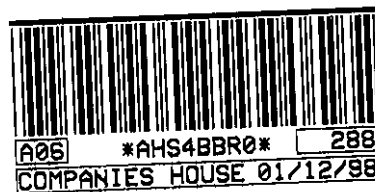


BABCOCK MANAGEMENT LTD

**DIRECTORS' REPORT AND
FINANCIAL STATEMENTS**

for the year ended 31 March 1998

Company number 107414



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

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 of 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 is that of an investment holding company.

RESULTS AND DIVIDENDS

The profit on ordinary activities was £2,265,000 (1997: profit £1,685,000). No dividend is recommended for the year (1997 : £Nil).

DIRECTORS AND THEIR INTERESTS

The directors who, unless otherwise noted, served during the year were as follows:

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

Dr TJ Parker and NR Young were also directors of the ultimate parent company, and their interests in the shares of that company are disclosed in that company's financial statements.

None of the directors had any beneficial interest in the company's own shares.

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

A handwritten signature in black ink, appearing to be 'J Allen', with a large loop at the end.

J Allen
Secretary

AUDITORS' REPORT
to the shareholders of Babcock Management Ltd

We have audited the financial statements on pages 4 to 8 which have been prepared under the historical cost convention and the accounting policies set on page 6.

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.

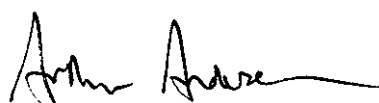
Basis of opinion

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 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 MANAGEMENT LTD
PROFIT AND LOSS ACCOUNT
for the year ended 31 March 1998

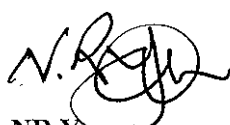
	Notes	1998	1997
		£000	£000
Dividend from joint venture		1,000	-
Administrative expenses		(11)	(4)
Exceptional item - profit on sale of fixed asset investments		-	600
Profit on ordinary activities before interest		989	596
Net interest receivable	2	1,276	1,089
Profit on ordinary activities before taxation		2,265	1,685
Taxation on ordinary activities	3	-	-
Profit on ordinary activities after taxation		2,265	1,685

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. The retained result in both the current and prior years represents the only movements in shareholders' funds.

BABCOCK MANAGEMENT LTD
BALANCE SHEET
as at 31 March 1998

	Notes	1998	1997
		£000	£000
FIXED ASSETS			
Investments	4	10,800	7,500
CURRENT ASSETS			
Debtors	5	12,349	10,509
Cash at bank and in hand		5,669	6,724
		18,018	17,233
CREDITORS: amounts falling due within one year	6	(3,259)	(4,739)
Net current assets		14,759	12,494
Net assets		25,559	19,994
CAPITAL AND RESERVES			
Called up share capital	8	48,000	44,700
Profit and loss account	9	(22,441)	(24,706)
Shareholders' funds - equity interests		25,559	19,994

The financial statements on pages 4 to 8 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. The company 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.

Investments

Fixed asset investments are shown at cost less provision for permanent diminution in value.

2 NET INTEREST RECEIVABLE	1998	1997
	£000	£000
Discount on deferred consideration	840	778
Bank interest receivable	436	311
	1,276	1,089

3 TAXATION

During the year, the Babcock Group has continued its policy of surrendering UK tax losses and advanced corporation tax for no consideration except where there is a minority interest in the subsidiary.

4 INVESTMENTS

The company has a 50% holding in a joint venture, Babcock Water Engineering Limited, and during the year acquired a 60% holding in Railcare Ltd from a fellow subsidiary for consideration of £3,300,060.

The principal activity of Babcock Water Engineering Limited is that of engineering design and the provision of project management services within the water industry. The principal activity of Railcare Limited is that of the repair, maintenance and refurbishment of railway rolling stock.

Both companies are incorporated, registered and operated in England and Wales.

The company has not made a provision against its investments.

5 DEBTORS

	1998	1997
	£000	£000
Dividend due from joint venture	1,000	-
Deferred consideration receivable on sale of investment	11,349	10,509
	12,349	10,509

The deferred consideration of £11.3 million relates to the disposal of the remaining holding of Mitsui Babcock Energy Ltd, of which £4.1million is receivable after more than one year.

6 CREDITORS: amounts falling due within one year

	1998	1997
	£000	£000
Other creditors	3	3
Amounts owed to joint ventures	2,400	3,850
Accruals and deferred income	856	886
	3,259	4,739

7 DEFERRED TAXATION

No provision has been made for deferred taxation as the directors are of the opinion that no liability will crystallise in the foreseeable future.

8 SHARE CAPITAL

	1998	1997
	£000	£000
Authorised:		
50,000,000 (1997: 44,750,000) ordinary shares of £1	50,000	44,750
Allotted, issued and fully paid:		
48,000,075 (1997: 44,700,015) ordinary shares of £1	48,000	44,700

During the year the company increased its authorised share capital by the creation of 5,250,000 new £1 ordinary shares. On 23 January 1998 the company issued 3,300,060 £1 ordinary shares at par to Babcock International Limited as consideration for the purchase of the investment in Railcare Limited.

9 PROFIT AND LOSS ACCOUNT

	£000
At 31 March 1997	(24,706)
Profit for the year	2,265
At 31 March 1998	(22,441)

10 CONTINGENT LIABILITIES

- (a) The Company has joint and several liability for bank facilities of £30.0 million (1997: £35.0 million) in respect of certain fellow Babcock International Group companies.
- (b) Throughout the Babcock International Group, contingent liabilities exist in respect of guarantees, 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 a total of £45.4 million (1997: £29.7 million) in respect of these contingent liabilities.

11 ULTIMATE PARENT COMPANY

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

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