

MEMORANDUM ON
DRAGON DATA LIMITED



Peat, Marwick, Mitchell & Co

National Westminster Bank Building,
113 Bute Street, Cardiff, CF1 6TD
Telephone: Cardiff (0222) 32245
Telex: 497987
Telegrams: VERITATEM CARDIFF

Resident Partners:

P. C. Westwood, D. P. L. Davies, R. T. Parkinson, A. P. Embiricos, B. G. Mitchell

Our Ref.

Your Ref.

PRIVATE AND CONFIDENTIAL

A. Sutton Esq.,
Welsh Development Agency,
Treforest Industrial Estate,
Treforest,
Glam.

16th October, 1982

Dear Sir,

Dragon Data Limited ("Dragon")

Following your verbal instructions received on 12th October, 1982, we have now completed our review of the matters raised by yourself in relation to the above company and report as follows:-

A. BASIS OF INFORMATION

The information in this report has been obtained from:-

- i) Management Accounts of "Dragon" for the 36 weeks ended 11th September, 1982, together with the draft Management Accounts for the 4 weeks ended 9th October, 1982.
- ii) Forecasts prepared by "Dragon" for the 12 weeks ended 31st December, 1982.
- iii) Sales forecast for the year ended 31st December, 1983.
- iv) Discussions with A.J. Clarke (Managing Director), R. Wadham (Sales Director) and D. Williams (Technical Director).
- v) The report of Deloitte, Haskins & Sells dated 21st September, 1982 addressed to Prutec Limited and discussions with James Shoemith of Deloitte's.

The information supplied to us has not been audited but nothing has come to light during our work which would give rise to any concern as to its accuracy. The factual content of this report has been confirmed by Mr. Clarke.

A. P. L. James, M. C. Llewellyn, T. D. Snowden, A. Tonkin, B. Jones
J. P. Grenside, CBE, G. C. Peat, J. K. Mather, A. W. Howitt, G. W. Dunkerley, O. H. Thompson, P. J. Butler, CBE, P. G. Corbett, A. J. Hardcastle,
T. W. Allen, C. N. Smith, CBE, J. R. Adcock, G. D. Bowic, J. B. Barton, G. T. E. Parsons, C. G. Sneath, J. White, H. W. E. Thompson,
R. V. J. Chadder, D. B. Vaughan, D. E. A. Morris, R. J. G. White, W. M. T. Fowic, C. M. Sharman, OBE.

The address, for the purposes of section 29, Companies Act 1981, is 1 Puddle Dock, Blackfriars, London, EC4V 3PD

B. BACKGROUND AND PRODUCTS

i) Background

"Dragon", which is currently trading as a division of The Mettoy Co. plc ("Mettoy"), developed in association with Patcentre a microcomputer which was launched in August 1982. Favourable press comment has resulted in a successful launch and currently the Dragon 32 has orders which exceed the available production capacity of 2,000 units per week for the remainder of this year.

The main board for the computer is assembled by Race Electronics, with the final assembly and testing being carried out by "Dragon" in the "Mettoy" premises in Swansea.

Our understanding is that the trading assets and business of "Dragon" are to be sold to a new company formed for the purpose which is referred to hereinafter as "Dragon 1982".

ii) Products

The current products of "Dragon" are as follows:-

- a) Dragon 32 - Microcomputer with 32K memory, currently being sold to certain major retailers (Boots, Dixons, Curry's), and specialist computer shops. The unit retails at £200 (including VAT) having been sold to the retailers by "Dragon" for approximately £120 per unit.
- b) Peripheral products - Full use of the Dragon 32 is obtained by utilising the various ancillary products such as joysticks (for use in computer games), cartridges (containing the software for the games) and cassettes (containing various programmes for loading into the unit). These products have not been available in quantity until October 1982.

C. OUTSTANDING ORDERS AT 11TH OCTOBER, 1982

The following information has been obtained from the Sales Director and represent written orders received up to 11th October, 1982:-

<u>Customer/Period</u>	<u>No. of Units</u>
Despatched	12,165
Orders booked not yet despatched	16,330
	<hr/>
	28,495
Orders received yet to be booked	
Spectrum	1,000
Databank	1,000
Curry's	1,000
Menzies	1,000
Norcom	2,000
Export	3,500
Other customers	6,048
	<hr/>
	44,043
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It should be noted that "Dragon" have informed their customers that there is little point in placing orders until the New Year as they are not in a position to satisfy the existing orders outstanding to date.

Orders outstanding for peripheral products include requests for in excess of 8,000 cartridges which are in the process of being made.

D. RETURNS FROM CUSTOMERS

The 200 returns from the first 5,500 Units despatched, represents a return rate of 3.6% which at first sight appears high. However, we have discussed this aspect with the Technical Director and he has given the following reasons for the returns:-

- i) Motorola sound chip - this chip has been self destructing in certain instances when the "Dragon" is being used in association with certain makes of Taiwanese tape recorders which suffer from power surges. The problem has been overcome by incorporating a small resistor which reduces any surge in power input. No further problems are now expected to occur.
- ii) Motorola SAM chip - early supplies of this important chip contained a higher than expected failure rate. The problem has been overcome by inserting the chip onto a socket for easy replacement and also improving the machine language testing cartridge which will result in any faults being discovered at the factory rather than by the customer.

Further improvements in quality will be obtained in 1983 by the purchase of a computerised test package ("ATE") and it is expected that the return rate should stabilise at approximately ½% of sales.

E. FIXED ASSETS

The following comprises a list of the fixed assets that will be transferred from "Mettoy" to "Dragon" and are available for sale to "Dragon 1982":-

	£'000
Data General Computer	32
8 Sony Televisions	2
Soak Test Equipment	21
Motorola Exorcisers	7
Other equipment	3
	<hr/>
Corgi Engineering - Tooling for mould re casing and fixing plate	65
	48
	<hr/>
Less: Depreciation	113
	8
	<hr/>
	105
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The Soak Test Equipment and the Mould Tooling are assets constructed by "Mettoy" and its subsidiaries. These have been capitalised at the cost of materials and labour with a reasonable addition for overheads. This cost has not been verified by reference to market value.

From discussions with the Managing Director, we understand that none of the above assets are subject to any reservation of title in favour of third parties.

We must point out that these assets obviously have a very low value as security for your proposed loan.

In addition to the above assets which will be taken over by "Dragon 1982", we understand that the following additional capital expenditure will be required in the early part of 1983.

	£'000
Automatic Test Equipment ("ATE")	250
Tape Duplicating Machine	5
Cartridge Duplicators	7
Sundry Test Equipment	30
Furniture and Benches	50
	<hr/>
	342
	<hr/> <hr/>

The major item of equipment is the "ATE" which is a computerised test package that will enable "Dragon" to automatically test boards returned from the assemblers and to identify specific fault areas. You might consider the possibility of deferring subscription of some part of your loan monies to enable you to secure it on the above assets.

F. FACTORY LOCATION AND ASSISTANCE AVAILABILITY

The factors relevant to the availability of government assistance have been discussed with Mr. Clarke, particularly those relating to factory location. Whilst Mr. Clarke appreciates fully the advantages to be obtained from locating in a Development Area, he maintains he has to take account also of such factors as mobility of labour and the suitability to "Dragon 1982" of the premises available in the various areas. The limited provision of office accommodation in standard Agency units is not sufficient for the new company's purposes but Mr. Clarke believes that facilities which are expected to become available at Hendy could be satisfactory. It appears also at the present time Hendy would be the most satisfactory location for the majority of the personnel to be involved in the transfer.

Overall, it is suggested that value of assistance likely to be foregone by locating in an intermediate area rather than a development area is unlikely to be significant in relation to the overall profitability of the project having regard to the anticipated level of capital expenditure.

G. EMPLOYEES CONTRACTS

It is intended that up to forty personnel will transfer from "Mettoy" to "Dragon" and subsequently to "Dragon 1982". Several of these personnel have extended service with "Mettoy" and the new company will be taking over liability for their accrued employment rights. In an ongoing situation this is probably of relevance only in relation to accrued pension rights and it is understood that the new company is to receive a transfer of benefits from the existing "Mettoy" scheme, the Trustees of which are the Prudential. It is considered important that an investor in "Dragon 1982" should be satisfied that the funds transferred by the "Mettoy" Trustees are fully adequate to fund both existing and future liabilities.

H. ROYALTY AGREEMENTS

The various royalty agreements held by the Company are with one exception in the name of "Dragon". The software agreement with Microsoft is held in the name of "Mettoy". We have discussed with the Sales Director the subject of transferring these agreements to "Dragon 1982" and he has informed us that he believes there will be no problem with the transfer of any of the agreements. In particular, we discussed the Microsoft agreement and he informed us that Microsoft would willingly transfer as the agreement was really with A. Clarke and himself rather than "Mettoy". Nevertheless, it is important that this matter is adequately covered in the legal documentation to obviate any possibility of losing the benefit of the royalty already paid by "Mettoy" to Microsoft (£50,000).

I. TAXATION TREATMENT OF "KNOW-HOW"

Any agreement for the acquisition of the business of "Dragon" should make it clear that any amount paid over and above the asset valuation is a payment for the technical "Know-how" developed and owned by "Mettoy". Any amount paid for such "Know-how" can be amortised for tax purposes over a period of 6 years in equal annual instalments.

The acquisition of the "Know-how" will be associated with the acquisition of a trade or a part of a trade. The purchaser and vendor should jointly elect, under Section 386(3) Income and Corporation Taxes Act 1970, that the amount is not treated as a payment for "Goodwill" and such an election should be provided for in any purchase agreement.

J. FUTURE DEVELOPMENTS

a) Products

The current sales of "Dragon" is limited to the Dragon 32 microcomputer, together with the cartridges, cassettes and joysticks. We have discussed with the Technical and Sales Directors the future product developments to be expected in 1983. These can be summarised as follows:-

- i) Dragon 64 - This is an improved version of the Dragon 32 which will incorporate 64K memory compared with the 32K memory of the current microcomputer. Production is expected to commence in January 1983 and will be sold to the retailers at a premium of approximately £90 per unit over the Dragon 32 against an increased material cost including royalties of £40.
- ii) Disk Controller/Drive - This system will be compatible with the Dragon 32/64 and will provide a disk facility to give the microcomputers a new range of applications with access to an enlarged data base. The new disk units will enable alternative computer languages to be used and especially Cobal for business use. Sales of the Disk units are expected to commence in March 1983.
- iii) Educational Unit - This microcomputer is being designed specifically for educational purposes for sale to schools and colleges. It comprises a Dragon 32/64, tape recorder and monitor contained in one casing. It is proposed that this machine will be sold direct to the end user at a price of £450 per unit.
- iv) Dragon Business Machine - This unit is being designed to sell in the small business use market for between £300 and £1,200 according to configuration. It will be a modular machine which in its complete form will comprise processor, 2 disk units, monitor and small printer. It is an 8 bit unit which will compete with the 16 bit unit produced by IBM which retails at £2,500 - £3,000. It is expected to be launched in September 1983 and is currently being developed by Patcentre at a cost of £100,000. This amount has been written off in the forecasts but no credit has been taken for any sales in 1983.
- v) Dragon "Future" Home Unit - This machine is to be developed during 1983 for launch in early 1984. It will replace over a period of time the Dragon 32 and should incorporate the facility to link with Prestel and other T.V. systems together with a limited "voice" capacity.

Whilst the management team have no track record of any length to support their ability to bring such a wide range of product developments on stream in such a limited time scale, their resounding success in launching the Dragon 32 suggests that they are more than capable of achieving their objective. Moreover, in relation to the size of the profit forecasts referred to later, a failure to achieve the launch date on any one product is unlikely to have a material effect.

b) Market

We have discussed the future market prospects with the Sales Director and he informs us, whilst Dragon is in the position of demand exceeding supply at present, he does feel that Japanese competition in the latter half of 1983 could force "Dragon 1982" to institute a reduction in the price of the Dragon 32/64. We have reduced the sale price of these units in our forecast by £15 per unit to allow for this market pressure.

The Sales Director feels that the Dragon 32/64 will be in demand throughout 1983 but expects reduced sales in the United Kingdom during the first half of 1984. The Dragon "Future" Home Microcomputer will then be in production and will fill any gap in the market left by the Dragon 32/64. Sales of the Dragon 32/64 will continue in Europe until at least December 1984, before being phased out.

The indications at present are that the Education Unit will sell very well during 1983/4 with strong interest being shown by educational establishments. The Sales Director believes that the "high" forecast sales of 5,000 units is very much a conservative estimate.

c) Production

At present all board "stuffing" is carried out by Race Electronics with the final assembly and testing being the responsibility of "Dragon". The production capacity of Race is approximately 2,000 boards per week and therefore "Dragon" have secured another source of supply, Control Data in Cheshire, who will come on stream by December 1982. This will enable the production of "Dragon" to be doubled by the New Year. It is further hoped that with the purchase of the new A.T.E. machine (required for testing completed boards), "Dragon" itself will be able to produce boards by March 1983 at a rate of 2,000 per week. This development will result in "Dragon" having more than one source of supply for its boards and also give the Company an in-house production capability using its existing expertise. This will obviously give "Dragon" a degree of flexibility not enjoyed by other United Kingdom manufacturers such as Sinclair and Acorn and is seen as a strength by Mr. Clarke and Mr. Williams the Technical Director.

K. 1982 TRADING RESULTS

The following results for the period have been extracted from the Management Accounts of "Dragon" for the 40 weeks ended 9th October, 1982:-

	<u>Management Accounts</u>		<u>Forecast</u>
	36 weeks ended 11th September, 1982	4 weeks ended 9th October, 1982	12 weeks ended 31st December, 1982
	£'000	£'000	£'000
Sales	817	820	3,050
Gross profit	261	295	1,090
Overheads	556	100	300
Contingency provision	-	-	140
	(295)	195	650

No provision has been made in the above results for any costs relating to the proposed move to a new factory site (estimated at £110,000), as the majority of such costs are of a capital nature and have been provided in the 1983 forecast.

The forecast for the 12 weeks to 31st December, 1982 appears to have been prepared with a requisite degree of conservatism and is dependent largely on the continued ability to achieve production levels of 2,000 units per week.

L. ASSETS TAKEN OVER BY DRAGON 1982

During our recent meeting we understood that "Dragon 1982" would purchase gross assets from Mettoy at book value paying an additional £750,000 for the purchase of "Know-how". After discussions with the Managing Director it has become clear that he proposes that the debtors and creditors of "Dragon" should be purchased in order to ensure prompt payment to the suppliers and to protect "Dragon 82" from any embarrassment that may be caused by Mettoy's current financial position. This method of purchase will have the additional advantage of ensuring that suppliers are paid and will therefore eliminate the possibility of claims under reservation of title clauses.

The Managing Director anticipates the transaction being completed on 21st October, 1982 and the forecast balance sheet of "Dragon" at that date is as follows:-

	£'000	£'000
Fixed assets		105
Stock	625	
Debtors	550	
	1,175	
Creditors	1,125	
Net current assets		50
Net assets		155

The estimated balance sheet of "Dragon 82" at the same date assuming an injection of £2,400,000 by the proposed investors, will be as follows:-

	£'000	£'000
Assets employed		
Fixed assets		105
Purchased "Know-how"		750
Stock	625	
Debtors	550	
Cash at bank	1,495	
	<hr/>	
	2,670	
Creditors	1,125	
	<hr/>	
		1,545
		<hr/>
		2,400
		<hr/> <hr/>
Financed by		
Share capital		
WDA (29%)	435	
Others (71%)	1,065	
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		1,500
Loans		
WDA (29%)	261	
Others (71%)	639	
	<hr/>	
		900
		<hr/>
		2,400
		<hr/> <hr/>

M. PROPOSED COST SAVINGS ON DRAGON 32

The current prime cost of production of the "Dragon" microcomputer is £77 per unit (excluding royalty payments of £4 per unit). Deloitte, Haskins and Sells have verified these costs and we have discussed their work with James Shoemith (Deloitte's Management Consultancy Firm). Based on our discussions we consider that the work undertaken was comprehensive and have no reason to suppose that the figure of £77 is not accurately stated. We have discussed with the Technical Director the various areas of cost savings that are immediately available to "Dragon". These are summarised below.

	<u>Saving per Unit</u>
	£
Volume savings	
Motorola SAM chip	1.50
Keyboard	1.45
Other components (minumum)	2.50
Technical savings	
Modified power modulator	2.05
Partial failure chips (64K)	3.50
Cartridge connector	1.20
	<hr/>
	£12.20
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In the forecasts shown in Appendices A - D, we have reduced the cost of sales per unit from £77 to £68 giving a cost saving of £9 per unit compared with Dragon's estimated immediate cost savings of £12 per unit. In addition to the above we are informed by the Managing Director that an additional £8 per unit can be saved by the middle of 1983 in part by resourcing Board "Stuffing" including an element of manufacture in house. We have taken no cognizance of this latter saving in our forecasts.

N. 1983 PROFIT AND LOSS ACCOUNTS AND CASH FLOW FORECASTS

a) Assumptions

The following assumptions have been used in arriving at the forecasts shown in Appendices A - D:-

- i) The present activity of "Dragon" will be transferred to a separate factory unit at the beginning of 1983.
- ii) Sales of the "Dragon" computers will continue to be made to retailers rather than direct selling to the public. The sales price has been forecast at the following rates:-

	<u>January-June 1983</u>	<u>July-December 1983</u>
	£	£
Dragon 32	120	105
Dragon 64	155	140
Dragon 32 "Secam"	123	108
Dragon 64 "Secam"	158	143
Dragon 32 "NTSC"	110	110

The reduction in the sales price of the Dragon 32 and 64 in July 1983 is to allow for increased competition expected in the later half of 1983 from Japanese and United Kingdom producers.

- iii) No major problems will be experienced with the supply of components or in the assembly of the P.C.B.'s from outside contractors.

b) "High" forecast on sales of 164,500 Units

i) Sales

The forecast (Appendix A) of profit before tax of £11,290,000 has been based on the sales forecast prepared by "Dragon" which anticipates sales of 164,500 Units. The analysis of sales over the year is as follows:-

<u>Product</u>	<u>Units</u>	<u>Sale price per unit</u>
		£
Units		
Dragon 32	127,500	See Section N(a)
Dragon 64	32,000	See Section N(a)
Educational	5,000	450
	<u>164,500</u>	
Peripherals		
Disk Controllers	21,600	90
Disk Drives	23,600	150
Cartridges	350,000	11
Cassette Tapes	400,000	4
Cassette Leads	149,000	1
Joysticks (pairs)	116,000	11

The sales of peripheral products has been based on the number of computer units sold in the year and conservative estimates of the ratio of peripheral products to units experienced by other manufacturers.

No credit has been taken in the forecast for sales of the new Dragon Business Machine (See Section J) which is expected to be launched in September 1983.

ii) Cost of sales

The cost of sales of the Dragon 32 has been forecast at £68 per unit, together with the £4 per unit royalty payable to Microsoft for the software programs. This compares with the current cost of sales per unit of £77 excluding the royalty payment as referred to in Section G.

The Dragon 64 is anticipated to cost £88 per unit by "Dragon" and this cost has been used in the forecast.

The cost of sale of the various peripheral products has been estimated by "Dragon" and includes all royalties payable on the cartridges/cassettes.

iii) Overheads

Promotional and advertising costs have been included at £1 million on the instructions of Mr. Clarke. Salaries have been projected having regard to anticipated staffing requirements for each department of the business.

iv) Cash flow (Appendix B)

The cash flow forecast has been prepared from the profit and loss account shown in Appendix A. The opening cash at bank in "Dragon 1982" (£1,450,000) has been derived from the opening asset position shown in Section L. "Dragon 1982" is forecast to show a small bank overdraft of £79,600 in February 1983 due to a high requirement for working capital to fund its increasing sales/production. Cash balances after that date are expected to increase rapidly and cash at bank of £9,033,000 is forecast at 31st December, 1983 after repayment of £665,000 shareholders' loans.

c) "Low" forecast based on 97,500 Units

i) Sales

The forecast (Appendix C) of profit before tax of £6,137,000, has been based on a 40% reduction in sales of both units and peripheral equipment expected by "Dragon" in 1983. Sales prices are the same as that used in the "high" forecast.

ii) Cost of sales

Cost of sales of all products is the same as that used in the "high" forecast despite the lower volume of production. Certain overheads such as Advertising and Salaries have been reduced appropriately to take account of the reduction in sales.

iii) Cash flow (Appendix D)

No bank overdraft is forecast for the year due to a smaller requirement for working capital on lower sales/production. Cash at bank by 31st December, 1983 is forecast at £5,227,000.

O. SALE OF ASSETS BY METTOY

Subject to any clause to the contrary in the "Mettoy" articles, we believe that it is within the competence of the "Mettoy" Board to sell the assets of "Dragon" without the approval of the "Mettoy" members.

However, certain statutory and listing requirements may be relevant in this case and we set out below our preliminary thoughts on this aspect.

- a) Companies Act 1980 - Section 48. This section requires approval by the members of any material transaction with a Director or a company in which a Director holds more than 20% of the equity. In this case it is proposed that the interest of Mr. Clarke in "Dragon 1982" will be less than 2% and therefore we feel the Section is not applicable.

- b) Stock Exchange - Listing Agreement. The transaction does not appear to fall within the definition of a class 4 transaction which would require consultation with the Stock Exchange before completion as Mr. Clark's proposed interest in "Dragon 1982" is less than 10%. However, the transaction appears to fall within Class 2 requiring notification to the Exchange immediately after completion with a possible Press Announcement.
- c) Moreover, in view of the increase in the "Mettoy" share price on the strength of the success of the "Dragon 32" launch, we feel it is inconceivable that the sale should go ahead without the Stock Exchange being informed.

In addition to the formal situation outlined above, we cannot ignore the possibility that "Dragon 1982" may be held to be a connected party to "Mettoy" in which case there may be difficulty in "Dragon 1982" proving good title to assets acquired from "Mettoy" in the event of a liquidator being appointed to the latter company.

The best safeguard for "Dragon 1982", against the loss of its assets in such an event, appears to be to ensure, so far as practical, that the Directors of "Mettoy" take appropriate steps to satisfy themselves that they are not acting dishonestly or fraudulently in entering into the transaction. We consider that at the very least the "Mettoy" Board should satisfy itself on these matters by obtaining the necessary letters of comfort from independent advisors, for example the Company's auditors and merchant bankers, that in entering into the transaction they are not acting unreasonably having regard to all the circumstances prevailing at the time.

The particular circumstances we have in mind would be:-

- i) The inability of "Mettoy" to fund the working capital requirement of the "Dragon" project at the levels of activity now envisaged.
- ii) The speculative nature of the project which despite its success to date is still in its early stages with a single product which requires development to support its future acceptability.
- iii) The volatility of the market segment involved and the unknown impact of the envisaged entry of competition from the United States and Japan.
- iv) The fact that the business is dependent significantly on the continued commitment of the four executive directors who may be minded to take up other offers of employment should the "Dragon" project be jeopardised.
- v) Should the consequence of failure by "Mettoy" to complete the transaction lead to the appointment of a Receiver, this would result in the withdrawal of support by Motorola the supplier of unique components and the termination of the vital Microsoft agreement. Moreover, component stocks held by Race Electronics could be subject to a lien against amounts owing to Race rendering it extremely difficult if not impossible for a Receiver to continue the trade without disruption leading to loss of confidence in the market.

P. CONCLUSIONS

The launch of the Dragon 32 has been an undoubted success; moreover the initial indications are that the transition from development to the manufacturing and delivery of the product has also been successful. The product appears to be acceptable in quality to the end user with only two minor recurring faults presenting themselves both of which have been corrected in subsequent production. Orders have been received in volumes which significantly outstrip existing manufacturing capacity and which secure the sales required to underpin the profit projections for the remainder of 1982.

This indicates the strength of the management team involved in the project and it is essential for the continuing success of the venture that the team is kept together and adequately motivated. Enquiries are proceeding to secure a Financial Executive to join the team which will release Mr. Clarke of routine involvement in this area.

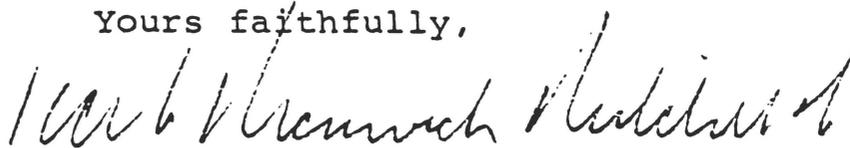
Apart from the vital importance of the people involved, the continuing success of the venture will depend largely on maintaining the present impetus in product design both in the development of a more complete range of hardware units and in the development of a comprehensive library of software. The management recognise this and have an ambitious programme of product introductions in varying stages of implementation for 1983. Whilst these are important for the long term development, their successful implementation on the planned launch dates is not necessarily vital to the achievement of currently forecast results for that year. It is extremely difficult to support forecasts for 1983 in the normally accepted manner as the project has no past track record on which to base comparisons and is operating in a volatile and rapidly developing market. Nevertheless, the success of the Dragon 32, with the significant unsatisfied demand for the product rolling forward to underpin the 1983 results must provide comfort that the return likely on the investment represented in the current proposals is very substantial.

This in itself points to the main problem in the proposed transaction, namely the propriety of the transaction for the Board of a listed company and their ability to demonstrate to their members, work force and creditors, (the latter possibly represented by a liquidator), that they were acting honestly in all the prevailing circumstances in completing the transaction. We consider that the Agency should obtain legal advice on the implications to them and to their investment in "Dragon 1982" of this aspect.

This report has been prepared for the exclusive use of your Agency in connection with the proposed investment in "Dragon 1982" jointly with Prutec Limited. The report is not to be distributed to any party other than Prutec Limited without our prior consent.

We are pleased to record that we were afforded every facility for the conduct of our enquiries. If you require any further information or assistance please let us know.

Yours faithfully,



APPENDIX A

"DRAGON 1982"

1983 FORECAST PROFIT AND LOSS ACCOUNT

BASED ON SALES OF 164,500 UNITS

	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>May</u>	<u>Jun</u>	<u>Jul-Dec</u>	<u>Total</u>
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
SALES	1,895.5	2,035.5	2,659.0	2,910.5	3,103.5	3,358.5	17,902.5	33,865.0
Discount	19.0	20.4	26.6	29.1	31.0	33.6	179.0	338.7
	<u>1,876.5</u>	<u>2,015.1</u>	<u>2,632.4</u>	<u>2,881.4</u>	<u>3,072.5</u>	<u>3,324.9</u>	<u>17,723.5</u>	<u>33,526.3</u>
DIRECT COSTS	1,086.2	1,161.8	1,471.3	1,615.8	1,712.8	1,833.1	10,169.6	19,050.6
GROSS MARGIN	<u>790.3</u>	<u>853.3</u>	<u>1,161.1</u>	<u>1,265.6</u>	<u>1,359.7</u>	<u>1,491.8</u>	<u>7,553.9</u>	<u>14,475.7</u>
OVERHEADS								
Salaries	39.4	40.4	46.8	46.8	48.8	48.8	292.8	563.8
Sundry	32.5	32.5	32.5	32.5	35.0	35.0	216.0	416.0
Property	10.0	10.0	10.0	11.0	10.0	10.0	65.0	126.0
Advertising	105.0	105.0	100.0	55.0	65.0	65.0	505.0	1,000.0
Depreciation	2.9	2.9	7.3	7.3	7.3	7.3	43.8	78.8
Additional salaries	10.0	10.0	20.0	20.0	20.0	20.0	120.0	220.0
Research expenditure	52.0	67.0	12.0	12.0	62.0	12.0	70.0	287.0
Amortisation of "Know-how"	38.1	39.9	41.4	45.9	45.9	46.5	235.8	493.5
	<u>289.9</u>	<u>307.7</u>	<u>270.0</u>	<u>230.5</u>	<u>294.0</u>	<u>244.6</u>	<u>1,548.4</u>	<u>3,185.1</u>
PROFIT BEFORE INTEREST	<u><u>500.4</u></u>	<u><u>545.6</u></u>	<u><u>891.1</u></u>	<u><u>1,035.1</u></u>	<u><u>1,065.7</u></u>	<u><u>1,247.2</u></u>	<u><u>6,005.5</u></u>	<u><u>11,290.6</u></u>

"DRAGON 1982"

1983 FORECAST CASH FLOW BASED ON SALES OF 164,500 UNITS

	<u>Oct-Dec</u>	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>May</u>	<u>Jun</u>	<u>Jul-Dec</u>	<u>Total</u>
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
PROFIT BEFORE INTEREST	490.0	500.4	545.6	891.1	1,035.1	1,065.7	1,247.2	6,005.5	11,780.6
Depreciation	7.0	2.9	2.9	7.3	7.3	7.3	7.3	43.8	85.8
Amortisation of "Know-how"	55.0	38.1	39.9	41.4	45.9	45.9	46.5	235.8	548.5
	<u>552.0</u>	<u>541.4</u>	<u>588.4</u>	<u>939.8</u>	<u>1,088.3</u>	<u>1,118.9</u>	<u>1,301.0</u>	<u>6,285.1</u>	<u>12,414.9</u>
Capital expenditure	80.0	272.0	-	-	-	-	-	80.0	432.0
Loan repayment	-	-	-	-	-	-	-	665.0	665.0
FUNDS GENERATED	<u>472.0</u>	<u>269.4</u>	<u>588.4</u>	<u>939.8</u>	<u>1,088.3</u>	<u>1,118.9</u>	<u>1,301.0</u>	<u>5,540.1</u>	<u>11,317.9</u>
WORKING CAPITAL									
Debtors	950.0	2,191.0	2,509.4	3,167.9	3,575.3	3,831.1	4,134.4	3,729.3	24,088.4
Stock	835.0	1,025.0	1,275.0	1,275.0	1,375.0	1,475.0	1,675.0	1,500.0	10,435.0
Creditors	(625.0)	(850.0)	(950.0)	(1,150.0)	(1,400.0)	(1,600.0)	(1,600.0)	(1,400.0)	(9,575.0)
	<u>1,160.0</u>	<u>2,366.0</u>	<u>2,834.4</u>	<u>3,292.9</u>	<u>3,550.3</u>	<u>3,706.1</u>	<u>4,209.4</u>	<u>3,829.3</u>	<u>24,948.4</u>
Working capital at beginning of period	50.0	1,160.0	2,366.0	2,834.4	3,292.9	3,550.3	3,706.1	4,209.4	21,169.1
(Increase)/decrease in working capital	<u>(1,110.0)</u>	<u>(1,206.0)</u>	<u>(468.4)</u>	<u>(458.5)</u>	<u>(257.4)</u>	<u>(155.8)</u>	<u>(503.3)</u>	<u>380.1</u>	<u>(3,779.3)</u>
Cash - inflow/ (outflow)	<u>(638.0)</u>	<u>(936.6)</u>	<u>120.0</u>	<u>481.3</u>	<u>830.9</u>	<u>963.1</u>	<u>797.7</u>	<u>5,920.2</u>	<u>7,538.6</u>
Cash at bank - Open	<u>1,495.0</u>	<u>857.0</u>	<u>(79.6)</u>	<u>40.4</u>	<u>521.7</u>	<u>1,352.6</u>	<u>2,315.7</u>	<u>3,113.4</u>	<u>1,495.0</u>
- Close	<u>857.0</u>	<u>(79.6)</u>	<u>40.4</u>	<u>521.7</u>	<u>1,352.6</u>	<u>2,315.7</u>	<u>3,113.4</u>	<u>9,033.6</u>	<u>9,033.6</u>

Note: VAT, an added cash flow benefit, has been ignored.

"DRAGON 1982"1983 FORECAST PROFIT AND LOSS ACCOUNTBASED ON SALES OF 97,500 UNITS

	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>May</u>	<u>Jun</u>	<u>Jul-Dec</u>	<u>Total</u>
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
SALES	1,102.8	1,214.9	1,552.9	1,736.3	1,861.6	1,983.1	10,791.2	20,242.8
Discounts	11.0	12.2	15.5	17.4	18.6	19.8	107.9	202.4
	<u>1,091.8</u>	<u>1,202.7</u>	<u>1,537.4</u>	<u>1,718.9</u>	<u>1,843.0</u>	<u>1,963.3</u>	<u>10,683.3</u>	<u>20,040.4</u>
COST OF SALES	630.2	692.4	859.4	965.7	1,025.5	1,084.8	6,088.8	11,346.8
	<u>461.6</u>	<u>510.3</u>	<u>678.0</u>	<u>753.2</u>	<u>817.5</u>	<u>878.5</u>	<u>4,594.5</u>	<u>8,693.6</u>
OVERHEADS								
Salaries	39.4	40.4	46.8	46.8	48.8	48.8	292.8	563.8
Advertising	52.5	52.5	50.0	27.5	32.5	32.5	252.5	500.0
Property	10.0	10.0	10.0	11.0	10.0	10.0	65.0	126.0
Amortisation of "know-how"	43.8	47.4	48.0	55.2	54.9	55.2	280.5	585.0
Depreciation	2.9	2.9	7.3	7.3	7.3	7.3	43.8	78.8
Sundry	32.5	32.5	32.5	32.5	35.0	35.0	216.0	416.0
Research expenditure	52.0	67.0	12.0	12.0	62.0	12.0	70.0	287.0
	<u>233.1</u>	<u>252.7</u>	<u>206.6</u>	<u>192.3</u>	<u>250.5</u>	<u>200.8</u>	<u>1,220.6</u>	<u>2,556.6</u>
PROFIT BEFORE INTEREST	<u><u>228.5</u></u>	<u><u>257.6</u></u>	<u><u>471.4</u></u>	<u><u>560.9</u></u>	<u><u>567.0</u></u>	<u><u>677.7</u></u>	<u><u>3,373.9</u></u>	<u><u>6,137.0</u></u>

"DRAGON 1982"1983 FORECAST CASH FLOW BASED ON SALES OF 97,500 UNITS

	<u>Oct-Dec</u>	<u>Jan</u>	<u>Feb</u>	<u>Mar</u>	<u>Apr</u>	<u>May</u>	<u>Jun</u>	<u>Jul-Dec</u>	<u>Total</u>
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
PROFIT BEFORE INTEREST	435.0	228.5	257.6	471.4	560.9	567.0	677.7	3,373.9	6,572.0
Depreciation	7.0	2.9	2.9	7.3	7.3	7.3	7.3	43.8	85.8
Amortisation of "Know-how"	110.0	43.8	47.4	48.0	55.2	54.9	55.2	280.5	695.0
	<u>552.0</u>	<u>275.2</u>	<u>307.9</u>	<u>526.7</u>	<u>623.4</u>	<u>629.2</u>	<u>740.2</u>	<u>3,698.2</u>	<u>7,352.8</u>
Capital expenditure	80.0	272.0	-	-	-	-	-	80.0	432.0
Loan repayment	-	-	-	-	-	-	-	665.0	665.0
FUNDS GENERATED	<u>472.0</u>	<u>3.0</u>	<u>307.9</u>	<u>526.7</u>	<u>623.4</u>	<u>629.2</u>	<u>740.2</u>	<u>2,953.2</u>	<u>6,255.8</u>
WORKING CAPITAL									
Debtors	950.0	1,419.5	1,490.6	1,856.6	2,124.5	2,295.7	2,448.5	2,248.2	14,833.6
Stock	835.0	975.0	1,125.0	1,225.0	1,325.0	1,325.0	1,425.0	1,275.0	9,510.0
Creditors	(625.0)	(750.0)	(900.0)	(1,000.0)	(1,050.0)	(1,050.0)	(1,100.0)	(950.0)	(7,425.0)
	<u>1,160.0</u>	<u>1,644.5</u>	<u>1,715.6</u>	<u>2,081.6</u>	<u>2,399.5</u>	<u>2,570.7</u>	<u>2,773.5</u>	<u>2,573.2</u>	<u>16,918.6</u>
Working capital at beginning of period	50.0	1,160.0	1,644.5	1,715.6	2,081.6	2,399.5	2,570.7	2,773.5	14,395.4
(Increase)/decrease in working capital	<u>(1,110.0)</u>	<u>(484.5)</u>	<u>(71.1)</u>	<u>(366.0)</u>	<u>(317.9)</u>	<u>(171.2)</u>	<u>(202.8)</u>	<u>200.3</u>	<u>(2,523.2)</u>
Cash - inflow/ (outflow)	<u>(638.0)</u>	<u>(481.3)</u>	<u>236.8</u>	<u>160.7</u>	<u>305.5</u>	<u>458.0</u>	<u>537.4</u>	<u>3,153.5</u>	<u>3,732.6</u>
Cash at bank - Open	<u>1,495.0</u>	<u>857.0</u>	<u>375.7</u>	<u>612.5</u>	<u>773.2</u>	<u>1,078.7</u>	<u>1,536.7</u>	<u>2,074.1</u>	<u>1,495.0</u>
- Close	<u>857.0</u>	<u>375.7</u>	<u>612.5</u>	<u>773.2</u>	<u>1,078.7</u>	<u>1,536.7</u>	<u>2,074.1</u>	<u>5,227.6</u>	<u>5,227.6</u>

Note: VAT, an added cash flow benefit, has been ignored.

80TH MEETING OF THE AGENCY

19 OCTOBER 1982