

Racal Electronics Plc  
ANNUAL REPORT & ACCOUNTS

1998

**RACAL**



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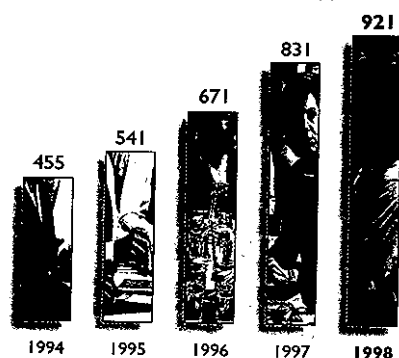
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# Financial Highlights

At 31 March 1998

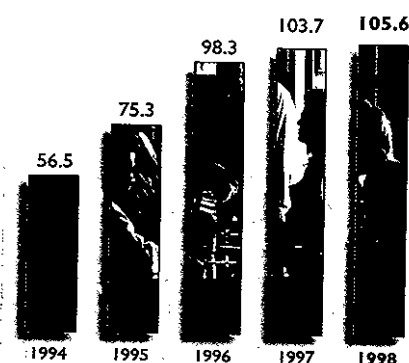
## Turnover (£m)

Ongoing operations



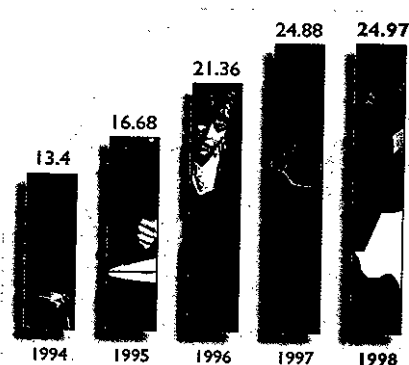
## Operating profit (£m)

Ongoing operations



## Earnings per share (p)

Adjusted



	1998 £m	1997 £m	% change
Turnover			
Ongoing operations	<b>920.7</b>	830.8	+10.8%
Operating profit			
Ongoing operations			
Before reorganisation costs	<b>115.6</b>	106.4	+8.7%
as % of sales	<b>12.6%</b>	12.8%	
After reorganisation costs	<b>105.6</b>	103.7	+1.8%
as % of sales	<b>11.5%</b>	12.5%	
Exceptional items	<b>(224.5)</b>	(19.3)	
(Loss)/profit before taxation	<b>(207.2)</b>	40.4	
(Loss)/earnings per share			
FRS 3	<b>(77.27)p</b>	11.30p	
Adjusted	<b>24.97p</b>	24.88p	
Dividend per share (net of tax)	<b>6.00p</b>	6.00p	

### SHARE PRICE INFORMATION

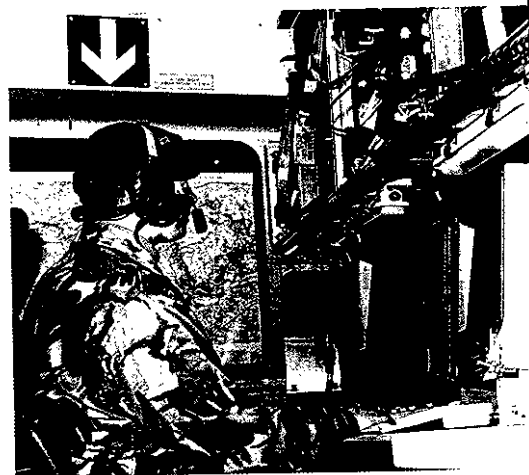
The current share price can be obtained by dialling  
FT Cityline on 0891 433752.  
Calls are charged at 50p per minute at all times.

# 1997/98 – Year in Brief

Turnover from ongoing operations up 10.8% to £920.7 million

*Sales:* leading provider of managed telecommunications services to the Government and rail sectors... revenues from commercial, Internet and international carrier services increased by 38%... Defence Electronics order book up 25% to a record £526 million, including production order for COBRA counter battery radar valued at £85 million... and good follow on orders for 'Searchwater' airborne

surveillance radar... Industrial Electronics sales grew 32% to £290 million... Survey group sales have more than doubled in three years... Instrumentation sales increased by over 60% with record profits... Camelot set new sales records...



Archer nominated as prime contractor on £2 billion Bowman project

*Strategic developments:* Racal Telecom signed infrastructure or partnership agreements with Vodafone, Metromedia Fiber Network (MFN), TeleWest, Teleglobe, NTL and ESAT... and formed ION joint venture with MFN to provide fully managed transatlantic services...



Racal led CityLink consortium successfully bid for London Underground's £1 billion Connect project... Archer Communications Systems consortium formed, with Racal taking a 30% stake... UK Ministry of Defence nominates Archer as prime contractor for its £2 billion Bowman tactical communications system... Racal leads a strong international consortium bidding for the electronic warfare system for the Common New Generation Frigate... joint venture formed with European Telecom plc to exploit the new field of vehicle telematics, combining vehicle tracking, navigation and information systems...



## World's first multimedia battlefield communications system launched

**Investment:** total capital expenditure of £116 million... spend of £38 million to enhance the nationwide SDH telecommunications network... over £130 million spent on R&D in ongoing operations... launched 'Panther' EDR, the world's first multimedia battlefield communications system... development of 'Squad Radio' for US Army nears completion... new seven-channel 'Satcom' terminal developed for launch in mid-1999... partnership with Airshow to develop direct broadcast satellite TV to aircraft... design work on new avionic communications audio management system peaked... cellular test sets now have on-air test capability... leading range of smart card transaction terminals developed...

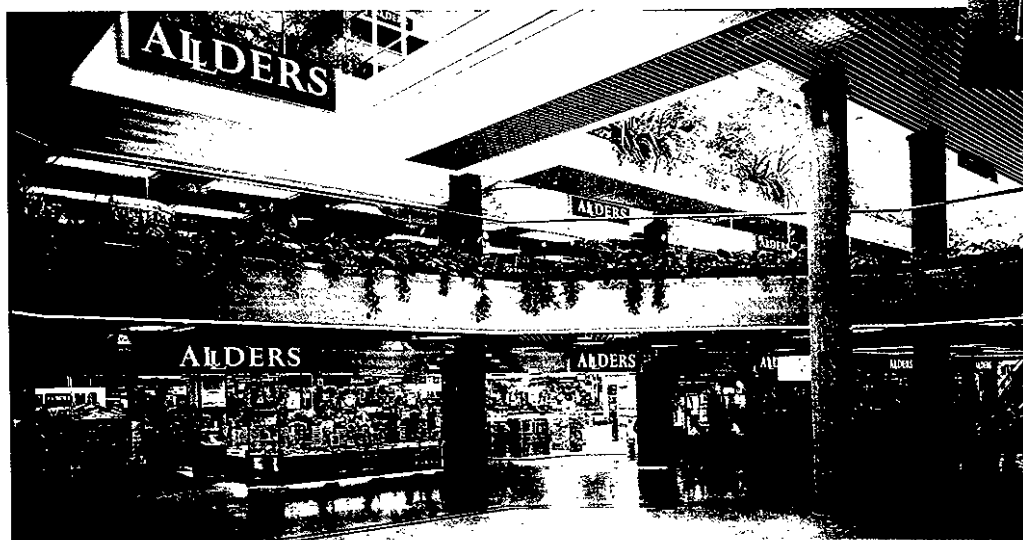
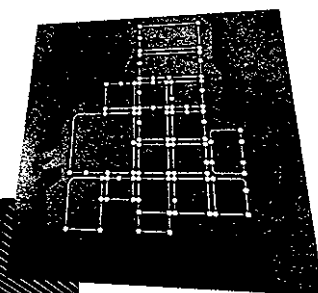


**Financial:** all costs associated with the exit from Data Communications activities charged to 1997/98 accounts... these and other exceptional costs total £224 million, resulting in pre-tax loss for the year of £207 million... operating profit, before reorganisation costs, from ongoing operations up 8.7% to £115.6 million... FRS 1 cash inflow of £27.2 million and debt reduced by £31.8 million... Industrial Electronics operating profit up by 65% before reorganisation costs... profit contribution from associates up 16% to £21.8 million...

Ongoing operations  
push profits up 8.7%

## Exit from Data Communications will transform Racal's prospects

**Going forward:** Health and Safety sold... exit from loss making Data Communications completed... retained tax losses of over £60 million available for future relief... profitable Security and Payments business retained in new Industrial Electronics group... recent alliances and major project opportunities, increasing productivity and investment in joint ventures and start-up companies will significantly enhance performance in 1999/2000... flotation of Racal Telecom at the right time remains the preferred option to maximise shareholder value.



# Statement by the Chairman



SIR ERNEST HARRISON OBE – CHAIRMAN

Good growth in sales and profit from ongoing operations

- turnover increased by 10.8 per cent to £920.7 million
- operating profit, before reorganisation costs, grew by 8.7 per cent to £115.6 million.

The exit from Data Communications is now complete.

Loss before tax was £207.2 million after charging £233.9 million related to the disposal of Data Communications.

Adjusted earnings per share increased to 24.97p.

Net debt is reducing, exit from Data Communications was cash positive.

The directors have approved the payment of a second interim dividend of 3.9p net per share, making 6.0p for the year, total unchanged from last year.

The board is committed to maximising shareholder value and the flotation of Racal Telecom remains the preferred option.

Our three ongoing principal activities; Telecommunications Services, Defence Electronics and Industrial Electronics had another year of sound growth.

## **Telecommunications Services**

Sales improved in the second half and margins remained healthy, reinforcing this group's position as one of our principal businesses.

In the commercial, Internet and international carrier services markets, the group achieved a 38 per cent increase in revenues which was largely offset by reduced revenues from its lottery and transport customers. Focused on the finance, retail and manufacturing sectors, Racal Telecom's corporate customer base continued to expand during the year. Its international carrier services business has benefited from the rapid rise in demand for capacity by telecommunications operators and Racal already supplies bandwidth to most of the newly established UK operators.

Exciting future opportunities in the rail sector include a Private Finance Initiative project to install, manage and operate an integrated digital radio and transmission system covering the entire London Underground network for the next 20 years. Racal is leading the CityLink consortium which has been chosen as single bidder for the £1 billion Connect contract.

Future growth prospects in Racal Telecom are enhanced by a number of key developments and partnerships. The company has improved its routes to market through agreements with Vodafone and COLT. The ION joint venture with the US telecommunications operator, Metromedia Fiber Network (MFN), launched a transatlantic service this Spring and has already attracted customers. Rollout of links into Europe has commenced with the announcement of reciprocal agreements with Esprit Telecom in France and AC-1 into Holland and Germany.

Ongoing investment in the network of some £70 million is planned in the current year to extend points of presence, improve the voice network and provide additional interconnect capability.

Telecommunications Services revenues in 1998/99 are expected to grow at an increasing rate. Margins will continue to be under pressure but, with improvements in productivity, should remain in excess of 10 per cent.

### **Defence Electronics**

A number of important new contracts were won by this group during the year. As a result, the order book increased by 25 per cent to £526 million, providing further strengthening of our position for the future. However, the financial upheaval in the Far East resulted in some orders being delayed and the situation is not expected to improve this year. Defence Radar and Avionics benefited from continuing growth in sales but margins were reduced slightly, principally due to an increased development spend in the second half of the year. The order intake in Radio Communications increased by 10 per cent during the year, reversing a four year trend of order book erosion.

Based on market leading positions in its chosen areas of focus, the group is currently involved in major opportunities in the fields of tactical and strategic communications, airborne surveillance radar and electronic warfare (EW). In tactical communications, Racal has a 30 per cent shareholding in Archer Communications Systems Limited, which has been nominated by the UK Ministry of Defence to address the £2 billion Bowman programme requirement for a new battlefield communications system for the British armed forces. In addition, Racal expects to undertake significant sub-contract work for this project.

In airborne surveillance radar, Racal is teamed with Lockheed Martin in the bid for the UK's Airborne Stand Off Radar (ASTOR). As the dominant supplier of EW to the Royal Navy, we are leading a strong international consortium bidding for the EW system for the tri-national Common New Generation Frigate (CNGF). For both CNGF and ASTOR selection is due in late 1998 with contract award during 1999.

With these prospects and a strong order book in Defence Radar and Avionics,

sales growth will increase, with margins maintained at over 10 per cent. We anticipate a reduction of losses and lower reorganisation costs in Radio Communications in the current financial year, as productivity is improved.

### **Industrial Electronics**

This group incorporates our Instrumentation, Recording and Survey businesses and now includes the security and payments activities retained from Data Communications. Impressive growth continued throughout the year with a strong increase in both turnover and operating profits.

Within this group, Instrumentation achieved outstanding growth in functional test systems, particularly in the USA. Total sales increased by over 60 per cent and profitability reached a record level. Building on this success in North America, Racal is now targeting potential markets in Europe and the Far East.

Modest growth in Recorders was achieved in the UK and Europe supported by a full year contribution from instrumentation recording specialist, Racal-Heim. The market for communications recording continues to grow strongly worldwide and further investment in products, systems and market support is planned in order to build this profitable business.

Survey has more than doubled its sales over the past three years. It has successfully evolved from providing precise positioning data for the offshore oil and gas industry to addressing non-oil markets, both on land and offshore. Following the recent significant increase in the turnover of this group, we are committed to improving its performance and profitability.

The Security and Payments business, with sales of over £40 million, comprises point of sale terminals and management systems, secure payment systems and network encryption products. It has strong market positions in each of these areas.

After its exceptional growth in 1997/98, the Industrial Electronics group's sales are

expected to increase at a significantly lower rate in 1998/99. There will be a substantial increase in development spend, amounting to some £6 million, leaving profit similar to that for last year.

### **Associates**

These continue to make an important contribution to Racal's overall profitability. In April 1998, our shareholding in Camelot increased to 26.67 per cent.

### **Disposals**

The board announced its decision to dispose of the Data Communications business last December. This decision reflected continuing delays in the development and introduction of new products, the disappointing first half results and the rapidly escalating costs of competing in this market. The exit was completed in September 1998 with the sale of the Racal Data Group.

The Health and Safety business, which was not core to Racal's strategy, was sold in early 1998.

These planned disposals of under-performing assets have removed businesses which were imposing a considerable burden on all other activities within the Company. Racal now has a portfolio of successful activities with good growth prospects and in which we enjoy strong positions in our chosen markets. The board is committed to the further development of these businesses in order to deliver value to shareholders.

### **OUR PEOPLE**

Racal has risen to the challenges of the past year and attained its present strong position thanks to the dedication and hard work of all our people. On behalf of the shareholders and the board I would like to thank all our staff and their families for their continuing support.

We would like to congratulate Roy Swatten, Customer Services Manager of Racal Avionics, on being made a Member of the Order of the British Empire (MBE) in the Queen's 1998 Birthday Honours in recognition of his services to Britain's defence forces.

### **FUTURE PROSPECTS**

The exit from the loss-making Data Communications business has transformed the operating profit of the Group. In 1996/97, the reported figure for continuing operations, including the losses of the Data Communications group, was £78.9 million compared with £115.6 million, before reorganisation costs, for ongoing operations in 1997/98. The exit from Data Communications will also allow management to concentrate on growing the ongoing operations.

Racal can look forward with confidence to the challenges and opportunities which lie ahead. Most of our businesses operate in growth markets and the turnover of the ongoing operations is expected to increase in 1998/99. Operating margins will be affected by the increasingly competitive nature of the telecommunications market, the difficult trading conditions in international markets, particularly the Far East and a £6 million increase in development spend. This is expected to result in broadly unchanged operating profits from the ongoing operations.

There have already been a number of important developments including strategic alliances in telecommunications, investment in international joint ventures and start-up companies, and the Company is well positioned to be awarded major project contracts resulting from the Connect and Bowman programmes. With other significant opportunities on which decisions are due this calendar year, the benefits will be seen in the 1999/2000 financial year when the Group's performance will be significantly enhanced.

Racal Telecom continues to grow and its flotation at the right time remains our preferred option to maximise the value for shareholders of this business.



Sir Ernest Harrison OBE



# Review of Operations

Our ongoing operations recorded a strong increase in sales and operating profit before reorganisation costs.

After a detailed review of Telecommunications Services, the board decided that we should position this business for flotation at the right time. We are planning to appoint a Chief Executive to strengthen the business. Growth prospects are being further enhanced by maintaining capital investment, broadening its portfolio of services and forming strategic alliances to improve routes to market and extend its international reach.

Defence Electronics has built a record order book and is well positioned to win further major contracts. Archer Communications Systems is ideally situated to win the £2 billion Bowman production contract in 1999.

The Industrial Electronics group had an excellent year, reinforcing our confidence in its growth prospects.

We saw a further increase in profits from our investments in Camelot, which continues to set new sales records, and Satellite Information Services.

Following the announcement of the decision to exit from Data Communications, the trading position in that group deteriorated significantly. The exit process proved far more difficult and time consuming than was anticipated, and was not helped by general market conditions. The sale of a major property in Florida and of the lease book was completed in the first half of 1998 and the sale of the Racal Data Group to Platinum Equity Holdings was completed in September. These transactions represent a clean break for Racal from this loss-making business with no further liabilities for reorganisation or severance costs. It also avoids significant closure costs which would otherwise have been incurred.

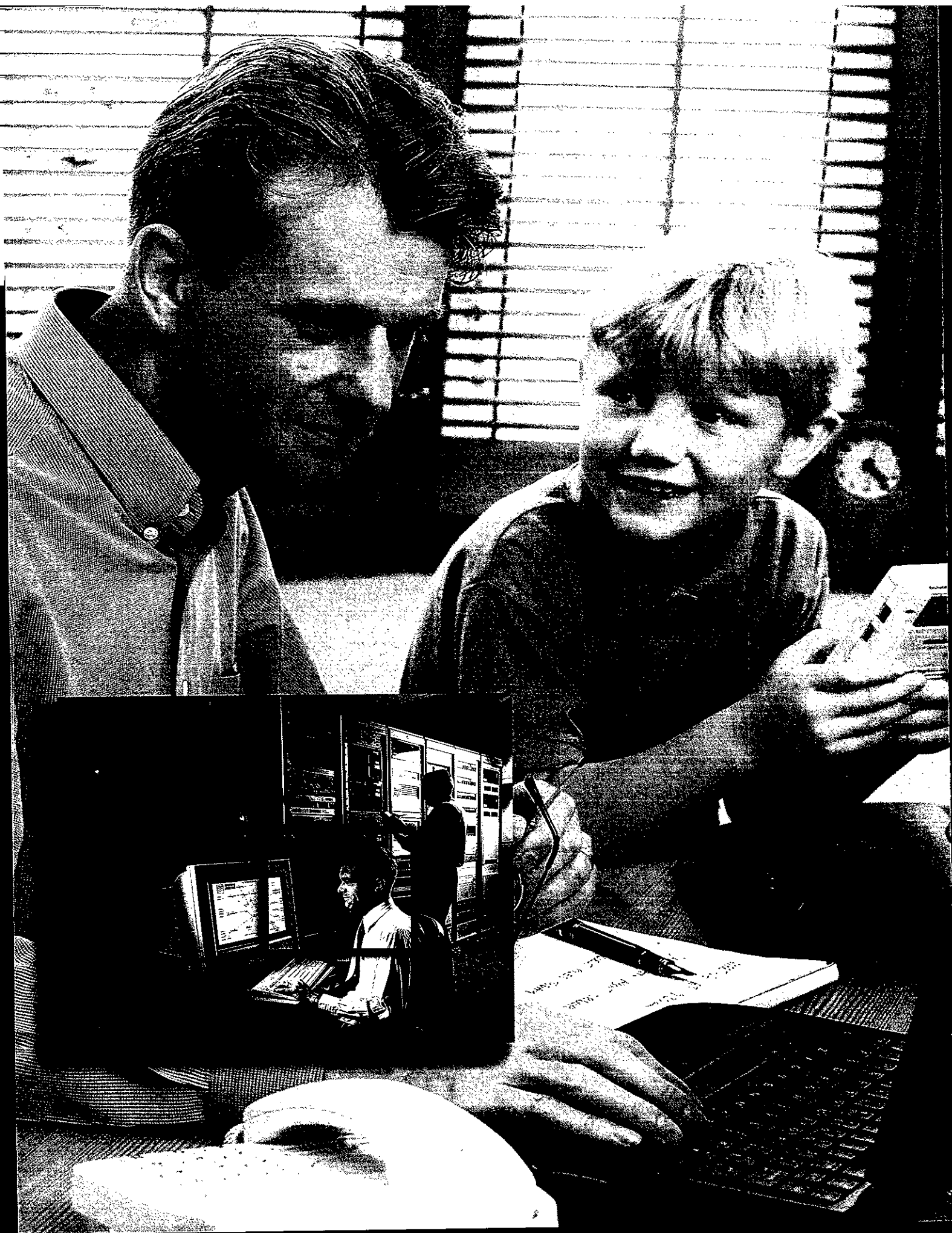
After December's decision to dispose of our Data Communications activities, we are now focused on three areas with good growth opportunities: Telecommunications Services; Defence Electronics; Industrial Electronics. We also benefit from our investment in associate companies – principally Camelot and Satellite Information Services.



DAVID ELSBURY OBE – CHIEF EXECUTIVE

As the Health and Safety business was not core to our strategy and had continued to yield disappointing results, we sold the Respiratory and Filtration activities worldwide to 3M in January 1998 and the Composite Pressure Vessel business to Harsco in February 1998.

During the year, all the Group's businesses and central activities established programmes to ensure that our products and business systems are Year 2000 compliant. Further details are given in the Report of the Directors.



# Telecommunications Services

Racal Telecom was formed in August 1997, integrating the activities of Racal Network Services and Racal-BR Telecommunications to provide managed telecommunications services for government, transport and commercial customers. Sales to commercial customers grew by 38 per cent. Turnover increased to £270.7 million.



Andy Bates is one of our senior network specialists. He leads a team of innovative designers whose work is vital in addressing the complex needs of our managed network services customers.

Success in commercial markets was largely offset by reduced revenues from the lottery and transport customers to give an overall growth of 4 per cent, while operating profit, before reorganisation costs of £2.5 million, was £38.3 million. Return on sales moved from 16.8 per cent to 14.1 per cent due to the lottery contract maturing and tariff reductions in the railway and government sectors. Capital investment in the business over the year amounted to £76 million.

## The Market

Racal Telecom focuses on markets in the public and business sectors where it can provide a selected range of managed telecommunications and value added services using its own infrastructure. It has developed services in the fastest-growing application areas – Internet, mobile voice and data, high speed data, multimedia services and virtual private networks.

Racal Telecom is concentrating on five market sectors: government, transport, manufacturing, retail, and banking/insurance/finance (BIF). It is the leading supplier in the government and transport sectors and expects to gain market share in the others – particularly BIF.

## Government and Transport

Racal Telecom is the leading supplier of managed telecommunication services to government and the rail industry.

These, together with revenue from operating the National Lottery network for Camelot, accounted for some 80 per cent of 1997/98 revenues. Our strategy in these markets is to maintain core revenues and build on them by renegotiating existing contracts, providing new value added services and pursuing further opportunities.

We continue to gain new government business including a £15 million order to supply fully managed voice services to all 21 offices and 8,550 staff of the Department for Education and Employment and a three year, £15 million contract to run the HM Customs and Excise Fixed Infrastructure Telephony Service.

We also won a three year contract worth £4.8 million to provide a fully managed LAN interconnection service across 160 sites for the Department of Social Security – the largest of the 32 departments taking managed services from the Government Data Network, which is owned and run by Racal. During the year we bid for a major contract to provide an international communications network for the Foreign and Commonwealth Office with single supplier selection expected to be confirmed before the end of 1998.

Transport is our largest market. Historically, rail operators signed a variety of separate contracts for services and maintenance.

Our strategy for new and renewed contracts is to move customers to a fully managed service under a single contract.

Racal Cellular, a service targeted initially at the 14,500 mobile phone users in the rail sector, has been an immediate success. Launched in August 1997, it has already notched up over 13,000 connections and contracts worth £5 million a year from 20 companies. One of the biggest orders is a three year contract to provide 1,500 connections for Jarvis, the railway maintenance specialist. Other new cellular customers include Balfour Beatty and English, Welsh & Scottish Railways, the UK's largest rail freight operator, for whom we provide services to 2,800 train crew based at over 40 depots.

A four year, £9 million contract to provide managed handset services to the entire Railtrack organisation lifted recent voice

orders in the rail sector to over £30 million. The contract is for enhanced services delivered over Racal's recently modernised rail voice network. Another significant voice service contract came from one of the largest train operating companies, National Express.

During the year we completed a major new CCTV system for Railtrack, serving the North London Line. The system, costing over £600,000, links

50 cameras by fibre optics to a central control room in Willesden and makes a significant contribution to customer safety.

Racal's leading position in the transport market has been further strengthened by the recent selection of CityLink Telecommunications as the single bidder for London Underground's £1 billion Connect communications project to install and operate enhanced network-wide radio and transmission services. The award of this 20 year contract is due later this year. Racal is likely to be the largest shareholder in CityLink with 33 per cent of the equity. In addition, Racal Telecom will benefit through the award of sub-contracts for the design, supply and operation of the fixed network, expected to be worth some £200 million over the licence period.

## Commercial

In the commercial, Internet and international carrier services markets Racal Telecom achieved revenue growth of 38 per cent. The proportion of sales represented by these sectors increased to some 20 per cent.

Our strategy is to exploit these high growth markets by packaging and providing new products and services, improving our routes to market, capitalising on the growth in Internet and intranet activity, and rolling-out an international managed network service (MNS).

A key new business gain was a five year MNS contract from NatWest, worth £22 million, to route authorisations for credit and debit card transactions in the UK. By the end of December some 10,000 outlets were using Racal's network and an additional 30,000 will join this year. The network is designed to handle an estimated 300 million transactions in 1998, rising to over 500 million by the turn of the century. Another important success was a contract from Barclays Merchant Services for a managed Internet service. Commercial customers for our managed services also include Allders, Cap Gemini, CommerzBank, Exel Logistics, Heinz, Norwich Union, Panasonic-Matsushita, WH Smith, Sun Life, Wessex Water and Zeneca.

The international carrier services business, established during the year, makes an important contribution to our commercial revenues. European liberalisation is accelerating the growth in demand for network capacity as international carriers and resellers use the UK as a gateway into mainland Europe. As a non-aligned carrier with a nationwide SDH (synchronous digital hierarchy) network, Racal Telecom is strongly positioned to exploit this opportunity: we already serve most of the newly established UK telecommunications operators including TeleWest and NTL.



In late 1997, Racal Telecom formed a partnership with Metromedia Fiber Network (MFN) in the USA - an established network provider of advanced fibre optic infrastructure for high bandwidth applications. The partnership established a 50/50 joint venture company, International Optical Network (ION), to provide fully managed, high bandwidth transatlantic services. ION is the first stage of Racal Telecom's strategy for expanding its international MNS reach into the heart of the USA and European business communities. It has also enhanced its connectivity into Europe through agreements with Esprit Telecom in France and AC-1 into Holland and Germany.

New carrier business included a contract to provide Teleglobe International, one of the world's leading intercontinental telecommunications carriers, with high capacity 'backhaul' links between London and the transatlantic cable landing station in Cornwall. These use Racal Telecom's SDH network to support the high levels of international traffic that Teleglobe handles on behalf of 25 UK-based carriers. In another contract, worth over US\$25 million, ION is supplying network infrastructure to AC-1, the major transatlantic optical fibre cable system operated by Global Crossing. ION is AC-1's only 'backhaul' network supplier providing high capacity shore-to-city links on both sides of the Atlantic.

Racal Telecom has formed several strategic alliances to increase its routes to market and harness additional expertise. These include partnerships with COLT for low-cost access to London's financial customers and Vodafone for fully integrated mobile and fixed managed services. In addition, it has added Internet/intranet to its portfolio of managed telecommunications services.

### **Investment and New Services**

Investment of over £38 million has enhanced the nationwide SDH telecommunications network and continuing investment will further increase 'last mile' connectivity. There has also been major investment in upgrading the rail voice network.

The company has concentrated on providing innovative services and has moved towards pricing based on value and risk. During the year it became the first UK provider with a comprehensive range of services accredited to the Cisco Powered Network Programme, an industry-wide stamp of approval for quality and service. Significant new services included:

- The 'Nsure' range of high speed data services for interconnecting Local Area Networks (LANs) and connecting fixed and mobile data users to corporate LANs.

- 'TORUS', a modular series of completely integrated customer information and security solutions for the rail industry.

- A fully managed international private circuit service, offering advanced communications to and from USA and European business centres, provided through Racal Telecom's partnership with MFN.

### **Outlook**

With the UK managed telecommunications services market growing at over 20 per cent annually, the company aims to increase revenue by winning new customers, introducing new standard products and services, developing new routes to market and leveraging its existing customer base.

Internationally, Racal Telecom will establish a European backbone network through major alliances and is currently in discussion with other carriers to gain a foothold in the Asia Pacific region. This will extend the reach of its fully managed services, reduce the cost of international services and enable it to profit from the increasing demand for capacity both domestically and internationally.



# Defence Electronics

In 1997/98, we continued to make progress with the integration of all our Defence Electronics activities into a single business and strengthened our position as a major supplier of specialist electronic equipment to defence customers worldwide. Sales were up by 2.6 per cent to £360.1 million and the order book grew strongly to £526 million.



Mike Kenyon is an executive technical manager leading a team of RF engineers. Their skills and expertise are essential in maintaining our position as a world leading supplier of advanced radio communications systems.

The key to our success is the strong position we hold in each of our chosen niche markets. In electronic warfare (EW) we are Europe's largest manufacturer of naval systems. We have a strong record of success with the UK Ministry of Defence (MoD) and other defence forces for our airborne surveillance radar systems, command information systems and airborne navigation systems. In tactical radio communications we are one of the world's leading exporters. In commercial markets we have achieved particular success with aeronautical satcom systems supplying about 65 per cent of those in use around the world.

Our strategy is to concentrate on these niche markets and form partnerships on a project-by-project basis, capitalising on opportunities as they arise. Our strength in our selected markets enables us to join forces with most prime contractors on major projects – an increasingly important asset as the defence industry continues to consolidate.

## Defence Radar and Avionics

Defence Radar and Avionics increased sales by 7.3 per cent from £210.8 million to £226.1 million and the year end order book grew 28 per cent to £453 million. However, increased development costs reduced operating profits by £1 million to £23.3 million, before charging £1.1 million for reorganisation.

### Electronic Surveillance

Major orders for naval EW systems have consolidated our position as the Royal Navy's dominant supplier. This has strengthened our bid for the EW system in the planned

tri-national Common New Generation Frigate; the competition between a strong Racal-led international consortium and one other will be adjudicated in 1998 and a contract for full development and initial production is expected in 1999.

Exports of naval EW and ground based intelligence gathering systems remain important areas of business where we are actively pursuing some £100 million of business. In the airborne sector we received a significant contract from Lockheed Martin for an advanced techniques generator which is a critical element in modern aircraft defensive aids systems. We anticipate further business in this area.

### Radar Systems

The success of the 'Searchwater' programmes for the Royal Navy Sea King Mk7 helicopter and the Royal Air Force Nimrod 2000 maritime patrol aircraft was reconfirmed by significant follow-on business during the year. In ground radar, our joint venture with Thomson-CSF, DASA and Lockheed Martin was awarded the production contract for the tri-national COBRA counter battery radar programme. Racal's share of production is worth in the region of £85 million. We are trialling an upgrade of the 'MSTAR' battlefield radar for the British Army. We expect further contracts from the UK MoD and export customers and already have an agreement for local manufacture in Saudi Arabia.

Looking ahead, the UK's ASTOR airborne stand-off radar programme is an important opportunity to reinforce our long term position in airborne high power surveillance radar.

Racal is teamed with Lockheed Martin in one of three competing consortia; a decision is expected at the end of 1998 for contract placement in early 1999.

#### **Command, Communication & Information Systems**

We continued to build our presence in ground based air defence systems, bidding successfully for a £12 million tactical air command centre for the UK MoD. This delivers a highly mobile capability to support out-of-area operations, combining proven core software from the USA with our significantly improved human-computer interface. This success provides good opportunities for further sales in the UK and export markets.

We were also successful in our £20 million bid to supply the 'Cheetah' satellite communication system to the MoD. 'Cheetah' provides extensive voice and message services on an extremely compact portable field terminal, integrating 'best of breed' hardware and software products from leading UK, French and American suppliers. Its success in combining a wide range of features with low weight and high endurance has attracted a great deal of interest worldwide.

Successful diversification into commercial applications has been achieved with an order from the Moroccan Government for an extensive fisheries management system. This comprises a number of operation centres integrated with a chain of coastal radars supported by maritime and air reconnaissance. We are exploring commercial applications for our naval radar track extractors and applying our radar technology to develop a low-cost, low-weight aircraft transponder.

#### **Navigation Systems**

Our CDNU airborne navigation computer has now been selected for EH101, Lynx and Sea King helicopters and has considerable export potential.

Traditional ground-based navigation aids will eventually be replaced by satellite-based systems using GPS-type technology. We are actively pursuing opportunities in the development of a European GNSS Navigation Overlay System (EGNOS) for aircraft precision landing.

Aeronautical Services (Aerad), acquired from British Airways last year, has been integrated with our Navigation Data Services business. The combined operation offers paper charts and electronic navigation information to airlines worldwide and has good growth prospects.

#### **Satellite Communications**

Demand for our 'Satcom' systems from airlines and for business jets continues to grow. With Honeywell, our partner in this business, we have begun development of a new seven-channel 'Satcom' terminal for launch in mid 1999, allowing voice/data operation over existing Inmarsat satellites and the new LEO low earth orbit satellite systems.

Another exciting development is direct broadcast satellite TV to aircraft. We have teamed with Airshow in the USA to develop an airborne antenna and electronics unit to receive up to four simultaneous TV channels, initially from DirecTV satellites providing coverage over the USA. Interest from business jet users is high; we have achieved certification on three aircraft types to date and user reports on reception quality have been very encouraging. Service will be extended to South America at the end of 1998 and to Europe in the second half of 1999.

#### **Radio Communications**

Radio Communications sales fell 4.5 per cent to £134 million, due primarily to the cancellation of a significant Far Eastern order caused by the economic downturn in that region.

The operating loss of £7.9 million, against £4.1 million in 1996/97, includes £4 million of restructuring costs which have reduced the annualised cost base significantly. These savings, and the growth in orders during the first half, reduced losses in the second half.

During the year the MoD nominated Archer as the prime contractor and systems integrator for its £2 billion Bowman tactical communications system. Racal Radio has a 30 per cent share in Archer with ITT Defence (40 per cent) and British Aerospace Defence Systems (30 per cent). In its maiden year, Archer has already won and executed a £20 million MoD contract.





It is currently negotiating the next phase of the programme leading to the award of the full production contract in 1999.

Racal has already been selected for the development of the VHF portable transceiver which forms part of the Bowman core system. We are bidding in partnership with Thomson-CSF for the £300 million Bowman digital battlefield local area system – a ground-based multimedia network used within and between British Army headquarters' vehicles. This is the largest of the Bowman sub-systems to be specified and put out to tender by Archer. We are also bidding for the important HF transceiver which forms a key element of the total Bowman system.

Building on the worldwide success of our 'Jaguar' frequency hopping radio, we are now taking battlefield communications into the 21st century with the new 'Panther' EDR (Enhanced Digital Radio), the world's first multimedia digital tactical communications system. Its wide range of advanced capabilities include tactical Internet messaging, weapon and sensor system integration, location awareness from GPS and video transmission. The launch of 'Panther' EDR will have a considerable impact on the world tactical communications market and we have already received orders from Europe, the Middle East and the Far East.

Although the tactical radio communications market is increasingly competitive, the successful reorganisation of our business, the launch of 'Panther' EDR and the potential of the MoD Bowman programme give grounds for optimism. Our overseas sales are supported by a wide product range and we have technology transfer agreements for manufacturing in a number of countries – including an important contract for producing 'Panther' VHF radios in Saudi Arabia with a long established local partner.

Governments are attaching growing importance to intelligence acquisition by electronic means. To meet this need we continue to expand our capability in communications intelligence.

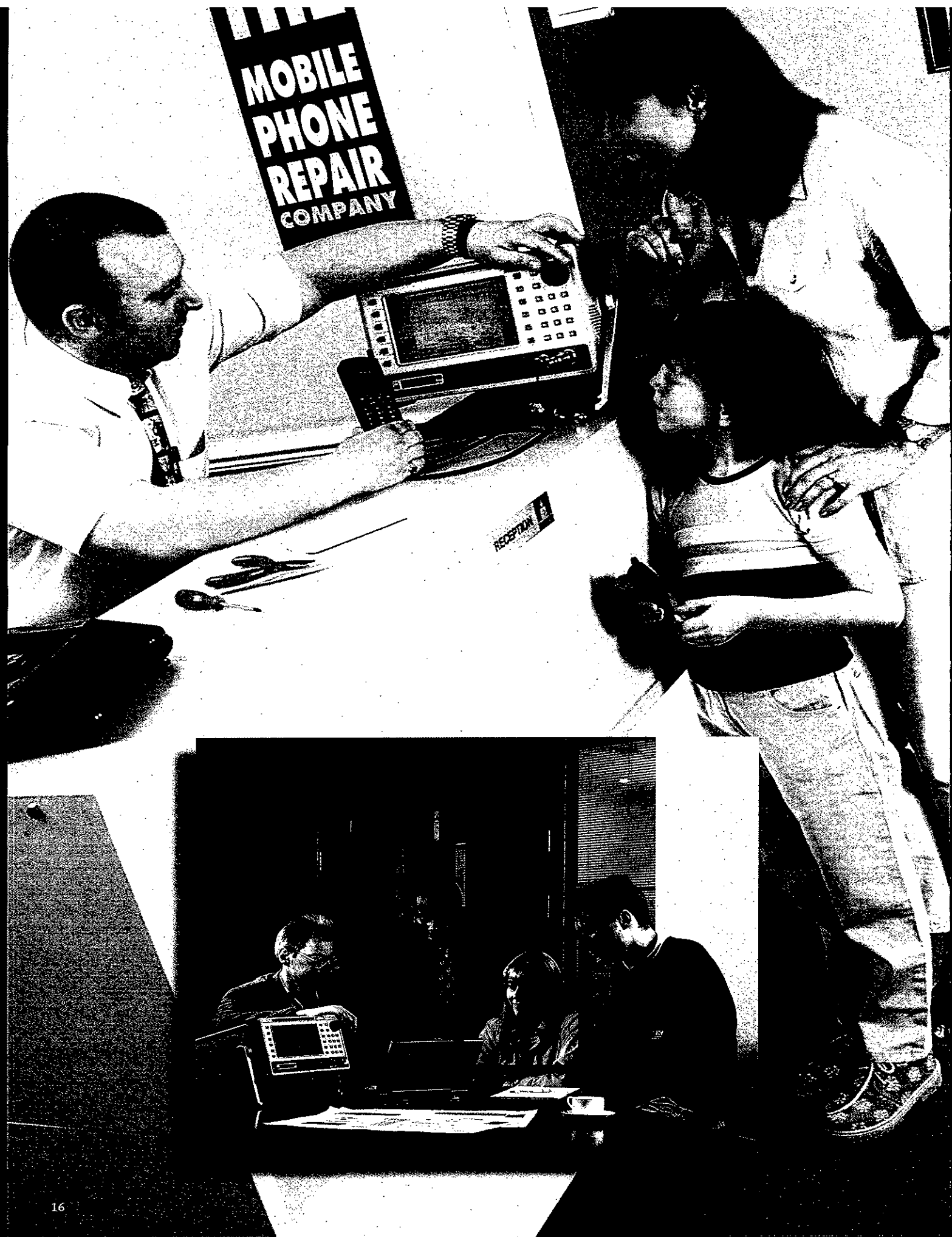
Racal systems supplied to the British Army and others have recently been deployed for peacekeeping roles in Bosnia and elsewhere.

We have won a number of production contracts; for our tactical automated security system for the US Air Force; for a miniature secure handheld radio for security and paramilitary forces. Total sales of equipment for law enforcement and paramilitary forces now exceed £180 million, mainly for the 'Cougar' range. These products have been well received and future prospects are encouraging.

Development of the 'Squad Radio' for the US Army Land Warrior programme is now near completion and ready for systems integration. Progress continues on other development contracts including the multiband inter-team radio for the US Special Operations Command and the combat survivor evader locator programme. Production options for these contracts are expected in 1998/99 and onwards, with significant quantities being required.

Continued product innovation generated further sales success in non-military markets. New contracts in South East Asia doubled sales of 'Widanet', a system to carry packet data for credit card transactions and other applications, to £4.9 million. Sales of the 'Talon' automatic vehicle licence plate recognition system increased in the UK and contracts for road tolling applications were gained in the USA. These now represent significant growth opportunities.

Audio ancillary sales volumes were lower than expected due to delays in shipment of military vehicle headsets for North American customers. Design activity on the new avionics communications audio management system reached its peak during the year, and series production will be aligned to aircraft construction schedules over the coming three years. The unique features of this exciting new product family make it a strong candidate for future aircraft refit programmes.



# Industrial Electronics

The impressive growth of the Industrial Electronics group continued throughout the year, with turnover increasing by 32 per cent to £290 million.

Instrumentation grew strongly in the USA and Survey grew worldwide. This group now includes the Security and Payments business which also had strong sales growth. Sales for Recording were broadly unchanged. Operating profit, before reorganisation costs of £2.1 million, rose 65 per cent to £39.7 million, due largely to the success of our functional test activity and security and payments systems.



Sandra Gilligan is a product manager with our instrumentation company and is part of a marketing team which is presently involved in helping our digital radio test equipment customers as they embrace future mobile communication systems.

## Instrumentation

This business provides complex electronic functional test systems for a broad range of industrial applications, digital radio test systems for cellular radio and custom electronic test suites for defence applications. It achieved outstanding growth in functional test systems, particularly in the USA, based on our world leading VXIbus instrumentation packages for manufacturing test and in-service support. Sales increased by over 60 per cent and profitability reached record levels.

The 'Freedom' family of functional test equipment gives users a unique ability to tailor automatic test stations to specific production and service requirements, using off-the-shelf units based on the latest VXIbus technology. It has achieved sales growth in the USA to systems integrators in the computer, defence and medical equipment markets. Building on success in North America, we are now targeting potential markets in Europe and the Far East.

For digital radio, we further enhanced our world leading range of cellular test sets by adding an on-air base station test capability. We won significant contracts in the new market for satellite-based cellular systems and see further opportunities in this field.

We also gained contracts for major defence electronic test systems in the UK and overseas.

Having completed a major functional test contract in the early months of the new financial year, we expect volume in this sector to be somewhat reduced in 1998/99. Nevertheless, the business as a whole will continue to progress, focusing on the development of advanced digital radio instrumentation to meet new opportunities; we also see good prospects for a new generation of specialist test facilities for defence applications based on VXIbus technology.

## Recording

We are a leading supplier of communications recording equipment for professional services and public safety markets, and of data acquisition recorders for industrial users. Modest growth was achieved in the UK and Europe, boosted by a full year's contribution from Racal-Heim, a specialist in instrumentation recording, which we acquired in September 1996. However, margins were reduced by increased investment in product development focused on new technology voice recording and software for the emerging networked IT and telephony environments in call centres and financial dealing rooms.

Results in North America were disappointing but we have now restructured our USA operation under new leadership. The market for communications recording continues to grow strongly worldwide and we will make further investment in products, systems and market support to build this profitable business.

### Survey

This business has successfully evolved from its origins of providing precise positioning data to the offshore oil and gas industry. It now supplies a broader spread of products and services to fulfil clients' changing requirements and has expanded its technological base to address non-oil markets, both on land and offshore. These developments have resulted in sustained growth, with 1997/98 sales rising 23 per cent to over £100 million.



Offshore construction support projects, which make use of our growing capability in remotely operated underwater survey vehicles (ROVs), are intrinsically long term. Together with our balanced geographical cover and penetration into submarine cable, underwater inspection, geophysical surveys and land positioning activities we have a strong base for the future. The wider spread of activity has reduced our exposure to the volatile exploration market with its dependence on oil prices, and highly cyclical investment profile.

Our expansion in the Americas following two acquisitions in 1996/97 yielded sales growth of 58 per cent in this strong market, with particular successes in the Gulf of Mexico and Latin America. ROV construction services and a strong position in the major international oil corporations' expanding activities in the Caspian Sea helped sales in the North Sea, Middle East and Africa regions to increase by 11 per cent. In South East Asia the weakness of local economies, which is likely to continue for some time, resulted in flat overall sales. We continued to expand our ROV fleet and now have 32 of these vehicles deployed worldwide – with support bases in the USA, Scotland and Singapore – underpinning our development of the oilfield construction support business.

We have sold Racal Geodia SA, the small French geotechnical services company we acquired in December 1996, to Sage Holding AG in exchange for a 6 per cent equity holding in the expanded entity. There are options, in the future, to increase this equity holding.

The Survey group's sales have more than doubled over the past three years. We will continue to invest in this business and expect profitability to improve.

### Security and Payment Systems

We have decided to retain and grow three profitable businesses which were previously part of the Data Communications group. These provide point-of-sale terminals and management systems (Racal-Transcom), secure payment systems (Racal-Airtech) and network encryption products (Racal-Guardata). All three have strong market positions. At present they operate separately but are being integrated into a single, focused organisation to address the growing market for security and payment systems.

In 1997/98, the Security and Payments businesses had sales of £40.9 million (1996/97 £27.0 million) and earnings before interest and tax of £9.9 million (1996/97 £3.5 million).

Racal-Transcom is the dominant supplier of card payment systems in the UK. Following success in winning a number of bank contracts, sales of card payment terminals increased in 1997/98 by over 70 per cent. It achieved record sales and profit. By the end of the year Racal-Transcom had become a supplier to each of the major UK acquiring banks. A major contract to supply smart card terminals to NatWest, worth in excess of £15 million, has recently been announced and these new products will become increasingly important as smart cards become more widely used in the UK and other markets.

Racal-Airtech is a market leader in secure payment systems in Europe and the Pacific Rim. Racal-Guardata has an installed base of 50,000 data encryption devices with a strong reputation in financial and government secure networks in North America. These operations also grew strongly in 1997/98, increasing sales by over 35 per cent.

## **Other Activities**

### **Research and Development**

We are committed to growing our technology base to provide quality products and services. In 1997/98, our ongoing businesses spent over £36 million on R&D, and substantial additional work was funded by our customers to the value of almost £100 million.

Racal Research is a central resource which provides many key elements of the Company's technology base, serving both product and service sectors. It is currently working in areas such as advanced processing for electronic warfare systems, where it has developed novel signal identification methods, and in precise positioning techniques using satellites to achieve centimetric accuracy over areas of several hundred square kilometres. It has been working closely with our radio company in the USA to produce the miniature secure handheld radio for that market and has pioneered new security services for electronic commerce, which are now being integrated into Racal Telecom's range of services.

Collaboration with UK universities has continued at a high level, with emphasis on the telecommunications sector.

The Racal Chair in Information Technology at the University of Surrey is now concentrating on next-generation network management techniques.

### **Training**

Racal's training and conference centre, Heckfield Place, provides facilities for the Group and non-Racal companies. Courses range in duration and content from a single day's introduction through to intensive tuition lasting several months. Currently, more than a quarter of the training we offer is in Information Technology. It is of the highest standard and has both technical and applications content. To achieve this we have invested in highly qualified staff and the latest training technology.

Heckfield Place provides accredited training in a diverse range of subjects. The staff are committed to making training as relevant as possible. They always endeavour to enhance courses by structuring tuition in relation to customers' own working environment and will run courses at customers' own sites, if required.

# Associates

Associates continue to make significant contributions to Group profits – including £16.8 million (1996/97 £13.7 million) from Camelot and £5.8 million (1996/97 £5.1 million) from Satellite Information Services, offset by a loss of £0.8 million from the newly formed Global Telematics.

## Camelot Group

The National Lottery operator had another record year. Sales increased 17 per cent to £5,513.7 million. Almost £1.6 billion was

received by the Good Causes during the year to take the total raised to over £5 billion, with a further £700 million for the nation in duty and tax.

Camelot is fulfilling its commitment to maximise returns for the Good Causes and continues to be the world's largest and most

efficient lottery operator. It is well on course to raise £10 billion for the Good Causes by September 2001 – £1 billion more than its original undertaking.

In April 1998, following the buy-back of shares by Camelot from GTECH, our shareholding in Camelot increased to 26.67 per cent.

## Global Telematics

Racal is well placed to benefit from its investment in the new field of vehicle telematics, which combines vehicle tracking

and navigation with information systems for commercial and private vehicle users. In August 1997, we joined forces with European

Telecom plc to address this growing market through a 50/50 joint venture company, Global Telematics Plc. Combining Racal's skills in high accuracy Differential Global Positioning Systems with our partner's expertise in the international cellular industry, the company has launched services in the UK and South Africa under the Orchid brand.

**ORCHID**<sup>TM</sup>

## Satellite Information Services (SIS)

SIS provides a range of satellite-based communication services. These include the daily provision of horse racing pictures and related text to nearly 10,000 licensed betting offices in the UK and Eire giving the company a stable and reliable baseload business.

Its 1997/98 growth came largely from two smaller activities; sales grew 23 per cent at its satellite news gathering arm, SISLink, and 50 per cent at The Racing Channel, the UK's only TV channel dedicated to horse racing. SISLink supplies transportable uplinks for TV news broadcasters and also covers more than 4,000 live outside broadcasts a year worldwide. The Racing Channel now serves over 20,000 subscribers. Profit growth is expected to slow this year, relying mainly on continued cost rationalisation, especially in satellite communication expenses.



# Financial Review

## GROUP RESULTS

### Turnover and Profit

Turnover of the ongoing operations at £920.7 million was £90 million higher than in the previous year, an increase of 10.8 per cent.

#### Turnover of ongoing operations

	Turnover (£m)	Growth
Defence Radar and Avionics	226.1	7.3%
Radio Communications	134.0	-4.5%
Defence Electronics	360.1	2.6%
Industrial Electronics	289.9	32.0%
Telecommunications Services	270.7	4.1%
<b>Total ongoing operations</b>	<b>920.7</b>	<b>10.8%</b>

Operating profit of the ongoing operations, before reorganisation costs, increased by 8.7 per cent to £115.6 million (1996/97 £106.4 million). The return on sales declined slightly from 12.8 per cent to 12.6 per cent and was affected by an increase in UK pension costs of more than £3 million, principally due to the abolition of advance corporation tax credits in respect of UK pension schemes. After charging for redundancy, severance and reorganisation costs of £10.0 million incurred during the year (1996/97 £2.7 million) the total operating profit of these operations increased to £105.6 million (1996/97 £103.7 million).

Operating losses of discontinuing operations of £59.2 million (1996/97 £23.7 million) reflect the deterioration in the trading conditions of the Data Communications group. The operating loss of £4.4 million for discontinued operations represents the losses of the Health and Safety activity prior to its sale in early 1998.

Exceptional losses amounting to £224.5 million (1996/97 £19.3 million) included the significant charge for the exit from Data Communications, partially offset by profit on the sales of property and of the Health and Safety activities.

Our prior investment of £2.1 million in the PayPoint service activity through Utilities Consortium Limited has been written off following a capital restructuring.

Net interest payable was £22.7 million (1996/97 £22.9 million). Interest cover for

ongoing operations was 4.7 times compared to 4.5 times in the previous year.

The exceptional costs relating to the exit from Data Communications were the main contributors to the pre-tax loss of £207.2 million (1996/97 £40.4 million profit).

Exchange rate movements had no material effect on either turnover or profitability.

### Exceptional Items

Profit on the sale of properties amounted to £1.0 million (1996/97 £0.6 million).

The exit from Data Communications resulted in an exceptional charge of £234 million, which included the write off of £107 million of goodwill. This latter item does not affect shareholders' funds.

The sale of Health and Safety gave rise to a profit of £11.3 million after charging a goodwill write off of £8.4 million.

### Data Communications Disposal

The decision to exit from the loss-making Data Communications activities was announced in December 1997. The main components of the exceptional cash flow and profit and loss charge are shown in the table below:

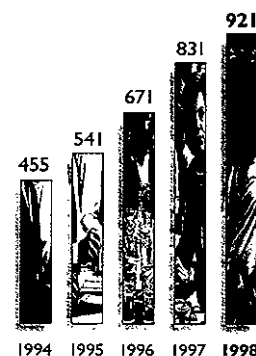
#### Data Communications Disposal

	Cash in/(out) to 31.3.98 £m	Total £m	Loss £m
Sale of assets			
– business (ex. royalty £21.3m)	–	6.8	(64.4)
– other assets	41.6	68.5	(4.3)
Cost of disposals			
– asset impairment	–	–	(27.9)
– severance & other labour costs	(3.6)	(9.6)	(9.6)
– other	(1.4)	(8.9)	(11.2)
Effect of disposal (ex. royalty)	36.6	56.8	(117.4)
Provision for losses 1998/99			(9.5)
Total per accounts (ex. goodwill)			(126.9)
<b>Pro-forma inc. royalty income</b>		<b>78.1</b>	<b>(105.6)</b>

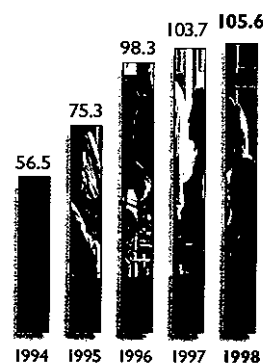
#### Cash Flow

The sale to Platinum Equity Holdings of the loss-making worldwide business of the Data Communications group, exclusive of its security and payments activities, was completed in September 1998 and is expected to yield

Turnover (£m)  
Ongoing operations



Operating profit (£m)  
Ongoing operations



£28.1 million, of which £6.8 million was paid in cash on completion. The balance is payable as a royalty on future sales of the Racal Data Group over the next ten years under Platinum's ownership to a maximum of £21.3 million and it is anticipated that the majority of this will be received in the first five years. The consideration may be subject to adjustment dependent upon the closing balance sheet on 11 September 1998. An interim balance sheet has been prepared and has resulted in a reimbursement by Racal of £0.8 million of the £7.6 million paid by Platinum on completion, producing net proceeds of £6.8 million. Should any further adjustment based on the final balance sheet be required this will be deducted from the future royalties payable by Platinum.

The sale of other assets including property, finance leases and investments has realised a further £68.5 million, giving total proceeds, excluding royalty income, of £76 million of which £41.6 million was received in 1997/98. Expenditure on reorganisation and other costs totalled £18.5 million of which £5 million was incurred in 1997/98. There was a net cash inflow from the disposal of £36.6 million in 1997/98 with a further £20.2 million inflow anticipated in 1998/99.

#### Profit and Loss

The disposal of the Data Communications group has resulted in a charge to the profit and loss account of £127 million excluding goodwill. This includes a loss of £64.4 million on the sale of the business to Platinum, asset write downs of £27.9 million and severance and other costs of £20.8 million. In arriving at the total charge a provision of £9.5 million has been made for estimated trading losses for the period from 1 April 1998 to the date of completion. These losses will not, therefore, affect the trading results for 1998/99.

#### Associates

Our associates continue to make a strong and growing contribution to the overall profitability of the Group. These include £16.8 million (1996/97 £13.7 million) from Camelot, £5.8 million (1996/97 £5.1 million) from Satellite Information Services. Shareholdings in Camelot and SIS remained unchanged during the year at 22.5 per cent and 22.0 per cent respectively.

#### Taxation

Taxation charge for the year was £11.3 million. Following the sale of Data Communications, Racal has retained tax losses in the USA and a number of European countries amounting to more than £60 million. These are available to offset tax on the future profits of our remaining businesses in these territories. As a result, it is anticipated that the tax rate will reduce to approximately 28 per cent for the medium term.

#### SHAREHOLDERS' RETURNS

##### Earnings Per Share

Adjusted earnings per share increased slightly to 24.97p (1996/97 24.88p). The FRS 3 loss per share was 77.27p (1996/97 earnings of 11.30p).

##### Dividends

The announcement of the results for 1997/98 was delayed so as to allow the inclusion of the effect of the exit from Data Communications. In order to pay a dividend close to the date of the usual final dividend, the board decided to pay a second interim dividend of 3.9p net per share making a total of 6.0p net per share for the year (unchanged from last year). This dividend was paid to shareholders on 11 September 1998 and replaced the usual final dividend. To enable this second interim dividend to be paid quickly, it was not possible to offer shareholders a scrip dividend alternative.

Dividend cover, on an adjusted basis, of 4.2 times is similar to that of 1996/97.

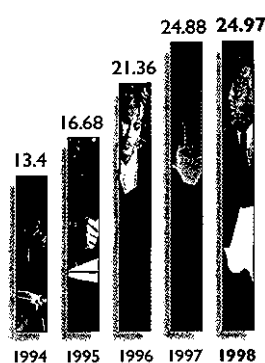
#### BALANCE SHEET

The value of the fixed assets continues to grow, reflecting further capital expenditure, net of disposals, of £115.9 million (1996/97 £118.7 million). Investment in the Telecommunications Services infrastructure rose, as part of a three year investment programme, to £76 million (1996/97 £65 million).

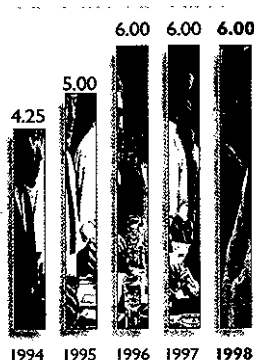
Provisions for liabilities and charges increased sharply from £18.4 million to £105.7 million largely due to the exit from Data Communications.

Net debt reduced to £307.6 million (1996/97

Earnings per share (p)  
Adjusted



Dividends (p per share)





£339.5 million). On 31 March 1998 the debt/equity ratio, including finance lease obligations of £96.5 million (1996/97 £112.5 million), was 95.0 per cent and compares with 75.9 per cent a year earlier. The increase in this ratio reflects the reduction in shareholders' funds to £324.0 million from £447.1 million.

## CASH FLOW

The total cash inflow for the year was £11.0 million (1996/97 outflow of £30.6 million). After adjusting for payments in respect of finance leases the inflow on an FRS 1 basis was £27.2 million, (1996/97 £16.9 million outflow). Net operating cash flow was £121.4 million (1996/97 £140.4 million) with the reduction mainly caused by the deterioration of the trading performance of the Data Communications group.

### Summary Cash Flow

	1997/98	1996/97
	£m	£m
Operating profit	42.0	82.6
Depreciation/amortisation	73.0	68.2
Profits of associated companies less dividends received	(12.7)	(12.4)
Working capital	18.9	29.9
Other operating items	0.2	(27.9)
Net operating cash flow	121.4	140.4
Capital expenditure	(115.9)	(118.7)
Interest	(23.8)	(22.6)
Tax paid	(17.4)	(1.0)
Acquisitions and disposals	77.7	7.0
Dividends	(16.9)	(16.9)
Other items	2.1	(5.1)
<b>FRS 1 cash inflow/(outflow)</b>	<b>27.2</b>	<b>(16.9)</b>
Capital element of finance lease/hire purchase payments	(16.2)	(13.7)
<b>Total cash inflow/(outflow)</b>	<b>11.0</b>	<b>(30.6)</b>

Working capital fell by £18.9 million of which £13 million related to the ongoing operations. This followed a £29.9 million fall in the previous year. As a result the ratio of sales to average working capital for the ongoing operations increased to 5 times from 3.8 times.

## Future Investment and Gearing

Due to the continuation of the programme to modernise the Telecommunications Services infrastructure, capital expenditure in 1998/99

will remain at similar levels to those of 1997/98.

Total cash flow is expected to be broadly neutral during the year but with enhanced earnings, a reduction in gearing is expected.

## TREASURY ACTIVITIES

The Company has a central treasury function which operates under strict rules approved by the directors.

At the end of 1995, the Company arranged a three year £400 million facility with a syndicate of banks. This was subsequently renegotiated in March 1998 and extended until the end of 1999, with the covenants modified to reflect the decision to exit from Data Communications. Since that time, the Group has complied with these covenants which are associated with net and gross gearing, interest cover and net assets. Under this arrangement we have maintained borrowings in United States Dollars, German Marks, French Francs, Dutch Guilders and Canadian Dollars in order to hedge assets denominated in those currencies in our overseas operations. Our policy is to hedge approximately 80 per cent of overseas assets with currency debt in the UK. We are planning to replace the Group's existing banking facilities before the end of the current financial year.

The Group closely monitors interest rates in respect of all currencies in which it borrows. In consultation with our bankers the Group has fixed its interest rate liability on a proportion of its debt by entering into interest rate swaps. At the end of March 1998 the principal amount fixed by the arrangement totalled £70 million which had reduced interest costs for the year ended 31 March 1998.

Surplus funds have been invested during the year with counterparties which have high credit ratings to ensure security of principal.

It is the Group's policy not to hedge translation exposure of the profit and loss account. However, for significant transactions denominated in a currency other than that of the particular Group company involved, the currency exposure is hedged by forward contracts. The Group policy is not to take speculative currency positions.

# Board of Directors

## Chairman

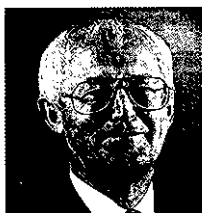
\*SIR ERNEST HARRISON OBE,  
HON DSC, HON D UNIV (SURREY),  
HON D UNIV (EDINBURGH), FCA,  
COMP IEE, HON FCGI

Aged 72. Joined Racal in 1951, was appointed to the board in 1958 and became Chairman in 1966. He is a director of Camelot Group plc and from August 1988 to July 1998 was Chairman of Vodafone Group Plc.

## Chief Executive

DAVID ELSBURY OBE

Aged 62. Joined Racal in 1956 and was appointed to the board in 1975. He has been Chief Executive since 1992 and is currently directly responsible for Telecommunications Services.



BARTON CLARKE CBE  
*Defence Electronics*

Aged 63. Joined the Group through the acquisition of Decca Limited in 1980 and was appointed to the board in 1985.

\*\*LORD INGE GCB, DL  
*Non-Executive*

Aged 63. Appointed to the board in 1997 following his retirement as Chief of the Defence Staff after a long and distinguished career in the Armed Forces. He is also a director of Greenly's Management Consultants.



PAUL KOZLOWSKI  
*Data Products*

Aged 60. Joined Racal in 1995 and appointed to the board in 1996.

MARTIN RICHARDSON BSc, FCMA  
*Industrial Electronics*

Aged 53. Appointed to the board in 1985, three years after joining the Group.



\*\*SIR GERALD WHENT CBE  
*Non-Executive*

Aged 71. Appointed to the board in 1982, becoming non-executive on the flotation of Vodafone Group Plc in 1988. He is a director of Mobile Systems International Plc and, until July 1998, was Deputy Chairman of Vodafone Group Plc.

\*\*SIR CLIVE WHITMORE GCB, CVO  
*Non-Executive*

Aged 63. Appointed to the board in 1994 following his retirement as Permanent Under Secretary of State at the Home Office. He is also a director of The Boots Company PLC, The Morgan Crucible Company PLC and NM Rothschild & Sons Limited.



DAVID WHITTAKER LLB, FCIS, FCCA,  
SOLICITOR  
*Company Secretary, Legal Services*

Aged 54. Has been with the Group since 1975, becoming Company Secretary in 1986 and joining the board in 1992.

ANDREW WOOD ACMA  
*Finance*

Aged 47. Appointed to the board in 1995, having joined the Group in 1984.



\* Member of the Audit Committee and the Nomination Committee  
\*\*Member of the Audit Committee, the Remuneration Committee and the Nomination Committee

Registered Office  
Western Road  
Bracknell, Berkshire  
RG12 1RG

Auditors  
Deloitte & Touche  
Hill House  
1 Little New Street  
London EC4A 3TR

Registrars & Transfer Office  
IRG plc  
Bourne House  
34 Beckenham Road  
Beckenham, Kent BR3 4TU

# Report of the Directors

The directors submit their annual report and audited financial statements for the year ended 31 March 1998.

## **Review of the Group's business**

Details of the Group's results, the second interim dividend and the development of the Group during the year are given in the Chairman's Statement, the Review of Operations and the Financial Review.

Racal Electronics Plc is the parent company of a group whose principal activities during the year were Telecommunications Services, Defence Electronics, Data Products and Industrial Electronics. The principal companies which materially contribute to the assets and profits appear on pages 34 and 35.

## **Research and development**

The Group maintains extensive laboratory facilities and continues to invest considerable resources in the development of new and existing products as referred to in the Chairman's Statement and the Review of Operations.

## **Future developments**

The Racal Electronics Group intends to continue its policy of growth as described in the Chairman's Statement and the Review of Operations.

## **Share capital**

A statement of changes in the share capital of the Company appears on pages 52 and 53 in Note 24.

## **Employee involvement**

The Company positively encourages the involvement of employees within the business and a variety of communication processes have been established throughout the Group to ensure regular contact and exchange of information. These include, but are not limited to, team briefings, staff councils, trade union committees, focus groups and departmental meetings.

The directors of the Company are committed to the principle of employee share participation in the Company through employee share schemes.

## **Disabled persons**

The Group is very conscious of the difficulties experienced by people with disabilities. Its attitude to the employment of disabled persons is the same as that relating to all other staff in matters of recruitment, continuity of employment, training, development and promotion, and it will take sympathetic account of individual circumstances.

The Group is a member of the Employers' Forum on Disability.

## **Charitable and political contributions**

During the year ended 31 March 1998 charitable contributions amounted to £148,000 (1997: £86,000). Of this amount £143,000 (1997: £86,000) was contributed on behalf of your Company to charitable foundations and £5,000 (1997: £nil) to support a university project. Registered charities active in the field of medical research received a major contribution, the rest was shared mainly by organisations supporting children, the sick and the aged.

A contribution of £75,000 (1997: £nil) was made to the Conservative Party.

## **Auditors**

Deloitte & Touche have expressed their willingness to continue in office and a resolution will be proposed at the Annual General Meeting to re-appoint them as auditors to the Company.

## **Goodwill**

As a result of acquisitions, £4,854,000 of goodwill has been transferred to the goodwill reserve. A total of £116,692,000 has been transferred from the goodwill reserve to the profit and loss account in respect of businesses sold (£8,378,000) and discontinuing operations (£108,314,000).

## **Payments to creditors**

It is the Group's normal practice to make payments to suppliers promptly provided that the supplier has performed in accordance with the relevant terms and conditions. Group trade creditors at 31 March 1998 were equivalent to 49 days' average daily amount invoiced by suppliers during the year (1997: 60 days).

## **Share capital – allotment of shares**

As in past years, the directors seek to obtain shareholder approval for the renewal of their authority to allot unissued shares in the capital of the Company for cash other than to existing shareholders.

The amount shown in Resolution No. 9 as the Section 89 amount is the maximum amount of share capital that may be allotted wholly for cash other than on a pre-emptive basis to existing shareholders for the period to the date of the 1999 Annual General Meeting and represents 5% of the present issued ordinary share capital. As in previous years, it is intended that the ordinary shares required for the Racal Electronics Corporate Personal Equity Plans will be allotted to participants under this power.

## **Employee Share Ownership Trust**

The Company has established an Employee Share Ownership Trust to purchase shares in the market for distribution at a later date in accordance with the terms of the Racal Share Option Scheme 1992, the Racal Share Option Scheme 1995 and the Racal Share Option Scheme 1997. The shares are held by an independent trustee and the right to dividend on the shares has been waived apart from a nominal amount. Accordingly, the executive directors and other executives of the Company have an interest in the shares held within the Trust. As at 31 March 1998, the number of shares held by the Trust totalled 3,149,000 shares (1997: 3,149,000 shares) and the cost of such shares amounted to £8,143,000 (1997: £8,143,000). These shares, whilst legally not the property of the Company, have been included in fixed asset investments as shown on page 49 in Note 13. During the year, the terms of this Trust were amended so that the Trustee could subscribe for the Company's shares and so that such shares could be used to satisfy options granted under the terms of the Share Option Schemes referred to above together with options to be granted under the terms of the Racal Share Savings Plan (1990). These amendments do not apply to those options granted under the Racal Share Savings Plan (1990) in October 1992.

## **Qualifying Employee Share Ownership Trust**

During the year, the Company established a Qualifying Employee Share Ownership Trust (QUEST) to operate in conjunction with the options granted under the Racal Share Savings Plan (1990) in October 1992. Accordingly, the executive directors and other executives of the Company have an interest in the shares held by the QUEST. As at 31 March 1998, 159,948 shares were held by the QUEST and the cost of such shares amounted to £466,000. These shares, whilst legally not the property of the Company, have been included in fixed asset investments as shown on page 49 in Note 13.

# Report of the Directors

## Corporate governance

The Company has continued to comply with the Code of Best Practice issued by the Committee on the Financial Aspects of Corporate Governance – “The Cadbury Report”. The Company has also complied with the disclosure requirements in respect of directors’ remuneration arising from the Greenbury Committee recommendations. These are included within the Report of the Remuneration Committee on pages 28 to 30.

## The board

The board of directors comprised seven executive directors and three independent non-executive directors throughout the year. One non-executive director resigned and one non-executive director was appointed during the year.

The board is responsible for policy and strategy. It meets at regular intervals to review progress and the Group’s financial performance and has agreed a formal schedule of matters reserved to it for collective decision.

Each of the non-executive directors has access to and is furnished with such information as he requires to enable him to bring an independent judgement to bear on issues brought before the board at board meetings and board committee meetings. The views of the non-executive directors carry significant weight in the board’s decisions.

A formal procedure exists to allow the directors of the Company to take independent professional advice at the expense of the Company in appropriate circumstances. All directors have access to the Company Secretary for his advice and services.

## Board committees

The board has a number of committees of which the following are the most significant:

### Remuneration Committee

Sir Gerald Whent – Chairman  
Sir Edward Ashmore (to 3 October 1997)  
Lord Inge  
Sir Clive Whitmore

The Committee meets as necessary and the Company Secretary attends these meetings as Secretary to the Committee. The Company Chairman and the Chief Executive are invited to attend the Committee meetings as the members consider appropriate.

The Committee decides upon all aspects related to the executive directors’ pay and benefits.

The fees of the non-executive directors are decided by the board with the non-executive directors abstaining.

The Committee’s report to shareholders appears on pages 28 to 30.

### Audit Committee

Sir Clive Whitmore – Chairman  
Sir Edward Ashmore (to 3 October 1997)  
Sir Ernest Harrison  
Lord Inge  
Sir Gerald Whent

The Committee meets at least twice a year and the Company Secretary attends these meetings as Secretary to the Committee. The Financial Director and the auditors are invited to attend as appropriate.

The Committee reviews the annual audit and interim accounts, internal financial controls and reports from the Company’s internal and external auditors.

Although the Code recommends only non-executive directors for this Committee, the board considers that Sir Ernest Harrison’s qualification as a Chartered Accountant makes his continued membership of this Committee entirely suitable.

## Nomination Committee

Sir Gerald Whent – Chairman  
Sir Edward Ashmore (to 3 October 1997)  
Sir Ernest Harrison  
Lord Inge  
Sir Clive Whitmore

The Committee meets as necessary and the Company Secretary attends these meetings as Secretary to the Committee.

The Committee assesses the suitability of persons for appointment as executive directors and non-executive directors and when appropriate nominates new candidates for the approval of the board.

The minutes of all of the above Committee meetings are circulated to all directors.

## Going concern

After making enquiries, the directors consider that the Group has adequate resources and committed borrowing facilities to continue in operational existence for the foreseeable future. Consequently they have continued to adopt the going concern basis in preparing the accounts.

## Internal financial control

The directors acknowledge that they are responsible for the Group’s systems of internal financial control.

On behalf of the board, the Audit Committee monitors the effectiveness of these systems. This is achieved primarily through a review of the internal audit programme and its findings and a review of the nature and scope of the external audit. Any identified risks are closely examined so that appropriate action can be taken.

The systems of internal financial control are designed to provide reasonable, but not absolute, assurance against material misstatement or loss. They operate within an established organisation structure with formally defined areas of responsibility. They include:

- a comprehensive budgeting system with an annual budget approved by the board;
- regular consideration by the board of actual results compared with budgets, forecasts and the prior year;
- regular reviews by the board of quarterly forecasts which are updated every period;
- regular reporting to the board on treasury, pensions, legal and insurance matters. All of these areas are subject to clearly defined policies and procedures;
- a continuous assessment of business risk by the executive directors in conjunction with operating management. Wherever possible, steps are taken to mitigate these risks. The executive directors regularly report to the board;
- an internal audit function located both in the UK and the USA, which reviews the systems and procedures in major operating companies and reports to the Audit Committee at least twice a year. The external auditors independently report to the Audit Committee.

The directors have reviewed the effectiveness of the Group’s systems of internal financial control. Whilst the directors are generally satisfied and consider the controls appropriate for their business a number of areas have been identified for improvement and appropriate actions have been agreed. None of these areas identified for improvement has resulted in any material loss or misstatement as at 31 March 1998.

# Report of the Directors

## Directors

The directors throughout the year were Sir Ernest Harrison, D C Elsbury, B J Clarke, P G Kozlowski, M R Richardson, Sir Gerald Whent, Sir Clive Whitmore, D Whittaker and A R Wood. Sir Edward Ashmore resigned as a director on 3 October 1997 and Lord Inge was appointed a director on 6 October 1997.

In accordance with the Company's Articles of Association, Sir Ernest Harrison and Sir Gerald Whent, each having reached the age of 70 years, retire and being eligible offer themselves for re-election.

In accordance with the Company's Articles of Association, B J Clarke and A R Wood retire by rotation and being eligible offer themselves for re-election.

Lord Inge, who has been appointed by the board since the last Annual General Meeting, retires and being eligible, offers himself for election.

Sir Ernest Harrison, who is aged 72 years, has a service agreement with the Company which is terminable on 12 months' notice. Sir Gerald Whent, who is aged 71 years, has accepted a letter of appointment with the Company for a fixed period of three years effective from 4 August 1996.

Lord Inge has accepted a letter of appointment with the Company which is for a fixed period of three years expiring on 5 October 2000.

B J Clarke has a fixed term service agreement with the Company expiring on 12 May 1999 and A R Wood has a service agreement with the Company which is terminable on 12 months' notice.

None of the directors had a material interest in any contract of significance to which the parent company or a subsidiary was a party during the financial year.

## Directors' share interests

The directors' share interests are set out in the Report of the Remuneration Committee on pages 29 and 30.

## Environment

Racal recognises the importance of protecting the environment in conducting its business. The Group seeks to protect the environment by:

- working with our customers and suppliers to develop sound product management;
- developing programmes for continuous improvement;
- minimising the use of energy, materials and the production of waste;
- participation with other industrial organisations seeking to promote product recycling and environmentally conscious design.

This programme is implemented throughout the Group by assigning responsibility to the operating companies and is supported by Group resources, which provide the necessary information and training to encourage all employees to be environmentally aware and responsible.

## Substantial holdings

As at 24 August 1998 the directors had been informed of the following interests in the Company's ordinary share capital in excess of 3%:

Guardian Royal Exchange plc*	5.89%
The State of Wisconsin Investment Board	3.92%
Prudential Corporation plc*	3.89%
Government of Singapore Investment Corporation Pte Limited	3.01%

\*includes shareholdings of subsidiary companies.

The directors are not aware of any other holdings in excess of 3%.

## Year 2000

A Group wide programme is under way to address the impact of Year 2000 on all aspects of our business.

At the Group level, a Year 2000 project team has been constituted which reports to the Company Secretary. This team, which is chaired by the Managing Director of Racal Research Limited, has the following specific objectives:

- to define Group policy and targets;
- to monitor progress of local programmes and to identify particular areas of exposure;
- to provide advice and assistance as required on programmes, standard wording and liability issues.

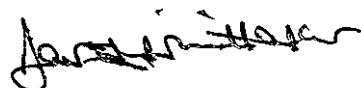
Each Group company and central function has responsibility for ensuring Year 2000 compliance in respect of its own products, business systems, site facilities and supply chain. All operations have prepared detailed plans to achieve compliance, incorporating measurable performance milestones, with implementation being the responsibility of a specific local director who reports monthly to the Group Year 2000 project team. The compliance process typically involves evaluation, implementation and testing, based upon the BSI definition of Year 2000 compliance (PD2000-1). This process is well under way in all Racal operating companies and central functions.

Most parts of the Group are planning to complete their Year 2000 compliance programmes during the early part of 1999. Much of the cost has been absorbed in normal operating activities, such as routine upgrades and replacement of systems. Incremental external expenditure identified to date to address the issue is approximately £9.3 million, of which approximately 90% is capital expenditure.

## European Monetary Union

The Group recognises the importance of European Economic and Monetary Union (EMU), particularly for its businesses operating in those countries which are committed to the introduction of a single European currency. In the short term, we believe that the impact of EMU on the Group will be minimal. The Group is assessing the risks and opportunities of EMU in the longer term. The financial costs of preparation for EMU are not expected to be material in the context of the Group.

By Order of the Board  
David Whittaker  
Director and Secretary



18 September 1998

# Report of the Remuneration Committee

## Constitution

The current members of the Remuneration Committee are Sir Gerald Whent, Lord Inge and Sir Clive Whitmore. The Chairman of the Committee is Sir Gerald Whent and D Whittaker, the Company Secretary, attends as Secretary to the Committee.

The composition of the Committee is therefore restricted to non-executive directors, although the Committee consults, as appropriate, with both the Company Chairman and the Chief Executive.

The Company has complied throughout the accounting period with Section A of the best practice provisions annexed to the Listing Rules of the London Stock Exchange.

The following report of the Committee includes all relevant information which is required by the Listing Rules of the London Stock Exchange in respect of this accounting period.

The London Stock Exchange published at the end of June 1998 the final version of the Principles of Good Governance and Code of Best Practice ('the Combined Code') initially drafted by the Committee on Corporate Governance chaired by Sir Ronald Hampel, together with the wording of the related new Listing Rules. The Company is not, however, required to disclose how it has applied the principles and complied with the detailed provisions of the Combined Code in this report, as this applies only in respect of accounting periods ending on or after 31 December 1998, but will do so, as required, in the annual report and accounts for the year ending 31 March 1999.

## The Company's policy on executive directors' remuneration and share options

The policy of the Committee in respect of the remuneration of the executive directors of the Company is to ensure that:

- (i) individuals are fairly rewarded for their personal contribution to the Company's overall performance in the short and longer term;
- (ii) the Company is able to attract, retain and motivate directors of the highest calibre; and
- (iii) due regard is given to the interests of the Company's shareholders and to the financial and commercial health of the Company and its performance relative to that of other comparable companies.

This policy is applied by the Committee in carrying out its responsibilities to develop and implement remuneration packages which are based on maintaining a strong link between reward and performance to align the interests of executive directors and shareholders.

## Directors' emoluments

	Salary and fees	Annual bonus	Benefits	Total emoluments excluding pension costs 1998	1997
	£	£	£	£	£
<b>Executive directors</b>					
Sir Ernest Harrison * (Note 3 below)	229,975	—	27,029	257,004	426,957
D C Elsbury *	409,738	—	33,580	443,318	305,040
B J Clarke	265,445	—	18,226	283,671	264,147
P G Kozlowski	289,673	108,683	7,169	405,525	285,187
M R Richardson	285,580	—	15,228	300,808	289,646
D Whittaker	265,445	—	16,542	281,987	267,723
A R Wood	215,438	—	16,353	231,791	198,350
<b>Non-executive directors</b>					
Sir Edward Ashmore (resigned 3.10.97)	36,944	—	7,075	44,019	83,532
Lord Inge (appointed 6.10.97)	21,889	—	—	21,889	—
Sir Gerald Whent	49,701	—	—	49,701	47,334
Sir Clive Whitmore	34,316	—	—	34,316	32,681
<b>Total</b>	<b>2,104,144</b>	<b>108,683</b>	<b>141,202</b>	<b>2,354,029</b>	<b>2,200,597</b>

The executive directors' total remuneration is made up of two components: salary and benefits and long term incentive in the form of Executive Share Option Schemes.

In addition, P G Kozlowski participated in a bonus arrangement operated in respect of key individuals in the Racal Data Group designed to maximise their continued motivation and commitment to the Racal Data Group.

The Committee's policy in approving grants of share options to directors is that the director's total remuneration package taken together with the option to be granted should not be excessive. Options should be granted in order to retain, recruit and motivate the director in question. In normal circumstances, options granted should not be exercisable in under three years. The options to be granted should be subject to appropriately challenging performance criteria.

In framing and implementing this remuneration policy the Committee gives full consideration to Section B of the best practice provisions annexed to the Listing Rules of the London Stock Exchange.

## Directors' service agreements

### Executive directors

Sir Ernest Harrison, D C Elsbury and A R Wood each have service agreements with the Company which are terminable by the Company or the director on 12 months' notice. B J Clarke has a fixed term contract expiring on 12 May 1999. M R Richardson and D Whittaker each have agreements with a rolling 36 month term which was the recognised term for agreements of this nature when they entered into their service agreements in 1990. P G Kozlowski, a US citizen, has a service agreement with a subsidiary company which is terminable by him or that company on 12 months' notice.

Sir Ernest Harrison, A R Wood and B J Clarke will be standing for re-election at the forthcoming Annual General Meeting.

The Committee has determined that notice or contract periods for 12 months should be offered to executive directors in the future. Longer periods will be avoided wherever possible.

### Non-executive directors

The remuneration of the non-executive directors continues to be determined by the board with the non-executive directors abstaining.

The non-executive directors currently serve under Letters of Appointment. Sir Gerald Whent's appointment will expire on 3 August 1999, Lord Inge's appointment will expire on 5 October 2000 and that of Sir Clive Whitmore on 31 October 2000.

Sir Gerald Whent will be standing for re-election and Lord Inge will be standing for election at the forthcoming Annual General Meeting.

# Report of the Remuneration Committee

## Directors' emoluments (continued)

### Notes:

1. Benefits include all assessable tax benefits arising from employment by the Company which mainly derive from the provision of a company car and private medical insurance.
2. There was no bonus scheme in operation in the year ended 31 March 1998 other than for P G Kozlowski.
3. The amounts charged to Vodafone Group Plc and Chubb Security Plc in respect of Sir Ernest Harrison's services as Chairman of those companies are as follows:

	1998 £	1997 £
Charged to Vodafone Group Plc**	213,404	201,882
Charged to Chubb Security Plc***	16,571	304,389
Sub total.....	229,975	506,271
Benefits other than pension borne by the Company****	27,029	16,098
Total*****	257,004	522,369

\* Sir Ernest Harrison and D C Elsbury agreed with the Company on 30 September 1997 to vary the rate of their contractual remuneration for the services provided by them to the Company in respect of the year ended 31 March 1998 and how it was to be paid. In respect of that year, Sir Ernest Harrison agreed to waive all of his salary borne by the Company, namely £497,234 and £188,494 of his pension entitlement and D C Elsbury agreed to waive £136,579 of his salary. The prepayments disclosed in last year's accounts were set off against the salary in the current year following these waivers. Following the set offs and the payment of the sum of £67,392 by Sir Ernest Harrison to the Company all such prepayments were satisfied in full by the end of the year.

\*\* Sir Ernest Harrison retired as Chairman of Vodafone Group Plc on 21 July 1998.

\*\*\* Sir Ernest Harrison ceased to be Chairman of Chubb Security Plc on 29 April 1997 following the acquisition of Chubb Security Plc by Williams PLC.

\*\*\*\* The 1998 pension costs are shown in the table below.

\*\*\*\*\* The 1997 total includes pension costs of £95,412. Net of pension costs this amounted to £426,957.

## Pension benefits

	(1) Contributions by Company to defined contribution retirement benefit arrangements	(2) Transfer value of increase in year of per annum pension payable at normal retirement age (calculated on the basis of actuarial guidance note GN11) less director's contributions	(3) Accumulated total accrued pension representing amount payable annually at normal retirement age based on service to 31 March of year	(4) Increase in accrued annual pension over year, excluding inflation
	1998 £	1998 £	1998 £	1998 £
Sir Ernest Harrison	57,494	—	—	—
P G Kozlowski	99,589	—	—	—
M R Richardson	—	102,269	110,385	8,631
D Whittaker	—	158,492	132,227	11,373
A R Wood	—	118,362	61,029	10,958

### Notes:

1. D C Elsbury and B J Clarke have retired from pensionable service under the Group's defined benefit pension arrangements and therefore do not accrue pension benefits. The non-executive directors have no pension arrangements with any Group company.
2. M R Richardson, D Whittaker and A R Wood participate in the Company's defined benefit scheme for the Group's directors and have the option to pay additional voluntary contributions; neither those contributions nor the resulting benefits are included in the above table.
3. The costs shown in column (2) have been calculated using the transfer basis and prevailing assumptions as at 31 March 1998, that is the Minimum Funding Requirement (MFR). The figures in column (2) would be up to 10% lower following the change in the MFR basis introduced with effect from 15 June 1998.

## Directors' interests in the shares of Racal Electronics Plc

	31 March 1998	1 April 1997
Sir Ernest Harrison	2,746,603	2,196,461
D C Elsbury	1,274,505	1,244,363
B J Clarke	87,812	70,170
Lord Inge	8,609	*—
P G Kozlowski	3,000	3,000
M R Richardson	14,500	2,000
Sir Gerald Whent	38,334	38,334
Sir Clive Whitmore	2,083	2,050
D Whittaker	92,385	92,385
A R Wood	15,294	10,128
	4,283,125	3,658,891

All the above interests are beneficial.

\* Interest on date of appointment

During the period 1 April to 24 August 1998, there have been the following changes in the directors' interests in the shares of the Company:

M R Richardson and D Whittaker each exercised their option under the Racal Share Savings Plan (1990) and were accordingly allocated 5,142 shares at the price of 105p per share.

No director had since 1 April 1997 any interest in, or acquired any rights to, shares in the Company or any subsidiary except as stated.

# Report of the Remuneration Committee

## Directors' share options

### 1. Racial Share Option Scheme 1992

	Option	Ordinary shares under option		Option Price
		1 April 1997	31 March 1998	
Sir Ernest Harrison	A	570,000	570,000	130.5p
	Parallel A	142,500	142,500	114p
	B	250,000	250,000	243p
	C	467,000	467,000	270p
D C Elsbury	A	566,000	566,000	130.5p
	Parallel A	141,500	141,500	114p
	B	200,000	200,000	243p
	C	210,000	210,000	270p
B J Clarke	A	218,000	218,000	130.5p
	Parallel A	54,500	54,500	114p
	B	82,000	82,000	243p
	C	114,000	114,000	270p
M R Richardson	A	218,000	218,000	130.5p
	Parallel A	54,500	54,500	114p
	B	100,000	100,000	243p
	C	81,000	81,000	270p
D Whittaker	A	227,000	227,000	130.5p
	Parallel A	56,750	56,750	114p
	B	82,000	82,000	243p
	C	115,000	115,000	270p
A R Wood	B	35,000	35,000	251p
	C	166,000	166,000	270p

No options were granted, exercised or lapsed during the year under this Scheme.

Notes: Option A – Granted on 5 October 1992 and exercisable during the period 5 October 1995 to 4 October 2002.  
 Parallel A – Granted on 8 October 1992 and exercisable during the period 8 October 1997 to 7 October 2002. This option is now exercisable as the earnings per share of the Company has grown over a five year period by at least 10 percentage points more than the Index of Retail Prices has grown over the same period. This option runs in parallel with Option A and is not additional thereto.  
 Option B – Granted on 19 July 1994 and exercisable during the period 19 July 1997 to 18 July 2004.  
 Option C – Granted on 13 July 1995 and exercisable during the period 13 July 1998 to 12 July 2005.

### 2. Racial Share Option Scheme 1995

Under the terms of the Racial Share Option Scheme 1995, P G Kozlowski was granted an option on 18 July 1995 to acquire 204,000 ordinary shares in the Company at the price of 275p per share. This option is exercisable during the period 18 July 1998 to 17 July 2005.

### 3. Racial Share Option Scheme 1997

Under the terms of the Racial Share Option Scheme 1997, the undermentioned directors have been granted options during the year, exercisable between 12 December 2000 and 11 December 2004, to acquire ordinary shares in the Company at the price of 235p per share:

Sir Ernest Harrison	100,000
D C Elsbury	100,000
B J Clarke	100,000
M R Richardson	100,000
D Whittaker	100,000
A R Wood	100,000

The exercise of these options is subject to the Company achieving growth in its earnings per share over a three year period in excess of the Index of Retail Prices by an average of 3% per year.

### 4. Racial Share Savings Plan (1990)

Under the terms of the Racial Share Savings Plan (1990), the undermentioned directors have been granted options to acquire ordinary shares in the Company as follows:

	Option A	Option B
Sir Ernest Harrison	*–	3,484
D C Elsbury	*–	3,484
B J Clarke	*–	3,484
M R Richardson	5,142	3,484
D Whittaker	5,142	3,484
A R Wood	–	3,484

Notes: Option A – Options exercisable at 105p per share during the period 1 December 1997 to 31 May 1998 which were exercised before the latter date.  
 Option B – Options exercisable at 198p per share during the period 1 April 2003 to 30 September 2003.

\*During the year ended 31 March 1998, Sir Ernest Harrison, D C Elsbury and B J Clarke each exercised their option for 5,142 shares at the price of 105p per share.

The A Options were held at 1 April 1997 and at 31 March 1998 and the B Options were granted during the year.

The closing mid-market value of an ordinary share on 31 March 1998 was 339.5p and during the year the mid-market value ranged from 201.5p to 339.5p.

On behalf of the Board  
 Sir Gerald Whent  
 Chairman, Remuneration Committee  
 18 September 1998



# Auditors' Report on Corporate Governance

## **Review report to Racal Electronics Plc by Deloitte & Touche on corporate governance matters**

In addition to our audit of the financial statements, we have reviewed the directors' statements on page 26 on the Company's compliance with the paragraphs of the 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 have also reviewed the statement of compliance with Section A of the best practice provisions on remuneration committees and the report to members by the Remuneration Committee set out respectively on pages 28 to 30 to the extent that they provide the disclosures specified by the Listing Rules.

### **Basis of opinion**

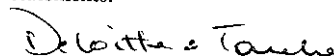
We carried out our review in accordance with guidance issued by the Auditing Practices Board. That guidance does not require us to perform the additional work necessary to, and we do not, express any opinion on the effectiveness of either the Company's system of internal financial control or its corporate governance procedures or on the appropriateness of the bases used in determining directors' remuneration or on the ability of the Company to continue in operational existence.

### **Opinion**

With respect to the directors' statement on internal financial control on page 26 (other than their opinion on effectiveness and statements going beyond internal financial control which are outside the scope of our report), and going concern on page 26, in our opinion the directors have provided the disclosures required by the Listing Rules referred to above and such statements are not inconsistent with the information of which we are aware from our audit work on the financial statements.

Based on enquiry of certain directors and officers of the Company, and examination of relevant documents, in our opinion the directors' statement on page 26 appropriately reflects the Company's compliance with the other paragraphs of the Code specified for our review by Listing Rule 12.43(j).

Also on this basis, in our opinion the directors' statements of compliance with Section A of the best practice provisions on remuneration committees and the report of the Remuneration Committee appropriately provide the disclosures specified by the Listing Rules and are not inconsistent with the information of which we have become aware from our audit work on the financial statements.



**Deloitte & Touche**  
Chartered Accountants  
Hill House  
1 Little New Street  
London EC4A 3TR  
18 September 1998

# Statement of 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 Group as at the end of the financial year and of the profit or loss of the Group 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;
- prepare the financial statements on a 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 the Group and to enable them to ensure that the financial statements comply with the Companies Act. They are also responsible for the Group's systems of internal financial controls and for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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## Report of the Auditors

### **To the Members of Racal Electronics Plc**

We have audited the financial statements on pages 34 to 59 which have been prepared under the accounting policies set out on page 36, and the detailed information disclosed in respect of any directors' remuneration and share options set out in the report to members by the Remuneration Committee on pages 28 to 30.

### **Respective responsibilities of directors and auditors**

As described above 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 and the 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 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 affairs of the Company and the Group as at 31 March 1998 and of the loss of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

*Deloitte & Touche*

### **Deloitte & Touche**

Chartered Accountants and Registered Auditors  
Hill House  
1 Little New Street  
London EC4A 3TR  
18 September 1998

# Comparative Summary for Five Years

	1994	1995	1996	1997	1998
	£000	£000	£000	£000	£000
<b>Turnover</b>					
Ongoing operations	454,508	541,137	670,730	830,752	920,705
Discontinuing operations	320,547	286,147	268,463	255,031	186,761
Discontinued operations	141,036	122,915	119,809	99,213	36,948
Total	916,091	950,199	1,059,002	1,184,996	1,144,414
<b>Profit</b>					
Ongoing operations					
Operating profit	56,510	75,301	98,288	103,729	105,637
Operating profit % sales	12.4%	13.9%	14.7%	12.5%	11.5%
Operating (loss)/profit – discontinuing operations	(12,776)	(23,261)	(26,909)	(23,715)	(59,228)
– discontinued operations	284	7,484	6,090	2,566	(4,384)
Exceptional (loss)/profit	(19,222)	2,508	3,945	(19,309)	(224,483)
Demerger costs	(49)	–	–	–	–
Amounts written off investments	–	–	–	–	(2,052)
Net interest receivable/(payable)	1,633	(3,730)	(11,003)	(22,851)	(22,670)
Profit/(loss) before taxation	26,380	58,302	70,411	40,420	(207,180)
Profit/(loss) after taxation and minority interests	15,297	38,237	46,126	31,778	(218,632)
Dividends per share	4.25p	5.0p	6.0p	6.0p	6.0p
Earnings/(loss) per share	5.47p	13.70p	16.54p	11.30p	(77.27)p
Adjusted earnings per share	13.40p	16.68p	21.36p	24.88p	24.97p
<b>Balance sheets</b>					
Fixed assets	204,014	240,451	406,664	474,536	485,960
Working capital	385,227	398,339	405,958	371,507	279,300
Other net liabilities	(28,470)	(29,922)	(36,292)	(40,077)	(27,098)
Net debt	(20,042)	(52,708)	(324,089)	(339,453)	(307,629)
Provisions for liabilities and charges	(7,657)	(24,110)	(18,168)	(18,414)	(105,703)
	533,072	532,050	434,073	448,099	324,830
Equity shareholders' funds	530,491	530,595	432,833	447,056	323,952
Equity minority interests	2,581	1,455	1,240	1,043	878
	533,072	532,050	434,073	448,099	324,830

# Principal Subsidiaries of Racal Electronics Plc

At 31 March 1998

## United Kingdom

(Registered in England and Wales except where stated)

(The country of registration is also the principal place of operation except where stated)

Wholly owned except where stated: sub-subsidiaries are shown inset

	<b>Business activity</b>
Decca Limited	Holding company
Fibre Form Limited	Polyurethane and fibre mouldings
Racal-Decca Limited	Holding company
Racal Avionics Limited	Avionics products
Racal Defence Radar Limited	Defence radar
Racal Radar Defence Systems Limited	Defence radar
Racal-MESL Limited (Scotland)	Microwave components and sub-systems
Racal Survey Limited	Survey and positioning services
Racal Tracs Limited	Survey and positioning services
Racal Survey Overseas Limited†	Survey and positioning services
Racal Acoustics Limited	Electro-acoustics products
Racal-Airtech Limited	Secure payment systems
Racal Antennas Limited	Antennas
Racal-Datacom Limited	Data communications products
Racal Engineering Limited	Metalwork machining
Racal Finance Limited	Financial services
Racal Group Services Limited	Central services
Racal Instruments Group Limited	Holding company
Racal Instruments Limited	Test and measurement products
Racal Recorders Limited	Data and communications recording
Racal International (Holdings) Limited	Holding company
Racal International Limited	Holding company
Racal Messenger Limited	'Widanet' and 'Talon'
Racal Network Services Group Limited	Holding company
Racal-Integralis Limited (60%)	Internet service provider
Racal Managed Services Limited	Managed network services
Racal Telecommunications Networks Limited	Managed network services
Racal Properties Limited	Property management
Racal Radio Limited	Radio communications
Racal Research Limited	Research and development
Racal Telecommunications Limited	Telecommunications services
Racal Training Services Limited	Training and education
Racal-Transcom Limited	Point of sale terminals and management systems

## Associated companies

Archer Communications Systems Limited (30%)*	Radio communications
Camelot Group plc (22.5%)	Lotteries
Global Telematics Plc (50%)*	Vehicle telematic products and services
Racal Insurance Services Limited (50%)	Insurance services
Satellite Information Services (Holdings) Limited (21.96%)	Satellite communications

† Principal place of operation – Abu Dhabi

\* Held by a subsidiary company

# Principal Subsidiaries of Racal Electronics Plc

At 31 March 1998

## International

(The country of incorporation is also the principal place of operation)

Wholly owned except where stated: no subsidiary listed below is directly owned by Racal Electronics Plc except where stated

	Country of incorporation	Business activity
The Racal Corporation	USA	Holding company
Racal Avionics Inc.	USA	Avionics products
Racal Communications Inc.	USA	Radio communications
Racal-Datacom Inc.	USA	Data communications products
Racal-Guardata Inc.	USA	Network encryption products
Racal Instruments Inc.	USA	Test and measurement products
Racal-NCS Inc.	USA	Survey and positioning services
Racal Pelagos Inc.	USA	Survey and positioning services
Racal Recorders Inc.	USA	Data and communications recording
Racal Telecommunications Inc.	USA	Telecommunications services
Racal-Datacom SA	France	Data communications products
Racal Geodia SA (60%)	France	Survey and positioning services
Racal-MESL (France) Sarl	France	Microwave components and sub-systems
Racal Systems Electronique SA	France	Test and measurement products*
Racal-Datacom GmbH	Germany	Data communications products
Racal Electronics Deutschland Holding GmbH	Germany	Holding company
Racal-Heim Systems GmbH	Germany	Data and communications recording
Racal Instruments GmbH	Germany	Test and measurement products*
Racal-Datacom SpA	Italy	Data communications products
Racal Systems Elettronica Srl	Italy	Test and measurement products
Nederland Survey Projecten en Apparatuur BV	Netherlands	Survey and positioning services
Racal-Datacom BV	Netherlands	Data communications products
Racal Electronics Europe BV	Netherlands	Holding company
Racal Telecommunications Networks BV	Netherlands	Managed network services
Racal Survey Norge A/S	Norway	Survey and positioning services
Racal Australia Pty Limited	Australia	Distributor for group products
Racal Survey Australia Limited	Australia	Survey and positioning services
Racal New Zealand Limited	New Zealand	Network services
Saracen Insurance Company Limited†	Bermuda	Insurance services
The Racal Corporation Canada Inc.	Canada	Holding company
Racal Canada Inc.	Canada	Radio communications
Racal-Datacom (Canada) Inc.	Canada	Data communications products
Racal Pelagos Canada Limited	Canada	Survey and positioning services
Racal Recorders (Canada) Inc.	Canada	Data and communications recording
Racal Survey Mexicana SA de CV	Mexico	Survey and positioning services
Racal Asia Limited	Hong Kong	Data communications products
Racal Survey (Malaysia) Sdn Bhd (70%)	Malaysia	Survey and positioning services
Racal Electronics (Singapore) Private Limited	Singapore	Data communications products*
Racal Survey (Singapore) Private Limited	Singapore	Survey and positioning services
Techno Transfer Industries Pte Limited (80%)	Singapore	Manufacture of remotely operated submersible vehicles
Racal Electronics South Africa Pty Limited	South Africa	Distributor for group products

## Associated companies

China Bohai Racal Positioning and Survey Company Limited (50%)	People's Rep. of China
China Nanhai Racal Positioning and Survey Company Limited (50%)	People's Rep. of China
Decca Survey (Saudi Arabia) Limited (40%)	Saudi Arabia
Euroart Advanced Radar Technology GmbH (25%)	Germany
International Optical Network LLC (50%)	USA

Survey and positioning services

Survey and positioning services

Survey and positioning services

Defence radar

Telecommunications services

\* also distributor for other group products

† directly owned by Racal Electronics Plc

# Statement of Accounting Policies

The financial statements have been prepared in accordance with applicable accounting standards. The particular accounting policies adopted are described below.

## 1 Basis of accounting

The accounts are prepared under the historical cost convention modified by the revaluation of certain tangible fixed assets.

## 2 Basis of consolidation

The Group financial statements are the result of the consolidation of the accounts of the Company and its subsidiaries and also include the Group's share of the results of associated companies. The accounts of all companies are made up to 31 March 1998. Where subsidiary or associated companies are acquired during the year, the surplus of cost over fair value attributed to the assets acquired (goodwill) is transferred to the goodwill reserve.

## 3 Turnover

Turnover represents invoiced sales (net of sales related taxes) by the Group to outside customers and in the case of long term contracts an estimate of the selling value of work done. In accordance with Statement of Standard Accounting Practice No. 21, the equivalent sales value of equipment sold under a finance lease arrangement is included in turnover. Revenue from equipment leased to customers under operating leases is recorded as turnover in equal amounts over the life of the leases.

## 4 Foreign currencies

The accounts of overseas subsidiary and associated companies, and assets and liabilities denominated in foreign currencies held by United Kingdom companies, have been translated at the rates ruling on 31 March 1998. Exchange differences arising on the retranslation of these accounts at the beginning of the year, and differences on long term foreign currency loans which relate to investments in overseas companies, are dealt with as a movement in reserves. All other differences are taken to profit and loss account. United Kingdom exports in foreign currencies are converted at the rates relative to the period of shipment.

## 5 Stocks

Stocks and work in progress are valued at the lower of cost and estimated net realisable value less progress payments received. Cost includes manufacturing overheads. Long term contract work in progress is valued at cost less foreseeable losses, less progress payments received.

## 6 Leases

Tangible fixed assets held under finance leases and the related lease obligations are recorded in the balance sheet at the fair value of the leased assets at the inception of the lease. The excesses of the lease payments over the recorded lease obligations are treated as finance charges which are amortised over each lease term to give a constant rate of charge on the remaining balance of the obligations.

Rental costs under operating leases are charged to profit and loss account in equal annual amounts over the periods of the leases.

## 7 Research and development

Private venture research and development expenditure is written off in the year in which it is incurred. Uninvoiced research and development fully funded by customers is carried forward as work in progress.

## 8 Depreciation

Depreciation is provided on all tangible fixed assets, except freehold land, at such rates as to write off the cost of those assets in equal instalments over their expected useful lives as follows:

Freehold buildings and long term leaseholds	50 years
Short term leaseholds	the term of the lease
Plant, machinery, furniture and vehicles	2-15 years
Equipment on lease or hire	3-10 years
Data and navigation transmitting networks (excluding freehold land and buildings and leasehold premises)	3-21 years

## 9 Know how

Payments made to acquire manufacturing licences for specific products are amortised against profits over a period of three to five years being the period of utilisation of such manufacturing knowledge.

## 10 Start up costs

Start up costs associated with customer networks are amortised against profits over the period of the contract or a shorter period if it is deemed more appropriate. Racal's share of Camelot Group's start up costs has been amortised over three years.

## 11 Investment in finance leases

The total net investment in finance leases included in the balance sheet represents total lease payments receivable net of finance charges relating to future accounting periods together with estimated residual values. Finance charges are allocated to accounting periods so as to give a constant rate of return on the net cash investment in the lease.

## 12 Deferred taxation

Deferred taxation is provided at the anticipated tax rates on differences arising from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements to the extent that it is probable that a liability or asset will crystallise in the future, with the exception of timing differences arising on pension surpluses where full provision is made irrespective of whether a liability or asset will crystallise in the foreseeable future.

## 13 Government grants

Grants in connection with fixed assets are released to trading profits over the expected useful life of the particular asset to which the grant relates. Grants relating to revenue expenditure are credited to revenue as they become receivable.

## 14 Pension costs

Pension costs, which are periodically calculated by professionally qualified actuaries, are charged against profits so that the expected costs of providing pensions are recognised during the period in which benefit is derived from the employees' services. The cost of the various pension schemes may vary from the funding dependent upon actuarial advice with any difference between pension cost and funding being treated as a provision or prepayment.

# Consolidated Profit and Loss Account

For the year ended 31 March 1998

Note	1998 Before reorganisation costs £000	1998 Reorganisation costs £000	1998 Total £000	1997 Before reorganisation costs £000	1997 Reorganisation costs £000	1997 Total £000
1 Turnover						
Ongoing operations .....			920,705			830,752
Discontinuing operations .....			186,761			255,031
Total continuing operations .....			1,107,466			1,085,783
Discontinued operations .....			36,948			99,213
Total .....			1,144,414			1,184,996
1 & 2 Operating profit/(loss)						
Ongoing operations .....	115,641	(10,004)	105,637	106,404	(2,675)	103,729
Discontinuing operations .....	(55,438)	(3,790)	(59,228)	(23,667)	(48)	(23,715)
Total continuing operations .....	60,203	(13,794)	46,409	82,737	(2,723)	80,014
Discontinued operations .....	(3,465)	(919)	(4,384)	3,156	(590)	2,566
Total .....	56,738	(14,713)	42,025	85,893	(3,313)	82,580
Exceptional items – ongoing operations						
Profit on sale of properties .....			1,045			582
3 Exceptional items – discontinuing operations						
Discontinuation of operations including goodwill of £108,314,000 written off on acquisitions in prior years .....			(236,862)			–
Cost of fundamental reorganisation .....			–			(28,966)
Exceptional items – discontinued operations						
Profit on disposal or closure of operations including goodwill of £8,378,000 (1997: £400,000) written off on acquisitions in prior years .....			11,334			9,075
Trading (loss)/profit .....			(182,458)			63,271
4 Amounts written off investments .....			2,052			–
5 Net interest payable .....			22,670			22,851
(Loss)/profit on ordinary activities before taxation .....			(207,180)			40,420
8 Tax on (loss)/profit on ordinary activities .....			11,334			8,917
(Loss)/profit on ordinary activities after taxation .....			(218,514)			31,503
(Profit)/loss attributable to minority interests .....			(118)			275
(Loss)/profit on ordinary activities attributable to members of the parent company .....			(218,632)			31,778
9 Dividends .....			17,130			16,910
25 Retained (loss)/profit for the year .....			(235,762)			14,868
10 (Loss)/earnings per share .....			(77.27)p			11.30p
10 Adjusted earnings per share .....			24.97p			24.88p

The profit calculated on the historical cost basis is not materially different from that shown above.

As provided by Section 230 of the Companies Act 1985, the profit and loss account of the parent company is not published as part of these accounts. The loss before dividends payable dealt with in the accounts of the Company is £82,506,000 (1997: profit £21,962,000).

# Consolidated Balance Sheet

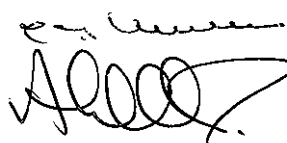
At 31 March 1998

Note	1998		1997	
	£000	£000	£000	£000
<b>Fixed assets</b>				
11 Intangible assets .....		126		274
12 Tangible assets .....		432,670		427,773
13 Investments .....		53,164		46,489
		<u>485,960</u>		<u>474,536</u>
<b>Current assets</b>				
16 Stocks .....	156,354		198,852	
17 Debtors due within one year .....	369,122		409,885	
18 Debtors due after more than one year .....	81,303		112,098	
Cash on deposit .....	24,562		65,689	
Cash at bank and in hand .....	93,606		79,321	
	<u>724,947</u>		<u>865,845</u>	
19 <b>Creditors: amounts falling due within one year</b> .....	<u>368,048</u>		<u>397,714</u>	
<b>Net current assets</b> .....		<u>356,899</u>		<u>468,131</u>
<b>Total assets less current liabilities</b> .....		<u>842,859</u>		<u>942,667</u>
20 <b>Creditors: amounts falling due after more than one year</b> .....	412,326		476,154	
23 <b>Provisions for liabilities and charges</b> .....	<u>105,703</u>		<u>18,414</u>	
		<u>518,029</u>		<u>494,568</u>
		<u>324,830</u>		<u>448,099</u>
<b>Capital and reserves</b>				
24 Called up share capital .....		72,362		71,222
25 Share premium account .....		173,665		163,447
25 Capital redemption reserve .....		279,325		279,325
25 Revaluation reserve .....		2,104		2,025
25 Goodwill reserve .....		(234,518)		(346,356)
25 Profit and loss account .....		31,014		277,393
<b>Equity shareholders' funds</b> .....		<u>323,952</u>		<u>447,056</u>
<b>Equity minority interests</b> .....		<u>878</u>		<u>1,043</u>
		<u>324,830</u>		<u>448,099</u>

These financial statements were approved by the Board on 18 September 1998 and were signed on its behalf by:

E T HARRISON  
A R WOOD

Chairman  
Financial Director





# Balance Sheet

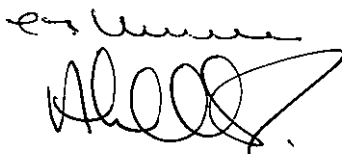
At 31 March 1998

Note	1998		1997	
	£000	£000	£000	£000
<b>Fixed assets</b>				
13 Investments .....		604,132		735,718
<b>Current assets</b>				
17 Debtors due within one year .....	409,034		390,941	
18 Debtors due after more than one year .....	2,984		3,062	
Cash on deposit .....	5,000		38,350	
Cash at bank and in hand .....	26,257		575	
	443,275		432,928	
19 <b>Creditors: amounts falling due within one year</b> .....	209,200		182,957	
<b>Net current assets</b> .....		234,075		249,971
<b>Total assets less current liabilities</b> .....		838,207		985,689
20 <b>Creditors: amounts falling due after more than one year</b> .....	294,066		354,720	
23 <b>Provisions for liabilities and charges</b> .....	1,450		—	
		295,516		354,720
		542,691		630,969
<b>Capital and reserves</b>				
24 Called up share capital .....		72,362		71,222
25 Share premium account .....		173,665		163,447
25 Capital redemption reserve .....		279,325		279,325
25 Profit and loss account .....		17,339		116,975
<b>Equity shareholders' funds</b> .....		542,691		630,969

These financial statements were approved by the Board on 18 September 1998 and were signed on its behalf by:

E T HARRISON  
A R WOOD

Chairman  
Financial Director



# Statement of Total Recognised Gains and Losses

For the year ended 31 March 1998

	1998 £000	1997 £000
(Loss)/profit for the financial year .....	(218,632)	31,778
Currency translation differences on foreign currency net investments .....	(4,189)	(9,470)
	<u>(222,821)</u>	<u>22,308</u>

## Reconciliation of Movements in Shareholders' Funds

For the year ended 31 March 1998

	1998 £000	1997 £000
(Loss)/profit for the financial year .....	(218,632)	31,778
Currency translation differences on foreign currency net investments .....	(4,189)	(9,470)
Dividends payable .....	(17,130)	(16,910)
Issue of ordinary share capital .....	11,358	1,504
Less: amounts received from subsidiary companies .....	<u>(6,349)</u>	<u>-</u>
	5,009	1,504
Goodwill arising on acquisitions, fair value adjustments and investment received from minority interests (charged)/credited to goodwill reserve ....	(4,854)	6,921
Goodwill in respect of businesses sold transferred to the profit and loss account .....	8,378	400
Goodwill in respect of discontinuing operations transferred to the profit and loss account .....	<u>108,314</u>	<u>-</u>
Net (reduction)/addition to shareholders' funds .....	(123,104)	14,223
Opening shareholders' funds .....	<u>447,056</u>	<u>432,833</u>
Closing shareholders' funds .....	<u>323,952</u>	<u>447,056</u>

# Consolidated Cash Flow Statement

For the year ended 31 March 1998

Note	1998		1997	
	£000	£000	£000	£000
26	<b>Net cash inflow from operating activities</b> .....		121,445	140,415
27	<b>Returns on investments and servicing of finance</b> .....		(23,805)	(22,639)
	<b>Taxation</b>			
	UK corporation tax paid .....	(15,729)	(7,073)	
	Overseas tax (paid)/received .....	(1,680)	6,056	
		(17,409)		(1,017)
28	<b>Capital expenditure and financial investment</b> .....		(118,814)	(125,569)
29	<b>Acquisitions and disposals</b> .....		77,681	6,950
	<b>Equity dividends paid</b> .....		(16,937)	(16,890)
	<b>Cash inflow/(outflow) before use of liquid resources and financing</b> ..		22,161	(18,750)
	<b>Management of liquid resources</b>			
30	Decrease/(increase) in cash on deposit .....		40,727	(5,123)
	<b>Financing</b>			
	Issue of ordinary share capital .....	5,009	1,504	
	Issue of shares to minority interests .....	-	373	
	Net (decrease)/increase in amounts borrowed .....	(56,117)	12,319	
	Capital element of finance lease/hire purchase payments .....	(16,161)	(13,775)	
	<b>Net cash (outflow)/inflow from financing</b> .....		(67,269)	421
	<b>Net decrease in cash in the year</b> .....		(4,381)	(23,452)
	<b>Reconciliation of net cash flow to movement in net debt</b>			
30	Decrease in cash in the year .....		(4,381)	(23,452)
30	Cash outflow from decrease in debt and lease financing .....		72,278	1,456
30	Cash (inflow)/outflow from (decrease)/increase in liquid resources .....		(40,727)	5,123
			27,170	(16,873)
	Loans and finance leases acquired with subsidiaries .....		-	(2,298)
30	New finance leases .....		(670)	(12,187)
30	Finance leases terminated .....		335	-
30	Finance leases disposed with subsidiaries .....		10	-
30	Exchange movement .....		4,979	15,994
			31,824	(15,364)
30	Net debt at start of year .....		(339,453)	(324,089)
30	Net debt at end of year .....		(307,629)	(339,453)
30	<b>Net debt at end of year</b>			
	Loans .....	(298,880)	(361,855)	
	Bank overdrafts .....	(30,374)	(10,133)	
	Cash on deposit .....	24,562	65,689	
	Cash at bank and in hand .....	93,606	79,321	
	<b>Net borrowings</b> .....		(211,086)	(226,978)
	Obligations under finance leases .....	(96,543)	(112,475)	
	<b>Net debt</b> .....		(307,629)	(339,453)

# Notes on the Financial Statements

## I Turnover, operating profit and net assets

### a) Divisional analysis

	External turnover 1998 £000	External and inter- divisional turnover 1998 £000	Operating profit before reorganisation costs 1998 £000	Reorganisation costs 1998 £000	Operating profit 1998 £000	Net assets 1998 £000
Defence Radar and Avionics.....	226,083	226,083	23,324	(1,074)	22,250	81,319
Radio Communications.....	134,045	134,045	(3,918)	(4,006)	(7,924)	93,823
Defence Electronics.....	360,128	360,128	19,406	(5,080)	14,326	175,142
Telecommunications Services.....	270,697	272,544	38,277	(2,473)	35,804	199,467
Industrial Electronics.....	289,880	293,748	39,733	(2,135)	37,598	130,157
Associates.....	-	-	21,817	-	21,817	34,016
Corporately funded Research and Development .....	-	-	(3,425)	-	(3,425)	4,566
Allocations to discontinuing/discontinued operations.....	-	-	(167)	(316)	(483)	11,701
Total ongoing operations.....	920,705	926,420	115,641	(10,004)	105,637	555,049
Discontinuing operations.....	186,761	186,786	(55,438)	(3,790)	(59,228)	86,570
Total continuing operations.....	1,107,466	1,113,206	60,203	(13,794)	46,409	641,619
Discontinued operations.....	36,948	36,949	(3,465)	(919)	(4,384)	-
Total.....	1,144,414	1,150,155	56,738	(14,713)	42,025	641,619

	External turnover 1997 £000	External and inter- divisional turnover 1997 £000	Operating profit before reorganisation costs 1997 £000	Reorganisation costs 1997 £000	Operating profit 1997 £000	Net assets 1997 £000
Defence Radar and Avionics.....	210,784	210,787	24,336	(388)	23,948	77,381
Radio Communications.....	140,307	140,307	(3,206)	(903)	(4,109)	102,284
Defence Electronics.....	351,091	351,094	21,130	(1,291)	19,839	179,665
Telecommunications Services.....	260,064	261,830	43,741	(653)	43,088	133,386
Industrial Electronics.....	219,597	224,322	24,102	(370)	23,732	117,630
Associates.....	-	-	18,769	-	18,769	27,912
Corporately funded Research and Development .....	-	-	(3,839)	4	(3,835)	4,203
Allocations to discontinuing/discontinued operations.....	-	-	2,501	(365)	2,136	15,261
Total ongoing operations.....	830,752	837,246	106,404	(2,675)	103,729	478,057
Discontinuing operations.....	255,031	255,961	(23,667)	(48)	(23,715)	188,670
Total continuing operations.....	1,085,783	1,093,207	82,737	(2,723)	80,014	666,727
Discontinued operations.....	99,213	99,213	3,156	(590)	2,566	26,764
Total.....	1,184,996	1,192,420	85,893	(3,313)	82,580	693,491

# Notes on the Financial Statements

## I Turnover, operating profit and net assets (continued)

### b) Geographical analysis by origin

	External turnover 1998 £000	External and inter- regional turnover 1998 £000	Operating profit before reorganisation costs 1998 £000	Reorganisation costs 1998 £000	Operating profit 1998 £000	Net assets 1998 £000
United Kingdom.....	716,482	757,465	101,122	(9,335)	91,787	482,537
Rest of Europe.....	39,848	41,910	2,133	(186)	1,947	8,615
The Americas.....	127,465	131,777	8,678	(365)	8,313	41,452
Asia and Australasia.....	33,167	43,195	3,947	(65)	3,882	20,546
Africa.....	3,743	4,979	(239)	(53)	(292)	1,899
Total ongoing operations.....	920,705	979,326	115,641	(10,004)	105,637	555,049
Discontinuing operations.....	186,761	194,136	(55,438)	(3,790)	(59,228)	86,570
Total continuing operations.....	1,107,466	1,173,462	60,203	(13,794)	46,409	641,619
Discontinued operations.....	36,948	44,877	(3,465)	(919)	(4,384)	-
Total.....	1,144,414	1,218,339	56,738	(14,713)	42,025	641,619

	External turnover 1997 £000	External and inter- regional turnover 1997 £000	Operating profit before reorganisation costs 1997 £000	Reorganisation costs 1997 £000	Operating profit 1997 £000	Net assets 1997 £000
United Kingdom.....	671,945	710,296	101,219	(2,473)	98,746	415,478
Rest of Europe.....	31,500	34,044	5	(137)	(132)	15,193
The Americas.....	84,166	87,928	3,695	7	3,702	29,396
Asia and Australasia.....	39,052	45,334	1,560	(43)	1,517	17,156
Africa.....	4,089	4,349	(75)	(29)	(104)	834
Total ongoing operations.....	830,752	881,951	106,404	(2,675)	103,729	478,057
Discontinuing operations.....	255,031	268,751	(23,667)	(48)	(23,715)	188,670
Total continuing operations.....	1,085,783	1,150,702	82,737	(2,723)	80,014	666,727
Discontinued operations.....	99,213	116,861	3,156	(590)	2,566	26,764
Total.....	1,184,996	1,267,563	85,893	(3,313)	82,580	693,491

### c) Geographical analysis by destination

	Turnover 1998 £000	Turnover 1997 £000
United Kingdom.....	546,695	501,875
Rest of Europe.....	92,243	78,249
The Americas.....	163,561	118,731
Asia and Australasia.....	92,718	108,033
Africa.....	25,488	23,864
Total ongoing operations.....	920,705	830,752
Discontinuing operations.....	186,761	255,031
Total continuing operations.....	1,107,466	1,085,783
Discontinued operations.....	36,948	99,213
Total.....	1,144,414	1,184,996

# Notes on the Financial Statements

## I Turnover, operating profit and net assets (continued)

### d) Net assets

Net assets employed are reconciled to the consolidated balance sheet as follows:

	1998 £000	1997 £000
Equity shareholders' funds.....	323,952	447,056
Equity minority interests.....	878	1,043
Provisions for liabilities and charges.....	105,703	18,414
Net borrowings (Page 41).....	211,086	226,978
	<u>641,619</u>	<u>693,491</u>

## 2 Operating profit

	Ongoing operations 1998 £000	Discontinuing operations 1998 £000	Total continuing operations 1998 £000	Discontinued operations 1998 £000	Total 1998 £000
Turnover.....	920,705	186,761	1,107,466	36,948	1,144,414
Cost of sales.....	684,627	155,109	839,736	27,600	867,336
Gross profit.....	236,078	31,652	267,730	9,348	277,078
Selling and distribution costs.....	65,916	52,678	118,594	8,087	126,681
Administrative expenses.....	86,801	38,202	125,003	5,645	130,648
	83,361	(59,228)	24,133	(4,384)	19,749
Share of profits of associated companies.....	22,276	—	22,276	—	22,276
Operating profit.....	105,637	(59,228)	46,409	(4,384)	42,025

The figures for ongoing operations include the following amounts relating to acquisitions in the year:

Turnover £2,770,000, cost of sales £2,398,000, gross profit £372,000, selling and distribution costs £93,000, administrative expenses £140,000 and operating profit £139,000.

	Ongoing operations 1997 £000	Discontinuing operations 1997 £000	Total continuing operations 1997 £000	Discontinued operations 1997 £000	Total 1997 £000
Turnover.....	830,752	255,031	1,085,783	99,213	1,184,996
Cost of sales.....	608,356	190,152	798,508	67,747	866,255
Gross profit.....	222,396	64,879	287,275	31,466	318,741
Selling and distribution costs.....	58,247	63,006	121,253	16,763	138,016
Administrative expenses.....	79,384	25,588	104,972	12,629	117,601
	84,765	(23,715)	61,050	2,074	63,124
Share of profits of associated companies.....	18,964	—	18,964	—	18,964
	103,729	(23,715)	80,014	2,074	82,088
Prior year provisions utilised.....	—	—	—	492	492
Operating profit.....	103,729	(23,715)	80,014	2,566	82,580

# Notes on the Financial Statements

## 2 Operating profit (continued)

Operating profit has been arrived at after:	1998 £000	1997 £000
Directors' emoluments excluding pension costs (Page 28) .....	2,354	2,201
Auditors' remuneration .....	1,198	1,263
Payments made to auditors in respect of non-audit work – UK only (see Note below) .....	148	466
Depreciation of tangible fixed assets:		
Own assets .....	57,654	52,410
Finance leased assets .....	15,199	15,763
Amortisation of know how .....	148	62
Research and development:		
Ongoing operations .....	36,607	38,363
Discontinuing operations .....	26,881	36,218
Discontinued operations .....	1,554	4,323
Reorganisation costs .....	14,713	3,313
Payments under operating leases:		
Land and buildings .....	15,461	17,022
Other assets .....	19,766	13,805
Receipts under operating leases .....	9,063	11,419

Note: Total payments made to auditors in respect of non-audit work was £180,000 (1997: £528,000). Of this amount £32,000 (1997: £62,000) related to work on disposal of businesses and acquisitions and has been included as a reduction in the proceeds of the sale of businesses or included in the consideration paid for acquisitions.

## 3 Discontinuing operations – exceptional items

The exceptional costs relating to discontinuing operations are analysed as follows:

	Costs incurred £000	Provisions £000	Total £000
<b>Data Communications</b>			
Fixed assets written off .....	4,119	188	4,307
Stock written off .....	20,304	–	20,304
Loss on sale of finance leases .....	4,652	–	4,652
Other assets written down .....	2,937	325	3,262
(Profit)/loss on sale of properties .....	(522)	124	(398)
Severance and other personnel related costs .....	3,668	5,885	9,553
Other items .....	4,832	6,426	11,258
Provision for loss on disposal .....	–	64,420	64,420
	39,990	77,368	117,358
Provision for losses 1998/99 .....	–	9,504	9,504
	39,990	86,872	126,862
Goodwill written off on acquisitions in prior years .....	107,002	–	107,002
Total .....	146,992	86,872	233,864
<b>Other discontinuing operations</b>			
Other items .....	1,686	–	1,686
Goodwill written off on acquisitions in prior years .....	1,312	–	1,312
Total .....	2,998	–	2,998
	149,990	86,872	236,862

## 4 Amounts written off investments

The prior investment of £2,052,000 in the PayPoint service activity through Utilities Consortium Limited was converted into preference shares in Utilities Consortium Limited as a result of a capital restructuring during the year. Although the preference shares may be redeemed in the future it was felt prudent to write off the investment.

# Notes on the Financial Statements

5	Net interest payable	£000	1998	£000	£000	1997	£000
	Interest payable:						
	Bank overdrafts, loans and other borrowings repayable within five years .....	23,603			23,494		
	Loans and other borrowings repayable wholly or in part after five years .....	138			212		
	Finance charges on hire purchase contracts and finance leases .....	8,256			9,388		
				31,997			33,094
	Less interest receivable:						
	Loans and deposits .....	(4,813)			(6,203)		
	Finance leases .....	(4,514)			(4,040)		
				(9,327)			(10,243)
				22,670			22,851

6	Employees	1998	1997
		Number	Number
	a) Average number of employees		
	United Kingdom .....	9,443	10,090
	Overseas .....	3,471	4,230
		12,914	14,320
		£000	£000
	b) Staff costs (including directors)		
	Wages and salaries .....	350,168	362,805
	Social security costs .....	28,938	34,255
	Pension costs .....	17,130	15,254
		396,236	412,314

## 7 Directors' emoluments

Details of emoluments by individual director are set out in the Report of the Remuneration Committee on page 28.

8	Tax on (loss)/profit on ordinary activities	1998	1997
		£000	£000
	Tax on (loss)/profit on ordinary activities was:		
	United Kingdom		
	Corporation tax at 31% (1997: 33%) .....	1,431	2,992
	Deferred taxation .....	840	6,281
	Associated companies .....	6,687	6,327
		8,958	15,600
	Overseas		
	Current taxation .....	2,617	(6,776)
	Deferred taxation .....	(312)	41
	Associated companies .....	71	52
		11,334	8,917

The charge for United Kingdom corporation tax has been decreased by £6,819,000 (1997: £5,467,000) as a result of capital allowances being greater than depreciation for which no provision has been made.

No tax arose in respect of the profit on sale of properties and profits on disposal of operations (1997: £nil).

A further liability to taxation would arise if the retained profits of overseas subsidiaries were distributed.



# Notes on the Financial Statements

## 9 Dividends

	1998 £000	1997 £000
<b>Dividends on equity shares</b>		
First interim 2.1p paid (1997: 2.1p) .....	5,941	5,914
Second interim 3.9p declared (1997: nil) .....	11,189	–
Final nil (1997: 3.9p) .....	–	10,996
	<u>17,130</u>	<u>16,910</u>

## 10 (Loss)/earnings per share

i) (Loss)/earnings per share has been calculated by reference to the average of 282,936,814 (1997: 281,327,005) ordinary shares of 25p each in issue during the year based on the consolidated loss of £218,632,000 (1997: profit £31,778,000) after deducting taxation and profits attributable to minority interests.

There would be no material dilution of earnings per share if the outstanding share options were exercised.

ii) Adjusted earnings per share has been calculated as follows:

	1998 Attributable profits £000	1998 Earnings per share p	1997 Attributable profits £000	1997 Earnings per share p
Consolidated (loss)/profit and (loss)/earnings per share .....	(218,632)	(77.27)	31,778	11.30
Adjustments:				
Profit on disposal of businesses .....	(11,334)		(9,075)	
Discontinued operations .....	4,384		(2,566)	
Taxation on discontinued operations .....	490		1,043	
Discontinuing operations .....	59,228		23,715	
Discontinuing operations – exceptional items .....	236,862		–	
Taxation on discontinuing operations .....	(2,412)		(227)	
Cost of fundamental reorganisation .....	–		28,966	
Taxation on cost of fundamental reorganisation .....	–		(3,636)	
Amounts written off investments .....	2,052		–	
Adjusted consolidated profits and adjusted earnings per share .....	<u>70,638</u>	<u>24.97</u>	<u>69,998</u>	<u>24.88</u>

The adjusted earnings per share has been shown for the ongoing operations to give an understanding of the base for the future.

## 11 Intangible fixed assets

### Know how Cost

	£000
Balance 1 April 1997 .....	590
Exchange movement .....	(26)
Additions .....	<u>206</u>
	770
Disposal of businesses .....	(339)
Disposals and write offs .....	<u>(161)</u>
Balance 31 March 1998 .....	<u>270</u>

### Aggregate amortisation

Balance 1 April 1997 .....	316
Exchange movement .....	(16)
Charge for the year .....	<u>148</u>
	448
Disposal of businesses .....	(167)
Disposals and write offs .....	<u>(137)</u>
Balance 31 March 1998 .....	<u>144</u>

### Net book value

31 March 1998 .....	<u>126</u>
31 March 1997 .....	<u>274</u>

# Notes on the Financial Statements

## 12 Tangible fixed assets

	Freehold premises £000	Leasehold premises Long term £000	Short term £000	Plant machinery furniture and vehicles £000	Equipment on lease or hire £000	Data and navigation transmitting networks £000	Total £000
<b>Cost or valuation</b>							
Balance 1 April 1997.....	104,454	8,250	10,146	390,101	23,520	360,859	897,330
Exchange movement.....	(1,407)	(647)	(93)	(7,517)	(701)	(710)	(11,075)
Additions at cost.....	4,069	113	1,437	44,328	9,024	71,210	130,181
Reclassifications to stock.....	-	-	-	-	(34)	-	(34)
Disposals at cost.....	(50,417)	(499)	(1,420)	(26,144)	(15,671)	(5,632)	(99,783)
Disposal of businesses.....	(1,590)	-	(372)	(14,410)	-	-	(16,372)
Assets written off.....	(241)	-	(1,134)	(34,577)	-	-	(35,952)
Reclassification of assets.....	2,054	(2,054)	(462)	(2,840)	3,602	(300)	-
Balance 31 March 1998.....	56,922	5,163	8,102	348,941	19,740	425,427	864,295
<b>Aggregate depreciation</b>							
Balance 1 April 1997.....	28,526	2,206	5,807	279,840	20,396	132,782	469,557
Exchange movement.....	(456)	(165)	(65)	(4,529)	(624)	(650)	(6,489)
Charge for the year.....	2,951	120	676	33,129	1,378	34,797	73,051
Reclassifications to stock.....	-	-	-	-	(18)	-	(18)
Elimination on disposals.....	(23,102)	(176)	(941)	(24,035)	(10,552)	(4,707)	(63,513)
Disposal of businesses.....	(255)	-	(218)	(8,945)	-	-	(9,418)
Assets written off.....	(81)	-	(1,092)	(30,372)	-	-	(31,545)
Reclassification of assets.....	1,253	(1,253)	(157)	(3,067)	3,481	(257)	-
Balance 31 March 1998.....	8,836	732	4,010	242,021	14,061	161,965	431,625
<b>Net book value</b>							
31 March 1998.....	48,086	4,431	4,092	106,920	5,679	263,462	432,670
31 March 1997.....	75,928	6,044	4,339	110,261	3,124	228,077	427,773

The net book value of the Group's tangible fixed assets includes £85,222,000 (1997: £101,495,000) of assets held under finance leases and hire purchase contracts.

Certain of the Group's properties in the United Kingdom were valued on an open market basis at 31 March 1982.

	Freehold premises £000	Leasehold premises - long term £000	Data and navigation transmitting networks £000
Premises, data and navigation transmitting networks are analysed as follows:			
At cost .....	49,235	4,038	425,387
At valuation in 1982 .....	7,687	1,125	40
	56,922	5,163	425,427

If these assets had not been revalued, the following amounts would have been included:

31 March 1998			
Cost .....	55,740	4,896	425,417
Aggregate depreciation .....	9,418	779	161,981
Net book value .....	46,322	4,117	263,436
31 March 1997			
Cost .....	103,402	7,983	360,849
Aggregate depreciation .....	29,154	2,258	132,798
Net book value .....	74,248	5,725	228,051

# Notes on the Financial Statements

## 13 Fixed asset investments

Group	Associated companies £000	Other investments £000	Own shares £000	£000	Total £000
Balance 1 April 1997 .....		30,264	8,082	8,143	46,489
Exchange restatement .....		(29)	(110)	—	(139)
Reclassification from debtors .....		—	657	—	657
Additions .....		798	1,625	466	2,889
Written off .....		—	(2,052)	—	(2,052)
		<u>31,033</u>	<u>8,202</u>	<u>8,609</u>	<u>47,844</u>
Share of retained profits for year:					
Results for the year net of tax .....	15,940	—	—	15,940	
Accounting policy alignments * .....	(422)	—	—	(422)	
	<u>15,518</u>			<u>15,518</u>	
Loss allocated to creditors .....	209	—	—	209	
	<u>15,727</u>			<u>15,727</u>	
Dividends received .....	(9,588)	—	—	(9,588)	
Dividend prepaid in prior years .....	(819)	—	—	(819)	
	<u>5,320</u>			<u>5,320</u>	
Balance 31 March 1998 .....	<u>36,353</u>	<u>8,202</u>	<u>8,609</u>		<u>53,164</u>

\* Adjustment required to bring the associated companies' accounting policies in line with the Group's accounting policies.

The principal associated companies in which the Group has a direct interest are:	Country of incorporation	Business activity	Issued equity Class	Value	Percentage of issued equity held	Latest financial accounts
Archer Communications Systems Limited	England	Radio communications	Ordinary shares	£1,000	30%	31.3.98
Camelot Group plc†	England	Lotteries	Ordinary shares	£50,000,000	22.5%	31.3.98
Global Telematics Plc	England	Vehicle telematic products and services	Ordinary shares	£1,125,000	50%	31.3.98
Satellite Information Services (Holdings) Limited†	England	Satellite communications	Ordinary shares	£22,161	21.96%	31.3.98
China Bohai Racal Positioning and Survey Company Limited **	People's Rep. of China	Survey and positioning services	Registered capital	US\$800,000	50%	31.3.98
China Nanhai Racal Positioning and Survey Company Limited **	People's Rep. of China	Survey and positioning services	Registered capital	US\$2,600,000	50%	31.3.98
Decca Survey (Saudi Arabia) Limited	Saudi Arabia	Survey and positioning services	Ordinary capital	SR1,000,000	40%	31.3.98
International Optical Network LLC**	USA	Telecommunications services	Common stock	US\$1,000	50%	31.3.98

† Interests held by Racal Electronics Plc.

\*\* The results of these companies brought into the consolidated accounts are derived from audited accounts to 31.12.97 and management accounts for the three months to 31.3.98.

Other investments includes an investment of £6,765,000 in Concentric Network Corporation, a company incorporated in the USA. This investment was sold during the period 28 April to 12 May 1998.

Company	Subsidiary companies £000	Associated companies £000	Other investments £000	Own shares £000	Total £000
Balance 1 April 1997 .....	691,419	35,062	1,094	8,143	735,718
Additional investments in certain subsidiary companies .....	1,500	—	—	—	1,500
Additions .....	—	—	958	—	958
	<u>692,919</u>	<u>35,062</u>	<u>2,052</u>	<u>8,143</u>	<u>738,176</u>
Written off .....	—	—	(2,052)	—	(2,052)
Provisions for permanent diminutions in value .....	(131,992)	—	—	—	(131,992)
Balance 31 March 1998 .....	<u>560,927</u>	<u>35,062</u>	<u>—</u>	<u>8,143</u>	<u>604,132</u>

Details of the principal subsidiaries are given on pages 34 and 35.

Fixed asset investments are carried at cost less any provision for permanent diminutions in value. The cumulative provision for permanent diminutions in value is £176,898,000 (1997:£44,906,000).

Own shares relates to two Employee Share Ownership Trusts (Note 15).

# Notes on the Financial Statements

## 14 Camelot Group plc

Due to the significance of Camelot Group plc to the Group's results additional information is provided in this Note on the results of Camelot Group plc and its balance sheet. This can be summarised as follows:

	1998		1997	
	£m	£m	£m	£m
Total turnover.....		5,513.7		4,723.0
Total profit before taxation .....	80.9		70.8	
Accounting policy alignments* .....	(6.3)		(10.1)	
Adjusted total profit before taxation .....		74.6		60.7
Total depreciation charge .....		22.5		23.2
Total fixed assets .....		70.0		89.9
Total current assets .....		444.2		434.3
Total liabilities .....		369.2		403.4

The Group's share of the adjusted total profit before taxation was £16.8 million (1997: £13.7 million).

\* Adjustment required to bring the accounting policies of Camelot Group plc in line with the Group's accounting policies.

## 15 Own shares

The Company has established an Employee Share Ownership Trust to purchase shares in the market for distribution at a later date in accordance with the terms of the Racal Share Option Scheme 1992, the Racal Share Option Scheme 1995 and the Racal Share Option Scheme 1997. The shares are held by an independent trustee and the right to dividend on the shares has been waived apart from a nominal amount. As at 31 March 1998 the number of shares held by the Trust totalled 3,149,000 shares with a nominal value of £787,250 (1997: 3,149,000 shares with a nominal value of £787,250) and the cost of such shares amounted to £8,143,000 (1997: £8,143,000). These shares, whilst legally not the property of the Company, have been included in fixed asset investments as shown in Note 13. The market value of these shares at 31 March 1998 was £10,691,000.

During the year, the terms of this Trust were amended so that the Trustee could subscribe for the Company's ordinary shares and so that such shares could be used to satisfy options granted under the terms of the Share Option Schemes referred to above together with options to be granted under the terms of the Racal Share Savings Plan (1990). These amendments do not apply to those options granted under the Racal Share Savings Plan (1990) in October 1992 as the Company had established a Qualifying Employee Share Ownership Trust (QUEST) to operate in conjunction with those options. As at 31 March 1998, 159,948 shares were held by the QUEST. The cost of these shares was £466,000 and their market value at 31 March 1998 was £543,000.

## 16 Stocks

	1998 £000	1997 £000
Raw materials and components.....	46,040	79,393
Work in progress .....	73,605	63,776
Finished goods stock.....	42,013	59,190
	161,658	202,359
Less progress payments .....	5,304	3,507
	156,354	198,852
Work in progress and progress payments include the following in respect of long term contracts:		
Net cost less foreseeable losses .....	6,934	7,427
Less applicable payments on account .....	2,642	2,654
	4,292	4,773

## 17 Debtors due within one year

	1998 Group £000	1998 Company £000	1997 Group £000	1997 Company £000
Trade debtors.....	235,102	—	255,304	—
Debtors – finance leases.....	5,801	—	29,634	—
Amounts owed by subsidiaries .....	—	399,710	—	378,686
Amounts owed by associated companies .....	4,616	—	5,778	262
Other debtors.....	44,253	3,554	28,271	9,439
Amounts recoverable on contracts .....	37,758	—	41,258	—
Taxation recoverable .....	433	4,785	881	—
Prepayments and accrued income .....	41,124	956	48,429	2,361
Interest receivable.....	35	29	330	193
	369,122	409,034	409,885	390,941

The aggregate amounts receivable during the year in respect of finance leases were £33,209,000 (1997: £38,321,000).

The cost of assets acquired during the year for the purpose of letting under finance leases was £8,332,000 (1997: £28,177,000).

# Notes on the Financial Statements

<b>18</b>	<b>Debtors due after more than one year</b>	<b>1998</b>	<b>1998</b>	<b>1997</b>	<b>1997</b>
		<b>Group</b> £000	<b>Company</b> £000	<b>Group</b> £000	<b>Company</b> £000
	Trade debtors .....	696	–	82	–
	Debtors – finance leases .....	9,663	–	49,610	–
	Other debtors .....	3,708	187	8,746	313
	Amounts recoverable on contracts .....	10,250	–	5,612	–
	Taxation recoverable .....	260	–	299	–
	Advance corporation tax .....	–	2,797	–	2,749
	Prepayments and accrued income .....	56,726	–	47,749	–
		<u>81,303</u>	<u>2,984</u>	<u>112,098</u>	<u>3,062</u>
<b>19</b>	<b>Creditors: amounts falling due within one year</b>	<b>1998</b>	<b>1998</b>	<b>1997</b>	<b>1997</b>
		<b>Group</b> £000	<b>Company</b> £000	<b>Group</b> £000	<b>Company</b> £000
	Loans (Note 22) .....	1,425	–	3,597	–
	Bank overdrafts .....	30,374	66,388	10,133	23,500
	Trade creditors .....	128,591	–	149,520	–
	Amounts owed to subsidiaries .....	–	123,847	–	134,649
	Amounts owed to associated companies .....	17	–	31	–
	Advance receipts .....	35,200	–	34,541	–
	Current corporation tax .....	15,634	6,701	26,406	9,762
	Obligations under finance leases (Note 21) .....	13,403	–	15,432	–
	Other taxes and social security costs .....	22,946	–	26,040	32
	Other creditors .....	9,631	73	21,009	75
	Accruals and deferred income .....	98,754	204	95,857	1,757
	Interest payable .....	884	798	2,323	2,186
	Deferred purchase consideration .....	–	–	1,829	–
	Dividend .....	11,189	11,189	10,996	10,996
		<u>368,048</u>	<u>209,200</u>	<u>397,714</u>	<u>182,957</u>
<b>20</b>	<b>Creditors: amounts falling due after more than one year</b>	<b>1998</b>	<b>1998</b>	<b>1997</b>	<b>1997</b>
		<b>Group</b> £000	<b>Company</b> £000	<b>Group</b> £000	<b>Company</b> £000
	Loans (Note 22) .....	297,455	294,066	358,258	354,720
	Advance receipts .....	19,029	–	1,627	–
	Corporation tax .....	119	–	33	–
	Obligations under finance leases (Note 21) .....	83,140	–	97,043	–
	Other creditors .....	5,844	–	11,016	–
	Accruals and deferred income .....	6,739	–	8,177	–
		<u>412,326</u>	<u>294,066</u>	<u>476,154</u>	<u>354,720</u>
<b>21</b>	<b>Obligations under finance leases</b>			<b>1998</b>	<b>1997</b>
				<b>£000</b>	<b>£000</b>
	Obligations under finance leases fall due as follows:				
	(a) between one and two years .....			13,880	16,280
	(b) between two and five years .....			28,997	39,294
	(c) in more than five years .....			40,263	41,469
				83,140	97,043
	(d) in one year or less .....			13,403	15,432
				<u>96,543</u>	<u>112,475</u>

# Notes on the Financial Statements

22	Loans	1998 Group £000	1998 Company £000	1997 Group £000	1997 Company £000
	<b>Bank loans</b>				
	Repayable other than by instalments within five years:				
	Unsecured multi-currency loans .....	294,066	294,066	354,720	354,720
	Repayable by instalments:				
	Unsecured loans repayable within five years .....	1,265	—	2,575	—
	Secured loans repayable 1998/2011 with interest at rates between 6¼% and 9¼% (secured by charges on buildings, plant and assets) .....	3,549	—	4,560	—
		<u>298,880</u>	<u>294,066</u>	<u>361,855</u>	<u>354,720</u>
	Repayment of the above falls due as follows:				
	(a) between one and two years .....	294,716	294,066	355,872	354,720
	(b) between two and five years .....	1,312	—	610	—
	(c) in more than five years .....	1,427	—	1,776	—
		<u>297,455</u>	<u>294,066</u>	<u>358,258</u>	<u>354,720</u>
	(d) in one year or less .....	1,425	—	3,597	—
		<u>298,880</u>	<u>294,066</u>	<u>361,855</u>	<u>354,720</u>

23	Provisions for liabilities and charges	Group Deferred taxation £000	Group Other provisions £000	Group Total £000	Company Other provisions £000
	Balance 1 April 1997 .....	18,414	—	18,414	—
	Exchange restatement .....	(63)	—	(63)	—
	Profit and loss account .....	528	86,872	87,400	1,450
	Increase in the amount of advance corporation tax recoverable on dividend offset against United Kingdom deferred taxation .....	(48)	—	(48)	—
	Balance 31 March 1998 .....	<u>18,831</u>	<u>86,872</u>	<u>105,703</u>	<u>1,450</u>
	<b>Deferred taxation</b>				
	<b>Group</b>				
	The provision for deferred taxation calculated on the liability method is as follows:				
	Accelerated capital allowances in the United Kingdom .....	5,481	19,996	5,811	14,545
	Timing differences relating to pension surpluses allocated to the Racal Telecommunications Shared Cost Section of the Railways Pension Scheme .....	8,844	8,844	8,844	8,844
	Other timing differences .....	<u>7,303</u>	<u>7,303</u>	<u>6,508</u>	<u>6,508</u>
		<u>21,628</u>	<u>36,143</u>	<u>21,163</u>	<u>29,897</u>
	Less advance corporation tax .....	<u>2,797</u>	<u>2,797</u>	<u>2,749</u>	<u>2,749</u>
		<u>18,831</u>	<u>33,346</u>	<u>18,414</u>	<u>27,148</u>

## 24 Called up share capital

At 31 March 1998, the authorised share capital of the Company was £400,000,000 in ordinary shares of 25p each (1997: £400,000,000 in ordinary shares of 25p each).

The issued share capital of the Company, all of which has been allotted, called up and fully paid, as at 31 March 1998 was £72,361,925.75 in ordinary shares of 25p each (1997: £71,222,079).

In August 1997, an issue of 192,261 ordinary shares (nominal value £48,065.25) was made at an effective price of 237.6p per share to shareholders who elected to receive such ordinary shares in lieu of the cash payment of the final dividend.

# Notes on the Financial Statements

## 24 Called up share capital (continued)

Allotments totalling 209,150 ordinary shares (nominal value £52,287.50) were made during the year in accordance with the rules of the Racal Share Option Scheme 1992. During the year, the Company amended the terms of its existing Employee Share Ownership Trust as referred to in Note 15. Of the 209,150 shares referred to above, 152,175 shares were subscribed for by the Trustee at a total market value of £422,000. Of this amount, £191,000 was received from employees and £231,000 from the Company's subsidiaries. The option prices paid by the participants for the shares were as follows:

50,075 shares at 114p per share
159,075 shares at 130.5p per share.

Allotments totalling 4,097,980 ordinary shares (nominal value £1,024,495.00) were made during the year in accordance with the rules of the Racal Share Savings Plan (1990). During the year, the Company established a further employee trust, the Racal Electronics QUEST, for the purpose of acquiring ordinary shares in the Company for allocation to employees on the exercise of options granted in October 1992 under the Racal Share Savings Plan (1990). Of the 4,097,980 shares referred to above, 3,794,777 shares were subscribed for by the Trustee, Racal Electronics QUEST Limited, a wholly owned subsidiary of the Company, at a market value of £9.9 million and all but 159,948 of these shares had been allocated to employees, including executive directors, in satisfaction of their options granted under the Racal Share Savings Plan (1990). Of this amount, £3.8 million was received from employees and £6.1 million from the Company's subsidiaries. The option price paid by employees, including executive directors, was 105p per share.

Allotments totalling 59,996 ordinary shares (nominal value £14,999.00) were made to Bradford & Bingley (PEPs) Nominees Limited during the year at various prices in respect of the Racal Electronics General and Single Company Corporate Personal Equity Plans (PEPs). The total consideration received amounted to £153,284.85.

Under the rules of the Racal Share Option Scheme 1992, options were outstanding on 31 March 1998 for executives to acquire 6,089,260 ordinary shares in the Company as follows:

Number of shares	Option price	Exercise period			
2,965,260	130.5p	5 October 1995	to	4 October 2002	
* 877,499	114p	8 October 1997	to	7 October 2002	
† 714,000	243p	19 July 1997	to	18 July 2004	
† 540,000	251p	19 July 1997	to	18 July 2004	
† 67,000	231p	19 January 1998	to	18 January 2005	
† 1,153,000	270p	13 July 1998	to	12 July 2005	
36,000	235p	12 December 2000	to	11 December 2007	
614,000	247p	21 January 2001	to	20 January 2008	

\* These options run in parallel to those granted at 130.5p per share and are not additional thereto. The parallel options are now exercisable as the earnings per share of the Company has grown over a five year period by at least 10 percentage points more than the Index of Retail Prices has grown over the same period.

† Shares under option held in the Employee Share Ownership Trust (Note 15).

Under the rules of the Racal Share Option Scheme 1995, an option was outstanding for an executive to acquire 204,000 ordinary shares in the Company at the price of 275p per share exercisable during the period 18 July 1998 to 17 July 2005. The shares under option are held in the Employee Share Ownership Trust (Note 15).

At 31 March 1998, 3,149,000 ordinary shares of the Company for use in satisfying the share options granted under these Schemes were held in an independently managed Employee Share Ownership Trust which was formed to purchase shares in the Company on the open market. Options have not yet been granted in respect of some of the shares held by the Trust.

Under the rules of the Racal Share Option Scheme 1997, options were outstanding on 31 March 1998 for executives to acquire 1,595,000 ordinary shares in the Company as follows:

Number of shares	Option price	Exercise period			
1,064,000	235p	12 December 2000	to	11 December 2004	
531,000	247p	21 January 2001	to	20 January 2005	

The exercise of these options is subject to the Company achieving growth in its earnings per share over a three year period in excess of the Index of Retail Prices by an average of 3% per year.

Under the rules of the Racal Share Savings Plan (1990), options were outstanding on 31 March 1998 for employees to acquire 10,290,176 ordinary shares in the Company as follows:

Number of shares	Option price	Exercise period			
266,180	105p	1 December 1997	to	31 May 1998	
10,023,996	198p	1 April 2003	to	30 September 2003	

# Notes on the Financial Statements

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Reserves

	Group £000	Company £000		
a) Share premium				
Balance 1 April 1997 .....	163,447	163,447		
Premium on allotment of ordinary shares .....	10,218	10,218		
Balance 31 March 1998.....	173,665	173,665		
	<b>Group £000</b>	<b>Company £000</b>		
b) Capital redemption reserve				
Balance 1 April 1997.....	279,325	279,325		
Balance 31 March 1998.....	279,325	279,325		
	<b>Group £000</b>			
c) Revaluation reserve				
Balance 1 April 1997 .....	2,025			
Realised on disposals .....	68			
Amortisation .....	11			
Balance 31 March 1998 .....	2,104			
	<b>Group £000</b>			
d) Goodwill reserve				
Balance 1 April 1997 .....	(346,356)			
Goodwill arising on acquisitions .....	(4,854)			
Goodwill in respect of businesses sold transferred to the profit and loss account .....	8,378			
Goodwill in respect of discontinuing businesses transferred to the profit and loss account.....	108,314			
Balance 31 March 1998 .....	(234,518)			
	<b>Group companies £000</b>	<b>Associated companies £000</b>	<b>Group Total £000</b>	<b>Company £000</b>
e) Profit and loss account				
Retained profits 1 April 1997 .....	258,347	19,046	277,393	116,975
Retranslation of net assets of overseas subsidiary and associated companies .....	(14,922)	(29)	(14,951)	-
Retranslation of long term foreign currency loans which relate to investments in overseas subsidiaries * .....	10,762	-	10,762	-
	254,187	19,017	273,204	116,975
Revaluation reserve realised on disposals .....	(68)	-	(68)	-
Amortisation of revaluation reserve .....	(11)	-	(11)	-
Contributions to employee share trusts by subsidiary undertakings .....	(6,349)	-	(6,349)	-
Retained (loss)/profit for the year .....	(241,692)	5,930	(235,762)	(99,636)
Retained profits 31 March 1998 .....	6,067	24,947	31,014	17,339

\*The amount for retranslation of long term foreign currency loans which relate to investments in overseas subsidiaries is shown net of a related taxation adjustment of £3,393,000.



# Notes on the Financial Statements

## 26 Reconciliation of operating profit to net cash inflow from operating activities

	1998	1997
	£000	£000
Operating profit .....	42,025	82,580
Depreciation .....	72,853	68,173
Amortisation of intangible fixed assets .....	148	62
Profit on sale of fixed assets .....	(68)	(1,851)
Release of closure provision .....	—	(276)
Fixed assets written off .....	300	789
Profits retained in associated companies .....	(22,276)	(18,964)
Less: Dividends received from associated companies .....	9,588	6,536
Profit of associated companies less dividends received .....	(12,688)	(12,428)
Decrease in stocks .....	7,677	4,455
Decrease/(increase) in debtors .....	26,183	(4,477)
(Decrease)/increase in creditors .....	(14,985)	29,961
Net cash inflow before exceptional non-trading items .....	121,445	166,988
Net cash outflow in respect of disposal or closure of operations .....	—	(216)
Net cash outflow in respect of prior year acquisition provisions .....	—	(11,990)
Net cash outflow in respect of fundamental reorganisation .....	—	(14,367)
Net cash inflow from operating activities .....	121,445	140,415

Cash outflow in respect of reorganisation costs was £14,232,000 (1997: £3,246,000).

## 27 Returns on investments and servicing of finance

	1998	1997
	£000	£000
Interest received .....	9,619	10,095
Interest paid .....	(25,168)	(23,346)
Interest element of finance lease/hire purchase payments .....	(8,256)	(9,388)
	(23,805)	(22,639)

## 28 Capital expenditure and financial investment

	1998	1997
	£000	£000
Purchase of tangible fixed assets .....	(129,511)	(131,179)
Purchase of intangible fixed assets .....	(206)	(127)
Purchase of investments .....	(2,889)	(6,961)
Sale of tangible fixed assets .....	13,775	12,607
Sale of intangible fixed assets .....	17	—
Sale of investments .....	—	91
	(118,814)	(125,569)

## 29 Acquisitions and disposals

	1998	1997
	£000	£000
Purchase of subsidiary undertakings (Note 31) .....	(6,650)	(19,181)
Cash at bank less bank overdrafts acquired with subsidiaries (Note 31) .....	802	(269)
Disposal of businesses (Note 32) .....	48,298	27,016
Cash at bank and in hand disposed with businesses (Note 32) .....	(1,366)	(616)
Discontinuing operations – net disposal proceeds (Note 33) .....	36,597	—
	77,681	6,950

# Notes on the Financial Statements

## 30 Analysis of net debt

	At 1 April 1997 £000	Cash flow £000	Disposals (excl. cash & overdrafts) £000	Other non-cash changes £000	Exchange movement £000	At 31 March 1998 £000
Net cash:						
Cash at bank and in hand.....	79,321	16,989	—	—	(2,704)	93,606
Bank overdrafts.....	(10,133)	(21,370)	—	—	1,129	(30,374)
	<u>69,188</u>	<u>(4,381)</u>	<u>—</u>	<u>—</u>	<u>(1,575)</u>	<u>63,232</u>
Liquid resources:						
Cash on deposit .....	<u>65,689</u>	<u>(40,727)</u>	<u>—</u>	<u>—</u>	<u>(400)</u>	<u>24,562</u>
Debt:						
Loans due within one year.....	(3,597)	1,674	—	108	390	(1,425)
Loans due in more than one year .....	(358,258)	54,443	—	(108)	6,468	(297,455)
Obligations under finance leases.....	<u>(112,475)</u>	<u>16,161</u>	<u>10</u>	<u>(335)</u>	<u>96</u>	<u>(96,543)</u>
	<u>(474,330)</u>	<u>72,278</u>	<u>10</u>	<u>(335)</u>	<u>6,954</u>	<u>(395,423)</u>
Net debt.....	<u>(339,453)</u>	<u>27,170</u>	<u>10</u>	<u>(335)</u>	<u>4,979</u>	<u>(307,629)</u>

## 31 Purchase of subsidiary undertakings

	1998 £000	1997 £000
Intangible fixed assets .....	—	16
Tangible fixed assets.....	—	5,437
Investments .....	—	60
Stocks.....	—	569
Debtors.....	—	30,807
Cash at bank less bank overdrafts (Note 29) .....	802	(269)
Creditors .....	(802)	(5,532)
Obligations under finance leases .....	—	(50)
Loans .....	—	(2,248)
Taxation.....	—	(175)
Deferred taxation.....	—	(8,844)
Goodwill .....	<u>4,854</u>	<u>(6,748)</u>
Cost of acquisitions.....	4,854	13,023
Less due under deferred purchase consideration.....	—	(1,829)
Add payments under deferred purchase consideration .....	<u>1,796</u>	<u>7,987</u>
Cash outflow in respect of purchase of subsidiary undertakings (Note 29) .....	<u>6,650</u>	<u>19,181</u>

## 32 Disposal of businesses

	1998 £000	1997 £000
Intangible fixed assets .....	172	—
Tangible fixed assets.....	6,954	3,205
Investments .....	—	4
Stocks.....	11,242	9,640
Debtors.....	8,875	16,844
Cash at bank and in hand (Note 29) .....	1,366	616
Creditors .....	(4,517)	(7,720)
Obligations under finance leases.....	(10)	—
Taxation.....	(107)	10
Goodwill .....	8,378	400
Profit on disposal .....	<u>11,334</u>	<u>9,075</u>
Proceeds.....	<u>43,687</u>	<u>32,074</u>
Satisfied by:		
Cash (Note 29).....	48,298	27,016
Amount receivable.....	(3,958)	3,958
Accrual for disposal costs.....	(1,367)	—
Pension surplus recognised on disposal of businesses .....	<u>714</u>	<u>1,100</u>
	<u>43,687</u>	<u>32,074</u>

Businesses which were sold during the year had a net cash outflow of £8,822,000 from operating activities, £190,000 in respect of returns on investments and servicing of finance, £4,049,000 in respect of taxation, £932,000 for capital expenditure and financial investment and £6,000 for financing.

# Notes on the Financial Statements

## 33 Discontinuing operations

	1998 £000
Tangible fixed assets – written off .....	4,119
Tangible fixed assets – disposals .....	21,879
Stocks written off .....	20,304
Debtors – written down .....	2,937
Debtors – finance leases sold .....	43,634
Debtors – property disposal .....	(20,359)
Creditors .....	5,561
Provisions .....	86,872
Depreciation .....	198
Goodwill written back .....	108,314
Cash received (Note 29) .....	(36,597)
	<u>236,862</u>

## 34 Acquisitions

The charting business division of British Airways Plc, Aerad, was acquired on 30 June 1997. The fair value of the assets acquired was £nil and the consideration was £4,850,000 giving rise to goodwill of £4,850,000. The profit before tax included in the consolidated profit and loss account for the year ended 31 March 1998 was £139,000. As Aerad was not a single reporting unit within British Airways Plc details of profits for the periods prior to the acquisition are not available.

## 35 Pension schemes

The Group operates a number of schemes throughout the world for the benefit of employees. The schemes are both defined benefit schemes and defined contribution schemes. The Group charge for pensions amounted to £17,130,000 (1997: £15,254,000).

The principal schemes are in the UK and are defined benefit schemes operated on a prefunded basis. The assets of these schemes are held in separate trustee administered funds. The UK schemes are subject to triennial valuations and annual interim investigations by independent actuaries. The last triennial valuations for the principal schemes were carried out as at 1 April 1995 using the projected unit method in which the actuarial liability makes allowance for projected pensionable earnings.

With effect from 2 July 1997, advance corporation tax credits on UK equities were abolished in respect of pension schemes. The financial assumptions both for valuation of the principal schemes and for the purposes of Statement of Standard Accounting Practice No. 24 (SSAP 24) were adjusted with effect from 1 April 1997 to reflect this:

Investment returns	8.5% per annum
General salary growth	6.5% per annum
Equity dividend growth	5.0% per annum

In addition to the principal schemes, Racal Telecommunications Limited is the designated employer of the Racal Telecommunications Limited Shared Cost Section of the Railways Pension Scheme (a defined benefit scheme operated on a prefunded basis). The last triennial valuation of this scheme was carried out as at 1 April 1996. For the purposes of SSAP 24 the assumptions applied to the principal schemes have also been applied to the Racal Telecommunications Limited Shared Cost Section of the Railways Pension Scheme.

At 1 April 1997, the market value of the assets of the UK schemes was £651,086,000 and the corresponding actuarial value was sufficient to cover 124% of the benefits which had accrued to members allowing for assumed increases in earnings.

The pension costs for the UK schemes amounted to £11,119,000 (1997: £7,705,000). The pension costs of the Group's overseas schemes amounted to £6,011,000 (1997: £7,549,000) having been determined in accordance either with SSAP 24, or with the accounting standard of the countries concerned. In the case of the latter, the costs of the overseas schemes would not be significantly different had they been calculated in accordance with SSAP 24.

A prepayment of £53,434,000 (1997: £46,276,000) is included in prepayments due after more than one year. This represents the excess of the amounts funded over accumulated pension costs.

# Notes on the Financial Statements

## 36 Future Group capital expenditure

	1998 £000	1997 £000
Contracted for but not provided for in the financial statements.....	10,746	15,163

## 37 Contingent liabilities

There are contingent liabilities in the event of any claim for breach or non-performance of the terms of overseas contracts against which bank guarantees have been issued amounting to £78,515,000 (1997: £69,301,000). In addition, the Company has issued a guarantee, not limited in value, in respect of the due and punctual performance of two subsidiaries under various agreements in relation to a European defence project.

Under the terms of an agreement entered into between Camelot Group plc and all of its shareholders, the Company has a contingent liability in an amount not exceeding £9 million in the unlikely event of Camelot's licence to operate the National Lottery being revoked by the Secretary of State for Culture, Media and Sport.

The Company has issued two guarantees, not limited in value, in respect of the performance of a subsidiary company and of an associated company of their respective obligations under various agreements in relation to a United Kingdom defence project. The guarantee in respect of the associated company's obligations is joint and several with the other shareholders of that company.

## 38 Financial commitments

### Group

Group companies have commitments under various operating lease agreements in connection with land and buildings and other assets. Under these agreements the payments to which the companies are committed during the next financial year and for which no provision has been made in these financial statements are as follows:

	1998 Land and buildings £000	1998 Other assets £000	1997 Land and buildings £000	1997 Other assets £000
Payable on operating leases that expire within one year.....	1,350	1,076	771	1,048
Payable on operating leases that expire between two and five years.....	7,942	8,272	5,061	5,797
Payable on operating leases that expire after five years .....	6,623	5	6,833	23
	<u>15,915</u>	<u>9,353</u>	<u>12,665</u>	<u>6,868</u>

### Company

The Company had no commitments under operating leases.

# Notes on the Financial Statements

## 39 Related party transactions

	1998 £000	1997 £000
<b>Transactions with associated companies</b>		
Turnover		
Camelot Group plc .....	20,407	23,340
Archer Communications Systems Limited .....	2,443	—
Other associated companies .....	2,660	1,399
	<u>25,510</u>	<u>24,739</u>
Purchases		
Racal Insurance Services Limited .....	5,003	3,816
Other associated companies .....	136	83
	<u>5,139</u>	<u>3,899</u>
Dividends received		
Camelot Group plc .....	7,875	4,250
Satellite Information Services (Holdings) Limited .....	1,713	1,509
Other associated companies .....	—	777
	<u>9,588</u>	<u>6,536</u>
Amounts due from associated companies (Note 17)		
Camelot Group plc .....	751	5,032
Archer Communications Systems Limited .....	2,339	—
Other associated companies .....	1,526	746
	<u>4,616</u>	<u>5,778</u>
Amounts due to associated companies (Note 19) .....	<u>17</u>	<u>31</u>

## 40 Post balance sheet events

### a) Camelot Group plc

On 31 March 1998 the board of Camelot Group plc agreed to proceed with the purchase of GTECH UK Limited's shareholding in Camelot Group plc for £51 million. The agreement was signed and the transaction completed on 20 April 1998, reducing the net assets of Camelot Group plc by £51 million. On completion, the 11,250,000 shares purchased were cancelled.

A further transaction took place on 24 April 1998 whereby International Computers Limited purchased shares from each of the remaining shareholders to increase its percentage shareholding in Camelot Group plc to 20 per cent. On that date Racal Electronics Plc sold 916,667 shares in Camelot Group plc to International Computers Limited for £4,906,000. After this transaction Racal Electronics Plc's revised percentage shareholding in Camelot Group plc became 26.67 per cent.

### b) Data Communications

On 11 December 1997 the Company announced its intention to exit from Data Communications. As part of that exit, on 6 August 1998 the Company exchanged contracts for the sale of the worldwide business of the Racal Data Group, exclusive of the Security and Payments activity, to Platinum Equity Holdings of Los Angeles, California. Completion occurred on 11 September 1998. The total consideration was expected to be US\$47.5 million, with US\$12.5 million payable in cash on completion and the balance payable as a royalty on future sales of the Racal Data Group over the next ten years under Platinum's ownership. The consideration was determined based on shareholders' funds as at 31 March 1998 and was subject to adjustment dependent on the closing balance sheet on 11 September 1998. An interim balance sheet has been prepared, requiring Racal to reimburse US\$1.4 million of the US\$12.5 million paid by Platinum on completion. Should any further adjustment based on the final balance sheet be required, this will be deducted from the royalties payable by Platinum, the majority of which are expected to be received in the next five years. Platinum will assume all future liabilities for reorganisation and severance costs, and Racal has retained tax losses in the USA and a number of European countries amounting to in excess of US\$100 million.

# Investor Information

## Registrars

IRG plc maintains the register of members of the Company. If you have any questions about your personal holding of Racal Electronics Plc shares please contact IRG plc at the address shown on page 24 or telephone 0181 650 4866.

If you change your name or address or if the details on the form of proxy enclosed with this Report and Accounts, including your post code, are incorrect or incomplete, please notify the Registrars in writing.

## Shareholder enquiries

If you have an enquiry about the Company's business, or about something affecting you as a shareholder (other than queries which are dealt with by the Registrars, as shown above), you should contact the Company Secretary by letter at the Company's registered office.

## Financial calendar 1998

Annual General Meeting – 16 October 1998

Record date for declared second interim dividend – 21 August 1998

Payment date for declared second interim dividend – 11 September 1998

The Company usually announces interim results in December and pays the interim dividend in February. Results for the full year are usually announced in June.

## American Depositary Receipts

The Company has established a sponsored American Depositary Receipt (ADR) programme in the United States. Each ADR, which represents two ordinary shares of the Company, may be publicly traded in the USA on the Over-The-Counter Market. The programme is administered on behalf of Racal Electronics Plc by The Bank of New York, ADR Division, 101 Barclay Street, New York, NY10286.

At 31 March 1998 there were 582 registered holders of ADRs representing approximately 4,000 beneficial holders.

## Corporate personal equity plans

The Racal Electronics General and Single Company Corporate Personal Equity Plans (PEPs) were introduced in 1993/94. A feature of these PEPs is that new Racal Electronics ordinary shares are issued thereby avoiding purchase costs and stamp duty. This allows shareholders to invest in the Company in a tax efficient and cost-effective manner.

For more details please contact Bradford & Bingley (PEPs) Limited, PO Box 198, Main Street, Bingley, West Yorkshire BD16 3YD. Telephone 01274 555700.

The PEPs are managed by Bradford & Bingley (PEPs) Limited which has approved this section and which is regulated by the Personal Investment Authority for Investment Business.

Please note that the levels and bases of taxation can change. The value of reliefs referred to depends upon individual circumstances. The value of shares can go down as well as up and as a result the return on a PEP may be less than the amount invested.

## Capital gains tax

The market value of one of the Company's ordinary shares at 31 March 1982 was 375p. After adjustment for the capitalisation issues made in August 1983 and August 1989 but before adjustment for the Vodafone Group demerger, the capital reorganisation and the Chubb Security demerger the market value at 31 March 1982 was 93.75p.

The demerger distribution rate of the Vodafone Group shares was 57.64622 ordinary shares of Vodafone Group for every 100 Racal Electronics shares held at 13 September 1991.

The following base cost apportionment will apply for UK capital gains tax purposes:

Racal Electronics	19.964%
Vodafone Group	80.036%.

Under the terms of the Chubb Security demerger, which incorporated a capital reorganisation of Racal Electronics immediately prior to the demerger, shareholders received one Racal Electronics share and one Chubb Security share for every five Racal Electronics shares held at the close of business on 2 October 1992.

The following base cost apportionment will apply for UK capital gains tax purposes:

Racal Electronics	41.195%
Chubb Security	58.805%.

## Analysis of shareholdings in Racal Electronics Plc at 31 March 1998

### Type of shareholder

	Number of accounts	% of total issued shares
Nominee companies	3,246	85.84
Assurance & Insurance companies	133	0.95
Pension funds & Pension trustees	6	0.03
Investment trusts & funds	127	1.54
Local & National institutions	48	0.69
Other corporate bodies	178	0.56
ADRs	1	0.65
Private individuals	19,601	9.74
	<u>23,340</u>	<u>100.00</u>

### Shareholders

Number of shares held	Number of accounts	% of total issued shares
1 – 500	10,131	0.81
501 – 2,500	9,115	3.77
2,501 – 5,000	2,063	2.51
5,001 – 10,000	1,083	2.53
10,001 – 25,000	404	2.23
25,001 – 50,000	155	1.94
50,001 – 75,000	71	1.49
75,001 – 100,000	50	1.57
More than 100,000	268	83.15
	<hr/> 23,340	<hr/> 100.00

# The Queen's Awards

Companies owned by Racal at the time  
have won 33 Queen's Awards for  
Technological or Export Achievement.



## TECHNOLOGY

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1978 Racal-Dana Instruments Limited  
1979 Racal Communications Limited  
1980 Racal Safety Limited  
1982 Racal-Redac Limited  
1984 Racal Defence Electronics (Radar) Limited  
1984 Racal-BCC & Racal Research Limited  
1987 Racal Marine Radar Limited  
1987 Racal Recorders Limited  
1988 Racal Marine Systems Limited  
1989 Racal-MESL Limited  
1992 Racal Radar Defence Systems Limited  
1995 Racal Instruments Limited  
1997 Racal Avionics Limited



## EXPORT

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1970 Racal-Mobilcal Limited  
1971 Racal-BCC  
1971 Racal-Mobilcal Limited  
1972 Racal-Mobilcal Limited  
1973 Racal-Milgo Limited  
1976 Racal-Mobilcal Limited  
1976 Racal Communications Limited  
1977 Racal-Tacticom Limited  
1980 Racal-Datacom Limited  
1980 Racal-Redac Limited  
1981 Racal Communications Limited  
1982 Racal Avionics Limited  
1982 Racal Security Limited  
1983 Racal Defence Electronics (Radar) Limited  
1984 Racal-Tacticom Limited  
1986 Racal Communications Systems Limited  
1986 Racal Safety Limited  
1991 Racal Survey Limited  
1992 Chubb Safe Equipment Company  
1993 Racal Radar Defence Systems Limited

# Notice of Meeting

Notice is hereby given that the forty sixth Annual General Meeting of the Company will be held at Le Meridien Waldorf Hotel, Aldwych, London WC2 on 16 October 1998 at 11.45 a.m. to transact the following business:

- 1 To receive the report of the directors and financial statements for the year ended 31 March 1998.
- 2 \* To re-elect Sir Ernest Harrison as a director.
- 3 \* To re-elect Sir Gerald Whent as a director.
- 4 \* To elect Lord Inge as a director.
- 5 \* To re-elect Mr B J Clarke as a director.
- 6 \* To re-elect Mr A R Wood as a director.
- 7 To re-appoint Deloitte & Touche as auditors to the Company until the next Annual General Meeting.
- 8 To authorise the directors to determine the remuneration of the auditors.
- 9 \* As special business to consider and, if thought fit, pass the following resolution which will be proposed as a special resolution:  
THAT the power conferred on the directors by Article 6(C) of the Company's Articles of Association be renewed for the period ending on the date of the Annual General Meeting in 1999 and that for such period the Section 89 amount shall be £3,625,000.

By Order of the Board  
David Whittaker  
Director and Secretary

Western Road  
Bracknell  
Berkshire RG12 1RG  
21 September 1998

## Notes:

1. A member entitled to attend and vote is entitled to appoint one or more proxies to attend and vote instead of him. A proxy need not be a member of the Company, but, except in the case of a proxy for a corporate member, is not entitled to vote except on a poll. A form of proxy is enclosed.
2. Lodgement of a proxy will not preclude a shareholder from attending and voting at the Meeting.
3. Pursuant to regulation 34 of the Uncertificated Securities Regulations 1995, the Company has specified that only those ordinary shareholders registered on the Register of Members of the Company at 11.45 a.m. on 14 October 1998 shall be entitled to attend and vote at the Meeting in respect of the number of ordinary shares registered in their name at that time. Changes to the Register of Members after 11.45 a.m. on 14 October 1998 shall be disregarded in determining the rights of any person to attend and vote at the Meeting.

\* For further information see the report of the directors on pages 25 to 27.