1993–$98,000; 1994–$849,000; 1996–$50,000. In addition, unused investment tax credits of $361,000, which have not been recognized in the accounts, are available to reduce future income taxes payable. None of these credits will expire before 1989.

The corporation's tax rate is favourably affected primarily by research and development tax credits and allowances, dividend income and, to a lesser extent, the 3% inventory allowance.

12. Leases, commitments and contingent liabilities

(a) Capital leases–

Fixed assets include vehicles and computer equipment acquired under capital leases amounting to $1,333,000 ($1,031,000 in 1982) at cost and accumulated depreciation of $462,000 ($382,000 in 1982).

Future lease payments required under capital leases are as follows:

1984	$ 518,000
1985	474,000
1986	203,000
1987	99,000
1988	27,000
Total future minimum lease payments	1,321,000
Less imputed interest	432,000
Present value of minimum lease payments	$ 889,000

(b) Operating leases–

Under premise and equipment leases, the corporation is obliged to make minimum payments of approximately $2,193,000 in 1984, $1,816,000 in 1985, $1,352,000 in 1986, $1,019,000 in 1987, $619,000 in 1988, and $1,231,000 thereafter. Fixed rental expense under premise and equipment leases for 1983 was $2,816,000 ($2,286,000 in 1982).

(c) Contingent liabilities–

The corporation is contingently liable for the bank indebtedness of certain of its investments in other companies to a maximum amount of $326,000. In addition, the corporation has also guaranteed a capital lease to a maximum amount of $720,000 (see note 9).

(d) Asset under construction–

The corporation is committed to additional outlays of approximately $2.2 million to complete its new Toronto reference facility which is scheduled for completion in March, 1984.

13. Subsequent events

(a) Acquisitions–

On December 1, 1983, the corporation signed an agreement, effective November 1, 1983, to acquire the assets and business operations of a Michigan laboratory company for $4,200,000 U.S., of which $1,200,000 was paid in cash and the remainder was satisfied by the issuance of a 10% $3,000,000 convertible debenture. Of the total purchase price, $200,000 is attributable to assets and $4,000,000 to goodwill.

At the date of the debenture's maturity on November 1, 1988, the holder has the option either to receive cash or convert any portion of the debenture into Class B Non-Voting shares of the corporation at the rate of 60 shares for each $1,000 portion of the debenture. Maximum conversion would result in the issuance of 180,000 Class B Non-Voting shares on November 1, 1988. According to the terms of the agreement, the principal amount of the debenture may be reduced if the Michigan operations do not obtain certain earning levels during the term of the debenture; conversely, if annual earnings exceed certain levels as defined in the agreement during the period, additional payments may be required.

In addition, on November 1, 1983, the corporation purchased a mobile diagnostic business in Ontario for $165,000 cash of which $30,000 has been ascribed to assets and $135,000 to goodwill.

(b) Government contract–

On November 24, 1983, the corporation's Sciex® division signed a $1.6 million contract with the Federal Government through its Source Development Fund. The purpose of the contract is to assist Sciex® in the development of an advanced high technology product, the Elan (Elemental Analyzer). The proceeds from the contract will be recorded as billed during 1984. As part of the contract, the Federal Government will receive three Elans, two of which will be leased, and royalties on future Elan sales.

Corporate Information

Board of Directors

°Dr. William Anderson,
Vice-President of Medical Affairs,
Toronto General Hospital

*Alan Grieve
Investment Consultant

°Dr. Louis R. Harnick
Chief Radiologist,
Toronto Western Hospital

†*Ralph Horner
Investment Consultant

Wilfred G. Lewitt
President and Chief Executive Officer,
MDS Health Group Limited

†R. Michael Warren
President and Chief Executive Officer,
Canada Post Corporation

*Roger D. Wilson, Q.C.
Partner, Fasken & Calvin

Ronald H. Yamada
Vice-President,
MDS Health Group Limited

†C. Robert Younger
Executive Vice-President and
Chief Operating Officer,
Dominion Securities Ames Limited

°Medical Advisory Committee
*Audit Committee †Compensation Committee

Officers and Corporate Management

Wilfred G. Lewitt
President and Chief Executive Officer

J. Edward Boyce
Vice-President,
Organization Development & Personnel

Douglas M. Phillips
Vice-President
President, MDS Laboratories

John A. Rogers
Vice-President, Finance

Edward K. Rygiel
Vice-President,
Corporate Development

Ronald H. Yamada
Vice-President

Betty R. Moffatt
Corporate Secretary

Dr. William Anderson
Chairman,
Medical Advisory Committee
MDS Health Group Limited

Dr. John C. Nixon
Medical Director, MDS Laboratories

Investors' Quick Reference Guide

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30 Meridian Road, Rexdale, Ontario
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Telephone: (416) 675-7661
TWX: 610 492 6137

Transfer Agents & Registrar
Guaranty Trust Company of Canada
Toronto

Auditors
Clarkson Gordon

Legal Counsel
Fasken & Calvin

Bankers
Canadian Imperial Bank of Commerce

Stock Listing
Toronto Stock Exchange
Symbols: MHG.A MHG.B

Both Class A Common and Class B Non-Voting shares are qualified investments for an Indexed Security Investment Plan (ISIP).

Trading Data
(by fiscal quarter and after the July, 1983 share split)

		High	Low
1st Quarter	Class A	7.81	6.75
	Class B	7.75	6.75
2nd Quarter	Class A	11.25	7.38
	Class B	11.50	7.13
3rd Quarter	Class A	17.50	10.88
	Class B	16.88	11.00
4th Quarter	Class A	16.00	13.50
	Class B	15.38	13.25

Dividend Information
Paid twice yearly in the Spring and Fall—The October, 1983 dividend was 5¢ on the Class A Common shares and 7½¢ on the Class B Non-Voting shares.

Annual Meeting
Shareholders are invited to attend the company's Annual and Special Meeting at 4 p.m., March 6, 1984 in the Quebec Room of the Royal York Hotel, Toronto, Ontario.

MDS Health Group Limited
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