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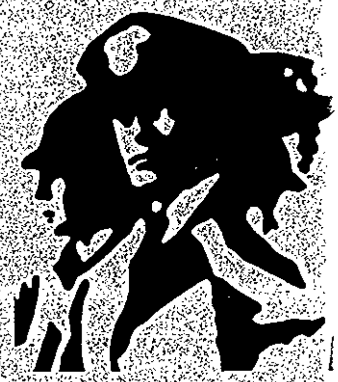

HORACE SMALL APPAREL PLC

annual
report
and
accounts
1996

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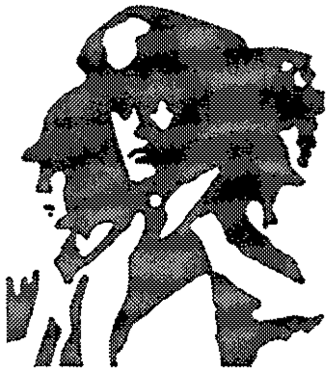

HORACE SMALL APPAREL PLC

Horace Small Apparel is a leading manufacturer and distributor of uniforms in the United States and Canada. Its products are supplied to consumers through its national network of independent distributors, company owned distributors and its unique national account distribution system.

Customers now include federal, state and local government agencies, major private sector commercial, telecommunications and transportation companies, public safety organisations and security forces.

Horace Small Apparel is committed to developing strong customer relationships based on a commitment to service, reliability and value.

CHAIRMAN'S STATEMENT

The company's results for the year ending 31st December 1996 were in line with expectations and showed a modest increase in turnover and profitability.

Our main priority during the year was to continue to identify and implement cost reduction measures in our manufacturing and distribution activities. Considerable progress was made in both areas during the year, resulting in some benefits in 1996 and with the potential for further benefits in future years.

RESULTS

"THE YEAR SAW ENCOURAGING IMPROVEMENT IN MARGINS IN OUR NATIONAL ACCOUNTS AND OUR COMPANY-OWNED DISTRIBUTION BUSINESS."

Turnover for 1996 was £91.3 million ($142.5 million) compared with £80.2 million ($126.6 million) in 1995 and pre-tax profits increased from £3.8 million ($6.0 million) before exceptional charges in 1995, to £4.0 million ($6.3 million). In US dollar terms, which is the basis on which substantially all our operating business is conducted, this represents a year-on-year increase of 12.6% in turnover and 5.1% in pre-tax profits. Earnings per share (adjusted for exceptional charges of £600,000 in 1995) were unchanged at 12.0p for both years. The main reason that earnings per share did not increase in proportion to profits is that we had a tax credit in 1995 of 0.7p per share which reduced to 0.3p in 1996. For 1996 the figures were calculated based on an average exchange rate of $1.561 to the pound ($1.579 in 1995).

OPERATING PERFORMANCE

As we had anticipated, there was a small decline in our gross margin in 1996 arising from our inability to increase prices to fully compensate for our cost increases. This was due entirely to our wholesale business, which had a disappointing year both by falling short of its sales budget and by earning a lower gross margin in a very competitive pricing environment. Corrective actions have been taken including the introduction of our new line of "Tuff Gear" law enforcement apparel and as a result we expect to see increased sales in 1997 and a restoration of margins to prior levels.

The year saw encouraging improvement in margins in our national accounts and our company-owned distribution business. There was a significant sales increase in national accounts. The new BellSouth account made a good initial contribution and there were increased revenues from FedEx and Continental Airlines. There was a small decline in sales at our company-owned distributors, a reflection of the reduced number of outlets. However, to the great credit of the new management group responsible for this business, there was an improvement in gross margin together with a reduction in operating expenses. As a result, the overall profit contribution from this activity was much better than in prior years.

Our efforts to identify opportunities for lower cost manufacturing continued throughout the year. Our project to re-engineer our Bassfield facility to flexible response production techniques was completed on schedule and within budget and we will realise the benefits in 1997. We also reached agreement in January 1997 to lease a new sewing facility in Brownsville, Texas, and initial production is scheduled for April. We expect that by year end this facility will be operating at a level which will produce significant cost savings in 1998.

We are closing our sewing plant in Guthrie, Kentucky which will cease operations in May 1997 with all production being transferred to Brownsville. We expect to take provisions and other charges related to the closure of Guthrie and start-up costs in Brownsville of an amount anticipated not to exceed £1.3 million ($2.0 million).

We have also continued to invest considerable effort and money in upgrading and expanding our MIS capabilities. Maintaining a leadership position in this area is critical to our having a competitive edge in our national accounts business as well as improving the internal control of our business.

I am pleased to report that cash flow from operations enabled us to reduce bank debt by approximately $6 million during the year and further reduction is expected by the end of 1997.

FINANCIAL YEAR END

We have decided to change the company's financial year-end to 30th September. Accordingly, our next financial accounting period will be for the nine months ending 30th September 1997. The principal reason for this change is that the three months ending December are by far our busiest period and taking year-end inventory places considerable strains on our business. After reviewing the alternatives, we have concluded that September is the most efficient time for us to make our physical inventory count and close our annual accounts. We will report our results for the six months ending 30th June 1997 in the normal way and, thereafter, we will move to September and March reporting periods.

FUTURE PROSPECTS

I said last year that our future success depends on our ability to improve our cost competitiveness, thereby enabling us to add profitable new business as well as retaining our existing customer base, and improving the performance of our company-owned distributors. The agenda remains the same. I believe that we have made considerable progress towards achieving our goals, with the most important element being the decision to establish the Brownsville operation.

"...WE HAVE MADE CONSIDERABLE PROGRESS TOWARDS ACHIEVING OUR GOALS..."

CHAIRMAN'S STATEMENT

"...WE ANTICIPATE A SIGNIFICANT IMPROVEMENT IN PROFITABILITY IN FISCAL 1998."

Due to the fact that we traditionally earn approximately sixty per cent of our operating profits in the three months ending December, we expect to show no more than a small profit for the nine month fiscal period ending 30th September 1997, particularly after taking into account the one-time charges related to the closure of Guthrie and start-up costs in Brownsville. Nonetheless, prior to such charges we are hopeful of a modest improvement in turnover and underlying profits compared to the corresponding nine months in 1996. Based on the benefits we expect from our manufacturing restructuring programme, we anticipate a significant improvement in profitability in fiscal 1998.

Our employees have responded to the challenges we face with hard work and enthusiasm and I would like to thank them all for their contribution. I would also like to thank all shareholders for their continuing support and to express my hope and belief that their patience will be rewarded.

J Colin Keith
CHAIRMAN

PRESIDENT'S REPORT

Our performance in 1996 gives us reasonable cause for satisfaction. Whilst not uniformly good across the board, most sectors of our business did better than in the previous year: our national accounts produced strong revenue growth, and our company-owned distributors produced a turnaround to show a considerable advance on 1995.

Our one area of disappointment was in wholesale where sales fell short of budget and competitive pricing pressures had a negative impact on margins. However, we are confident that greater flexibility in production and a series of new products will improve this situation in 1997.

ONE COMPANY

During the year we took steps to reinforce our 'one company' philosophy. In 1995 we established four strategic business units - national accounts, wholesale, manufacturing and company-owned distributors - which clearly identified the areas in which we operate. It was in part a recognition that different markets demanded separate and clearly focused attention and a range of specialist skills. The next stage has been to strengthen the lines of communication between each group, utilising common services wherever possible, bringing together aspects of manufacturing, product sourcing, purchasing, financial reporting and marketing services in order to maximise the economies of scale that flow from such unity.

Our identity in the market place is also being more sharply defined through the introduction of a new company logo in which R & R, the name applied to our company-owned distributors and national accounts, is directly linked with Horace Small. This clearly establishes the connection between the two names while presenting a more up-to-date image.

NATIONAL ACCOUNTS

The national accounts team produced excellent results with a 33% improvement in sales and a 55% advance in operating profits. These margins were due to a combination of increased business through existing accounts and the addition of one major new uniform programme.

BellSouth - the new account - is one of America's largest telecommunications companies. A significant factor in the success of this programme has been the ability of our Nashville facility to handle the distribution, enabling us to make increasingly efficient use of existing resources. We are focusing on leveraging the Ft. Worth (American Airlines) and Montreal (Air Canada) distribution centres in a similar manner to Nashville.

"THE NATIONAL ACCOUNTS TEAM PRODUCED EXCELLENT RESULTS WITH A 33% IMPROVEMENT IN SALES AND A 55% ADVANCE IN OPERATING PROFITS."

"THE TURNAROUND IN PERFORMANCE OF OUR COMPANY-OWNED DISTRIBUTORS HAS BROUGHT GREAT CREDIT UPON EVERYONE INVOLVED."

FedEx, one of our largest National Accounts programmes, experienced an excellent growth year with the introduction of a new uniform image. Our Memphis distribution centre with responsibility for this programme has just been awarded the international quality standard certification IS09002. We intend to bring our other distribution centres up to this standard in the future.

The success of our uniform distribution programmes in air transport, courier services, and telecommunications, encourages us to seek further business in these and other major US industries.

COMPANY-OWNED DISTRIBUTORS

The turnaround in performance of our company-owned distributors has brought great credit upon everyone involved. Eighteen months ago they were causing concern with a few outlets performing well but the majority producing disappointing results.

In 1996, a senior vice president was appointed to direct this operation, followed by continued strengthening of the management team. Individual managers were given greater autonomy in the running of their stores: empowered to make decisions, determine inventory mix within designated levels, and effectively run their own businesses. We analysed the strengths and weaknesses of each outlet: costs, inventory, locations and the size and type of display areas. New cost controls and a cap on administrative expenses brought significant improvements in profit levels.

Our Charlotte and Dallas stores both suffered the twin handicaps of an unsatisfactory location and business conducted on multiple floors. Their subsequent moves to new locations brought them the advantages of operation on a single level, a more favourable location and much improved prospects. Similar action is to be taken with the Houston, Philadelphia and Richmond outlets.

Further savings are being achieved through our storefront programme. This concept allows for a store presence in a smaller community with the major order processing done in a regional distribution centre. Our Raleigh store was the first beneficiary of this plan with total store area cut from 15,000 square feet to 3,000 square feet and most distribution moved to the Charlotte store. This has brought substantial savings, and similar actions are currently being reviewed in several of our smaller store locations.

The combination of management changes, relocation to better sites, and quicker delivery have boosted morale, brought new levels of confidence, improved efficiency and substantially advanced the future prospects of our company-owned distributors.

WHOLESALE

The wholesale business is product and relationship driven and success depends on a strong relationship driven sales force combined with the right merchandise.

In response to market requirements, a new line of outerwear will be introduced in 1997. The new outerwear collection includes a range of easy-care, lightweight jackets with interchangeable liners which give exceptional warmth and protection even in the most extreme weather conditions. Employing state-of-the-art materials with unique insulation properties, these jackets give full protection against wind, rain and temperatures as low as -30°F.

Another new line, Tuff Gear, was introduced in late October at a meeting of the International Association of Police Chiefs, the largest exhibition of its kind. Tuff Gear is a tactical dress uniform designed to meet the more rigorous requirements of police work and utilises a new synthetic fabric that feels like wool and has the ability to breath like wool. These wool-like capabilities allow the fabric to function well in both hot and cold conditions.

We are confident these new products developed to meet the requirements of an ever-changing and competitive marketplace will bring the wholesale business back to the strong position of 1994-1995.

MANUFACTURING

Our entire manufacturing processes required a radical change in our production methods if we were to meet our inventory targets and maintain customer service levels. Team based quick response was the method we selected, but this required an intensive programme of retraining and the purchase of additional machinery.

Training, which took more than a year, was completed in our Bassfield shirt plant in November, and those concerned are to be congratulated on their success in carrying this through while, at the same time, maintaining normal production schedules. The result is that we now have a team-based, multi-skilled workforce capable of handling a range of production tasks with a throughput time reduced from six weeks to two weeks.

Our new production unit in Brownsville, considerably larger than the Bassfield plant, will add significantly to our manufacturing capabilities. Under previous ownership, this unit operated as a sewing facility for more than 20 years. It has skilled workers operating in a team based quick response mode with a throughput time of less than two weeks. We have retained some of the machinery, appointed a supervisory staff and re-employed 150 of the former workforce which is approximately the same number we employ in Bassfield. There is scope for significant expansion in the future for Brownsville as demand increases.

"...WE NOW HAVE A TEAM-BASED, MULTI-SKILLED WORKFORCE CAPABLE OF HANDLING A RANGE OF PRODUCTION TASKS..."

"THE RESURGENCE OF COMPANY-OWNED STORES IS EXPECTED TO TAKE THEM TO IMPROVED LEVELS OF PROFITABILITY."

We continue to expand our sourcing organisation whose task is to select and supervise outside contractors capable of manufacturing products to our specification. This is an increasingly important function because there are many items unsuited to our manufacturing lines which can be produced more efficiently elsewhere.

CORPORATE DEVELOPMENTS

Activity throughout Horace Small is now permeated by our 'one company' vision, and developments within each department have been directed towards promoting this philosophy.

New corporate services have been introduced and others have been reorganised. Changes in the finance department, with all credit functions reporting to one corporate treasurer, brought substantial results in accounts receivable collection in 1996. An inventory planning group now monitors stock levels throughout the company and has developed inventory audit functions. New management has been appointed to run information services and a comprehensive review of all our information systems is being conducted by EDS, a world leader in this field, with the objective of recommending further improvements.

NEXT YEAR

Our future plans are now clearly defined, based on the successful initiatives of the past year. Our 'one company' philosophy has brought real, practical benefits which show up on the balance sheet and will be pursued wholeheartedly in 1997. Further cash flow improvements will be sought through inventory and accounts receivable management.

A build-up in manufacturing facilities will take place at both Bassfield and Brownsville, with particular emphasis on the latter. We plan to expand our wholesale business through sales of Tuff Gear and new outerwear products and are hopeful of increased police business resulting from major participation in a police mail order catalogue. The resurgence of company-owned stores is expected to take them to improved levels of profitability. We are now pursuing several new opportunities to expand our national accounts business.

I congratulate everyone on the real progress made during the past year. Much has been accomplished, attitudes are positive, team spirit is improving and efficiency levels are on the rise. The stage is set for further advances in 1997.

Robert W. Gates, Jr.

Robert W. Gates, Jr.
PRESIDENT AND CHIEF OPERATING OFFICER

FINANCIAL REVIEW

Since the group conducts substantially all of its operations in the United States and substantially all of its assets, liabilities, revenues and expenses are denominated in US dollars, all amounts included in this Financial Review are in US dollars, except for earnings per share, which are denominated in pence sterling. Also, all amounts are before the impact, where applicable, of exceptional charges of $0.9 million incurred in 1995 for costs of an aborted merger and final payments due under a terminated employment contract.

The effects of exchange rate movements on sterling results were not significant in relation to the profit and loss account and cash flow statement as the average exchange rate of $1.561 in 1996 moved less than 1% from $1.579 in 1995. The year end exchange rates in relation to the group balance sheet showed a more significant movement of approximately 10% to $1.712 in 1996 from $1.554 in 1995 reflecting the strengthening of the pound during the latter part of 1996.

RESULTS OF OPERATIONS

Turnover increased 13% to $142.5 million in the year ended 31st December 1996 from $126.6 million in 1995. A 33% increase in sales to national accounts contributed virtually all of the year-to-year growth as wholesale sales increased only 3% and sales from company-owned distributors declined 3%. Decreased sales in the company-owned distributors were primarily the result of a reduced number of outlets.

First year sales from the new BellSouth account combined with growth in sales to FedEx, Continental Airlines and the federal government agencies accounted for the increase in the national account business.

Gross profit increased 12% to $44.6 million in 1996 from $40.0 million in 1995 primarily as a result of the increase in group turnover and improved gross margins from company-owned distributors and national accounts. However, the group gross profit margin declined from 31.6% to 31.3% because of a lower gross margin from wholesale sales and increased costs in the company's manufacturing operation. Competitive pressures prevented the company from raising prices to fully cover the cost increases.

Group operating expenses increased at the same rate as sales growth which, when combined with the decrease in the gross margin, resulted in a decline in the operating margin to 6.1% in 1996 compared to 6.5% in 1995.

Company-owned distributors reduced operating expenses through streamlining the sales and marketing effort, improving operating efficiencies and significantly reducing administrative expenses. Operating expenses in national accounts increased at a rate slightly less than the rate of sales growth reflecting economies of scale realized from the increased business handled by the Nashville and Memphis distribution facilities. Increased wholesale operating expenses disproportionate to sales growth are indicative of the efforts required in response to the competitive environment.

The group's pre-tax profit increased 5% to $6.3 million in 1996 from $6.0 million before exceptional charges in 1995. As a percentage of sales, pre-tax profits declined to 4.4% in 1996 from 4.7% in 1995 which was in line with the decline in the operating margin. Interest expense increased 12% in 1996 compared to the prior year as average bank borrowings were higher in the year to finance working capital requirements in the start-up of the new national accounts. However, by year-end 1996, bank debt was $5.9 million less than the prior year-end.

The group recorded a $0.1 million US tax credit in 1996 compared to a $0.4 million credit in 1995. Tax losses available for offset against future profits subject to United States Federal taxation now stand at approximately $13.7 million.

Profits after tax were virtually unchanged in 1996 from 1995 and adjusted earnings per share were 12.0p in both years.

RESTRUCTURING PROGRAMME

In 1996, utilization of the accrual for restructuring costs was almost entirely the result of expenditures for the project to re-engineer the Bassfield manufacturing facility to flexible response production techniques. At 31st December 1996, the remaining accrual balance was $0.6 compared to $1.6 million at year-end 1995 and an original total of $6.6 million. It is expected that this balance will be utilized in 1997 in the continuing effort to implement the manufacturing cost reduction and restructuring strategy.

CASH FLOW AND FINANCING

Net cash provided by operating activities was $10.5 million compared to cash used of $9.0 million in 1995. Reduction of working capital requirements for new national accounts was the primary reason for this significant improvement in cash flow.

Trade debtors decreased $3.8 million in 1996 compared to an $8.8 million increase in 1995 primarily as a result of a $6.0 million decrease in balances due from national account programmes begun in 1995 compared to a $7.7 million increase in the same account balances during 1995. Stock balances increased $3.1 million in 1996 compared to a $7.0 million increase in 1995. The increase in both years was primarily for new national account contracts and sales growth of existing programmes serviced by the national account business.

During 1996, the company reduced its bank borrowing by $5.9 million. Internally generated funds and availability under bank credit facilities at current levels will provide necessary capital for the start-up of the Brownsville manufacturing facility, seasonal working capital requirements and the group's capital expenditure programme in 1997.

Richard B Vacek, Jr.
FINANCE DIRECTOR

DIRECTORS' REPORT

The directors have pleasure in submitting their report together with the audited accounts for the year ended 31st December 1996.

Activities

The company's principal operating subsidiary undertaking, Horace Small Manufacturing Company ("Horace Small"), and its subsidiary undertakings together are integrated manufacturers and distributors of fitted uniforms and corporate clothing as well as being distributors of accessories and equipment. Horace Small currently serves US Federal (non-military), State and Local Government agencies, a number of safety and security work forces and a range of large and small corporations.

A detailed review of the business and future prospects is contained in the Chairman's Statement, the President's Report and the Financial Review on pages 2 to 11.

Results

The results for the year are set out in the profit and loss account. The profit on ordinary activities after taxation amounted to £4,112,000 (1995 - £3,414,000).

Dividends and transfers to reserves

The directors are not recommending the payment of a dividend (1995 - nil).

Substantial interests

At the date of this report the company has been notified of the following substantial interests in the shares of the company:

	No. of shares	%
North Atlantic Smaller Companies Investment Trust PLC	4,400,000	12.8
Second Consolidated Trust PLC	4,083,110	11.9
Seaway Ltd	4,081,100	11.9
Douglas Small	1,977,573	5.8
Schroder Unit Trusts Limited*	1,975,000	5.8
Credit Suisse Smaller Companies Fund	1,710,000	5.0
Cumberland Partners	1,115,000	3.3

*Schroder Unit Trusts Limited is a wholly owned subsidiary of Schroder investment Management Limited. The company has been informed that in total Schroder Investment Management Limited in its capacity as discretionary portfolio manager has an interest in 4,587,600 shares representing 13.4% of the issued share capital.

Directors

The directors who held office during the year were as follows:

J. Colin Keith (Chairman), Richard B. Vacek, Jr., Robert W. Gates Jr., The Hon. William D.Eberle, Christopher H. B. Mills, R. James P. Morton, Irvin L. Small, Paul G. Dumond (appointed 8th May 1996) and Douglas A. Small (retired 8th May 1996).

In accordance with the Articles of Association, Mr J. Colin Keith and The Hon. William D. Eberle retire by rotation at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election.

Supplier payment policy

It is Horace Small's policy to negotiate payment terms with its suppliers and to ensure that they know the terms on which payment will take place when business is agreed. It is Horace Small's policy to abide by these terms.

Close company status

So far as is known the company is not, and has not been, a close company as defined by the Income and Corporation Taxes Act 1988.

Auditors

A resolution to reappoint Arthur Andersen as auditors will be proposed at the forthcoming Annual General Meeting.

Masters House
107 Hammersmith Road
London W14 0QH

7th April 1997

By order of the Board
Paul G. Dumond
Secretary

CORPORATE GOVERNANCE

Directors' Statement on Corporate Governance Matters

Following the publication in December 1992 of the Code of Best Practice by the Committee on the Financial Aspects of Corporate Governance, the Board has reviewed the company's compliance during the year ended 31st December, 1996. The Code covers four broad areas, namely the composition and procedures of the Board of Directors, the appointment and role of non-executive directors, the service contracts and pay of executive directors and the directors' responsibilities with respect to financial reporting and controls. The Code contains nineteen specific provisions in respect of these four areas.

The company has complied throughout the year with the Code except that non-executive directors are not appointed for specific terms. However, the board periodically reviews their performance and effectiveness.

Internal financial control

The Board of Directors has overall responsibility for ensuring that the group maintains a system of internal financial control to provide them with reasonable assurance regarding the reliability of financial information used within the business and for publication and that assets are safeguarded. There are inherent limitations in any system of internal financial control and accordingly even the most effective system can provide only reasonable, and not absolute, assurance with respect to the preparation of financial information and the safeguarding of assets.

The key features of the internal financial control system that operated throughout the period covered by the accounts are described under the following headings:

Management information systems	Incorporating planning, budgeting and forecasting systems and a monthly review of actual results compared with budget.
Group controls	Common accounting systems and controls are in place throughout the group and are monitored on a regular on-going basis.
Organisation	There are well structured financial and administrative functions at both head office and operational level staffed by appropriately qualified personnel. The key functions include: *Group accounting* *Corporate planning and group treasury* *Legal and company secretarial* *Group taxation* All functions report to the Board of Directors on a regular basis to provide assurance that their respective areas of responsibility are adequately controlled.
Monitoring procedures	All aspects of internal financial control are considered and monitored regularly by the Board of Directors and the Audit Committee.

Going concern

After making enquiries, the directors have a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Directors' responsibilities

Company law requires the directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the company and group and of the profit or loss of the group for that period. In preparing those accounts, 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 accounts; and
- prepare the accounts on the going concern basis unless it is inappropriate to presume that the group will continue in business.

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

Auditors' responsibilities
Company law requires auditors to form an independent opinion on the accounts presented by the directors based on their audit and to report their opinion to the shareholders. The Companies Act 1985 also requires auditors to report to the shareholders if the following requirements are not met:

- that the companies in the group have maintained proper accounting records;
- that the accounts are in agreement with the accounting records;
- that directors' emoluments and other transactions with directors are properly disclosed in the accounts; and
- that the auditors have obtained all the information and explanations which, to the best of their knowledge and belief, are necessary for the purpose of their audit.

The auditors' opinion does not encompass the directors' report on pages 12 and 13. However, the Companies Act 1985 requires auditors to report to the shareholders if the matters contained in the directors' report are inconsistent with the accounts.

Remuneration committee report
The members of the remuneration committee during the year were The Hon. William D. Eberle (Chairman), Christopher H. B. Mills and Irvin L. Small.

The group's policy on the granting of share options is to motivate and reward key management that are in a position to influence the future of the group. The share options are issued at the discretion of the Remuneration Committee, subject to a maximum of 10% of the issued share capital. There are no group performance requirements attached to the grant of the options. Options under the U.S. scheme which comprise the substantial majority of those outstanding at the year end are exercisable between the third and tenth anniversaries of the date of grant.

The group has complied throughout the year with Section A "Remuneration Committees" of the best practice provisions on directors' remuneration annexed to the Listing Rules of the London Stock Exchange. In framing the group's remuneration policy, the committee has given full consideration to the provisions of Section B "Remuneration Policy, Service Contracts and Compensation" also annexed to those rules.

The group's policy on executive directors remuneration is to provide remuneration packages to attract, retain and motivate executive directors of the quality required taking into account the levels paid by comparable companies and the relative performance of those companies. These packages principally comprise a basic salary, which is reviewed annually, a performance related bonus and executive share options. The performance related element of remuneration for the executive directors is directly related to the profitability of the group and to their performance compared with individual achievement goals.

J. Colin Keith and The Hon. William D. Eberle are being proposed for re-election at the forthcoming Annual General Meeting. Neither J. Colin Keith nor The Hon. William D. Eberle have service contracts with any group company.

Full details of the remuneration packages of the individual directors and information on share options and the executives' performance related bonus scheme are set out in note 4 to the accounts.

REPORT BY THE AUDITORS TO HORACE SMALL APPAREL PLC ON CORPORATE GOVERNANCE MATTERS

Report by the Auditors on Corporate Governance Matters
In addition to our audit of the accounts, we have reviewed the directors' statement on page 14 concerning the company's compliance with the paragraphs of the Cadbury Code of Best Practice specified for our review by the London Stock Exchange and their adoption of the going concern basis in preparing the financial statements. The objective of our review is to draw attention to non-compliance with Listing Rules 12.43(j) and 12.43(v).

We carried out our review in accordance with guidance issued by the Auditing Practices Board. That guidance does not require us to perform the additional work necessary to, and we do not, express any opinion on the effectiveness of either the company's system of internal financial control or its corporate governance procedures nor on the ability of the company and group to continue in operational existence.

Opinion
With respect to the directors' statement on internal financial control and going concern on page 14, in our opinion the directors have provided the disclosures required by the Listing Rules as referred to above and such statements are not inconsistent with the information of which we are aware from our audit work on the accounts.

Based on enquiry of certain directors and officers of the company, and examination of relevant documents, in our opinion the directors' statement on page 14 appropriately reflects the company's compliance with the other aspects of the Code specified for our review by Listing Rule 12.43(j).

Arthur Andersen

Arthur Andersen
Chartered Accountants
London

7th April 1997

AUDITORS' REPORT

To the shareholders of Horace Small Apparel PLC

We have audited the accounts on pages 17 to 34 which have been prepared under the historical cost convention and the accounting policies set out on pages 21 and 22.

Respective responsibilities of directors and auditors
As set out on pages 14 and 15 the company's directors are responsible for the preparation of the accounts. It is our responsibility to form an independent opinion, based on our audit, on those accounts 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 accounts. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the circumstances of the company and group, 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 accounts 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 accounts.

Opinion
In our opinion the accounts give a true and fair view of the state of affairs of the company and group as at 31st December 1996 and of the group's profit and cash flows for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Arthur Andersen

Arthur Andersen
Chartered Accountants and Registered Auditors
London

7th April 1997

GROUP PROFIT AND LOSS ACCOUNT

FOR THE YEAR ENDED 31ST DECEMBER, 1996

	Notes	1996 £000	1995 £000
Turnover	1	**91,307**	80,160
Cost of sales		**(62,707)**	(54,831)
Gross profit		**28,600**	25,329
Distribution costs		**(11,917)**	(10,835)
Administrative expenses - Normal		**(11,195)**	(9,420)
- Exceptional		–	(600)
Other operating income		**126**	122
Operating profit	2	**5,614**	4,596
Interest receivable and similar income		**24**	13
Interest payable and similar charges	5	**(1,614)**	(1,424)
Profit on ordinary activities before taxation		**4,024**	3,185
Taxation on profit on ordinary activities	6	**88**	229
Retained profit for the year		**4,112**	3,414
Earnings per share:			
Basic earnings per share	7	**12.0p**	10.2p
Adjustment for exceptional items		–	1.8p
Adjusted earnings per share	7	**12.0p**	12.0p
Average exchange rate applied	£1=	**$1.561**	$1.579

Movements on reserves are set out in note 15.

The accompanying notes are an integral part of these accounts.

GROUP BALANCE SHEET

AT 31ST DECEMBER, 1996

	Notes	1996 £000	1995 £000
Fixed assets			
Tangible assets	8	**10,864**	11,198
Current assets			
Stocks	10	**26,449**	27,124
Debtors	11	**15,943**	20,813
Cash at bank and in hand		**363**	1,087
		42,755	49,024
Creditors: amounts falling due within one year	12	**(15,651)**	(13,777)
Net current assets		**27,104**	35,247
Total assets less current liabilities		**37,968**	46,445
Creditors: amounts falling due after more than one year	13	**(10,939)**	(20,752)
Net assets		**27,029**	25,693
Capital and reserves			
Called up share capital	14	**1,714**	1,714
Share premium account	15	**20,881**	20,881
Exchange translation reserve	15	**(5,538)**	(2,762)
Profit and loss account	15	**9,972**	5,860
Shareholders' funds	16	**27,029**	25,693
Year end exchange rate applied	£1=	**$1.712**	$1.554

As approved by the Board of Directors on 7th April 1997 and signed on its behalf by:

J. Colin Keith
Richard B. Vacek, Jr. } Directors

The accompanying notes are an integral part of these accounts.

COMPANY BALANCE SHEET

AT 31ST DECEMBER, 1996

	Notes	1996 £000	1995 £000
Fixed assets			
Investments	9	**45,260**	45,475
Current assets			
Debtors	11	**48**	45
Cash at bank and in hand		**–**	27
		48	72
Creditors: amounts falling due within one year	12	**(576)**	(462)
Net current liabilities		**(528)**	(390)
Net assets		**44,732**	45,085
Capital and reserves			
Called up share capital	14	**1,714**	1,714
Share premium account	15	**20,881**	20,881
Special reserve	15	**17,296**	17,296
Profit and loss account	15	**4,841**	5,194
Shareholders' funds		**44,732**	45,085

As approved by the Board of Directors on 7th April 1997 and signed on its behalf by:

J. Colin Keith
Richard B. Vacek, Jr. } Directors

GROUP STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

FOR THE YEAR ENDED 31ST DECEMBER, 1996

	1996 £000	1995 £000
Profit on ordinary activities after taxation	**4,112**	3,414
Currency translation differences on foreign currency net investments	**(2,776)**	208
Total gains recognised since previous balance sheet date	**1,336**	3,622

The accompanying notes are an integral part of these accounts.

GROUP CASH FLOW STATEMENT

FOR THE YEAR ENDED 31ST DECEMBER, 1996

	Notes	1996 £000	1995 £000
Net cash inflow (outflow) from operating activities	20a	**6,723**	(5,679)
Returns on investments and servicing of finance	20b	**(1,703)**	(1,347)
Taxation	20b	**(58)**	(21)
Capital expenditure and financial investment	20b	**(1,856)**	(2,051)
Cash inflow (outflow) before financing		**3,106**	(9,098)
Financing - Issue of shares (net of expenses)	20b	**–**	2,599
Financing - (Decrease) increase in debt	20b, c	**(3,789)**	6,422
		(3,789)	9,021
(Decrease) in cash in the year	20c	**(683)**	(77)

The accompanying notes are an integral part of these accounts.

NOTES TO THE ACCOUNTS

1. ACCOUNTING POLICIES

The accounts have been prepared under the historical cost convention and in accordance with applicable Accounting Standards. The following paragraphs describe the principal policies, all of which have been applied consistently throughout the current and preceding years.

The accounting policies of some overseas subsidiary undertakings do not conform with UK Accounting Standards and, where appropriate, adjustments are made on consolidation in order to present the group accounts on a consistent basis.

Basis of consolidation

The group accounts include the accounts of the company and all of its subsidiary undertakings at any time during the financial year. All group undertakings make up their accounts to 31st December annually. The results of subsidiary undertakings and businesses acquired during the year are included from the date of acquisition. The results of subsidiary undertakings and businesses disposed of during the year are included to the date of their disposal. Goodwill arising on consolidation is written off to reserves on acquisition.

By virtue of Section 230(4) of the Companies Act 1985, the company is exempt from presenting a profit and loss account.

Turnover

Turnover comprises invoiced sales of fitted uniforms, corporate clothing, accessories and equipment, excluding sales taxes. Advances on contract sales are recorded as deferred income and released to turnover only when the goods are dispatched.

The directors are of the opinion that the group operates in one unified segment, the manufacture of uniforms and the distribution of uniforms and accessories. All turnover arose in North America. Turnover by destination is not materially different from that by origin.

Tangible fixed assets

Property and equipment are stated at cost.

Depreciation and amortisation is provided in order to write off assets on a straight line basis over their estimated useful lives as follows:

Buildings and leasehold improvements	25 years
Plant, machinery and vehicles	4 to 10 years
Furniture, fixtures and fittings	5 to 10 years
Freehold land is not depreciated	

Leases

Assets held under finance leases are initially reported at the fair value of the asset, with an equivalent liability categorised as appropriate under creditors due within or after one year. The asset is depreciated over the shorter of the lease term and its useful economic life. Finance charges are allocated to accounting periods over the period of the lease to produce a constant rate of return on the outstanding balance. Rentals are apportioned between finance charges and reduction of the liability, and allocated to cost of sales and other operating expenses as appropriate.

Annual rentals payable in respect of operating leases are charged to the profit and loss account on a straight line basis over the lease term.

Investments

Fixed asset investments are shown at cost less amounts written off. No provision is made for temporary fluctuations in value. Income is included in the accounts for the year in which it is receivable.

Stocks

Stocks are valued at the lower of first-in first-out cost and net realisable value. The valuation of work-in-progress and finished goods includes the cost of direct materials and labour, plus a reasonable proportion of manufacturing overheads based on normal levels of activity.

NOTES TO THE ACCOUNTS

1. ACCOUNTING POLICIES (continued)

Set up and start up costs attributable to long term contracts
Incremental costs that are directly attributable to the set up of new facilities and systems required to service long term National Account contracts are capitalised and shown under debtors. The costs are normally amortised over the term of the contract as follows:

i) one half is amortised on a straight line basis over the first twelve months following the commencement of full shipping operations; and

ii) the balance is amortised on a straight line basis over a period not exceeding the term of the contract commencing with the first anniversary of full shipping operations.

Deferred taxation
Provision is made, at rates expected to be in force at the time of reversal, for taxation deferred in respect of all material timing differences to the extent that, in the opinion of the directors, there is a reasonable probability that the liability will arise in the foreseeable future (the liability method).

Foreign currencies
Foreign currency transactions are converted at the rate of exchange ruling at the date of the transaction or translated at the year end rate in the case of transactions not then finalised. Assets and liabilities denominated in foreign currencies at the year end are expressed in sterling at the rate of exchange ruling at that date. The results of United States subsidiary undertakings have been translated into sterling at the average rate of exchange for the year.

Currency adjustments are included in trading profits except that the difference arising on the retranslation of the group's share of the net assets of overseas subsidiary undertakings at the beginning of the year, or on acquisition if later, is treated as a movement on reserves.

Pensions
Entry to Horace Small's pension scheme was closed during 1993 and there is no longer a regular pension cost charged to the profit and loss account. Independent actuarial valuations on a going concern basis are carried out annually and the resultant actuarial surplus or deficit is spread in the profit and loss account over the average remaining service lives of employees, currently estimated at 8.5 years.

2. OPERATING PROFIT

	1996 £000	1995 £000
This is stated after charging:		
Auditors' remuneration	92	91
Other fees paid in the UK to the auditors	7	12
Exceptional charge for payments to Douglas Small and associated payroll taxes	–	450
Exceptional charge arising from the termination of proposed merger	–	150
Depreciation of tangible fixed assets:		
Owned	937	779
Held under finance leases	135	148
Loss on disposal of tangible fixed assets	17	–
Hire of plant and machinery and motor vehicles under operating leases	307	395
Payments under operating leases – premises	1,203	1,030

3. EMPLOYEES

The monthly average number of employees was made up as follows:	1996 Number	1995 Number
Production	**765**	804
Warehousing and distribution	**460**	437
Sales	**120**	112
Administration	**50**	48
	1,395	1,401

All employees, including executive directors, are employed in North America.

Staff costs, including directors' remuneration during the year comprised:	£000	£000
Salaries and wages	**19,036**	18,346
Social security costs	**1,645**	1,623
Other pension credits (note 19a)	**(13)**	(25)
	20,668	19,944

4. DIRECTORS' REMUNERATION AND INTERESTS

Directors' remuneration

Name of Director	Fees £000	Basic salary and other emoluments £000	Taxable benefits £000	Prior year performance related bonus £000	Profit sharing retirement plan £000	1996 total £000	1995 total £000
Executive							
J. C. Keith	5	35	–	–	–	**40**	40
R. W. Gates, Jr.	5	115	12	17	4	**153**	159
R. B. Vacek, Jr.	5	99	11	15	4	**134**	139
D. A. Small *(retired 8th May, 1996)*	2	88	6	–	3	**99**	295
Non-executive							
W. D. Eberle	5	5	–	–	–	**10**	10
C. H. B. Mills	5	25	–	–	–	**30**	30
R. J. P. Morton	5	5	–	–	–	**10**	10
I. L. Small	5	5	–	–	–	**10**	10
P. G. Dumond *(appointed 8th May, 1996)*	3	3	–	–	–	**6**	–
Aggregate emoluments	40	380	29	32	11	**492**	693

The emoluments of the chairman, J. C. Keith, totalled £40,000 (1995 – £40,000). The emoluments of the highest paid director for services rendered in the UK in the year totalled £30,000 (1995 – £30,000).

4. DIRECTORS' REMUNERATION AND INTERESTS (continued)

The emoluments of all directors, excluding pension contributions, fell within the following ranges:

	1996 Number	1995 Number
£5,001 - £10,000	4	3
£25,001 - £30,000	1	1
£35,001 - £40,000	–	1
£40,001 - £45,000	1	–
£95,001 - £100,000	1	–
£130,001 - £135,000	1	–
£135,001 - £140,000	–	1
£150,001 - £155,000	1	–
£155,001 - £160,000	–	1
£290,001 - £295,000	–	1

Executives' performance related bonuses

The executive directors, excluding J. C. Keith, are entitled to participate in a management bonus pool which is available to all of the group's senior management. The level of each director's bonus is determined in the year following the year to which the bonus relates.

Directors' interests

The aggregate emoluments disclosed above do not include any amounts for the value of options to subscribe for ordinary shares in the company granted to or held by the directors. Details of the options are as follows:

	31st December, 1996	31st December, 1995	Date of grant	Exercise price
Directors:				
R. W. Gates, Jr.	102,300	102,300	30th May, 1990	122.19p
	20,460	20,460	24th September, 1992	68.43p
	25,000	25,000	7th June, 1995	106.00p
	100,000	100,000	26th September, 1995	98.00p
	33,000*	–	13th May 1996	88.00p
R. B. Vacek, Jr.	102,300	102,300	30th May, 1990	122.19p
	20,460	20,460	24th September, 1992	68.43p
	20,000	20,000	7th June, 1995	106.00p
	33,000*	–	13th May 1996	88.00p
J. C. Keith	409,200	409,200	13th July, 1993	68.43p
	90,800	–	12th December, 1996	84.00p
W. D. Eberle	102,300	102,300	30th May, 1990	122.19p
C. H. B. Mills (UK scheme)	409,200	409,200	30th May, 1990	122.19p
R. J. P. Morton	102,300	102,300	30th May, 1990	122.19p
I. L. Small	102,300	102,300	3rd November, 1992	70.38p
P. G. Dumond	15,345	15,345	30th May, 1990	122.19p

*Options granted during the year.

4. DIRECTORS' REMUNERATION AND INTERESTS (continued)

Options granted under the company's US Stock Option Plan may be exercised between the third and tenth anniversaries of the date of grant.

Options granted under the company's UK Executive Share Option Scheme may be exercised between the third and seventh anniversaries of the date of grant.

Since the year end there have been no changes in the numbers of options held by directors or their exercise prices.

The directors' beneficial interests in the share capital of the company, are set out below:

	Ordinary Shares of 5p each	
	At 31st December, 1996	At 31st December, 1995
J. C. Keith	**505,000**	330,000
R. W. Gates, Jr.	**144,967**	144,967
R. B. Vacek, Jr.	**30,178**	30,178
W. D. Eberle	**–**	–
C. H. B. Mills	**168,000**	168,000
R. J. P. Morton	**158,000**	151,000
I. L. Small	**106,911**	81,911
P. G. Dumond (appointed 8th May, 1996)	**–**	–

Since the year end, there have been no changes in the holdings shown above.

5. INTEREST PAYABLE AND SIMILAR CHARGES

	1996 £000	1995 £000
Interest on bank loans and overdrafts	**1,590**	1,400
Interest on finance leases	**15**	13
Other interest	**9**	11
	1,614	1,424

6. TAXATION ON PROFIT ON ORDINARY ACTIVITIES

	1996 £000	1995 £000
UK Corporation tax charge at 33%	**–**	–
US Federal tax credit	**88**	229
Total tax credit	**88**	229

At 31st December, 1996 the group had tax losses of approximately $13.7 million (1995 - $15.3 million) available for offset against future profits subject to United States Federal taxation. The losses begin to expire in 2006.

No deferred taxation has been provided and no potential liability arises in the group or company due to the availability of tax losses to offset reversals of other short term timing differences and the excess of the book value of tangible assets over their tax value.

7. EARNINGS PER SHARE

The calculation of the basic earnings per share is based on the profit after tax of £4,112,000 (1995 - £3,414,000) and on the average number of ordinary shares in issue during the year of 34,281,526 (1995 - 33,367,922). The adjusted earnings per share in 1995 is based on adjusted profits after tax of £3,989,000 after excluding exceptional charges totalling £575,000, net of taxation.

The fully diluted earnings per share are not materially different from the basic earnings per share.

8. TANGIBLE ASSETS

The Group

	Freehold property £000	Long leasehold property £000	Plant, machinery & vehicles £000	Furniture, fixtures & fittings £000	Total £000
Cost					
At 1st January, 1996	1,468	5,982	5,471	1,710	14,631
Additions	4	310	1,338	210	1,862
Disposals	–	–	(9)	(29)	(38)
Exchange movement	(134)	(577)	(625)	(177)	(1,513)
At 31st December, 1996	1,338	5,715	6,175	1,714	14,942
Depreciation					
At 1st January, 1996	64	722	2,070	577	3,433
Charge for the year	13	149	731	179	1,072
Disposals	–	–	(3)	(13)	(16)
Exchange movement	(9)	(79)	(255)	(68)	(411)
At 31st December, 1996	68	792	2,543	675	4,078
Net book value					
At 31st December, 1996	1,270	4,923	3,632	1,039	10,864
At 31st December, 1995	1,404	5,260	3,401	1,133	11,198
Leased assets included in the above: **Net book value**					
At 31st December, 1996	–	4,541	205	–	4,746
At 31st December, 1995	–	5,260	6	–	5,266

Freehold property includes freehold land with a book value of £947,000 (1995 - £1,043,000) which is not being depreciated. Long leasehold property includes land, with a book value of £1,655,000 (1995 - £1,823,000), which is not being depreciated as the group has an option to acquire the freehold of the property for a nominal sum at any time prior to the year 2008.

9. FIXED ASSET INVESTMENTS

	The Company	
	1996 £000	1995 £000
Investment in subsidiary undertakings at cost	**41,000**	41,000
Long term loans to subsidiary undertakings	**4,260**	4,475
	45,260	45,475
Movements in the year comprise:		
Issue of shares by subsidiary undertakings for cash	–	2,509
Increase in loans to subsidiary undertakings	**217**	64
Exchange movement on long term loans	**(432)**	26
	(215)	2,599

The company's principal subsidiary undertakings are set out below:

Company	Proportion and class of shares held	Country of incorporation and operation	Principal activity during the year
Horace Small Holdings Corporation of Delaware, Inc.[1]	100% common stock	USA	Holding company
Horace Small Holdings Corporation[2]	100% common stock	USA	Holding company
Horace Small Manufacturing Company[3]	100% common stock	USA	Manufacture and distribution of fitted uniforms and corporate clothing
Greenbrier Garment Company[4]	100% common stock	USA	Manufacture of fitted uniforms and corporate clothing
R&R Uniforms, Inc.[4]	100% common stock	USA	Distribution of uniforms
R&R Uniforms of Florida, Inc.[5]	100% common stock	USA	Distribution of uniforms

[1] Held by Horace Small Apparel PLC
[2] Held by Horace Small Holdings Corporation of Delaware, Inc.
[3] Held by Horace Small Holdings Corporation
[4] Held by Horace Small Manufacturing Company
[5] Held by R&R Uniforms, Inc.

A full list of subsidiary undertakings will be included in the company's annual return.

10. STOCKS

	The Group	
	1996 £000	1995 £000
Raw materials	**3,996**	2,812
Work-in-progress	**1,068**	1,907
Finished goods	**21,385**	22,405
	26,449	27,124

Finished goods comprise stocks of uniforms, clothing and accessories held for resale. The replacement cost of stock is not considered to be materially different from the balance sheet value.

11. DEBTORS

	The Group		The Company	
	1996 £000	1995 £000	**1996 £000**	1995 £000
Amounts falling due within one year:				
Trade debtors	**14,525**	18,418	**–**	–
Amounts owed by subsidiary undertakings	**–**	–	**13**	8
Other debtors	**214**	160	**–**	–
Value added tax recoverable	**16**	18	**16**	18
Prepayments and accrued income	**256**	830	**19**	19
	15,011	19,426	**48**	45
Amounts falling due after more than one year:				
Other debtors	**13**	17	**–**	–
Overseas tax	**–**	88	**–**	–
Prepayments and accrued income	**604**	672	**–**	–
Deferred start up costs	**315**	610	**–**	–
	932	1,387	**–**	–
	15,943	20,813	**48**	45

12. CREDITORS: amounts falling due within one year

	The Group		The Company	
	1996	1995	**1996**	1995
	£000	£000	**£000**	£000
Bank Loans and overdrafts	**4,567**	–	**3**	–
Obligations under finance leases	**72**	10	**–**	–
Payments received on account	**146**	322	**–**	–
Trade creditors	**7,912**	8,261	**–**	–
Amounts owed to subsidiary undertakings	**–**	–	**460**	379
Other creditors	**45**	34	**–**	–
UK corporation tax	**3**	4	**3**	4
Overseas tax	**229**	373	**–**	–
Accruals	**2,677**	4,773	**110**	79
	15,651	13,777	**576**	462

At the end of 1993 the group embarked upon a programme to restructure its operations, the estimated costs of which were provided for in the 1993 accounts. The restructuring programme is continuing and £0.35 million (1995 - £1.0 million) of the original charges remain within accruals at 31st December, 1996 to be utilised as the planned actions are completed. The bank loans, which are unsecured and drawn on the SunTrust Bank, are repayable by 31st December 1997 and bear interest at the bank's base rate plus 0.25% to 1.0% or US dollar LIBOR plus 2.0% to 3.25%

13. CREDITORS: amounts falling due after more than one year

	The Group	
	1996	1995
	£000	£000
Obligations under finance leases:		
Payable over one to two years	**77**	8
Payable over two to five years	**100**	65
Payable over five years	**67**	69
Bank loans:		
Payable over one to two years	**6,840**	15,178
Payable over two to five years	**3,186**	3,510
Payable over five years	**531**	1,755
Other creditors:		
Payable over two to five years	**117**	138
Payable over five years	**21**	29
	10,939	20,752

The bank loans, which are unsecured, are drawn under a revolving credit facility of $15 million from the SunTrust Bank, Nashville, N.A. and a term loan of $10 million from Creditanstalt. The SunTrust Bank facility bears interest, at the group's option, at either the bank's base rate to the bank's base rate plus 0.75% or US dollar LIBOR plus 1.75% to 3.0% and the Creditanstalt facility bears interest, at the group's option, at either base rate plus 0.25% to 1.0% or US dollar LIBOR plus 2.0% to 3.25%.

14. CALLED UP=HARE CAPITAL

(a) Share Capital

This comprises ordinary shares of 5 pence each as follows:

	Authorised		Allotted, called up and fully paid	
	No. of shares	£000	No. of shares	£000
At 1st January, 1996	45,000,000	2,250	34,281,526	1,714
At 31st December, 1996	50,000,000	2,500	34,281,526	1,714

(b) Options

The following options, including those detailed in note 4, granted under the UK Executive Share Option Scheme and the US Stock Option Plan, were outstanding at 31st December:

Date of Grant	Price per fully paid share	**1996 Number of ordinary shares**	1995 Number of ordinary shares
30th May, 1990	122.19p	**557,538**	1,155,993
30th May, 1990 (UK scheme)	122.19p	**567,765**	567,765
26th June, 1992	84.07p	**96,165**	108,953
24th September, 1992	68.43p	**40,920**	40,920
3rd November, 1992	70.38p	**102,300**	102,300
30th November, 1992	79.18p	**51,150**	51,150
13th July, 1993	68.43p	**409,200**	409,200
8th November, 1993	62.56p	**51,150**	51,150
15th August, 1994	82.11p	**71,612**	89,515
7th June, 1995	106.00p	**127,500**	165,500
26th September, 1995	98.00p	**100,000**	100,000
18th December, 1995	91.00p	**30,000**	30,000
13th May, 1996	88.00p	**415,000**	–
18th December, 1996	84.00p	**145,800**	–
		2,766,100	2,872,446

Options granted under the company's US Stock Option Plan may be exercised between the third and tenth anniversaries of the date of grant.

Options granted under the company's UK Executive Share Option Scheme may be exercised between the third and seventh anniversaries of the date of grant.

No options were exercised during the year. Options held to acquire up to 667,146 shares lapsed during the year.

The market price of the ordinary shares at 31st December, 1996 was 84.5p and the range during 1996 was 74.5p to 101.0p.

15. RESERVES

	Share Premium £000	Exchange Translation Reserve £000	Profit and Loss Account £000	Total £000
Group				
At 1st January, 1996	20,881	(2,762)	5,860	23,979
Profit for the year	–	–	4,112	4,112
Currency translation differences	–	(2,776)	–	(2,776)
At 31st December, 1996	20,881	(5,538)	9,972	25,315

	Share Premium £000	Special Reserve £000	Profit and Loss Account £000	Total £000
Company				
At 1st January, 1996	20,881	17,296	5,194	43,371
Loss for the year	–	–	(353)	(353)
At 31st December, 1996	20,881	17,296	4,841	43,018

At 31st December, 1996 the profit and loss account of the company included £4,257,000 (1995 - £4,643,000) of unrealised exchange gains on the translation of amounts denominated in US dollars advanced to subsidiary undertakings. Accordingly, the distributable reserves of the company at 31st December, 1996 totalled £584,000 (1995 - £551,000).

Of the group profit for the year, a loss of £353,000 (1995 - loss £50,000) has been dealt with in the accounts of the company.

At 31st December, 1996 the cumulative amount of goodwill resulting from acquisitions which had been written off to reserves, net of goodwill attributable to subsidiary undertakings or businesses disposed of, amounted to £22,436,000 (1995 - £22,436,000).

16. RECONCILIATION OF MOVEMENT IN SHAREHOLDERS' FUNDS

	The Group	
	1996 £000	1995 £000
Profit on ordinary activities after taxation	**4,112**	3,414
Issue of new ordinary shares	–	2,599
Currency translation differences on foreign currency net investments	**(2,776)**	208
Net movement of shareholders' funds	**1,336**	6,221
Shareholders' funds at the beginning of the year	**25,693**	19,472
Shareholders' funds at the end of the year	**27,029**	25,693

17. OPERATING LEASE COMMITMENTS

Commitments under leases to pay rentals during the year following the year of these accounts, analysed by year of expiry of each lease, are given in the tables below:

	1996 £000	1995 £000
Operating leases – land and buildings:		
Within one year	135	59
From one to five years	581	574
Over five years	271	319
	987	952
Operating leases – other assets:		
Within one year	57	82
From one to five years	134	120
Over five years	8	–
	199	202

18. CAPITAL COMMITMENTS

Capital commitments at 31st December, 1996 which had been contracted for but not provided for in these accounts totalled £256,000 (1995 - £79,000).

19. PENSION AND RETIREMENT ARRANGEMENTS

(a) Horace Small operates a funded defined benefit pension scheme for certain US employees.

Entry to this scheme was closed on 30th June, 1993; however, previous contributions remain in the trust funds to pay vested retirement benefits. The group plans to make no contributions to the pension scheme in the future, unless independent professionally qualified actuaries, in their annual review of the scheme, determine a payment is necessary to fund vested benefits.

The pension cost and related prepayment are assessed in accordance with the advice of the actuaries under the principles of US Accounting Standards. The projected unit credit actuarial cost method is used to determine the normal cost of the pension plan and estimate pension benefit obligations. In the most recent actuarial valuation the main assumptions were that (a) salaries would increase by 3.0% p.a., (b) pensions in payment remain constant, and (c) the return on scheme investments would be 8.0% p.a.

The market value of the assets of the scheme at 31st December, 1996 was £3,142,000 (1995 - £3,348,000) and the actuarial value of the assets was sufficient to cover 103% of the benefits that had accrued to members after allowing for expected future increases in earnings.

The pension credit for the year, reflecting the benefit of amortisation of the actuarial surplus, was £13,000 (1995 - credit £25,000). No contributions were paid to the scheme during the year (1995 - nil). Prepaid contributions of £299,000 (1995 - £317,000) at the year end are shown in the balance sheet under 'Prepayments'. The directors consider that no material adjustment would arise if these amounts were revised to reflect UK Accounting Standards, the expense of which exercise is therefore not justified.

(b) The Horace Small Profit Sharing Retirement Plan includes a profit sharing component, made at the group's discretion, for all eligible employees. Horace Small also contributes amounts equal to one-half of the employees' contribution up to a maximum of 3% of covered wages. The total charge for the year was £348,000 (1995 - £394,000).

20. NOTES TO THE GROUP CASH FLOW STATEMENT

a) Reconciliation of operating profit to operating cash flows

	1996 £000	1995 £000
Operating profit	5,614	4,596
Depreciation charges	1,072	927
Loss on sale of fixed assets	17	–
(Increase) in stocks	(2,004)	(4,411)
Decrease (increase) in debtors	3,236	(6,874)
(Decrease) increase in creditors and provisions	(1,348)	62
Other translation adjustments	136	21
Net cash inflow (outflow) from operating activities	6,723	(5,679)

b) Analysis of cash flows

Returns on investments and servicing of finance	1996 £000	1995 £000
Interest received	24	13
Interest paid	(1,705)	(1,338)
Interest element of finance lease rentals	(22)	(22)
Net cash outflow	(1,703)	(1,347)
Taxation		
UK corporation tax paid (including ACT)	(1)	(14)
Overseas tax paid	(57)	(7)
Net cash outflow	(58)	(21)
Capital expenditure and financial investment		
Purchase of tangible fixed assets	(1,862)	(2,057)
Sale of tangible fixed assets (proceeds)	6	6
Net cash outflow	(1,856)	(2,051)
Financing		
Issue of ordinary share capital (rights offering)	–	2,599
(Decrease) Increase in other loans	(7,609)	111
Increase in unsecured loan	3,844	6,333
Capital element of finance lease rental payments	(24)	(22)
Net cash (outflow) inflow	(3,789)	9,021

20. NOTES TO THE GROUP CASH FLOW STATEMENT (continued)

c) Analysis and reconciliation of net debt

	1st January 1996 £000	Cash flow £000	Other non-cash changes £000	Exchange movement £000	31st December 1996 £000
Cash at bank and in hand	1,087	(683)		(41)	363
Debt due after 1 year	(20,443)	3,765	5,008	1,113	(10,557)
Debt due within 1 year	–	–	(5,008)	441	(4,567)
Finance leases	(152)	24	(220)	31	(317)
Net debt	(19,508)	3,106	(220)	1,544	(15,078)

	1996 £000	1995 £000
(Decrease) in cash in the year	**(683)**	(77)
Cash outflow (inflow) from increase/decrease in debt and lease financing	**3,789**	(6,422)
Change in net debt resulting from cash flows	**3,106**	(6,499)
New finance leases	**(220)**	–
Translation difference	**1,544**	(197)
Movement in net debt in the year	**4,430**	(6,696)
Net debt at 1st January	**(19,508)**	(12,812)
Net debt at 31st December	**(15,078)**	(19,508)

21. POST BALANCE SHEET EVENT

In January 1997 agreement was reached to lease a new sewing facility in Brownsville, Texas and production will begin in April 1997. The company is closing its sewing plant in Guthrie, Kentucky which will cease operations in May 1997 with all production transferring to Brownsville. Provisions and other charges related to the closure of Guthrie and start-up costs in Brownsville are anticipated not to exceed £1.3 million.

CORPORATE INFORMATION

US OFFICES	350 28th Avenue North P.O. Box 1269 Nashville, Tennessee 37202-1269, USA Tel: (615) 320 1000 Fax: (615) 327 1912
LONDON OFFICE AND REGISTERED ADDRESS	Masters House 107 Hammersmith Road London W14 0QH Tel: 0171 603 1515 Fax: 0171 603 8448
COMPANY NUMBER:	153088
SECRETARY	Paul G. Dumond
BANKERS	SunTrust Bank, Nashville, N.A. 201 Fourth Avenue North, Nashville, Tennessee 37244, USA Creditanstalt Two Ravinia Drive, Suite 1680, Atlanta, Georgia 30346, USA
AUDITORS	Arthur Andersen 1 Surrey Street, London WC2R 2PS
LEGAL ADVISORS	Boult, Cummings, Connors & Berry 414 Union Street, Suite 1600 Nashville, Tennessee 37219, USA Ashurst Morris Crisp 5 Appold Street, London EC2A 2HA
REGISTRARS	Independent Registrars Group Limited Broseley House, Newlands Drive Witham, Essex CM8 2UL
STOCKBROKERS	Collins Stewart & Company 21 New Street, London EC2M 4HR
ADR DEPOSITARY	Bank of New York ADR Division 101 Barclay Street, 22nd Floor New York, New York, 10286, USA

DIRECTORS

J. Colin Keith (Chairman and Chief Executive)

Colin Keith, aged 52, was appointed a non-executive Director in April 1993, Chairman in June 1993 and Chief Executive in March 1996. He currently serves as Chairman of Denison International Limited, a private international group engaged in the manufacture and distribution of hydraulic pumps and valves. He is also a non-executive director of Scholl PLC.

Robert W. Gates, Jr. (President and Chief Operating Officer)(USA)

Robert Gates, aged 50, was one of the founders of R&R Uniforms and has served as its President since its inception in 1972. He became President and Chief Operating Officer of Horace Small in March 1996.

Richard B. Vacek, Jr. (Finance Director)(USA)

Richard Vacek, aged 48, became a Certified Public Accountant in 1973. Prior to joining Horace Small in July 1989, he spent over 15 years in various financial management positions in the health care industry.

Paul G. Dumond (Company Secretary)

Paul Dumond, aged 41, has served as Company Secretary since 1990 and was appointed a non-executive director in May 1996. He is also a director of Mid-States PLC and was Finance Director of Aberdeen Petroleum PLC from 1987 to 1993.

The Hon. William D. Eberle (USA)*†

The Hon. William Eberle, aged 73, was appointed a non-executive Director in June 1990. He served as a Special Trade Representative during the Nixon and Ford administrations. A director of various U.S. corporations, he was a founder of Boise Cascade and served as Chairman and Chief Executive Officer of American Standard. He is currently Deputy Chairman of Mid-States PLC and Vice Chairman of the US Council of the International Chamber of Commerce.

Christopher H.B. Mills*†

Christopher Mills, aged 44, was appointed a non-executive Director in January 1988. He is Managing Director of North Atlantic Smaller Companies Investment Trust PLC and American Opportunity Trust PLC. He is also chairman of Paramount plc and a director of a number of other publicly listed companies.

R. James P. Morton*

James Morton, aged 43, was appointed a non-executive Director in May 1990. He is a director of European American Securities Inc. He is also a director of Knox d'Arcy plc and of a number of private companies.

Irvin ('Jimmy') L. Small (USA)†

Jimmy Small, aged 68, the son of the founder, Horace Small, joined his father in 1950. He was Chief Executive Officer from 1962 until 1989 and President from 1962 until 1986. He is a past president of the National Association of Uniform Manufacturers and Distributors and is widely respected within the uniform industry. He retired from Horace Small in 1992 after 42 years, but remains a non-executive Director of the company.

* Member of the Audit Committee

† Member of the Remuneration Committee

ANNUAL GENERAL MEETING

The Company's Annual General Meeting will be held at the offices of JO Hambro & Company Ltd, 10 Park Place, London SW1 1LP on Wednesday 21st May 1997 at 2.00pm. The Notice of Meeting follows, and sets out the business to be transacted. An explanation of each of the resolutions follows below.

ORDINARY BUSINESS

Resolutions 1 and 2: Re-election of Directors

The Company's Articles of Association require that every year, a third of the directors retire from office and, where appropriate, seek re-election. This year, Mr J. Colin Keith and The Hon. William D. Eberle retire in this way and resolutions 1 and 2 are for their re-election.

Resolution 3: Reappointment of Auditors

The Company's Auditors are required to be reappointed at every Annual General Meeting. Resolution 3 is for the reappointment of Arthur Andersen and, in accordance with normal practice, to authorise the Directors to fix their remuneration.

SPECIAL BUSINESS

Resolution 4: Allotment of Relevant Securities

This is an ordinary resolution to renew the authority granted to the directors at last year's Annual General Meeting to allot relevant securities in terms of Section 80 of the Companies Act 1985, up to an aggregate nominal amount of £571,358.

Resolution 5: Disapplication of Pre-emption Rights

Resolution 5 is a special resolution which would renew the power granted to the directors at last year's Annual General Meeting to disapply the statutory pre-emption rights under section 95 of the Companies Act 1985 thus overcoming certain technical difficulties that may arise in connection with a rights issue or grant of options. It also permits issues of the company's share capital for cash, other than pro-rata to shareholders, up to an aggregate nominal value of £85,703. This represents approximately 5% of the ordinary share capital currently in issue.

Resolution 6: Authority to Buy Back the Company's Own Shares

This is a special resolution to renew the authority granted at last year's Annual General Meeting for the company to buy back its own shares. No purchases will be made unless the effect is expected to increase earnings per share and the directors consider the purchases to be in the interests of shareholders generally. The proposed authority will be limited by the terms of the resolution to purchases of up to 3,428,152 ordinary shares (representing approximately 10% of the share capital of the company currently in issue) made through The Stock Exchange at prices not exceeding 105% of the average of the middle market quotations derived from The London Stock Exchange Daily Official Listing for the ten business days before each purchase.

NOTICE OF MEETING

Notice is hereby given that the Annual General Meeting of Horace Small Apparel PLC will be held at the offices of JO Hambro & Company Ltd, 10 Park Place, London SW1 1LP on Wednesday 21st May, 1997 at 2.00pm.

Agenda

1. To re-elect Mr J. Colin Keith as a director.

2. To re-elect The Hon. William D. Eberle as a director, who is also a member of the Remuneration Committee, special notice having been given pursuant to Sections 379 and 293(5) of the Companies Act 1985 of the intention to propose the following as an ordinary resolution:
That The Hon. William D. Eberle who has attained the age of 73 years be re-elected a director of the Company.

3. To reappoint the auditors and authorise the directors to fix their remuneration.

4. Special Business: To consider and, if thought fit, approve the following Ordinary Resolution:
That the directors be and they are hereby generally and unconditionally empowered, in place of all existing authorities under Section 80 of the Companies Act 1985, to exercise all powers of the company to allot relevant securities (within the meaning of Section 80 of the Companies Act 1985) up to an aggregate nominal amount of £571,358 provided that this authority shall expire on the earlier of the date of the next Annual General Meeting and 20th August, 1998, save that the company may before such expiry make an offer or agreement which would or might require relevant securities to be allotted after such expiry and the board may allot relevant securities in pursuance of such an offer or agreement as if the authority conferred hereby had not expired.

5. Special Business: To consider and, if thought fit, approve the following Special Resolution:
That subject to the passing of the previous resolution the directors be and they are hereby generally and unconditionally authorised to exercise all powers of the company to allot equity securities (within the meaning of Section 94(2) of the Companies Act 1985), as if Section 89(1) of the Companies Act 1985 did not apply to such allotment, provided that this authority shall:

(i) expire on the earlier of 20th August, 1998 and the date of the next Annual General Meeting of the company save that the directors may allot equity securities under this authority after the expiry thereof pursuant to any offer or agreement made by the company on or before such expiry date pursuant to this authority as if such authority had not expired; and

(ii) be limited to the allotment of equity securities:

(a) in connection with a rights issue or any other pre-emptive offer concerning equity securities in the company where it is, in the opinion of the directors, necessary or expedient to allot equity securities otherwise than in accordance with Section 89 of the Companies Act 1985 by reason of the rights attached to any shares or securities of the company or in relation to fractional entitlements or legal or practical problems under the laws of or the requirements of any recognised regulatory body or stock exchange in any territory; and

(b) pursuant to the terms of any stock option plan or share option scheme or other plan for employees and/or executive or non-executive directors approved by the company in General Meeting, up to an aggregate nominal value of £171,400; and

(c) otherwise than pursuant to sub-paragraphs (a) and (b), up to an aggregate nominal value not exceeding £85,703.

NOTICE OF MEETING (continued)

5. Special Business: To consider and, if thought fit, approve the following Special Resolution:

That the company is hereby generally and unconditionally authorised to make market purchases (within the meaning of section 163 of the Companies Act 1985) of ordinary shares of 5p each in the capital of the company ("Ordinary Shares") with effect from the conclusion of this meeting provided that:

(a) the maximum aggregate number of Ordinary Shares authorised to be purchased is 3,428,152;

(b) the minimum price which may be paid for each such Ordinary Share is 5p;

(c) the maximum price (inclusive of expenses) which may be paid for each such Ordinary Share is an amount equal to 105 per cent of the average of the middle market quotations as derived from The London Stock Exchange Daily Official List for the ten business days immediately preceding the day on which such Ordinary Share is purchased; and

(d) the company may make a contract to purchase its Ordinary Shares under this authority prior to the expiry thereof, which will or may be executed wholly or partly after the expiry of such authority, and may make a purchase of its Ordinary Shares pursuant to any such contract.

The authority will expire at the conclusion of the next Annual General Meeting of the company, or, if earlier, 20th August, 1998.

By order of the Board
Paul G. Dumond
Secretary

7th April 1997

Note:

Any member entitled to attend and vote at the meeting may appoint one or more proxies to attend and, on a poll, to vote instead of him or her. A proxy need not be a member of the company. A form of proxy is enclosed which, to be effective, must be deposited with the company's registrars, Independent Registrars Group Limited, Balfour House, 390/398 High Road, Ilford Essex, 1G1 1NQ not later than 48 hours before the time appointed for the holding of the meeting. The register of directors' interests together with copies of any service contracts for periods in excess of one year between each director and the company are available for inspection at the Registered Office during normal business hours and at the place of the meeting from 15 minutes prior to the meeting until its conclusion.

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