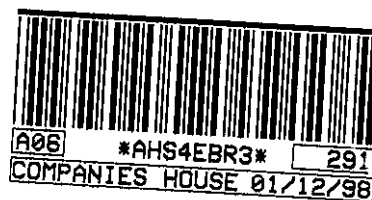


BABCOCK INTERNATIONAL LIMITED

**DIRECTORS' REPORT AND
FINANCIAL STATEMENTS**

for the year ended 31 March 1998

Company number 65805



BABCOCK INTERNATIONAL LIMITED

DIRECTORS AND ADVISORS

DIRECTORS

Dr TJ Parker
NR Young

SECRETARY

J Allen

REGISTERED OFFICE

Badminton Court
Church Street
Amersham
Buckinghamshire
HP7 0DD

AUDITORS

Arthur Andersen
1 Surrey Street
London
WC2R 2PS

BABCOCK INTERNATIONAL LIMITED

DIRECTORS' REPORT for the year ended 31 March 1998

FINANCIAL STATEMENTS

The directors present their report and financial statements for the year ended 31 March 1998.

DIRECTORS' RESPONSIBILITIES

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and the profit or loss for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for maintaining proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

PRINCIPAL ACTIVITY

The principal activity of the company continues to be that of a holding company. The directors do not anticipate any change in the nature of the company's activities during the next financial year.

RESULTS AND DIVIDENDS

The profit after taxation for the year was £2,239,000 (1997: Loss £2,515,000). The directors do not propose a dividend (1997 : NIL).

BABCOCK INTERNATIONAL LIMITED

DIRECTORS' REPORT for the year ended 31 March 1998

DIRECTORS

The members of the Board during the year and since the year end were:

Dr TJ Parker
NR Young (appointed 30 July 1997)
NR Salmon (resigned 31 May 1997)
Sir Frank Gibb (resigned 30 July 1997)
EAS Porter (resigned 30 July 1997)

None of the directors had any beneficial interest in the company's shares. All of the directors are also directors of the ultimate parent company and their interests in the shares of group companies are shown in that company's financial statements.

AUDITORS

Binder Hamlyn, having become part of the Andersen Worldwide organisation in 1994, resigned during the year in order that Arthur Andersen could be appointed. Special notice of the Resolution appointing the Auditors has been given to the Company in accordance with section 388 (1) of the Companies Act 1985.

This report was approved by the Board on 17th November 1998



J Allen
Secretary

AUDITORS' REPORT

to the shareholders of Babcock International Limited

We have audited the financial statements on pages 4 to 15 which have been prepared under the historical cost convention and the accounting policies set out on pages 6 and 7.

Respective responsibilities of directors and auditors

As described on page 1, the company's directors are responsible for the preparation of the financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

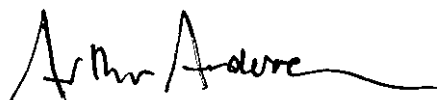
Basis of opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the company, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs as at 31 March 1998 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



Arthur Andersen
Chartered Accountants and Registered Auditors
1 Surrey Street
London, WC2R 2PS

17 November 1998

BABCOCK INTERNATIONAL LIMITED

PROFIT AND LOSS ACCOUNT
for the year ended 31 March 1998

	Notes	1998	1997
		£000	£000
Turnover	2	-	114
Cost of sales		-	(96)
Gross profit		-	18
Administrative expenses	6, 4	(3,626)	(7,912)
Income from fixed asset investments	3	9,171	6,429
Operating profit/(loss)		5,545	(1,465)
Profit/(loss) on ordinary activities before interest		5,545	(1,465)
Net interest	5	(3,940)	(1,844)
Profit/(loss) on ordinary activities before taxation	6	1,605	(3,309)
Tax credit on ordinary activities	9	634	794
Profit/(loss) on ordinary activities after taxation		2,239	(2,515)
Transferred to/(from) reserves	18	2,239	(2,515)


During the year there were no recognised gains and losses other than those dealt with in the profit and loss account. All of the above results derive from continuing activities.

BABCOCK INTERNATIONAL LIMITED

BALANCE SHEET as at 31 March 1998

	Notes	1998	1997
		£000	£000
FIXED ASSETS			
Tangible assets	10	217	181
Investments	11	43,297	33,701
		43,514	33,882
CURRENT ASSETS			
Debtors	12	43,162	46,987
Cash at bank and in hand		3,008	4
		46,170	46,991
CREDITORS: amounts falling due within one year	13	(69,962)	(63,401)
Net current liabilities		(23,792)	(16,410)
Total assets less current liabilities		19,722	17,472
CREDITORS: amounts falling due after more than one year	14	(18,578)	(18,567)
Net assets/(liabilities)		1,144	(1,095)
CAPITAL AND RESERVES			
Called up share capital	17	10,000	10,000
Share premium account		4,632	4,632
Profit and loss account	18	(13,488)	(15,727)
Shareholders' funds - equity interests	19	1,144	(1,095)

The financial statements on pages 4 to 15 were approved by the Board on 17th November 1998


 NR Young
 Director

1 ACCOUNTING POLICIES**Basis of accounting**

The financial statements have been prepared under the historical cost convention and in accordance with applicable United Kingdom accounting standards.

The company has taken advantage of Section 228 of the Companies Act 1985 and has not prepared group financial statements as it is a wholly owned subsidiary undertaking of another company registered in England and Wales.

A cash flow statement has not been prepared as the company is a wholly owned subsidiary undertaking of a company which published consolidated financial statements which included a consolidated cash flow statement.

Fixed asset investments

Fixed asset investments are stated at cost less provisions for permanent diminution in value.

Tangible fixed assets

Tangible fixed assets are stated at cost less depreciation. Depreciation is provided on a straight line basis to write off the cost or valuation of fixed assets over their estimated useful lives at the following annual rates:

Furniture, fittings and equipment	10% to 33.3%
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Deferred taxation

Provision is made for deferred taxation, using the liability method, on all timing differences to the extent that it is probable that a liability will crystallise in the foreseeable future.

Pension

The company is a member of the Babcock International Group pension scheme and has also contributed to certain employees' personal defined contribution pension schemes. Contributions to the group scheme are based on periodic actuarial calculations and are charged so as to spread the cost of pensions over the expected service lives of the employees who are members of the scheme.

Foreign currencies

Transactions denominated in foreign currencies are translated into sterling at the rate of exchange ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the year end exchange rates. Any exchange differences arising are dealt with in the profit and loss account.

BABCOCK INTERNATIONAL LIMITED**NOTES TO THE FINANCIAL STATEMENTS**

1 ACCOUNTING POLICIES *continued***Turnover**

The turnover of the company, derived from the provision of patent registration services, excludes VAT.

Hire purchase contracts

Assets acquired under hire purchase contracts are capitalised and the outstanding capital element of instalments is included in creditors. The interest element is charged against profits so as to produce a constant periodic rate of charge on the outstanding obligations. Depreciation is calculated to write the assets off over their expected useful lives or over the lease terms where they are shorter. Rentals under operating leases are charged to the profit and loss account as incurred.

2	SEGMENTAL INFORMATION	1998	1997
		£000	£000
	The analysis of turnover by geographical market is as follows:		
	United Kingdom	-	107
	North America	-	1
	Rest of Europe	-	6
		-	114

3	INCOME FROM FIXED ASSET INVESTMENTS	1998	1997
		£000	£000
	Dividend received from group companies	9,171	6,429

4 EXCEPTIONAL ITEMS

Included within Administration expenses in 1997 is a provision of £4.0 million against the investment in Babcock King Wilkinson Limited.

BABCOCK INTERNATIONAL LIMITED

NOTES TO THE FINANCIAL STATEMENTS

5	NET INTEREST PAYABLE AND SIMILAR CHARGES	1998	1997
		£000	£000
	Interest receivable	(90)	(25)
	Interest payable on bank borrowings repayable within 5 years	4,030	1,869
		3,940	1,844

6	PROFIT/(LOSS) ON ORDINARY ACTIVITIES BEFORE TAXATION	1998	1997
	is stated after charging:	£000	£000
	Auditors' remuneration		
	- audit services	96	205
	- other services	121	124
	Depreciation		
	- owned assets	33	35
	- assets under lease/HP agreements	68	57
	Operating lease rentals		
	- land and buildings	112	110
	- short term plant hire	13	2

7 DIRECTORS' REMUNERATION
The remuneration of the directors was as follows:

	1998	1997
	£000	£000
Emoluments	858	1,009
Company contributions to money purchase and personal pension schemes	183	244
	<u>1,041</u>	<u>1,253</u>

The above amounts for the remuneration include the following in respect of the highest paid director.

	1998	1997
	£	£
Emoluments	549,818	395,383
Company contributions to money purchase scheme	149,462	132,111
	<u>699,280</u>	<u>527,494</u>

The number of directors who were members of pension schemes was as follows:

Money purchase and personal schemes	4	3
Defined benefit scheme	3	2

The accrued pension entitlement under the company defined benefit scheme of the highest paid director at 31 March 1998 was £6,300 (1997 - £4,987)

BABCOCK INTERNATIONAL LIMITED

NOTES TO THE FINANCIAL STATEMENTS

8 PARTICULARS OF EMPLOYEES

	1998	1997
The average number of persons (including directors) employed by the company during the year was:		
Executive and administration	27	30
<hr/>		
Their total remuneration was:	£000	£000
Wages and salaries	1,476	1,481
Social security costs	166	168
Other pension costs	252	424
	<hr/>	<hr/>
	1,894	2,073
	<hr/>	<hr/>

9 TAXATION

During the year the Babcock International Group has continued its policy of surrendering tax losses and advance corporation tax to group undertakings for no consideration except where there is a minority interest in the subsidiary.

	1998	1997
	£000	£000
UK group relief receivable at 31% (1997 - 33%)	660	797
Prior year adjustment	(26)	(3)
	<hr/>	<hr/>
Taxation credit	634	794
	<hr/>	<hr/>

BABCOCK INTERNATIONAL LIMITED

NOTES TO THE FINANCIAL STATEMENTS

10 TANGIBLE FIXED ASSETS

**Furniture, fittings
and equipment
£000**

Cost	
31 March 1997	469
Additions	180
Disposals	(99)
31 March 1998	550
Depreciation	
31 March 1997	288
Charge for the year	101
Disposals	(56)
31 March 1998	333
Net book value	
31 March 1998	217
31 March 1997	181

Included in the above are assets held under finance leases or hire purchase contracts, with a net book value of £278,000 (1997: £129,000) and a depreciation charge for the year of £68,000 (1997: £57,000).

The company had no capital commitments at 31 March 1998 or at 31 March 1997.

BABCOCK INTERNATIONAL LIMITED
NOTES TO THE FINANCIAL STATEMENTS

11 FIXED ASSET INVESTMENTS

	Shares in subsidiary undertakings
	£000
Cost	
31 March 1997	63,854
Additions	13,596
Disposals	(8,000)
31 March 1998	69,450
Provision for diminution in value	
31 March 1997	(30,153)
Disposals	4,000
31 March 1998	(26,153)
Net book value	
31 March 1998	43,297
31 March 1997	33,701

During the year the company increased its investment in Stirling Boiler Company by £12,650,000 and Babcock Management by £946,000.

Details of the company's principal subsidiary undertakings are given in note 23.

In the opinion of the directors the value of the company's investments in its subsidiary undertakings is not less than the amount at which they are stated in the company's balance sheet.

BABCOCK INTERNATIONAL LIMITED

NOTES TO THE FINANCIAL STATEMENTS

12 DEBTORS	1998 £000	1997 £000
Trade debtors	-	20
Amounts owed by subsidiary undertakings	42,071	45,900
Amounts owed by Associated Undertakings	239	-
Other debtors	147	164
Prepayments and accrued income	43	106
Recoverable taxation	662	797
	43,162	46,987

Included in Amounts Owed by subsidiary undertakings is £500,000 (1997: £500,000) due after more than one year.

13 CREDITORS: amounts falling due within one year	1998 £000	1997 £000
Corporation tax	10	10
Bank overdraft (note 15)	64,905	31,574
Bank loans (note 15)	1,506	4,000
Amounts owed to parent and fellow subsidiary undertakings	-	25,000
Amounts owed to subsidiary undertakings	1,695	1,603
Other creditors	754	675
Accruals and deferred income	1,025	480
Obligations under hire purchase contracts (note 15)	67	59
	69,962	63,401

14 CREDITORS: amounts falling due after more than one year	1998 £000	1997 £000
Obligations under hire purchase contracts (note 15)	109	98
Amounts owed to parent and fellow subsidiary undertakings	18,469	18,469
	18,578	18,567

15 BORROWINGS

The total borrowings of the company are repayable as follows:

	-----1998-----			-----1997-----		
	Bank overdraft £000	Hire purchase contracts £000	Bank loan £000	Bank overdraft £000	Hire purchase contracts £000	Bank Loan £000
Within one year	64,905	67	1,506	31,574	59	4,000
Between two and five years	-	109	-	-	98	-
	64,905	176	1,506	31,574	157	4,000

BABCOCK INTERNATIONAL LIMITED

NOTES TO THE FINANCIAL STATEMENTS

16 DEFERRED TAXATION

	Provided		Potential	
	1998 £000	1997 £000	1998 £000	1997 £000
Short term timing differences	-	-	211	(236)

17 CALLED UP SHARE CAPITAL

	Authorised		Allotted, issued and fully paid	
	Number	£000	Number	£000
31 March 1997 and 31 March 1998 Ordinary 10p shares	155,000,000	15,500	100,000,000	10,000

18 RESERVES

	Profit and loss account £000
1 April 1997	(15,727)
Profit/(Loss) retained for the year	2,239
31 March 1998	(13,488)

19 RECONCILIATION OF MOVEMENT IN SHAREHOLDERS FUNDS

	1998 £000	1997 £000
Retained profit/(loss) for the year	2,239	(2,515)
Shareholders' funds at start of year	(1,095)	1,420
Shareholders' funds at end of year	1,144	(1,095)

BABCOCK INTERNATIONAL LIMITED**NOTES TO THE FINANCIAL STATEMENTS**

20 FINANCIAL COMMITMENTS

	Land and Buildings 1998 £000	Land and Buildings 1997 £000
Operating leases expiring: Within five years	120	108

21 CONTINGENT LIABILITIES

- (a) The company has joint and several liability for bank facilities of £30.0 million (1997: £35.0 million) for certain fellow Babcock International Group companies.
- (b) Throughout the Babcock International Group contingent liabilities exist in respect of guarantees, performance bonds and indemnities issued on behalf of group companies by banks and insurance companies in the ordinary course of business. At 31 March 1998 the company had counter-indemnified £45.4 million (1997: £29.7 million).

22 ULTIMATE PARENT COMPANY

The company's ultimate parent company is Babcock International Group PLC, a company registered in England and Wales. Copies of the Babcock International Group PLC financial statements are available to the public at the following address:

Company Secretary
Babcock International Group PLC
Badminton Court
Church Street
Amersham
Buckinghamshire
HP7 ODD

23 PRINCIPAL SUBSIDIARY AND ASSOCIATED UNDERTAKINGS

Facilities Management Division

Facilities Management Division operates in the defence, maritime, rail and water industries.

Babcock Facilities Management Limited #

Babcock Rosyth Defence Limited

Rosyth Royal Dockyard Limited

Railcare Limited (60%)

Babcock Defence Systems Limited

Babcock Rosyth Industries Limited

Rosyth 2000 Limited (20%)*

Babcock Water Engineering Ltd (50%) **

Others

Including principally Management Holding companies and an Insurance company)

Babcock International Holdings Limited #

Babcock Management Limited #

Cleveland Insurance Limited (Isle of Man)

Babcock Contractors Limited

BMH Limited #

All undertakings are wholly owned unless otherwise stated.

Except as otherwise stated, all shares held comprise ordinary share capital.

All undertakings are incorporated, registered and operated in England and Wales unless otherwise stated. Undertakings located overseas operate principally in the country of incorporation.

Denotes shareholdings held directly by Babcock International Limited

* Denotes associates.

** Denotes joint ventures.

24 PENSION FUNDING

The employees of the company are eligible to join the Babcock Group defined benefit pension scheme. The group scheme is funded by company and employee contributions which are determined with the advice of an independent qualified actuary. Due to the Group scheme being in surplus the Company is currently on a contribution holiday.

Details of the latest valuation of the group pension scheme are contained within the financial statements of Babcock International Group PLC.