



KELSEY-HAYES CANADA LIMITED



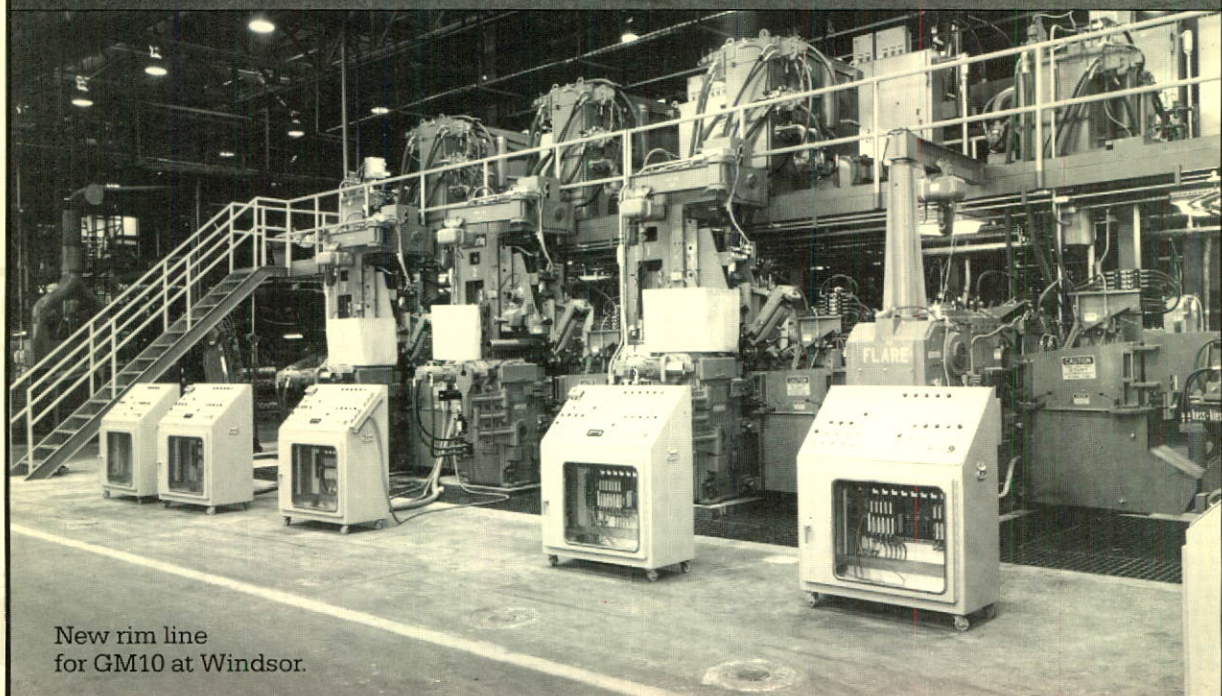
1986

ANNUAL REPORT

YEAR ENDING DECEMBER 31, 1986



The Company was founded in 1913 as Kelsey Wheel Company Limited. In 1961, Eureka Foundry and Manufacturing Company Limited, Woodstock, Ontario, was acquired. In 1966, Conroy Manufacturing Company Limited, St. Catharines, Ontario, was acquired. Effective February 1, 1967, a statutory merger of the three companies was carried out and the name of the successor Company became Kelsey-Hayes Canada Limited.



New rim line
for GM10 at Windsor.

Letter to Shareholders

OF KELSEY-HAYES CANADA LIMITED

For 1986, we had projected a year of declining sales for our Company as new car lines were being constructed and tooled for the 1988 model year. Current model sales were also adversely impacted by foreign competition.

In 1986, sales of Kelsey-Hayes Canada Limited declined to \$156,749,060 from \$209,161,057 in 1985. Net earnings were \$10,572,158 or \$1.60 per share which was a significant reduction from the record high earning of \$20,563,768 or \$3.12 per share achieved in 1985.


Investment in capital improvements was \$8,539,000 in 1986. This was a capital investment record for our Company. An addition was built at the Woodstock Division Beards Lane machining plant to house three new lines. These lines will build the 1988 model Premier front rotor and rear hub and drum for AMC and a drum for the new 1988 General Motors light truck. Windsor also invested in a new wheel line for the G.M. 10 program for the 1988 model year.

Our goal to achieve top quality awards from our customers was further enhanced by the Woodstock Division achieving the Ford Q-1 award. Woodstock Division retained their coveted Chrysler Pentastar award for the second straight year. This award was based on quality, price, timely delivery and technical expertise. Both Woodstock and Windsor have maintained their quality achievement awards from Chrysler. The Windsor Division has a Ford Q-1 award and the General Motors Spear II award. Quality, along with price and delivery, is necessary to supply parts to the foreign vehicle assemblers now building plants in Canada as well as to our current domestic customers.

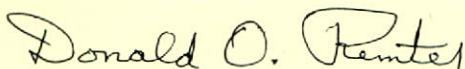
1986 was a difficult year in labour relations. The contract at Windsor expired in January 1986. After a strike of several weeks duration, a three year contract was signed in February 1986. A three year contract was also signed in September 1986 at our St. Catharines Division. The Woodstock Division contracts expired January 31, 1987. Three year contracts were signed in March 1987 after a strike at both Eureka Foundry and the Beards Lane Plant.

Management emphasis in 1986 was on cost control and productivity enhancement. Beginning in the third quarter of 1987, sales levels are expected to increase as the new lines at Woodstock and Windsor begin to produce for the 1988 model year. We are continuing our emphasis on cost control.

Your Directors appreciate the efforts of our employees in achieving the results in 1986 despite the difficult year.

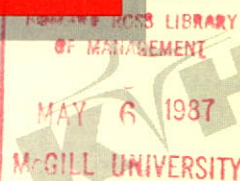


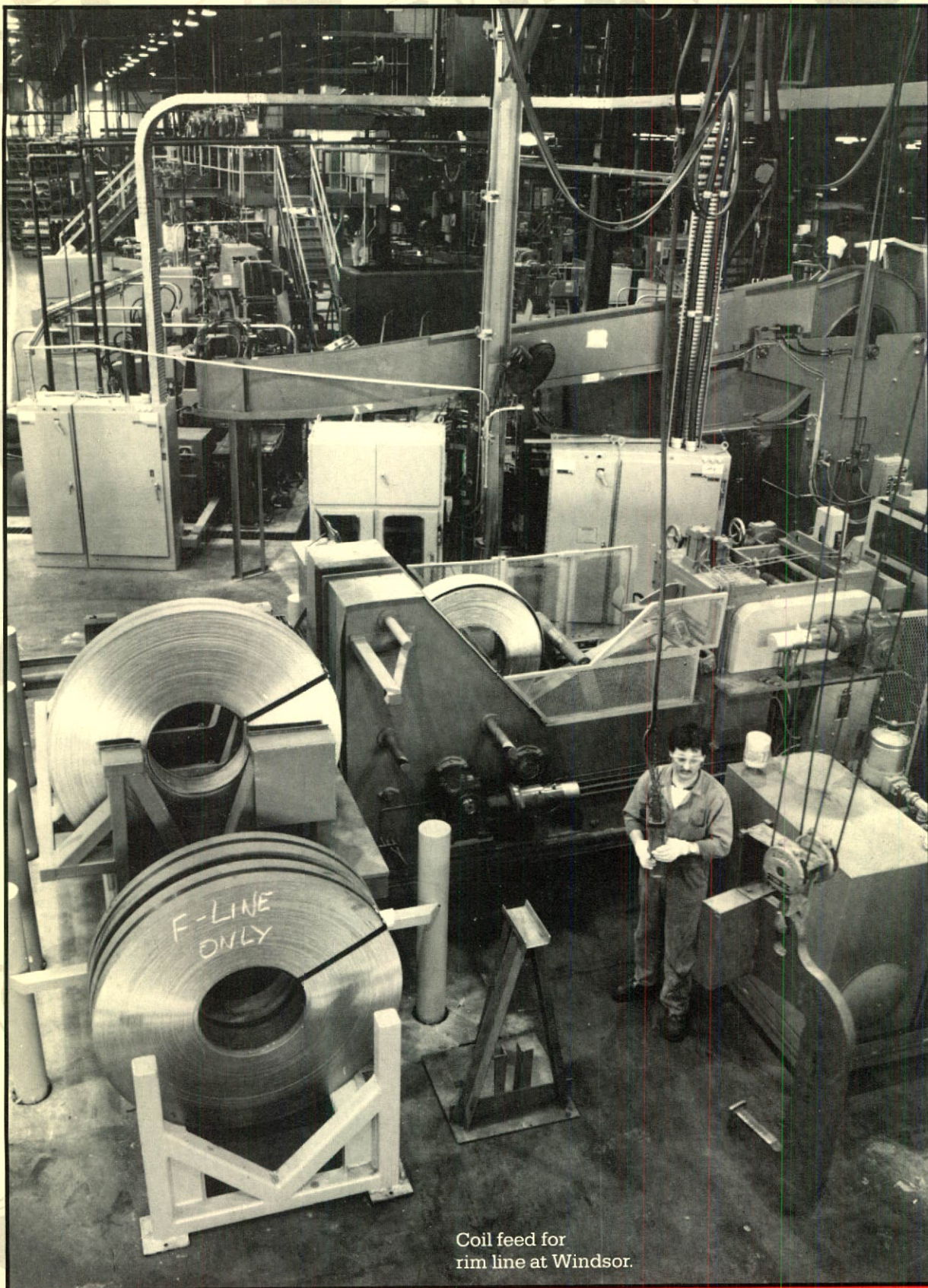
R. Siefert
Chairman of the Board



D. O. Remter
President

Windsor, Ontario
March 12, 1987





Coil feed for
rim line at Windsor.

Financial Statements

1986 FINANCIAL HIGHLIGHTS

	1986	1985
Net Sales	\$156,749,000	\$209,161,000
Net Earnings	10,572,000	20,564,000
Net Earnings per Share	1.60	3.12
Working Capital	80,902,000	77,673,000
Property, Plant and Equipment		
Expenditures	8,539,000	5,973,000
Depreciation	4,145,000	4,129,000
Book Value per Share of Common Stock	15.93	15.08

STATEMENT OF EARNINGS AND RETAINED EARNINGS

For the year ended December 31, 1986	1986	1985
Sales	\$156,749,060	\$209,161,057
Investment income	5,751,628	5,395,620
	<u>\$162,500,688</u>	<u>\$214,556,677</u>
Earnings before providing for the following	\$ 25,604,733	\$ 44,281,797
Deduct		
Depreciation of plant and equipment	4,144,706	4,129,307
Employees' pension plans (Note 2)	87,869	1,588,722
	<u>4,232,575</u>	<u>5,718,029</u>
Earnings before income taxes	21,372,158	38,563,768
Income taxes (Note 3)	10,800,000	18,000,000
Net earnings for the year	10,572,158	20,563,768
Retained earnings, at beginning of year	98,418,422	82,969,654
	<u>108,990,580</u>	<u>103,533,422</u>
Dividends	4,950,000	5,115,000
Retained earnings, at end of year	<u>\$104,040,580</u>	<u>\$ 98,418,422</u>
Earnings per share, after giving retroactive effect to the subdivision of shares as referred to in Note 6	<u>\$ 1.60</u>	<u>\$ 3.12</u>

(See Accompanying Notes to the Financial Statements)

Kelsey-Hayes Canada Limited

(INCORPORATED UNDER THE BUSINESS CORPORATIONS ACT - ONTARIO)

BALANCE SHEET as at December 31, 1986

ASSETS	1986	1985
Current		
Cash and short-term deposits	\$ 63,432,552	\$ 67,730,667
Accounts receivable	14,626,899	14,521,591
Due from affiliated companies	521,836	477,132
Income taxes receivable	5,536,563	—
Inventories	14,056,218	16,533,094
Special tooling for current production	2,753,221	1,080,813
Prepaid taxes, insurance and other expenses	100,473	152,861
	<u>101,027,762</u>	<u>100,496,158</u>
Property, plant and equipment		
Land	513,751	560,229
Buildings and land improvements	12,608,809	12,420,134
Machinery and equipment	73,658,317	65,548,167
Total — at cost	<u>86,780,877</u>	<u>78,528,530</u>
Less accumulated depreciation	<u>50,516,749</u>	<u>46,658,639</u>
	<u>\$137,291,890</u>	<u>\$132,366,049</u>
LIABILITIES	1986	1985
Current		
Accounts payable	\$ 11,883,011	\$ 11,818,832
Payroll and taxes withheld from employees	4,108,936	5,436,152
Dividends payable	1,980,000	2,640,000
Other accrued expenses	2,154,363	1,662,000
Income taxes	—	1,265,643
	<u>20,126,310</u>	<u>22,822,627</u>
Deferred income taxes	<u>12,000,000</u>	<u>10,000,000</u>
SHAREHOLDERS' EQUITY		
Share Capital (Note 6)		
Authorized		
Unlimited number of common shares		
Issued		
6,600,000 shares	1,125,000	1,125,000
Retained earnings	<u>104,040,580</u>	<u>98,418,422</u>
	<u>105,165,580</u>	<u>99,543,422</u>
	<u>\$137,291,890</u>	<u>\$132,366,049</u>
On behalf of the Board:		
R. G. Siefert, Director		
D. O. Remter, Director		

(See Accompanying Notes to the Financial Statements)

STATEMENT OF CHANGES IN FINANCIAL POSITION
for the year ended December 31, 1986

	1986	1985
Funds provided by (used in) operating activities		
Net earnings for the year	\$10,572,158	\$20,563,768
Non-cash items		
Depreciation	4,144,706	4,129,307
Deferred income taxes	2,000,000	1,400,000
	<u>16,716,864</u>	<u>26,093,075</u>
Changes in working capital		
(Increase) decrease in accounts receivable	(105,308)	768,776
Decrease (increase) in inventories	2,476,876	(2,887,781)
Increase (decrease) in accounts payable and accrued expenses	556,542	(572,194)
(Decrease) in income taxes	(6,802,206)	(3,479,515)
Other	(3,651,940)	375,466
	<u>(7,526,036)</u>	<u>(5,795,248)</u>
Funds provided by operations.	9,190,828	20,297,827
Funds used for		
Dividends	<u>4,950,000</u>	<u>5,115,000</u>
Funds remaining for investment.	4,240,828	15,182,827
Funds used in investing activities		
Purchases of property, plant and equipment	<u>8,538,943</u>	<u>5,972,873</u>
(Decrease) increase in funds for the year	(4,298,115)	9,209,954
Funds:		
Cash and short-term deposits at beginning of year	<u>67,730,667</u>	<u>58,520,713</u>
Cash and short-term deposits at end of year	<u>\$63,432,552</u>	<u>\$67,730,667</u>

(See Accompanying Notes to the Financial Statements)

Notes to Financial Statements

DECEMBER 31, 1986

1. Summary of significant accounting policies

(a) Inventories

Inventories are valued at the lower of cost and net realizable value, cost being determined substantially on a first-in, first-out basis.

(b) Depreciation

Property, plant and equipment are recorded at cost less accumulated depreciation. Depreciation is provided on a basis which amortizes the cost of depreciable assets over their estimated useful lives.

(c) Income taxes

The Company provides for income taxes under the tax allocation basis of accounting whereby income taxes are provided for in the year in which the related income is reflected in the financial statements. Deferred income tax provisions result from timing differences in the recognition of income and expense for income tax and financial statement purposes. Investment tax credits are recorded using the cost reduction approach.

(d) Pension and other retirement benefits

Current service costs of pension plans are accrued and funded on a current basis. Past service costs are amortized and funded over a period not exceeding fifteen years.

(e) Foreign currency conversion

Assets and liabilities of the Company in United States dollars are converted into Canadian dollars at the year-end exchange rate. Transactions during the year are converted at the current rates then in effect.

2. Pensions

Unfunded past service costs under pension plans for employees are estimated at approximately \$160,000 (1985 - \$675,000) at December 31, 1986. Pension costs for the year have been reduced by an actuarial experience gain of \$1,307,200.

3. Income taxes

	1986	1985
Currently payable	\$ 8,800,000	\$16,600,000
Deferred	2,000,000	1,400,000
	<u>\$10,800,000</u>	<u>\$18,000,000</u>

The basic corporate tax rate of 53.3% has been reduced to the effective provision rate of 50.5% by the application of the manufacturing and processing credit of 5.8% and increased by other tax adjustments netting 3.0%.

4. Segmented information

The Company is a supplier of parts components to the automotive industry. Approximately 77% (1985 - 79%) of the Company's sales are to its customers in the United States.

5. Related party transactions

Approximately 5% (1985 - 5%) of the total sales are to the Company's parent and related companies. Additionally the Company pays to its parent a royalty charge of .75% on sales to non-related parties.

6. Share capital

On January 17, 1986 the Company obtained Articles of Amendment which divided each of the 3,300,000 issued common shares into two common shares and changed the authorized capital to consist of an unlimited number of common shares.

AUDITORS' REPORT

The Shareholders,
Kelsey-Hayes Canada Limited.

We have examined the balance sheet of Kelsey-Hayes Canada Limited as at December 31, 1986 and the statements of earnings and retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the Company as at December 31, 1986 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Touche Ross & Co.

Chartered Accountants

Windsor, Ontario
January 19, 1987

5 YEAR FINANCIAL REVIEW	1986	1985	1984	1983	1982
OPERATING RESULTS:	December 31 (Dollar Amounts in Thousands)				
Net sales	\$156,749	\$209,161	\$222,249	\$179,382	\$120,131
Net earnings before income taxes	21,372	38,564	34,773	23,342	12,174
Income taxes	10,800	18,000	15,700	10,500	5,400
Net earnings for the year	10,572	20,564	19,073	12,842	6,774
Dividends	4,950	5,115	4,455	2,706	2,310
Net increase in retained earnings	5,622	15,448	14,618	10,136	4,464
Expenditures for property, plant and equipment	8,539	5,973	7,949	4,401	6,614
Depreciation of plant and equipment	4,145	4,129	3,588	3,093	2,713
Per share of Common stock:					
Net earnings	\$ 1.60	\$ 3.12	\$ 2.89	\$ 1.95	\$ 1.03
Dividends	\$.75	\$.78	\$.68	\$.41	\$.35
FINANCIAL POSITION:					
Current assets	\$101,028	\$100,496	\$ 88,840	\$ 73,324	\$ 52,547
Current liabilities	20,126	22,823	26,172	21,718	10,058
Working capital	80,902	77,673	62,668	51,606	42,489
Property, plant and equipment (net)	36,264	31,870	30,026	25,720	24,452
Shareholders' investment	105,166	99,543	84,095	69,476	59,340
Book value per share of Common stock	\$ 15.93	\$ 15.08	\$ 12.74	\$ 10.53	\$ 8.99

CORPORATE OFFICE:

Windsor, Ontario, Canada

Plants located in:
Windsor, Woodstock and
St. Catharines, Ontario

BOARD OF DIRECTORS

J. L. Callaghan
T. Neal Combs
J. G. Crean
W. C. McIvor
Morgan Reid
D. O. Remter
R. G. Siefert

OFFICERS

R. G. Siefert
Chairman of the Board
D. O. Remter
President
D. A. Robinson
Secretary-Treasurer
L. E. Wilson
Assistant Secretary-Treasurer

TRANSFER AGENT AND REGISTRAR

The National Victoria
and Grey Trust Company
Toronto, Montreal, Winnipeg
and Vancouver

AUDITORS

Touche Ross & Co.,
Windsor, Ontario



Use of Microcomputer
in Spc. & Personnel



Conroy Division, St. Catharines, Ontario



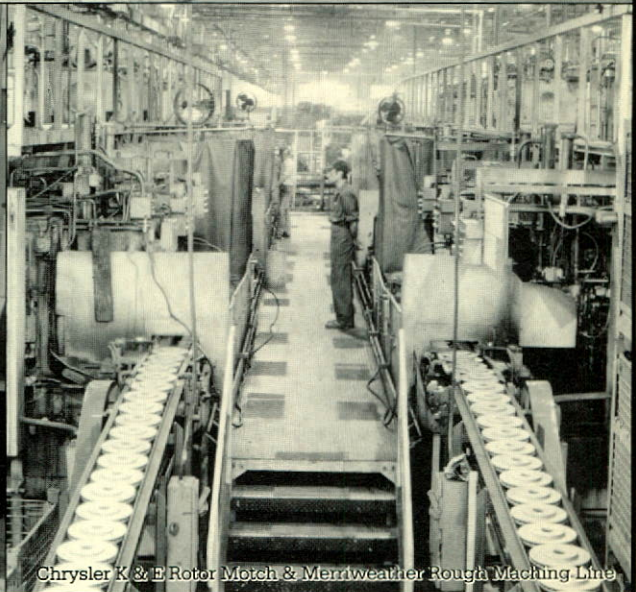
Finished Chrysler K & E Rotor



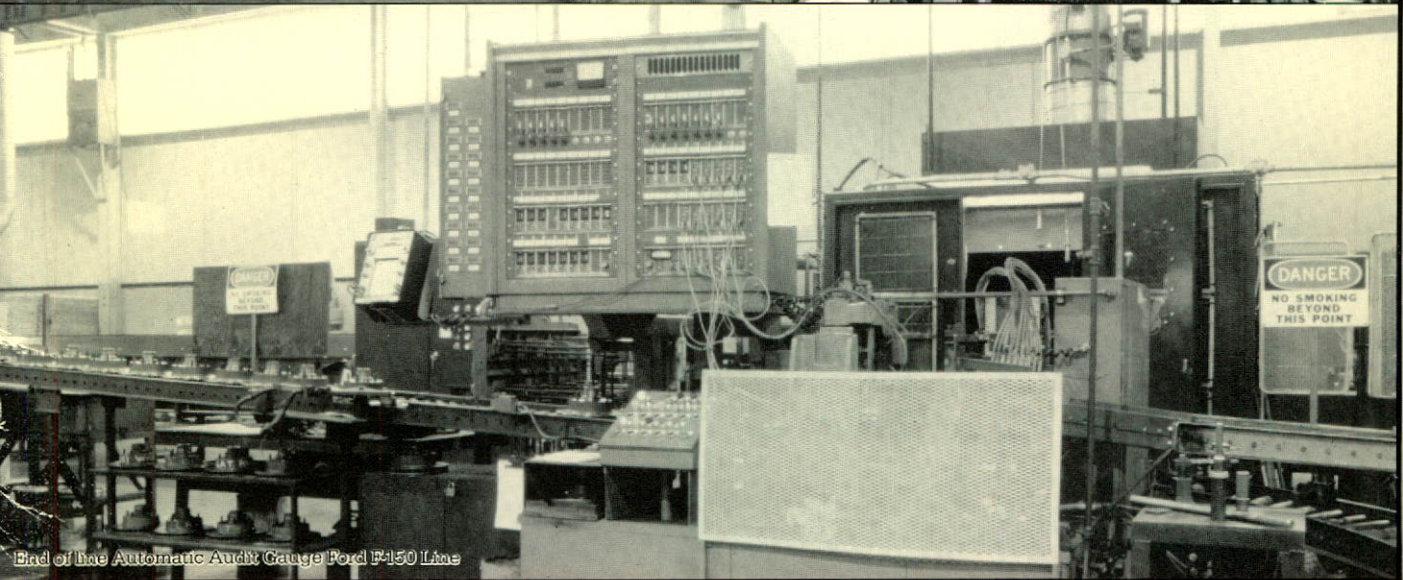
Woodstock Division, Beards Lane Plant



Statistical Process Control Station



Chrysler K & E Rotor Moxh & Merrweather Rough Maching Line



End of Line Automatic Audit Gauge Ford F-150 Line



Company-Wide Excellence

KELSEY-HAYES CANADA LIMITED