



ANNUAL REPORT 1975

Industrial Nucleonics designs, manufactures, and markets computer-based automation and management information systems for basic manufacturing processes to save raw materials and energy, increase productivity, lower costs, and improve quality—all benefits which translate into substantial profit gains for the customer. These systems are marketed under the AccuRay® trademark in more than 35 countries.

ACCURAY PROCESS AUTOMATION SYSTEMS —25 YEARS OF LEADERSHIP EXPERIENCE

Based upon 25 years' experience in developing automation systems for industry, Industrial Nucleonics today offers a step-by-step program to couple AccuRay systems for measurement and control at the process level of manufacturing with plantwide and corporate management information systems. These programs are being implemented successfully in the pulp and paper, tire and rubber, plastics, textiles, steel, aluminum, mining, and tobacco industries.

Each AccuRay process automation system begins with the measurement of basic properties of materials, such as weight, thickness, and moisture content, as they are being manufactured. Measurement data is combined with other process inputs to provide a series of automatic controls to optimize the process and to provide timely production reports to operating and management personnel. AccuRay systems, incorporating the newest developments in computers, measurement technologies, and optimum control strategies, are designed to best match the customer's application with the most advanced technologies.

Key to effectively implementing these automation programs are the professional personnel, skills, and corporate commitment backing each application. Industry-oriented marketing teams appraise the needs of a customer business and recommend the most effective and feasible solutions. Highly skilled engineers specify an integrated system package appropriate to the customer's operation. Manufacturing and system-test engineers provide for prompt delivery, rapid start-up, and maximum reliability of each system. A worldwide systems and service support organization ensures optimum usage and customer results.

TO OUR STOCKHOLDERS AND EMPLOYEES:

The year 1975 for Industrial Nucleonics reflected a strengthening financial position in the balance sheet but a significant disappointment in the results of operations. A decline in sales, the foreign currency loss, special charges for various discontinued operations, and an increase in internal reserves for equipment returns and inventory adjustments were factors contributing to the 1975 results. The following summary figures represent the consolidated performance of Industrial Nucleonics and its subsidiaries:

	1975	1974	1973
	(\$ Thousands, except for per share data)		
Highlights of Operations			
Operating revenues			
Sales	\$37,923	\$48,797	\$42,436
Service and leasing	34,206	27,258	19,091
Total operating revenues	72,129	76,055	61,527
Less cost of sales	42,769	47,276	37,144
Gross profit	29,360	28,779	24,383
Less operating expenses and interest	31,321	30,528	21,775
Operating income (loss) before foreign currency gain (loss)	(1,961)	(1,749)	2,608
Foreign currency gain (loss)	(1,779)	266	(140)
Income (loss) before income taxes	(3,740)	(1,483)	2,468
Provision (credit) for income taxes	(1,500)	(511)	376
Net income (loss)	(2,240)	(972)	2,092
Net income (loss) per share	(0.65)	(0.28)	0.61
Highlights in Financial Position			
Increase (decrease) in debt	(5,310)	24,724	31,567
Increase (decrease) in inventories	(3,666)	(691)	9,816
Backlog at Year End			
Equipment and related commitments for services to be performed within 12 months	17,770	15,804	13,441

During 1975 we noted a tendency for customers in many industries and markets served by Industrial Nucleonics to delay commitments for significant capital expenditures which in turn slowed our incoming order rates during the first nine months. The lower order level contributed to a decline in sales to \$37.9 million from the \$48.8 million achieved in 1974. For the year, pulp and paper was the only industry in which new orders exceeded the level of 1974. In the fourth quarter we experienced an increase in incoming orders and by a small margin the quarter had the highest order total in our history.

As a result of lower shipment forecasts, internal cost cutting programs remained in effect throughout the year and approximately \$4.9 million of planned expenditures were trimmed from company budgets. Employment was reduced 10% to 1,917 personnel at year end. While these cost reduction programs were effectively implemented during the year, we also made the decision to maintain our primary engineering and marketing programs in anticipation of the economic recovery now in evidence.

Key new product development programs were not interrupted during 1975 and total expenditures for research and development were approximately 4% higher than in 1974. As a result, on March 15-18, 1976, the latest AccuRay 1180 Micro System for the paper machine control market - with expanded use of microprocessor technology and other new features - was introduced at the TAPPI (Technical Association of the Pulp and Paper Industry) meeting and annual exhibit at the New York Hilton Hotel. We recently delivered the first AccuRay 520 Automatic Gauge Control Modules - using microprocessors - for the steel and aluminum industry. The AccuRay 2800 systems for the plastics industry are scheduled for initial deliveries in the first quarter of 1976.

The final record for 1975 was adversely affected by the following factors:

- In the fourth quarter we recorded a loss of \$1,563,000 on foreign currency exchange of which \$1,396,000 represents an unrealized loss caused by the translation of the balance sheets of our foreign subsidiaries into U.S. dollars at December 31, 1975. Industrial Nucleonics has historically followed the accounting policy that "gains and losses from year-end translation into United States dollars are deferred and recorded at the time of realization." However, as noted in our last quarterly report, the Financial Accounting Standards Board issued Statement No. 8 entitled "Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements" on October 21, 1975. This statement establishes accounting standards which were optional for 1975 and became mandatory for fiscal years beginning on or after January 1, 1976, and requires unrealized gains and losses to be included in determining net income. We have elected to adopt the new standard in 1975 with the result that a total loss of \$1,779,000 on foreign currency exchange was recorded for the year compared with a net realized gain of \$266,000 in 1974.

In order to minimize future exposure to foreign currency fluctuations, we are placing a greater emphasis on taking overseas business in U.S. dollar denominated contracts, using hedging transactions whenever feasible, and increasing overseas borrowings in relation to the level of outstanding trade receivables in each country. As a result of international marketing efforts, approximately half of all incoming orders for equipment outside the U.S. were in dollar contracts or the equivalent during 1975.

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- During 1975 we completed a divestment program for various business activities having an unsatisfactory past record of profitability. They included our instrumentation product lines for density, level and can-fill measurement, non-destructive testing and inspection service, and materials planning and inventory control business. The cost of discontinuing these operations and selling the remaining assets during the year resulted in an aggregate loss of \$690,000 which has been charged against 1975 earnings.
 - The 1974-1975 recession contributed both to the decline in sales in 1975 and also to a higher level of equipment returns and allowances from prior year shipments. In the fourth quarter, we increased our internal reserve for equipment returns and allowances by making a pre-tax charge of \$900,000 against 1975 earnings. We also increased our reserve for inventory adjustments by \$366,000 at year end.

In reviewing our financial position at the end of 1975, we were pleased at the improving trend in cash flow as evidenced by the reduction in debt during the year of \$5.3 million compared with an increase in borrowing of \$24.7 million in 1974 and \$31.6 million in 1973. This improvement was caused by the following:

- Total inventory levels, which include both manufacturing and field inventories, were reduced \$3.7 million during 1975. Better utilization of inventories in manufacturing was achieved through the use of the AccuRay 3300 computerized inventory control system installed in our factory in 1974. In addition, a new computerized field inventory control system for field replacement parts was placed in operation in November 1975.
- During the year we completed the sale to third parties of approximately \$10.0 million of the leasing portfolio being financed by Industrial Nucleonics. Since this program was initiated in the fourth quarter of 1974, we have sold \$14.0 million of leasing receivables on a non-recourse basis.
- The percentage of incoming orders in 1975 requiring direct financing by Industrial Nucleonics was reduced to approximately 25% as compared with 58% in 1974. This change was primarily caused by customers leasing directly from independent leasing companies or third party financial institutions as opposed to obtaining the financing from Industrial Nucleonics. Since our beginning backlog in 1975 had the higher percentage of internally financed commitments, the impact of these programs became more visible in the fourth quarter during which the reduction in bank debt was \$4.1 million.

At the beginning of 1976 our backlog for equipment and related services to be provided within 12 months was \$17.8 million - approximately 12% higher than a year earlier. We expect our business to be better in 1976 based upon the improvement in the business climate in the United States. We anticipate a lagging but gradual improvement in international markets which produced 44% of our total incoming orders in 1975.

Industrial Nucleonics has truly become an international company in recent years, with AccuRay systems currently being marketed in over 35 countries. The mid-1970's were especially trying, and we found ourselves vulnerable in many areas - record inflation, fluctuating currency exchange, shortage of capital, rising interest rates, and a worldwide recession. In spite of these adversities our business has flourished, and we sell and service AccuRay systems entirely through our own personnel - in ten subsidiary companies and a Japanese joint venture. Our worldwide service business with revenues of \$27.9 million in 1975 is of itself profitable. In anticipation of an upturn in worldwide capital expenditures, our AccuRay equipment is newly designed and ready to increase productivity, reduce cost and improve quality for our clients in the pulp and paper, rubber, plastics, steel, aluminum, textiles and tobacco industries. In 1976 we will concentrate on these industries and take advantage of their diversified business base.

Sincerely,



David L. Nelson
President

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