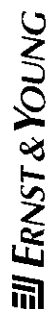


Horstman Defence Systems Limited

Report and Accounts

31 March 2002

Company Number: 1511975

 ERNST & YOUNG



Horstman Defence Systems Limited

DIRECTORS' REPORT

The directors present their report and accounts of the company for the eight months ended 31 March 2002.

Principal activities

The principal activity of the company continues to be the design and manufacture of gearboxes, auxiliary power units and components, hydraulic dampers for military vehicles, high precision aircraft and torpedo parts and naval instrumentation equipment.

Review of the business and future developments

The business has been restructured to adjust to the changing market conditions which has resulted in significant reorganisation costs being incurred in the period. However, trading volume has improved with further growth anticipated as the benefits of cost reduction and other business improvements are realised.

Results and dividends

The results for the period are shown in the profit and loss account on page 4.

The directors do not recommend the payment of a final dividend (2001: £nil). The retained loss of £308,038 for the eight months to 31 March 2002 (2001: profit of £16,002 for the seven months to 31 July 2001) will be transferred from (2001: to) reserves.

Directors

The directors who served during the period were:

Mr J G Harris	(Appointed	12 th Nov 2001)
Mr A Brooks	(Resigned	12 th Nov 2001)
Mr G Norris	(Resigned	12 th Nov 2001)
Mr J Edwards	(Resigned	12 th Nov 2001)

Directors' interests

None of the directors had an interest in the share capital of the company. J G Harris is a director of the ultimate parent company, Harris Watson Holdings plc, and his shareholding is disclosed in that company's accounts.

Research and development

The company is committed to a policy of investment in the future both by acquisition of new capital equipment and by expenditure on product development and improvement.

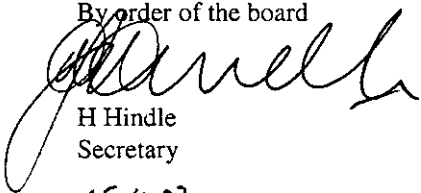
Payment policy

It is the company's payment policy to negotiate terms with its suppliers in all sectors to ensure that they know the terms on which payment will take place when the business is agreed. It is our policy to abide by these terms. The number of days purchases outstanding at the year end was 54 (2001: 50 days).

Auditors

During the period, the directors appointed Ernst & Young LLP as the company's auditors. In accordance with the provision of Section 386 of the Companies Act 1985 the company has resolved to dispense with the obligation to appoint auditors annually.

By order of the board


H Hindle
Secretary

15.11.02

Horstman Defence Systems Limited

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ACCOUNTS

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

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent; and
- Prepare the accounts on the going concern basis unless it is inappropriate to presume that the company will continue in business.

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

REPORT OF THE AUDITORS
to the members of Horstman Defence Systems Limited

We have audited the company's accounts for the period ended 31 March 2002 which comprise the Profit and Loss Account, Balance Sheet and the related notes 1 to 22. These accounts have been prepared on the basis of the accounting policies set out therein.

Respective responsibilities of directors and auditors

As described in the Statement of Directors' Responsibilities the company's directors are responsible for the preparation of the accounts in accordance with applicable United Kingdom law and accounting standards.

Our responsibility is to audit the accounts in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

We report to you our opinion as to whether the accounts give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the accounts, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the company is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

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

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

Opinion

In our opinion the accounts give a true and fair view of the state of affairs of the company as at 31 March 2002 and of its loss for the period then ended and have been properly prepared in accordance with the Companies Act 1985.



Ernst & Young LLP
Registered Auditor
Birmingham

18/1/02.

Horstman Defence Systems Limited

PROFIT AND LOSS ACCOUNT

For the period ended 31 March 2002

	Notes	8 months to 31 March 2002 £	7 months to 31 July 2001 £
TURNOVER	2	5,496,421	4,388,175
Cost of sales		(4,781,184)	(3,773,376)
GROSS PROFIT		715,237	614,799
Distribution and selling costs		(213,750)	(173,402)
Administrative expenses		(817,206)	(424,717)
Other operating income	4	53,800	58,835
OPERATING (LOSS)/PROFIT		(261,919)	75,515
Interest payable	7	(105,010)	(44,249)
(LOSS)/PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	3	(366,929)	31,266
Taxation on (loss)/profit on ordinary activities	8	58,891	(15,264)
RETAINED (LOSS)/PROFIT FOR THE PERIOD	17	(308,038)	16,002

STATEMENT OF RECOGNISED GAINS AND LOSSES

There are no recognised gains or losses other than the loss attributable to shareholders of the company of £308,038 for the 8 months ended 31 March 2002 and the profit of £16,002 for the 7 months ended 31 July 2001.

Note of historical cost profits and losses

	8 months to 31 March 2002 £	7 months to 31 July 2001 £
Reported (loss)/profit on ordinary activities before taxation	(366,929)	31,266
Difference between depreciation based on historical cost and on revalued amounts	5,277	4,617
Historical cost (loss)/profit on ordinary activities before taxation	(361,652)	35,883
Historical cost (loss)/profit for the period, retained after taxation and dividends	(302,761)	20,619

Horstman Defence Systems Limited

BALANCE SHEET

at 31 March 2002

	Note	31 March 2002 £	31 July 2001 £
FIXED ASSETS			
Tangible assets	9	1,971,415	2,077,980
CURRENT ASSETS			
Stocks	10	1,135,306	1,642,169
Debtors	11	3,445,479	1,036,247
Cash at bank and in hand		<u>438,511</u>	<u>4,332</u>
		5,019,296	2,682,748
CREDITORS: amounts falling due within one year	12	<u>(3,420,165)</u>	<u>(2,551,666)</u>
NET CURRENT ASSETS		1,599,131	131,082
TOTAL ASSETS LESS CURRENT LIABILITIES		3,570,546	2,209,062
CREDITORS: amounts falling due after more than one year	13	(1,425,222)	-
Provisions for liabilities and charges	15	(411,494)	(167,194)
		<u>1,733,830</u>	<u>2,041,868</u>
CAPITAL AND RESERVES			
Called up share capital	16	50,000	50,000
Share premium account	17	207	207
Revaluation reserve	17	88,964	94,241
Profit and loss account	17	1,594,659	1,897,420
EQUITY SHAREHOLDERS' FUNDS		<u>1,733,830</u>	<u>2,041,868</u>

The accounts were approved by the board of directors on 15/11/02.

J. G. Harris

J G Harris - Director

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

1. ACCOUNTING POLICIES

Accounting convention

The financial statements have been prepared under the historical cost convention as modified by the revaluation of certain fixed assets, and in accordance with applicable accounting standards.

In preparing the accounts for the current year, the company has adopted FRS 18 'Accounting Policies', FRS 19 'Deferred Tax' and the transitional arrangements of FRS 17 'Retirement Benefits'. The adoption of FRS 19 has resulted in a change in accounting policy for deferred tax. Deferred tax is recognised on a full provision basis in accordance with the accounting policy described below. Previously, deferred tax was provided for on a partial provision basis, whereby provision was made on all timing differences to the extent that they were expected to reverse in the future without replacement.

Royalty Income

Income relating to royalties is accounted for on a receipts basis.

Depreciation

Depreciation is provided on all tangible fixed assets at rates calculated to write off the cost of each asset evenly over its expected useful life as follows:

Fixtures and Fittings	10% to 20%
Plant and Machinery	7% to 25%
Freehold buildings	2% to 4%

No depreciation is charged on freehold land.

Stocks and work-in-progress

Stocks and work-in-progress are stated at the lower of cost and net realisable value. Cost is calculated to include an appropriate proportion of manufacturing overhead.

Research and development

Research and development expenditure is written off against profit in the year in which the expenditure arises.

Deferred taxation

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay more, or a right to receive more, tax, with the following exceptions:

- provision is made for tax on gains arising from the revaluation of fixed assets, and gains on disposal of fixed assets that have been rolled over into replacement assets, only to the extent that, at the balance sheet date, there is a binding agreement to dispose of the assets concerned. However, no provision is made where, on the basis of all available evidence at the balance sheet date, it is more likely than not that the taxable gain will be rolled over into replacement assets and charged to tax only where the replacement assets are sold;
- deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse.

Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Balances denominated in a foreign currency are translated into sterling at the exchange rates ruling on the balance sheet date or where there are matching forward contracts in respect of trading transactions, the rates of exchange specified in the contracts are used. All realised differences are taken to the profit and loss account and unrealised differences on forward contracts are taken to the balance sheet.

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

1. ACCOUNTING POLICIES (continued)

Cash flow statement

In accordance with Financial Reporting Standard 1 (Revised 1996), the company is exempt from the requirement to prepare a cash flow statement on the grounds that the company is included in the consolidated accounts of its ultimate parent company, Harris Watson Holdings plc.

Pensions

The company operates a defined contribution pension scheme. Contributions are charged in the profit and loss account as they become payable in accordance with the rules of the scheme.

Leases

Assets acquired under finance leases and hire purchase contracts are capitalised in the balance sheet and depreciated in accordance with the company's depreciation policies. The interest element of leasing payments represents a constant proportion of the capital balance outstanding and is charged to the profit and loss account over the period of the lease. The capital elements of future obligations under the leases and hire purchase agreements are included as liabilities in the balance sheet. All other leases are accounted for as operating leases and the rental is charged to the profit and loss account in the period in which these are incurred.

2. TURNOVER

Turnover, which is stated net of value added tax, represents the total amount receivable by the company for goods supplied and services provided. All turnover is attributable to the continuing principal activity.

The geographic analysis of turnover is as follows:

	<i>8 months to 31 March 2002</i>	<i>7 months to 31 July 2001</i>
	£	£
United Kingdom	3,636,819	3,603,562
Asia, Far East and Australia	1,447,955	591,417
North, South and Central America	202,275	60,727
Europe	209,372	132,469
	<u>5,496,421</u>	<u>4,388,175</u>

3. (LOSS)/PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

The (loss)/profit on ordinary activities before taxation is stated after charging the following items:

	<i>8 months to 31 March 2002</i>	<i>7 months to 31 July 2001</i>
	£	£
Auditors' remuneration - audit services	11,500	10,946
Depreciation on owned assets	41,921	142,624
Depreciation on leased assets	118,448	-
Restructuring provision	250,000	-
Operating lease charges - plant and machinery	38,195	33,132
Research and development expenditure	100,057	222,701
Exchange loss/(gain) on foreign currencies	8,425	(4,532)
	<u></u>	<u></u>

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

4. OTHER OPERATING INCOME

	<i>8 months to 31 March 2002</i>	<i>7 months to 31 July 2001</i>
	£	£
Royalties received	53,800	58,835

5. DIRECTORS' EMOLUMENTS

	<i>8 months to 31 March 2002</i>	<i>7 months to 31 July 2001</i>
	£	£
Emoluments for services as directors	28,550	36,169
	<i>No</i>	<i>No</i>
Members of defined benefit schemes	-	3

6. STAFF COSTS

The average number of employees, including directors, during the period was as follows:

	<i>8 Months to 31 March 2002</i>	<i>7 months to 31 July 2001</i>
	<i>No</i>	<i>No</i>
Sales, administration and distribution	14	16
Manufacturing	67	66
	81	82

The aggregate payroll costs of these persons were as follows:

	<i>8 months to 31 March 2002</i>	<i>7 months to 31 July 2001</i>
	£	£
Wages and salaries	1,301,677	1,133,180
Social security costs	114,217	89,887
Other pension costs	67,767	85,913
	1,483,661	1,308,980

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

7. INTEREST PAYABLE

	8 months to 31 March 2002 £	7 months to 31 July 2001 £
Bank overdrafts	-	39,850
Finance leases	35,628	311
Mortgage	15,694	-
Invoice discounting	12,000	-
Other	41,688	4,088
	<u>105,010</u>	<u>44,249</u>

8. TAXATION ON (LOSS)/PROFIT ON ORDINARY ACTIVITIES

(a) The tax (credit)/charge is made up as follows:

	8 months to 31 March 2002 £	7 months to 31 July 2001 £
Based on the (loss)/profit for the period:		
Corporation tax at 30% (2001: 30%)	-	9,380
Group relief	(52,868)	-
Deferred taxation	(15,700)	-
Overseas taxation	5,380	5,884
Taxation relating to prior years:		
Corporation tax charge/(credit)	4,297	-
	<u>(58,891)</u>	<u>15,264</u>

The company has surrendered tax losses to utilise as group relief for which payment has been received.

(b) The tax assessed on the loss on ordinary activities for the period is lower than the standard rate of corporation tax in the UK of 30%. The differences are reconciled below:

	2002 £
Loss on ordinary activities before tax	(366,929)
Loss on ordinary activities multiplied by standard rate of corporation tax in the UK of 30%	(110,079)
Other expenditure deductible for tax purposes	(28,365)
Decelerated capital allowances	12,810
Other timing differences	72,766
Total current tax (note 8(a))	<u>(52,868)</u>

(c) Factors that may affect future tax charges

No provision has been made for deferred tax on gains recognised on revaluing property to its market value. Such tax would become payable only if the property were sold without it being possible to claim rollover relief. The total amount not provided for is £39,858 (2001: £39,858). At present, it is not envisaged that any tax will become payable in the foreseeable future.

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

9. TANGIBLE FIXED ASSETS

	<i>Freehold land and buildings</i>	<i>Plant and machinery</i>	<i>Total</i>
	£	£	£
Cost/Valuation:			
At 1 August 2001	956,701	4,089,452	5,046,153
Additions	-	53,806	53,806
Disposals	-	(210,423)	(210,423)
At 31 March 2002	956,701	3,932,835	4,889,536
Depreciation:			
At 1 August 2001	291,359	2,676,814	2,968,173
Charge for period	16,470	143,899	160,369
Disposals	-	(210,421)	(210,421)
At 31 March 2002	307,829	2,610,292	2,918,121
Net book value:			
At 31 March 2002	648,872	1,322,543	1,971,415
At 1 August 2001	665,342	1,412,638	2,077,980

Assets held under finance leases and capitalised in plant and machinery:

	<i>31 March 2002</i>	<i>31 July 2001</i>
	£	£
Cost	3,171,175	-
Aggregate depreciation	(2,019,452)	-
	1,151,723	-

The freehold land and buildings includes assets valued in 1980 at £386,848 (2001: £386,848). The company has taken advantage of the transitional arrangements of Financial Reporting Standard 15 and consequently, the valuation has not been updated. If stated under the historical cost convention the comparable amounts for freehold land and buildings would be:

	<i>31 March 2002</i>	<i>31 July 2001</i>
	£	£
Cost	805,687	805,687
Depreciation	(245,779)	(234,586)
	559,908	571,101

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

10. STOCKS

	<i>31 March 2002 £</i>	<i>31 July 2001 £</i>
Raw materials	31,690	32,861
Work-in-progress	<u>1,931,889</u>	<u>2,571,308</u>
	1,963,579	2,604,169
Payments received on account	(828,273)	(962,000)
	<u>1,135,306</u>	<u>1,642,169</u>

The stock value is not materially different from the replacement cost.

11. DEBTORS

	<i>31 March 2002 £</i>	<i>31 July 2001 £</i>
Trade debtors	1,087,849	972,207
Amounts owed by group undertakings	2,193,749	15,069
Other debtors	23,879	1,430
Prepayments and accrued income	140,002	47,541
	<u>3,445,479</u>	<u>1,036,247</u>

12. CREDITORS: amounts falling due within one year

	<i>31 March 2002 £</i>	<i>31 July 2001 £</i>
Overdrafts	-	986,805
Mortgage	72,535	-
Finance leases	309,320	-
Trade creditors	1,556,740	941,823
Corporation tax	-	54,942
Other taxation and social security	53,584	122,409
Amounts owed to group undertakings	1,165,887	139,190
Accruals and deferred income	262,099	306,497
	<u>3,420,165</u>	<u>2,551,666</u>

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

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

	31 March 2002 £	31 July 2001 £
Finance leases	508,547	-
Mortgage	916,675	-
	<u>1,425,222</u>	<u>-</u>

The mortgage is secured by a charge over the freehold property included in fixed assets as disclosed in note 9 and also by a guarantee given by the holding company.

	31 March 2002 £	31 July 2001 £
Repayable within one year	72,535	-
Repayable between one and two years	66,660	-
Repayable between two and five years	199,980	-
Repayable after five years	650,035	-
	<u>989,210</u>	<u>-</u>

The original amount of the mortgage was £1,000,000 repayable by October 2016 and interest is charged at base rate plus 2.25% per annum.

14. OBLIGATIONS UNDER FINANCE LEASES AND HIRE PURCHASE CONTRACTS

	31 March 2002 £	31 July 2001 £
Finance Leases	817,867	-
Future minimum payments under finance leases are as follows:		
Within one year	403,397	-
In more than one year, but not more than five years	661,072	-
Total gross payments	1,064,469	-
Less finance charges included above	246,602	-
	<u>817,867</u>	<u>-</u>

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

15. PROVISIONS FOR LIABILITIES AND CHARGES

	£
At 1 August 2001 – Warranty Provision	118,194
Debited to the profit and loss account during the period: –	
Warranty Provision	10,000
Restructuring Provision	250,000
	<hr/>
At 31 March 2002	378,194
	<hr/>
	<i>Deferred Tax</i>
	£
At 1 August 2001	49,000
Charge/(credit) for the period	(15,700)
	<hr/>
At 31 March 2002	<u>33,300</u>

	Amount provided	
	<i>31 March</i>	<i>31 July</i>
	<i>2002</i>	<i>2001</i>
	£	£
Deferred taxation:		
Capital allowances	89,190	102,000
Surplus on revaluation	-	-
Other timing differences	(55,890)	(53,000)
	<hr/>	<hr/>
	33,300	49,000
	<hr/>	<hr/>

16. SHARE CAPITAL

	<i>31 March</i>	<i>31 July</i>
	<i>2002</i>	<i>2001</i>
	£	£
Authorised		
50,000 ordinary shares of £1 each	50,000	50,000
	<hr/>	<hr/>
Allotted, issued and fully paid		
50,000 ordinary shares of £1 each	50,000	50,000
	<hr/>	<hr/>

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

17. RESERVES

	<i>Share premium account £</i>	<i>Revaluation Reserve £</i>	<i>Profit and loss account £</i>
At 1 January 2001	207	98,858	1,876,801
Retained profit for the period	-	-	16,002
Transfer of difference between depreciation based on historical costs and on revalued amounts	-	(4,617)	4,617
At 31 July 2001	207	94,241	1,897,420
Retained loss for period	-	-	(308,038)
Transfer of difference between depreciation based on historical costs and on revalued amounts	-	(5,277)	5,277
At 31 March 2002	207	88,964	1,594,659

18. CONTINGENT LIABILITIES

	<i>31 March 2002 £</i>	<i>31 July 2001 £</i>
Guarantees in respect of indebtedness of third parties	27,064	27,064

19. COMMITMENTS

a) Capital commitments

There were no capital commitments contracted but not provided in the financial statements at 31 March 2002 or at 31 July 2001.

b) Operating lease commitments

At 31 March 2002 the company had annual commitments under non-cancellable operating leases as follows:

	<i>31 March 2002 £</i>	<i>31 July 2001 £</i>
Plant and machinery		
Operating lease expiry:		
Within 1 year	15,399	3,172
Between 1 and 5 years	20,561	52,785
	35,960	55,957

Horstman Defence Systems Limited

NOTES TO THE ACCOUNTS

at 31 March 2002

20. PENSIONS

The company operates a defined contribution pension scheme for the benefit of its employees. The assets of the scheme are held separately from those of the company in an independently administered fund. There were no unpaid contributions outstanding at the period end.

21. RELATED PARTIES

As permitted by FRS 8 'Related Party Disclosures' the accounts do not disclose transactions with the parent company and fellow subsidiaries where 90% of the voting rights are controlled within the group.

22. ULTIMATE PARENT UNDERTAKING

The company's ultimate parent undertaking is Harris Watson Holdings plc.

Until 11 November 2001 the company's ultimate parent undertaking was Smiths Group plc, which is incorporated in Great Britain and registered in England and Wales and whose accounts are available to the public and may be obtained from 765 Finchley Road, London, NW11 8DS.

Harris Watson Holdings plc is incorporated in Great Britain and registered in England and Wales. Copies of its group accounts which include the company are available from the company's registered office, 45 Waterlinks House, Richard Street, Birmingham, West Midlands B7 4AA.