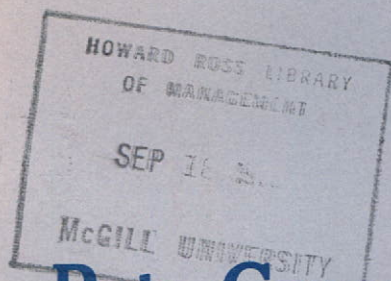


PATO

1978 ANNUAL REPORT



Pato Consolidated Gold Dredging Limited

PATO CONSOLIDATED GOLD DREDGING LIMITED

(Incorporated under the laws of Bermuda)

DIRECTORS

Lewis B. Harder, *Chairman of the Board of the Corporation, Vice Chairman of the Board, Pacific Holding Corporation, Los Angeles, California, U.S.A.*

John W. Butterfield, *Partner, Rawlinson, Hunter, Butterfield & Co., Chartered Accountants, Hamilton, Bermuda*

Geoffrey C. Colclough, *Secretary of the Corporation, Member of Appleby, Spurling & Kempe, Barristers, Hamilton, Bermuda*

John S. C. Goold, *President and Managing Director of the Corporation, Hamilton, Bermuda*

David H. Murdock, *Chairman of the Board and Chief Executive Officer, Pacific Holding Corporation, Los Angeles, California, U.S.A.*

OFFICERS

John S. C. Goold, *President and Managing Director*

Edward Moseley-Williams, *Vice President*

Patrick H. O'Neill, *Vice President*

Geoffrey C. Colclough, *Secretary*

AUDITORS

Price Waterhouse & Co., *Chartered Accountants*

REGISTRARS AND TRANSFER AGENTS

Bank of Bermuda
Hamilton, Bermuda

Manufacturers Hanover Trust Company
New York, New York, U.S.A.

BUSINESS DESCRIPTION

Pato Consolidated Gold Dredging Limited was incorporated under the laws of British Columbia, Canada in 1934 to conduct gold dredging operations on the Nechi River in Colombia, South America. The Company sold the mining operations to Colombian investors in July 1974. In 1976 the Company transferred its domicile to Bermuda and was reincorporated there under The Companies Act of 1923. Pato continues its involvement in mining activities through its 16.5% interest in a Brazilian joint venture which mines and processes columbium at an open cut mine near Araxa, Brazil. The Company has stock interests in other companies and has interests in certain resort hotel facilities.

CORPORATE OFFICE

Washington Mall
Church Street
Hamilton 5, Bermuda

STOCK LISTING

American Stock Exchange
(Ticker symbol "PO")

STOCK PRICES

	1978		1977	
	High	Low	High	Low
1st quarter	7 ³ / ₈	6	9 ³ / ₈	6 ¹ / ₂
2nd quarter	7 ³ / ₄	6 ¹ / ₂	9 ¹ / ₄	7 ⁷ / ₈
3rd quarter	10 ³ / ₈	7	9 ¹ / ₄	6 ¹ / ₈
4th quarter	11	7 ³ / ₈	6 ³ / ₄	5 ³ / ₄

PATO CONSOLIDATED GOLD DREDGING LIMITED

WASHINGTON MALL. CHURCH STREET. HAMILTON 5. BERMUDA
P.O. BOX 778 TELEPHONE (809) 292-4106

April 23, 1979

TO THE STOCKHOLDERS OF

PATO CONSOLIDATED GOLD DREDGING LIMITED

Subsequent to most of our work in connection with the preparation of the 1978 Annual Report of Pato, an offer was announced by Pacific Holding Corporation to acquire the 35.6% of the shares of Pato not currently owned by Pacific or companies wholly owned by it. The Pato Board of Directors intends to meet in the near future to consider the offer.

The Pato Annual General Meeting of Stockholders has been postponed from its originally scheduled date of June 4, 1979 until the Board can meet. You will be fully advised after Pato's Board meets concerning further developments relating to Pacific Holding Corporation's offer and the Annual General Meeting.

A copy of the press release issued by Pacific Holding Corporation concerning its offer is set forth below.

Sincerely,

JOHN S. C. GOOLD
President and Managing Director

* * * * *

PACIFIC HOLDING CORPORATION PROPOSES TO ACQUIRE BALANCE OF PATO CONSOLIDATED GOLD DREDGING LIMITED FOR CASH

LOS ANGELES, CALIFORNIA, April 18, 1979—Pacific Holding Corporation, privately held by David H. Murdock, announced today an offer through companies wholly owned by Pacific to purchase the 35.6% of the shares of Pato Consolidated Gold Dredging Limited (AMEX) not currently owned by Pacific or companies wholly owned by it. Public stockholders of Pato would receive \$14 per share in cash pursuant to the offer which provides for the amalgamation of Pato, a Bermuda corporation, with another Bermuda corporation wholly owned by Pacific.

The offer to Pato is subject to various conditions, including approval of the transaction by a committee of three outside directors of Pato, receipt by Pato of an opinion of an independent investment banking firm retained by the outside directors concerning the fair price to the public stockholders of Pato for the Pato shares, approval of the transaction by $\frac{3}{4}$ of the shares voted by the Public stockholders, approval by $\frac{1}{2}$ of the actual number of public stockholders voting on the transaction, and approval of the transaction by a Bermuda court in accordance with provisions of Bermuda law. Pacific's offer to acquire the outstanding stock of Pato held by public stockholders is further subject to receipt of an opinion of Goldman, Sachs & Co., which has been retained by Pacific, concerning the fair price to the

(over)

public stockholders of Pato for the Pato shares. Under Pacific's proposal, Goldman, Sachs & Co. and the investment banking firm to be retained by the outside directors of Pato may issue separate opinions or a joint opinion, as such investment bankers may choose. In addition, Pacific stated that the proposed transaction would be subject to certain other conditions customary in acquisition transactions.

Pacific stated that among other things, the acquisition of Pato would greatly enhance its flexibility in dealing with Pato and would resolve possible conflicts of interest. Pacific noted that it wished to resolve a dividend payment issue arising from Pato's status for tax purposes as a foreign personal holding company. Pacific further stated that the acquisition of Pato would also resolve any question relating to the possible applicability to Pato of the Investment Company Act of 1940.

Pacific noted that in August 1978, Pato became a foreign personal holding company for United States federal income tax purposes. The United States Internal Revenue Code provides that to the extent that taxable income (computed with certain adjustments) of a foreign personal holding company in any taxable year exceeds the amount of dividends paid to stockholders during such year, each person who is a United States shareholder of Pato on the last day of the year must report as taxable dividend income the pro rata share of such excess for the entire year. Pato shareholders as of December 31, 1978 were subject to this requirement. Pato's Board of Directors declared an extra dividend on November 14, 1978, in the amount of \$1.50 per share, which was paid December 20, 1978, to shareholders of record as of November 30, 1978. This dividend brought total 1978 dividends to \$2.00 per share which was in excess of Pato's 1978 taxable earnings which were approximately \$1.88 per share.

Pato has stated that future dividends are payable when, as and if declared by Pato's Board of Directors, which periodically reviews policy with respect to the payment of dividends. Pato further stated that the declaration of future dividends is dependent upon Pato's future earnings, financial condition, need for capital and other factors. Pato's Board of Directors has made no decision concerning whether Pato will continue in the future to pay dividends equal to its estimated taxable income under United States Income Tax laws.

Pacific, through companies owned by it, is the principal stockholder of Pato and does not wish Pato to continue paying dividends of such magnitude, preferring instead to retain the flexibility to use a portion of such funds in the business of Pato. Such a dividend policy may adversely affect persons who are United States shareholders on the last day of the fiscal year since they would be taxed on the pro rata share of Pato's taxable income, perhaps without receiving dividend income equal to their tax liability. Pato's common stock closed today at \$11.50 per share on the American Stock Exchange.

DIRECTORS' REPORT TO THE SHAREHOLDERS

On behalf of the Board of Directors I am pleased to submit the forty-fifth Annual Report of the Company, together with the audited financial statements for the year ended December 31, 1978.

INCOME

Net income in 1978 was \$9,046,000 or \$2.58 per share, compared to \$6,474,000 or \$1.85 per share in 1977. Included in the 1978 results is a gain of \$2,937,000 (\$0.84 per share) on sale of the Company's investment in Kawecki Berylco Industries, Inc. and an unrealized gain in 1977 of \$1,982,000 (\$0.57 per share) on the exchange of shares of Molycorp, Inc. for shares of Union Oil Company of California.

Pato's equity share of the net income of the Brazilian mining joint venture rose to \$5,175,000 in 1978, an increase of 29%.

Pato currently owns 350,200 shares of common stock of Ticor which announced recently a proposed merger with Southern Pacific Company. If the merger is consummated as announced, Pato expects to receive approximately \$40 per share for its Ticor stock, expected to be paid partly in cash and partly in debt securities of Southern Pacific Company, for a gain of approximately \$6,600,000. Since Pato is a Bermuda corporation, the gain on this transaction would not be subject to corporate taxation. See the discussion below of Pato's status as a foreign personal holding company.

DIVIDENDS

Pato is 64.4% owned by International Mining Corporation which in turn is wholly owned by Pacific Holding Corporation. In August 1978, Pato became a foreign personal holding company for United States Federal Income Tax purposes. The United States Internal Revenue Code provides that to the extent the taxable income (computed with certain adjustments) of a foreign personal holding company in any taxable year exceeds the amount of dividends paid to stockholders during such year, each

person who is a United States shareholder of such company on the last day of the year must report as taxable dividend income the pro rata share of such excess for the entire year. Pato's United States shareholders on December 31, 1978 are subject to this requirement. Pato's Board of Directors declared an extra dividend on November 14, 1978 in the amount of \$1.50 per share, which was paid December 20, 1978 to shareholders of record as of November 30, 1978. This dividend along with two \$0.25 cash dividends per share paid on May 4 and November 30 brought total 1978 dividends to \$2.00 per share which is in excess of Pato's 1978 taxable earnings, which were approximately \$1.88 per share. Two cash dividend payments of \$0.25 each per share were made on April 11 and October 11, 1977.

Future dividends are payable when, as and if declared by Pato's Board of Directors, which periodically reviews its policy with respect to the payment of dividends. The declaration of future dividends is dependent upon Pato's future earnings, financial condition, need for capital and other factors. No decision has been made concerning whether Pato will continue in the future to pay dividends equal to its estimated taxable income under United States income tax laws.

Shareholders who have not received dividends in the last two years are again reminded that Pato moved its domicile to Bermuda in October 1976 and issued new certificates to replace the certificates issued by Pato of British Columbia, Canada. Holders of the prior Pato (Canada corporation) shares will not receive dividends paid since 1976 until they have exchanged their certificates for Pato (Bermuda corporation) shares. If you hold Pato (Canada) shares dated prior to October 1976, they should be sent by registered mail, for exchange, to Manufacturers Hanover Trust Company, 4 New York Plaza, 10th Floor, New York, N.Y. 10015: attention G. F. Ruddy, Stock Transfer Department.

OPERATIONS

The Company has a 16.5% interest in a Brazilian joint venture, Companhia Brasileira de Metalurgia e Mineracao (CBMM) which produces and markets columbium concentrates and ferrocolumbium from a large ore deposit located near Araxa, Brazil. Columbium is an important alloying agent used in the production of high strength steels. In recent years there has been a significant increase in the use of such high quality steels in the manufacture of automobiles and large-diameter Arctic pipelines. CBMM's sales increased in 1978 and

earnings reached a new high. Pato received dividends from CBMM, before withholding taxes, of \$2,496,000 in 1978, and \$2,452,000 in 1977.

CBMM is continuing its exploration program in Brazil. Evaluation studies are proceeding on several titanium prospects, in the State of Minas Gerais, acquired in recent years.

Pato has increased its ownership in Island Gem Enterprises, Ltd. N.V. to approximately 18%. Island Gem owns and operates hotels and resort facilities in the Netherlands Antilles.

Hamilton, Bermuda
April 16, 1979

On behalf of the Board,

John S. C. Goold
President and Managing Director

REPORT OF INDEPENDENT ACCOUNTANTS

To the Shareholders of Pato Consolidated Gold Dredging Limited

In our opinion, the accompanying balance sheets and the related statements of income and retained earnings and of changes in financial position present fairly the financial position of Pato Consolidated Gold Dredging Limited at December 31, 1978 and 1977, the results of its operations and the changes in its financial position for the years then ended, in conformity with accounting principles generally accepted in the United States of America applied on a consistent basis after restatement for the change, with which we concur, in the presentation of the balance sheet and the related statement of changes in financial position as described in Note 1. Our examinations of these statements were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Hamilton, Bermuda
January 30, 1979

PRICE WATERHOUSE & CO.
Chartered Accountants

PATO CONSOLIDATED GOLD DREDGING LIMITED

STATEMENTS OF INCOME AND RETAINED EARNINGS

	For the Year Ended December 31	
	1978	1977
REVENUES		
Equity in net income of Brazilian joint venture (Note 3) . . .	\$ 5,175,390	\$ 4,003,230
Gain on sale and exchange of securities (Note 2):		
Kawecki Berylco Industries, Inc.	2,937,425	—
Molycorp, Inc.	—	1,982,441
Other	1,304,445	1,376,461
Dividends and other income	990,760	534,648
Interest income	435,075	96,280
	<u>10,843,095</u>	<u>7,993,060</u>
EXPENSES		
Administrative and general	277,599	370,219
Interest	143,808	165,816
	<u>421,407</u>	<u>536,035</u>
Income from continuing operations before income taxes . . .	10,421,688	7,457,025
Provision for income taxes (Note 5)	1,375,897	1,095,598
Income from continuing operations	9,045,791	6,361,427
Gain on disposal of assets of discontinued operations (Note 6)	—	112,597
Net income	9,045,791	6,474,024
Retained earnings, beginning of year	25,513,441	20,790,602
	<u>34,559,232</u>	<u>27,264,626</u>
Deduct: Dividends (\$2.00 per share in 1978 and \$0.50 in 1977)	7,004,740	1,751,185
Retained earnings, end of year	<u>\$27,554,492</u>	<u>\$25,513,441</u>
Income per share:		
Income from continuing operations	\$ 2.58	\$ 1.82
Gain on disposal of assets of discontinued operations . . .	—	0.03
Net income	<u>\$ 2.58</u>	<u>\$ 1.85</u>
Average number of shares outstanding	<u>3,502,370</u>	<u>3,502,370</u>

PATO CONSOLIDATED GOLD DREDGING LIMITED

BALANCE SHEETS (Note 1)

	December 31	
	1978	1977*
ASSETS		
Cash	\$ 10,235	\$ 134,253
Investment in securities, at lower of cost or market (Notes 2 and 4)	20,437,627	25,710,943
Dividends and interest receivable	76,577	46,446
Interest in Brazilian joint venture (Note 3)	12,765,793	10,167,578
Other investments	952,448	460,554
	<u>\$34,242,680</u>	<u>\$36,519,774</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES		
Bank loan (Note 4)	\$ 950,000	\$ 5,300,000
Accounts payable and accrued expenses	28,190	140,808
Deferred income taxes (Note 3)	591,538	365,390
	<u>1,569,728</u>	<u>5,806,198</u>
SHAREHOLDERS' EQUITY		
Share capital		
Authorized—5,000,000 shares of \$1 each— <u>\$5,000,000</u>		
Issued and fully paid—3,502,370 shares	3,502,370	3,502,370
Share premiums	2,764,655	2,764,655
Retained earnings	27,554,492	25,513,441
Shareholders' equity before valuation allowance	33,821,517	31,780,466
Share of Brazilian joint venture's net unrealized loss on noncurrent marketable equity securities (Note 3)	(1,148,565)	(1,066,890)
Shareholders' equity	<u>32,672,952</u>	<u>30,713,576</u>
	<u>\$34,242,680</u>	<u>\$36,519,774</u>

* Restated see Note 1.

PATO CONSOLIDATED GOLD DREDGING LIMITED

STATEMENTS OF CHANGES IN FINANCIAL POSITION (Note 1)

	For the Year Ended December 31	
	1978	1977*
FINANCIAL RESOURCES WERE PROVIDED BY:		
Income from continuing operations	\$ 9,045,791	\$ 6,361,427
Add (deduct) — Items not affecting cash:		
Equity in undistributed net income of Brazilian joint venture	(2,679,890)	(1,551,327)
Gain on sale and exchange of securities:		
Kawecki Berylco Industries, Inc.	(2,937,425)	—
Molycorp, Inc.	—	(1,982,441)
Other	(1,304,445)	(1,376,461)
Deferred income taxes	226,148	21,526
Increase in dividends and interest receivable	(30,131)	(6,189)
(Decrease) increase in accounts payable and accrued expenses	(112,618)	60,263
Financial resources provided from continuing operations ..	2,207,430	1,526,798
Proceeds from sale of securities	18,355,607	4,435,342
Exchange of Molycorp, Inc. shares	—	2,804,281
Proceeds of bank loans	5,550,000	5,500,000
Proceeds from disposal of assets of discontinued operations	—	405,478
Total financial resources provided	26,113,037	14,671,899
FINANCIAL RESOURCES WERE USED FOR:		
Purchases of securities	8,840,421	7,746,299
Exchange of Molycorp, Inc. shares	—	2,804,281
Repayment of bank loans	9,900,000	2,100,000
Cash dividends paid	7,004,740	1,751,185
Increase in other assets — net	491,894	442,775
Total financial resources used	26,237,055	14,844,540
(Decrease) in cash	(124,018)	(172,641)
Cash at beginning of the year	134,253	306,894
Cash at end of the year	\$ 10,235	\$ 134,253

* Restated see Note 1.

PATO CONSOLIDATED GOLD DREDGING LIMITED
NOTES TO FINANCIAL STATEMENTS
for the years ended December 31, 1978 and 1977

NOTE 1 — Summary of Significant Accounting Policies

General

Pato Consolidated Gold Dredging Limited is 64.4% owned by Pacific Holding Corporation, a privately held company, and in 1978 Pato became a foreign personal holding company as defined by the United States Internal Revenue Code.

The United States Internal Revenue Code provides that to the extent that undistributed foreign personal holding company income as defined in any taxable year exceeds the amount of dividends paid to shareholders during such year, each person who is a United States shareholder of the Company on the last day of such year must report as taxable dividend income his pro rata share of such excess for the entire year. The Company believes it has distributed within the year all of its foreign personal holding company income to its shareholders.

The accompanying financial statements which have been prepared in conformity with accounting principles generally accepted in the United States of America are presented in United States dollars.

Changes in financial statements presentation

In 1978 the Company changed the presentation of the balance sheet and the statement of changes in financial position to eliminate separate classifications of current assets and current liabilities in the balance sheet and to express changes in financial position in terms of cash rather than of working capital. The change in presentation was made to better reflect the nature of the Company's operations and assets.

Financial statements of prior years have been restated for comparative purposes.

Interest in Brazilian joint venture

The Company accounts for its investment in its Brazilian joint venture, Companhia Brasileira de Metalurgia e Mineracao (CBMM), which is engaged in producing and marketing columbium concentrates and ferrocolumbium, on the equity basis of accounting.

Investment in securities

The Company's investment securities are comprised of marketable equity securities and other securities. Marketable equity securities are carried at the lower of aggregate average cost or aggregate market value. The amount by which the aggregate cost of marketable equity securities exceeds the aggregate market value would be, together with the Company's share of a similar provision of its Brazilian joint venture, recorded as a reduction of shareholders' equity. Other securities are carried at cost.

Income taxes

The Company is not subject to income taxes in Bermuda. Deferred taxes are provided for withholding taxes expected to be payable upon anticipated remittances of the undistributed earnings of the Company's Brazilian joint venture. Taxes are also provided for withholding taxes on interest and dividend income from investments.

NOTE 2 — Investment in Securities

The investments in securities held at December 31, 1978 and 1977, carried at cost, comprise the following:

<u>Companies</u>	<u>Number of Shares or Face Amount</u>	<u>Cost</u>	<u>Quoted Market Value</u>
1978			
Marketable Equity Securities:			
Allied Chemical Corporation	5,000	\$ 168,581	\$ 141,000
Boeing Company	7,800	470,908	557,000
Brandywine Sports Inc.	50,720	150,995	159,000
Canadian International Power Co. Ltd.	98,600	71,529	127,000
Dan River, Inc.	20,500	222,788	251,000
Gulf United Corp.	26,700	359,754	347,000
International Paper Company	10,000	415,753	365,000
Newmont Mining Corp.	17,000	356,634	366,000
RLC Corp.	380,400	2,382,477	4,660,000
Rouse Company	440,500	2,060,884	3,524,000
Signal Companies, Inc.	50,000	1,195,815	1,000,000
Southwest Forest Industries, Inc.	96,000	1,140,081	1,296,000
Teledyne, Inc.	6,000	551,133	581,000
TICOR	311,100	6,557,430	6,961,000
UAL, Inc.	8,700	273,826	253,000
Union Oil Company of California	50,301	2,804,281	2,861,000
Union Pacific Corporation	17,000	932,648	876,000
United Brands Company	33,000	322,110	326,000
		<u>\$20,437,627</u>	<u>\$24,651,000</u>

1977			
Marketable Equity Securities:			
Brandywine Sports Inc.	50,720	\$ 150,995	\$ 165,000
Canadian International Power Co. Ltd.	23,100	27,389	26,000
Canal Randolph Corp.	8,900	91,265	102,000
General American Oil Company of Texas	66,126	1,522,947	2,091,000
Inspiration Consolidated Copper Company	54,800	1,501,158	1,021,000
Kennecott Copper Corporation	134,100	4,482,005	2,984,000
Lomas & Nettleton Financial Corp.	18,800	192,356	183,000
RLC Corp.	380,400	2,382,477	3,994,000
Republic Corp.	26,300	285,445	286,000
Rouse Company	440,500	2,060,884	3,414,000
TICOR	313,100	6,599,586	5,910,000
Union Oil Company of California	50,301	2,804,281	2,660,000
		<u>22,100,788</u>	<u>22,836,000</u>
Other securities:			
Kawecki Berylco Industries, Inc.	194,559	2,793,573	3,429,000
RLC Corp. 6¼ % convertible debentures	\$1,266,000	816,582	1,329,000
		<u>3,610,155</u>	<u>4,758,000</u>
		<u>\$25,710,943</u>	<u>\$27,594,000</u>

On July 29, 1977 the Company exchanged its shares of Molycorp, Inc. for 50,301 common shares of Union Oil Company of California. The shares received were valued at \$55.75 per share based on market quotations resulting in an unrealized gain of \$1,982,441.

At December 31, 1978 and 1977 the aggregate market value of the Company's portfolio exceeded cost; the valuation allowances charged to shareholders' equity represents the Company's share of a valuation reserve recorded by the Brazilian joint venture.

The gross unrealized gains were \$4,577,750 and \$3,557,987 and gross unrealized losses were \$364,377 and \$2,822,775 in the Company's marketable equity securities at December 31, 1978 and 1977, respectively. At January 30, 1979 the market value of the marketable equity securities held at December 31, 1978 was \$27,094,000.

All marketable equity securities were pledged as collateral for the Company's bank loan at December 31, 1978.

NOTE 3 — Interest in Brazilian Joint Venture

The Company has a 16.5% interest in Companhia Brasileira de Metalurgia e Mineracao (CBMM). The amounts carried in the balance sheet at December 31, 1978 and 1977 include the cost of the investment plus equity in the undistributed earnings of the joint venture since acquisition, less equity in CBMM's unrealized loss on marketable equity securities. Dividends of \$2,495,500 and \$2,451,903 before withholding taxes were received in 1978 and 1977, respectively.

The Company's interest in CBMM is as follows:

	1978	1977
Equity in net assets	<u>\$12,765,793</u>	<u>\$10,167,578</u>
Equity in net income	\$ 5,175,390	\$ 4,003,230
Provision for withholding taxes ..	<u>1,091,287</u>	<u>916,000</u>
Net equity in CBMM's income	<u>\$ 4,084,103</u>	<u>\$ 3,087,230</u>

Condensed financial statement data for CBMM is as follows:

	1978	1977
Assets	\$83,658,000	\$68,567,000
Liabilities	6,291,000	6,947,000
Net assets	<u>\$77,367,000</u>	<u>\$61,620,000</u>
Sales	<u>\$72,040,000</u>	<u>\$50,443,000</u>
Net income	<u>\$31,366,000</u>	<u>\$24,262,000</u>

The net foreign currency translation loss included in CBMM's net income amounted to US\$8,697,000 in 1978 and US\$6,043,000 in 1977.

Retained earnings of the Company include at December 31, 1978 approximately \$13,602,000 of undistributed earnings of CBMM. Brazilian withholding taxes have been provided on the portion of undistributed earnings of \$2,366,000 which are expected to be realized in the form of dividends. No taxes have been provided with respect to the remaining undistributed earnings of \$11,236,000 which are considered to be indefinitely reinvested in Brazil.

NOTE 4 — Bank Loan

During 1978 maximum short-term borrowings were \$5,400,000. The daily average of such borrowings was \$1,562,000 at a weighted average interest rate of 9.08%. The interest rate on borrowings outstanding at December 31, 1978 was 12.25%.

During 1977 the maximum short-term borrowings were \$5,300,000. The daily average of such borrowings was \$2,179,000 at a weighted average interest rate of 7.6%.

Bank loans outstanding at December 31, 1978 are payable on demand and secured by all marketable equity securities. There are no compensating balance agreements between the Company and the bank.

NOTE 5 — Income Taxes

The provision for income taxes on continuing operations in 1978 and 1977 comprises the following:

	1978	1977
Current provision for income taxes	\$1,149,749	\$1,074,072
Deferred provision for taxes	226,148	21,526
	<u>\$1,375,897</u>	<u>\$1,095,598</u>

NOTE 6 — Discontinued Operations

Effective December 31, 1976 the Company decided to discontinue in 1977 operations of its wholly owned subsidiary, Consolidated Purchasing and Designing, Incorporated (CP&D) a mining consulting and engineering company.

CP&D was sold in May 1977. During 1977 funds were received pertaining to certain assets of CP&D previously written down. The recovery is presented as a gain on the disposal of assets of discontinued operations.

NOTE 7 — Quarterly Financial Information — Unaudited

	(in thousands)			
	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
1978				
Revenues	\$1,632	\$5,117(a)	\$2,409	\$1,685
Expenses	183	82	66	90
Income from continuing operations before income taxes	1,449	5,035	2,343	1,595
Provision for income taxes	233	418	322	403
Net income	<u>\$1,216</u>	<u>\$4,617</u>	<u>\$2,021</u>	<u>\$1,192</u>
Income per share	<u>\$0.35</u>	<u>\$1.32</u>	<u>\$0.57</u>	<u>\$0.34</u>
1977				
Revenues	\$1,265	\$1,504	\$3,854(b)	\$1,370
Expenses	93	157	113	173
Income from continuing operations before income taxes	1,172	1,347	3,741	1,197
Provision for income taxes	244	177	436	239
Income from continuing operations	928	1,170	3,305	958
Gain on disposal of assets of discontinued operations	—	101	—	12
Net income	<u>\$ 928</u>	<u>\$1,271</u>	<u>\$3,305</u>	<u>\$ 970</u>
Income per share	<u>\$0.27</u>	<u>\$0.36</u>	<u>\$0.94</u>	<u>\$0.28</u>

(a) Includes gain of \$2,937,425 on sale of shares of Kawecki Berylco Industries, Inc.

(b) Includes gain of \$1,982,441 on exchange of shares of Molycorp, Inc. for shares of Union Oil Company of California.

NOTE 8 — Event (Unaudited) Subsequent to Date of The Report of Independent Accountants

On March 28, 1979 Southern Pacific Company and Ticor entered into a merger agreement, subject to shareholder approval, wherein each share of Ticor common stock would be exchanged for approximately \$40.00 per share

either in Southern Pacific Company debt securities or, at the option of the holder, a combination of debt securities and cash. If the merger is consummated, Pato expects to report a gain of approximately \$6,600,000.

SUMMARY OF OPERATIONS *(Not covered by Auditor's report)*

	1978	1977	1976	1975	1974
REVENUES					
Equity in net income of Brazilian joint venture	\$ 5,175,390	\$4,003,230	\$5,210,530	\$2,125,785	\$ 3,282,358
Gain (loss) on sale and exchange of securities:					
Kawecki Berylco Industries, Inc.	2,937,425	—	—	—	—
Molycorp, Inc. (Note A)	—	1,982,441	—	—	—
Other, including reserve for possible loss of \$1,479,629 in 1974	1,304,445	1,376,461	3,434,933	(983)	(1,301,596)
Interest income	435,075	96,280	203,333	795,032	603,621
Foreign currency translation gain (loss)	—	—	12,306	(33,676)	(70,394)
Dividends and other income	990,760	534,648	288,977	490,800	250,526
	<u>10,843,095</u>	<u>7,993,060</u>	<u>9,150,079</u>	<u>3,376,958</u>	<u>2,764,515</u>
EXPENSES					
Administrative and general	277,599	369,142	439,473	356,314	254,769
Interest	143,808	165,816	77,066	61,963	125,462
Exploration	—	1,077	119,266	103,708	215,810
	<u>421,407</u>	<u>536,035</u>	<u>635,805</u>	<u>521,985</u>	<u>596,041</u>
Income from continuing operations before income taxes	10,421,688	7,457,025	8,514,274	2,854,973	2,168,474
Provision for income taxes	1,375,897	1,095,598	1,209,570	684,226	539,259
Income from continuing operations	9,045,791	6,361,427	7,304,704	2,170,747	1,629,215
Income (loss) from discontinued operations, net of applicable income taxes (Note B)	—	—	(167,319)	17,568	1,168,445
Net gain on sale or disposal of assets, net of applicable income taxes (Note B)	—	112,597	212,417	—	7,264,330
Net income	<u>\$ 9,045,791</u>	<u>\$6,474,024</u>	<u>\$7,349,802</u>	<u>\$2,188,315</u>	<u>\$10,061,990</u>
Income per share:					
Income from continuing operations	\$2.58	\$1.82	\$2.09	\$0.62	\$0.47
Net income	\$2.58	\$1.85	\$2.10	\$0.62	\$2.87
Average number of shares outstanding	3,502,370	3,502,370	3,502,459	3,502,500	3,502,500
Dividends per share	\$2.00	\$0.50	\$1.18	\$0.45	\$0.51

Notes to Summary of Operations *(Not covered by Auditor's report)*

- (A) On July 29, 1977 the Company exchanged its shares of Molycorp, Inc. for 50,301 common shares of Union Oil Company of California. The shares received were valued at \$55.75 per share based on market quotations resulting in an unrealized gain of \$1,982,441.
- (B) In 1974 the Company sold its Colombian mining assets for \$16,000,000 at a gain of \$7,264,330 net of related income taxes. Of the total proceeds \$12,000,000 was payable in installments through 1979. During 1976 the remaining installments of \$5,493,566 were prepaid. In the fourth quarter of 1976 the Company recorded a credit of \$684,417 representing a reversal of prior tax accruals no longer needed less the write-off of certain remaining assets of the Colombian branch in liquidation and considered unrecoverable.

Effective December 31, 1976 the Company decided to discontinue in 1977 operations of its wholly-owned subsidiary, Consolidated Purchasing and Designing, Incorporated (CP&D) a mining consulting and engineering company. CP&D was sold in May 1977. During 1977 funds were received pertaining to certain assets of CP&D previously written down. The recovery is presented as a gain on the disposal of assets of discontinued operations.

A summary of financial data related to discontinued operations is as follows:

	Colombian Branch	CP&D	Total
1977			
Net gain on sale of assets	\$ —	\$ 112,597	\$ 112,597
1976			
Revenues	\$ 39,750	\$ 327,367	\$ 367,117
(Loss) from operations, net of income tax benefit of \$62,000	\$ (29,569)	\$ (137,750)	\$ (167,319)
Net gain (loss) on sale or disposal of assets:			
Adjustment of gain on sale originally recorded in 1974	\$ 684,417	\$ —	\$ 684,417
Provision for (loss) on disposal of assets	—	(472,000)	(472,000)
	\$ 684,417	\$ (472,000)	\$ 212,417
1975			
Revenues	\$ 76,902	\$ 531,820	\$ 608,722
Income (loss) from operations net of income tax of \$70,000	\$ (83,347)	\$ 100,915	\$ 17,568
1974			
Revenues	\$4,029,515	\$ 332,873	\$4,362,388
Income from operations, net of income taxes of \$782,000	\$1,136,662	\$ 31,783	\$1,168,445
Gain on sale of Colombian assets, net of income taxes of \$915,000	\$7,264,330	\$ —	\$7,264,330

Management Discussion and Analysis of Operations

1978-1977

The increase in earnings for 1978 was attributable to (1) increased equity in the earnings of CBMM reflecting greater demand in the steel industry, (2) higher gains on sales of securities, (3) increases in dividend and interest income, (4) a decrease in administrative and general expense, and (5) lower interest expense reflecting a lower level of bank borrowings in 1978. The increase was partially offset by (1) the increase in taxes on higher equity in net income of CBMM and increased dividend income, and (2) the absence of income from discontinued operations in 1978.

1977-1976

The decline in earnings for 1977 resulted from (1) a decrease in equity in earnings of CBMM due to reduced volume in the steel industry, particularly the production of pipelines, and to increased columbium production by two competitors, (2) lower interest income due to the fact that the balance of the long-term receivable from the sale of the Colombian operations was paid in full at the end of March 1976, (3) lower realized gains on sale of securities in 1977 which were, however, offset partially by a gain of \$1,982,000 on the exchange of shares of Molycorp, Inc. for shares of Union Oil Company of California as a result of the merger of Molycorp into Union Oil on July 29, 1977, and (4) an increase in interest expense reflecting the higher level of bank borrowings in 1977. The decline was partially reduced by (1) an increase in dividend income, (2) a decrease in administrative and general expenses from 1976 which included costs in connection with relocation to Bermuda, (3) a decline in exploration expenditures, and (4) a lower provision for income taxes in line with the decrease in the equity in earnings of CBMM.

1976-1975

The improvement in the earnings for 1976 was principally due to (1) increased equity in the earnings of CBMM reflecting increased demand for columbium and rising prices reversing the decline in the prior year, and (2) substantial capital gains on sales of marketable securities. This improvement was reduced by (1) lower interest income as notes receivable were prepaid in March 1976, (2) decreased dividend income, (3) increased administrative and general expenses including costs in connection with relocation to Bermuda, and (4) increase in taxes on equity in net income of CBMM.

1975-1974

The decline in earnings for 1975 results from (1) lower equity in earnings of CBMM in line with the general decline in economic activity, (2) the continuing inflationary increase in administrative and general expenses including legal expense related to the proposed relocation to Bermuda, (3) higher income taxes, and (4) substantially no income from discontinued operations. The decline was offset by (1) higher interest income, (2) higher dividends reflecting the increased holding of marketable securities, and (3) a decline in exploration expenditures.

FORM 10-K

Shareholders may obtain, without charge, a copy of the Company's current Form 10-K Annual Report to the Securities and Exchange Commission of the United States, upon written request to the Corporate Secretary, P. O. Box 778, Hamilton 5, Bermuda.

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