

BRITISH STEEL ENGINEERING STEELS LIMITED
REGISTERED NUMBER : 1992636

REPORT OF THE DIRECTORS
for the year ended 3 APRIL 1999

The directors present their report and the financial statements for the year ended 3 April 1999. The comparatives are for the year ended 28 March 1998.

Directors' Responsibilities for the Preparation of the Financial Statements

The directors are required by UK company law to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company at the end of the financial year and of the profit or loss and total recognised gains and losses of the Company for that period.

The directors confirm that suitable accounting policies have been used and applied consistently, and reasonable and prudent judgements and estimates have been made, in the preparation of the financial statements for the year ended 3 April 1999. The directors also confirm that applicable accounting standards have been followed and that the financial statements have been prepared on the going concern basis.

The directors are responsible for keeping proper accounting records, for safeguarding the assets of the Company and for taking reasonable steps to prevent and detect fraud and other irregularities.

Principal Activities

The principal activities of the Company are the manufacture of steel and the re-rolling of engineering steels. The Company produces a wide range of steel products including billets, slabs, bars and rods for the automotive, agricultural, marine and petrochemical industries.

Review of Business

The profit and loss account is set out on page 6. Falling levels of demand and selling prices, and the continuing strength of sterling, have adversely affected the performance of the company, and will continue to do so into 1999/00. However, the directors are of the opinion that the results and year end financial position were satisfactory in these conditions.

Results and Dividends

No dividend was paid during the year (1998: £15.3m). No final dividend is recommended (1998: nil). The £2.2 million profit was transferred to reserves (1998: £4.0m loss was taken from reserves). Details of dividends paid are set out in note 8 on page 14.

Changes in Fixed Assets

The movements in fixed assets during the year are set out in note 9 to the financial statements. The directors are of the opinion that the market value of the Company's properties is in excess of their book values at 3 April 1999 but, in the absence of any recent professional valuations, are unable to quantify such excess.

Directors

The directors of the company during the year ended 3 April 1999 were :-

H Homer - Chairman

J L Rennocks

D Turner

W J Cain - resigned 31st March 1999

C D Gardner

Directors' Interests in Shares of the Group

The directors had the following interests in the ordinary shares of British Steel plc, the company's ultimate holding company:

	<u>Ordinary Shares</u>		<u>Share Options</u>			
	<u>3 April</u> <u>1999</u>	<u>28 March</u> <u>1998</u>	<u>28 March</u> <u>1998</u>	<u>Granted</u>	<u>Exercised</u>	<u>3 April</u> <u>1999</u>
H Homer	80,954	66,065	438,110	-	14500	423,610
J L Rennocks	11,846	11,846	318,128	-	-	318,128
D Turner	482	482	74,828	-	-	74,828
C D Gardner	-	-	33,828	-	-	33,828

Insurance of Directors

British Steel plc, the parent undertaking, maintains insurance for the directors and officers in respect of their duties as directors and officers of the Company.

Research and Development

The Company's management recognises the emphasis which needs to be placed on research and development activities to enhance the competitive position of the Company's products and processes in their respective market places. For this reason, substantial research and development projects continue to be undertaken by the Company.

Employee Involvement

The policy of the directors is to encourage the involvement of all employees in the development and performance of the Company. There are regular meetings at all plants between management, employees and trade union representatives.

Disabled Persons

All job applications, including those received from disabled persons, are given full consideration. Selection is on the basis of ability and, where necessary, disabled applicants are given appropriate training to enable them to meet the requirements of the job. Efforts are made to enable employees, who become disabled during employment, to continue their careers with the Company. Training, career development and promotion of disabled persons is, as far as possible, identical to that of other employees who are not disabled.

Charitable Donations

Donations totalling £18,197 were made by the Company during the period for charitable purposes (1998: £6,157).

Taxation Status

The Company is not a close company within the definition of Section 414 of the Income and Corporation Taxes Act 1988 and there has been no change in this respect since the end of the financial period.

Payment Record

It is the policy of the company to establish terms of payment with suppliers when agreeing the terms of business transactions. The aim is to despatch cheques on the due date or, where other means of payment are adopted, to deliver funds to suppliers as if payment had been made by cheque.

The Company had 48 days of purchases outstanding at 3 April 1999 (1998: 51 days).

EMU and Year 2000

The Company is able to transact in euros with customers and suppliers.

The Company recognises the significance of the risks arising from the Year 2000 date change and is carrying out a comprehensive programme with a view to renovating or replacing essential systems and equipment.

A Manager with responsibility for Year 2000 compliance within the Company has been appointed and a system to ensure consistent methodology and management of Year 2000 compliance within the wider British Steel Group, of which the Company is a member, has been adopted.

The overall cost of the Year 2000 project in British Steel Engineering Steels Ltd was £4.5m in the year to 3 April 1999 (1998:nil).

While every reasonable effort is in place to overcome the Year 2000 problem, the scale of complexity makes a complete assurance that everything will be compliant difficult to achieve. It cannot be certain that Year 2000 issues will not have a significant impact on the Company's operations or its financial condition, particularly if there are unforeseen compliance problems with the systems operated by the Company's customers, suppliers, vendors or sub-contractors.

Auditors

PricewaterhouseCoopers will remain in office as the Company's auditors in accordance with Section 386 of the Companies Act 1985.

By order of the Board



A L Scandrett,
Company Secretary

24 June 1999

AUDITORS' REPORT

to the members of British Steel Engineering Steels Limited

We have audited the financial statements on pages 6 to 18 which have been prepared under the historical cost convention and the accounting policies set out on page 8 to 10.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the Annual Report, including as described on page 1 the financial statements. Our responsibilities, as independent auditors, are established by statute, the Auditing Practices Board and our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, 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 is not disclosed.

We read the other information contained in the Annual Report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

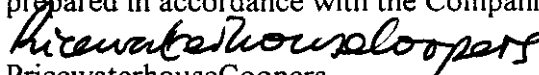
Basis of audit opinion

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 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 financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion, the financial statements give a true and fair view of the state of the company's affairs at 3 April 1999 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.


PricewaterhouseCoopers
Chartered Accountants and Registered Auditors
Sheffield

30 June 1999

BRITISH STEEL ENGINEERING STEELS LIMITED

Profit and loss account for the year ended 3 APRIL 1999

	Note	1999 £m	1998 £m
Turnover			
Continuing operations		428.8	501.8
Discontinued operations		-	7.8
	2	428.8	509.6
Operating profit			
Continuing operations		5.6	8.0
Discontinued operations		-	(0.1)
	3	5.6	7.9
Non operating items - Continuing operations			
Profit/(loss) on sale of fixed assets		-	0.3
Profits less losses on closure/sale of businesses	5	-	3.6
Profit on ordinary activities before interest		5.6	11.8
Interest receivable less payable	6	0.1	8.8
Profit on ordinary activities before taxation		5.7	20.6
Taxation on profit on ordinary activities	7	(3.5)	(9.3)
Profit on ordinary activities after taxation		2.2	11.3
Dividends	8	-	(15.3)
Profit/(loss) retained for the year		2.2	(4.0)

STATEMENT OF MOVEMENTS IN PROFIT AND LOSS ACCOUNT for the year ended 3 April 1999

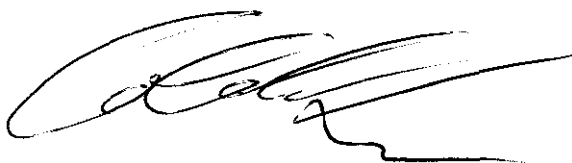
	Note	Mar 1999 £m	Mar 1998 £m
At 28 March 1998		58.1	62.1
Profit for the period		2.2	11.3
Dividends	8	-	(15.3)
At 3 April 1999		60.3	58.1

The company has no recognised gains or losses for the period other than as disclosed in the above profit and loss account.

BRITISH STEEL ENGINEERING STEELS LIMITED
Balance Sheet as at 3 April 1999

	Note	1999 £m	1998 £m
FIXED ASSETS			
Tangible assets	9	181.7	198.0
CURRENT ASSETS			
Stocks	10	44.5	55.9
Debtors - amounts falling due:			
- within one year	11	391.4	392.1
- after more than one year	11	9.3	3.1
Cash at bank and in hand		10.3	3.9
		455.5	455.0
Creditors - amounts falling due:			
- within one year	12	(97.3)	(113.0)
NET CURRENT ASSETS		358.2	342.0
TOTAL ASSETS LESS CURRENT LIABILITIES		539.9	540.0
Creditors - amounts falling due:			
- after more than one year	13	-	(2.6)
Provisions for liabilities & charges	14	(17.5)	(17.2)
		522.4	520.2
CAPITAL AND RESERVES			
Called up share capital	15	462.1	462.1
Profit and loss account	16	60.3	58.1
Shareholder's funds	17	522.4	520.2
Analysis of shareholder's funds:			
Equity		487.4	485.2
Non-equity		35.0	35.0
		522.4	520.2

The financial statements on pages 6 to 18 were approved by the Board of Directors on 24 June 1999 and were signed on its behalf by:



Notes to the financial statements

1. Principal Accounting Policies

The financial statements have been prepared in accordance with applicable Accounting Standards in the United Kingdom. A summary of the more important accounting policies, which have been applied consistently, is set out below.

(a) Basis of accounting

The financial statements have been prepared under the historical cost convention.

(b) Foreign exchange

Assets and liabilities expressed in foreign currencies are stated at the exchange rates ruling at the balance sheet date or, where appropriate, at the rates of matching forward contracts or transactions. The exchange differences arising are reflected in the profit and loss account.

The sterling value of export sales orders is protected by means of forward exchange contracts. Profits or losses arising from these contracts are accounted for in the financial period in which the related sales revenue arise.

(c) Turnover

Turnover, all of which is derived from the United Kingdom, represents the invoiced value of goods and services charged to external customers excluding value added taxes.

(d) Tangible fixed assets

The cost of fixed assets initially acquired is based on the fair value of those assets at the date of acquisition. Subsequent additions are included at cost, including any incidental expenses of acquisition.

Included in tangible fixed assets are loose plant and tools which are stated at cost less amounts written off related to their expected useful lives and estimated scrap value; and also spares, against which provisions are made where necessary to cover slow moving and obsolescent items.

Depreciation is calculated to write off the cost of fixed assets on a straight line basis over the expected remaining useful economic lives of the assets concerned. The principal asset lives used for this purpose are:

Freehold buildings	25 to 50 years
Leasehold land and buildings:	
Industrial	25 years
Office	50 years
(or at rates based on the life of the lease where shorter than period stated)	
General plant and machinery	10 to 15 years
Steel plant, presses and hammers	25 years

No depreciation is charged on freehold land or capital work in progress. In general, depreciation is not charged on fixed assets purchased during the year but a full year's depreciation is charged on fixed assets sold in the year. For significant individual projects, depreciation is charged from the date of commissioning.

(e) *Finance and operating leases*

Assets subject to finance leases are recorded as fixed assets and are depreciated over the useful life of the asset or the term of the lease, if shorter. The capital element of future rentals is treated as a liability and the interest element is charged to the profit and loss account over the primary lease period. Rentals paid in respect of operating leases are charged to the profit and loss account as incurred.

(f) *Government grants*

Government grants received in respect of specific capital expenditure are treated as deferred income which is then credited to the profit and loss account over the related asset's life. Other revenue grants are credited to the profit and loss account when received.

(g) *Research and development expenditure*

Research and development expenditure is written off as incurred.

(h) *Stocks*

Stocks of raw materials are valued at cost or, if they are to be realised without processing, at the lower of cost and net realisable value. Process stocks and stores are valued at the lower of cost and estimated net realisable value after appropriate provisions for slow-moving or obsolete stock. In general, cost is determined on a first-in-first-out basis. Cost of process stocks comprises direct expenditure, including production overheads, calculated on the basis of a normal level of activity.

(i) *Deferred Taxation*

Provision is made for deferred taxation only to the extent that there is a reasonable probability that such tax will become payable in the foreseeable future.

(j) *Post Retirement Benefits*

The Company is a member of Group defined benefit pension schemes covering a substantial majority of its employees. The assets of the schemes are independent of the Company's and the Group's finances. The schemes are funded by contributions partly from the employees and partly from the Company at rates determined by independent actuaries.

The cost of providing retirement pensions and related benefits is charged to the profit and loss account, over the periods benefiting from the employees' services. Independent actuarial valuations on a going concern basis are carried out on a triennial basis and any surpluses or deficits disclosed are spread evenly from the date of valuation over the remaining service lives of the Scheme members. Details of the latest actuarial valuation of the principal Group scheme as at 6th April 1996 are disclosed in the accounts of British Steel Engineering Steels Holdings Limited.

The cost of providing other post retirement benefits is recognised on a basis similar to that adopted for pensions.

(k) *Cash flow statement*

A cash flow statement has not been prepared since the Company is a wholly owned subsidiary of British Steel plc, which company presents a consolidated cash flow statement in its financial statements in accordance with Financial Reporting Standard Number 1 (revised).

(l) *Goodwill*

Goodwill arising on acquisitions, being the excess of the cost of acquisition over the fair value of the net assets acquired, is written off against reserves in the year in which it arises.

(m) *Related Party Transactions*

As the Company is a wholly owned subsidiary of British Steel plc, a Company incorporated in England, it has not disclosed details of transactions with other Group Companies by virtue of the exemption contained in paragraph 3, Financial Reporting Standard Number 8.

2. Turnover

The geographical markets supplied by the Company are:

	1999	1998
	£m	£m
United Kingdom	257.8	321.2
Continental Europe	118.5	124.6
North America	49.3	57.1
Rest of World	3.2	6.7
	<u>428.8</u>	<u>509.6</u>

The directors consider that the Company operates in one industrial segment, namely steel.

3. Operating Profit

	1999	1998
	£m	£m
Turnover	428.8	509.6
Change in process stock	(13.8)	(4.8)
Other operating income	0.2	0.5
Raw materials /consumables	(199.1)	(260.1)
Other external charges	(70.0)	(78.3)
Staff costs (see note 4)	(94.9)	(97.5)
Depreciation normal and accelerated	(20.7)	(24.6)
Other operating charges	(24.9)	(36.9)
Operating profit	<u>5.6</u>	<u>7.9</u>
Operating profit is stated after charging/(crediting):		

	1999	1998
	£m	£m
Reorganisation and restructuring costs	-	0.7
Hire of plant and machinery	1.7	1.5
Research and development	1.7	1.4
Auditors remuneration	0.1	0.1

4. Directors' and Employees' Remuneration

The emoluments of the highest paid director during the year, excluding pension contributions, are set out below. Salaries of executive directors include supplements following the restrictions imposed on maximum pension payments under the Finance Act 1989:

	1999 £000	1998 £000
Highest paid director		
Aggregate emoluments	156	174
Defined benefit pension schemes:		
Accrued pension at end of year	84	77
Accrued lump sum at end of year	-	-
	Year to April 1999	Year to Mar 1998
	£000	£000
Directors' emoluments for management services:		
Aggregate emoluments	244	246

Retirement benefits are accruing to 1 director (1998: 1 director) under the Company's defined benefits schemes.

The emoluments of Mr. Homer, Mr. Rennocks and Mr. Cain were paid by the ultimate holding company. It is not possible to make an accurate apportionment of their emoluments in respect of this subsidiary. Accordingly the above details include no emoluments in respect of these directors.

Employment costs of the Company, including executive directors, were as follows:

	1999 £m	1998 £m
Aggregate gross wages and salaries	82.2	85.2
Employer's national insurance contributions	6.3	6.1
Employer's pension costs under the Company pension scheme	6.4	6.2
	94.9	97.5

The average number of persons, including executive directors, employed by the Company during the year was 3435 (1998: 3549)

5. **Profits less losses on sale or closure of businesses**

In January 1997 the Company sold its Forgings business. The movements on net assets arising from this disposal are as follows:

	1999 £m	1998 £m
Net assets less liabilities disposed of	-	3.6
Reversal of goodwill write off	-	-
Profit on disposal	-	3.6

An amount of £3.6m was credited to the profit and loss account in the previous year. This amount represented the reduction in the provision for pension liabilities resulting from the disposal of the Forgings business. This amount was estimated by the scheme's actuary and is made up of £6.9m in respect of the capitalised value of the variation credit relating to transferring the Forgings business' members, less £3.3m being the estimated scheme surplus transferred in respect of the Forgings business' members.

6. **Interest Receivable less Payable**

	1999 £m	1998 £m
Interest from Group Undertakings	-	8.7
Other	0.1	0.1
	0.1	8.8

7. **Taxation**

	1999 £m	1998 £m
On profit for the period:		
United Kingdom corporation tax charge at 31% (1998: 31%)	(2.5)	(11.6)
Deferred taxation	-	4.5
Prior year (under)/over provision	(1.0)	(2.2)
	(3.5)	(9.3)

8. **Dividends**

	1999 £m	1998 £m
Dividends on equity shares:		
Ordinary shares:		
Interim paid of nil pence per share (1998: 3.1684p)	-	10.6
Capped participation shares:		
Interim paid of nil pence per share (1998: 3.1684p)	-	2.9
Total dividends on equity shares	-	13.5
Dividends on non-equity shares:		
5% non-cumulative redeemable convertible preference shares:		
nil pence per share paid (1998: 5p)	-	1.8
	-	15.3

9. **Tangible Fixed Assets**

	Freehold Land & Buildings	Plant and Machinery Owned	Leased	Capital Work in Progress	Total
	£m	£m	£m	£m	£m
Cost at 28 March 1998	51.5	327.4	0.1	6.1	385.1
Additions	0.1	4.0	-	0.3	4.4
Disposals	(2.9)	(4.9)	(0.1)	-	(7.9)
Reclassifications	-	3.7	-	(4.5)	(0.8)
Cost at 3 April 1999	48.7	330.2	-	1.9	380.8
Depreciation at 28 March 1998	(22.9)	(182.4)	(0.1)	-	(205.4)
Charge for period	(1.9)	(18.8)	-	-	(20.7)
Disposals	2.7	3.6	0.1	-	6.4
Reclassifications	-	0.4	-	-	0.4
Depreciation at 3 April 1999	(22.1)	(197.2)	-	-	(219.3)
Net book value at 3 April 1999	26.6	133.0	-	1.9	161.5
Net book value of loose plant, tools and spares					20.2
					181.7

Net book value at 28 March 1998	179.7
Net book value of loose plant, tools and spares	18.3
Net book value of tangible fixed assets at 28 March 1998	<u>198.0</u>

(i) The net book value of loose plant, tools and spares comprises:

	1999 £m	1998 £m
Cost	37.7	36.1
Provisions	(17.5)	(17.8)
	<u>20.2</u>	<u>18.3</u>

10. **Stocks**

	1999 £m	1998 £m
Raw materials	13.1	10.7
Process stocks	29.0	42.3
Finished goods	2.4	2.9
	<u>44.5</u>	<u>55.9</u>

11. **Debtors**

	1999 £m	1998 £m
Amounts falling due within one year:		
Trade debtors	62.2	91.2
Other debtors	4.6	2.1
Amounts owed by group undertakings	324.6	298.8
	<u>391.4</u>	<u>392.1</u>
Amounts falling due after more than one year:		
Other debtors	9.3	3.1

12. **Creditors - amounts falling due within one year**

	1999 £m	1998 £m
Bank loans and overdrafts	4.5	-
Trade creditors and bills of exchange payable	54.0	61.7
Amounts owed to fellow group undertakings	19.7	21.2
Corporation tax	1.8	10.9
Other taxation and social security	0.6	0.6
Other creditors	16.7	18.6
	<u>97.3</u>	<u>113.0</u>

13. **Creditors - Amounts Falling due After More than One Year**

	1999 £m	1998 £m
Other creditors	-	2.6

14. **Provisions for Liabilities and Charges**

	Deferred Taxation £m	Post Retirement Benefits £m	Other £m	Total £m
At 28 March 1998	-	10.3	6.9	17.2
Profit and loss account	-	0.1	2.4	2.5
Transfers in	-	-	1.1	1.1
Utilised in the period	-	(0.1)	(3.2)	(3.3)
At 3 April 1999	-	10.3	7.2	17.5

Post retirement benefits include provisions other than pensions of £1.6 million (1998: £1.5 million) - see note 18.

Other liabilities and charges include rationalisation and redundancy provisions.

The deferred tax liability provided for and the full potential deferred tax liability of the Company at 3 April 1999 can be summarised as follows:

	Provided for		Full potential liability	
	1999 £m	1998 £m	1999 £m	1998 £m
Accelerated capital allowances	4.0	-	32.5	39.1
Other timing differences	(4.0)	-	(4.7)	(8.0)
	-	-	27.8	31.1

15. **Called up Share Capital**

	Authorised 1999 & 1998 £m	Issued and Fully Paid 1999 & 1998 £m
Ordinary £1 shares	400.0	334.0
Capped participation shares of £1 each	100.0	93.1
5% non-cumulative redeemable convertible preference shares of £1 each	35.0	35.0
	535.0	462.1

The capped participation shares enjoy the same rights as ordinary shares subject to a maximum dividend distribution of £1 per share in any financial year.

In any year, preference shares can be redeemed up to a maximum of one third of the dividends paid on the ordinary and capped participation shares. Providing the relevant conditions are met, a 5% non-cumulative dividend is payable in priority to other dividends and the preference shares can also participate equally with the other shares in any excess of dividends declared over 5%.

Under certain circumstances, the capped participation shares can be converted into ordinary shares and the preference shares can be converted into ordinary or capped participation shares.

16. **Profit and Loss Account**

At 3 April 1999, cumulative goodwill written off directly to reserves amounted to £40.4 million (1998: £40.4 million).

17. **Reconciliation of Movement in Shareholder's Funds**

	1999	1998
	£m	£m
Profit for the financial year	2.2	11.3
Dividends	-	(15.3)
Opening shareholder's funds	520.2	524.2
Closing shareholder's funds	522.4	520.2

18. **Post Retirement Benefits**

As stated in note 1(j) the Company is a member of group defined pension schemes covering a substantial majority of its employees. Details of the latest valuation of the schemes as at 6th April 1996 are disclosed in the accounts of British Steel Engineering Steels Holdings Limited.

The Company operates a retirement plan which provides certain employees with post retirement healthcare benefits. In accordance with UITF 6 - "accounting for post retirement benefits other than pensions" issued by the Accounting Standards Board - the liability for providing these benefits is now recognised on an actuarial basis and included in post retirement and other provisions disclosed in note 14. The principal actuarial assumptions are that medical costs will initially increase by 8% per annum falling to 6.5% over ten years with a discount rate of 9%.

19. **Financial Commitments**

	1999 £m	1998 £m
Capital Expenditure:		
- Sanctioned and contracted for	2.9	0.5

The minimum payments which the Company is committed to make in the next financial year under operating leases are as follows:

	Plant and Equipment	
	1999 £m	1998 £m
Leases which expire:		
Within one year	0.1	0.1
Two to five years	0.5	0.4
	0.6	0.5

The Company has entered into forward exchange contract commitments in the normal course of business.

20. **Contingent Liabilities**

There are no contingent liabilities (1998 : nil) for the Company comprising guarantees given and bills discounted in the normal course of business .

21. **Ultimate Parent Undertaking**

The Directors regard British Steel plc, a company registered in England and Wales, as the Company's ultimate parent undertaking and controlling party. The consolidated financial statements of British Steel plc are available to the public and may be obtained from British Steel plc, 15 Marylebone Road, London, NW1 5JD.