PLAINTIFF'S EXHIBIT
CE-2



Financial Highlights

Thousands of dollars except per share statistics	1979	1978
Net Sales	$2,757,504	$2,331,751
Net Income	$ 97,641	$ 80,316
Per Share	$ 5.96	$ 4.97
Cash Dividends Declared	$ 35,892	$ 29,105
Per Common Share	$ 2.20	$ 1.80
Unfilled Orders	$2,986,465	$2,879,929

Heavy Oil Recovery (Cover photo): Production of known reservoirs of thick crude oil is increasing in the United States. This installation of six C-E Natco high-pressure steam generators is part of a complex of more than 100 such systems now on line in Kern County, California.

Annual Meeting: Shareholders are cordially invited to attend the annual meeting, which will be held at 2:30 p.m., Tuesday, April 22, 1980, in the Casino on the Park of the Essex House, 160 Central Park South, New York City.

Combustion Engineering, Inc.
Corporate Headquarters:
900 Long Ridge Road, Stamford, Conn. 06902
Telephone (203) 329-8771

COMBUSTION ENGINEERING ANNUAL REPORT 1979 — FINANCIAL SECTION

Financial Highlights

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Financial Report

Acquisition of Basic Incorporated

In early 1979, substantially all of the outstanding common and 5% convertible preference shares of Basic Incorporated were acquired for approximately $74,000,000 in cash. Basic Incorporated is primarily a producer of refractory materials. It also produces specialized chemicals and is a manufacturer of electronic products.

The investment in Basic Incorporated has been allocated to the various assets acquired. Property, plant and equipment acquired in this transaction are being amortized based on their fair market value and estimated useful lives.

The operations of Basic Incorporated have been included in the accompanying Consolidated Statement of Income beginning with the month of February, 1979. However, the adjustment of Basic's assets to reflect fair market values as of the date of acquisition, particularly the upward valuation of inventories, adversely affected its contribution to consolidated earnings in 1979. Earnings subsequent to 1979, however, will be considerably less affected by these adjustments.

Working Capital

Working capital (current assets less current liabilities) increased in 1979 despite the use of funds to acquire Basic Incorporated. Working capital at December 31, 1979, amounted to $284,302,000 compared to $273,594,000 at December 31, 1978.

Funds provided from operations of $181,059,000 in 1979 compare to $201,308,000 provided in 1978. This decline was due primarily to the increase in the amount of income taxes currently payable at the end of 1979 over those at the previous year-end. The increase in income taxes currently payable is due primarily to timing differences caused by using the completed contract method of accounting for federal income tax purposes as opposed to the percentage of completion method for financial reporting purposes.

Accounts receivable at December 31, 1979, of $439,726,000 were $63,430,000 above those at the end of 1978. The increase resulted primarily from a higher level of shipments and billings in 1979 and the inclusion of Basic Incorporated receivables.

Inventories at year-end increased to $528,369,000 which was $69,729,000 above those at December 31, 1978. The increase is largely attributable to higher work in process inventories, including work on long-term contracts, and to the addition of Basic Incorporated inventories.

A more detailed analysis of the factors affecting working capital in 1979 and 1978 is provided in the accompanying Consolidated Statement of Changes in Financial Position.

Property, Plant and Equipment

Amounts invested in property, plant and equipment during the year, including those acquired from Basic Incorporated ($54,202,000), aggregated $146,741,000. This compared to expenditures of $74,901,000 in 1978.

The principal manufacturing facilities of Basic Incorporated are located in Maple Grove, Ohio; Gabbs, Nevada; Port St. Joe, Florida and Waterford, Pennsylvania.

Some of the more significant facility projects in progress during 1979 are noted below:

Work was completed in 1979 on the new Pasadena, Texas plant for the production of intermediate chemicals used in the production and processing of oil and gas. The Pasadena plant became operational in November, 1979.

Construction began in June, 1979, on the facility to house an 11,000 ton multi-ram hydraulic press and auxiliary equipment at Beaumont Well Works, Houston plant. The press is expected to be installed in September, 1980, and will be used to produce forgings required for oil field valves, wellheads and equipment.

A further expansion of fused silica capacity at the Greeneville, Tennessee plant was initiated during 1979. Fused silica is used as a resin extender by the electronics industry and for the production of investment castings and high temperature refractories.

The new plant for coating oil country tubular goods at Gladbeck, West Germany, was completed and became operational in 1979.

A major addition to Gray Tool's manufacturing capacity in Houston, Texas, for the production of wellhead assemblies, valves and high pressure pipe connectors was completed in 1979.

The new plant in Moncton, New Brunswick, to produce nuclear fuel bundles for heavy water moderated nuclear power plants was completed and became operational in 1979.

An expansion of Basic's capacity to produce chemical grade magnesium oxide was authorized in 1979. This project includes a new multiple hearth furnace at the Gabbs, Nevada plant. This product is used as a supplement to animal food and has many industrial uses as well.

Work was begun on a new computer center in Houston, Texas. The new center will process technical and commercial programs for Gray Tool and other Company operations in the Southwestern area as well as serve as a back-up processing center for the present Corporate data center in Windsor, Connecticut. The Houston computer center will become operational in mid 1980.

In addition, other facility programs involving the expansion and modernization of manufacturing, engineering and research facilities for each of the operating groups continued during the year.

Total facility projects authorized in 1979 aggregated $85,262,000, including $4,154,000 for Basic Incorporated projects which were partially completed at the time of the acquisition. The unexpended balance on all projects underway at December 31, 1979 totaled $81,995,000.

Additions to the Company's manufacturing, research and other facilities during the years 1975 through 1979 aggregated $475,764,000, exceeding depreciation and amortization provisions during the same period by $254,746,000. This level of capital spending has been accomplished primarily by means of funds generated internally.

Investments

At December 31, 1979, investments in associated and other companies aggregated $68,545,000, reflecting an increase of $16,833,000 over the prior year-end. The increase was due largely to an additional investment in the common stock of Yara Engineering Corporation as well as the Company's equity in its 1979 net earnings. The Company's equity is equal to approximately 44% of the outstanding shares. Yara Engineering Corporation's principal activity is the mining and processing of kaolin clay by its wholly owned subsidiary Georgia Kaolin Company.

Long-term Debt

Long-term debt increased to $144,386,000 at December 31, 1979 from $139,639,000 at December 31, 1978. Long-term debt of Basic Incorporated at the date of acquisition was $9,000,000. Other issues of long-term debt were reduced in 1979 by the purchases of bonds for sinking fund purposes and by other regularly scheduled payments.

In January, 1980 the Company received the required consents from holders of its 5¾% Sinking Fund Debentures due 1992 to amend the Indenture under which these debentures were issued in 1967. In general, the amendments conform certain covenants contained in the Indenture to those of the Indenture under which the 7.45% Sinking Fund Debentures due 1996 were issued in 1971 and thereby expand the Company's debt capacity. In addition, the amendments increased the interest rate from 5¾% to 6¾% effective from January 15, 1980, and increased the mandatory annual sinking fund payment from $2,222,000 to $2,750,000 beginning with the July 15, 1981, sinking fund payment.

Dividends and Net Worth

The dividend rate on the common stock was increased twice in both 1979 and 1978 and is currently at the rate of $2.40 per share per annum. Quarterly dividends declared on the common stock totaled $2.20 in 1979 and $1.80 in 1978.

At December 31, 1979, the total equity of the common shareholders represented by the stated value of common stock and by consolidated retained earnings was $559,674,000 equal to $34.26 per share.

Consolidated Balance Sheet

December 31.	1979	1978
Assets		
Current Assets:		
Cash and short-term investments (1b)	$ 445,681,286	$ 406,253,128
Accounts receivable (less unearned billings of $195,400,543 in 1979 and $186,225,642 in 1978) (1c and 1d)	439,725,672	376,295,735
Inventories (1d and 1e)	528,368,829	458,639,747
Prepaid expenses	14,863,397	11,353,636
Total current assets	$1,428,639,184	$1,252,542,246
Investments in Associated and Other Companies (1a):		
At equity	$ 50,713,296	$ 33,172,345
At cost	17,831,999	18,538,077
	$ 68,545,295	$ 51,710,422
Property, Plant and Equipment (1g):		
Land and buildings	$ 272,729,674	$ 244,049,757
Machinery and equipment	624,525,964	542,069,083
	$ 897,255,638	$ 786,118,840
Less—Accumulated depreciation and amortization	381,272,201	335,252,493
	$ 515,983,437	$ 450,866,347
Other Assets:		
Goodwill and, in 1978, patents and other intangible assets (1h)	$ 64,514,458	$ 75,224,685
Deferred charges	5,277,801	6,603,077
	$ 69,792,259	$ 81,827,762
	$2,082,960,175	$1,836,946,777

Reference is made to the accompanying notes to financial statements

	Combustion Engineering, Inc. and Subsidiary Companies	
December 31,	1979	1978
Liabilities		
Current Liabilities:		
Notes payable and current portion of long-term debt (4)	$ 11,612,521	$ 4,502,775
Accounts payable	137,178,742	133,025,910
Accrued liabilities (1i)	418,910,059	371,174,755
Federal, state and foreign income taxes (1k)	63,542,799	10,505,956
Advance payments on contracts	503,323,661	451,653,234
Dividends payable	9,769,188	8,085,031
Total current liabilities	$1,144,336,970	$ 978,947,661
Deferred Income Taxes and Investment Tax Credit (1k)	$ 232,981,000	$ 222,999,000
Long-term Debt (5)	$ 144,386,069	$ 139,639,449
Minority Interests in Subsidiary Companies	$ 1,581,926	$ 1,367,730
Shareholders' Equity (5, 7 and 8):		
Preferred Stock, no par value—		
Authorized—2,000,000 shares		
Issued—none in 1979 and 1978	$ —	$ —
Common Stock, $1 par value—		
Authorized—50,000,000 shares		
Issued—16,480,606 shares in 1979 and 16,280,611 shares in 1978, stated at	66,416,638	62,484,401
Retained earnings (see accompanying statement)	492,317,339	431,568,303
	$ 559,733,977	$ 494,052,704
Deduct shares held in treasury, at cost:		
Common Stock—143,487 shares in 1979 and 123,855 shares in 1978	59,767	59,767
	$ 559,674,210	$ 493,992,937
	$2,082,960,175	$1,836,946,777

Reference is made to the accompanying notes to financial statements.

Consolidated Statement of Income

Combustion Engineering, Inc. and Subsidiary Companies

For the Years Ended December 31	1979	1978
Net Sales (1d)	$2,757,504,278	$2,331,751,133
Costs and Expenses:		
Cost of sales (1e)	$2,373,357,740	$2,006,265,603
Selling, general and administrative expenses	213,401,782	178,041,245
	$2,586,759,522	$2,184,306,848
Operating income	$ 170,744,756	$ 147,444,285
Other Income and (Deductions):		
Interest expense	($ 16,613,121)	($ 18,399,812)
Interest earned	26,956,016	26,873,891
Equity in net earnings of associated and other companies (1a)	4,340,294	1,396,768
Miscellaneous, net	1,203,119	1,701,160
	$ 15,836,308	$ 11,572,007
Income before income taxes	$ 186,581,064	$ 159,016,292
Federal, State and Foreign Taxes on Income (1k)	88,940,000	78,700,000
Net income	$ 97,641,064	$ 80,316,292
Net Income per Share (1l)	$5.96	$4.97

Reference is made to the accompanying notes to financial statements.

Consolidated Statement of Retained Earnings

Combustion Engineering, Inc. and Subsidiary Companies

For the Years Ended December 31	1979	1978
Balance at beginning of year	$ 431,568,303	$ 379,230,787
Addition resulting from pooling of interests	—	1,859,913
Net income	97,641,064	80,316,292
	$ 529,209,367	$ 461,406,992
Deduct:		
Cash dividends declared—		
Preferred Stock—None in 1979 and $3.85 per share through redemption in 1978	—	104,979
Common Stock—$1.20 per share in 1979 and $1.80 in 1978	35,892,028	28,895,516
Pooled company prior to acquisition	—	105,000
Excess of redemption price of Series A Convertible Preferred Stock over stated value	—	624,261
Transfer to Common Stock of amount equal to stated value of redeemed shares of Series A Convertible Preferred Stock	—	99,834
Adjustment for fractional shares on conversion of Series A Convertible Preferred Stock	—	9,099
Balance at end of year	$ 493,317,339	$ 431,568,303

Reference is made to the accompanying notes to financial statements.

Consolidated Statement of Changes in Financial Position

Combustion Engineering, Inc. and Subsidiary Companies

For the Years Ended December 31.	1979	1978
Source of Funds:		
Operations—		
Net income	$ 97,641,064	$ 80,316,292
Charges (credits) not requiring funds—		
Depreciation and amortization	66,137,562	52,567,333
Deferred income taxes (noncurrent) and investment tax credit	9,962,000	53,039,000
Equity in net earnings of associated and other companies adjusted for dividends received	(3,634,319)	(1,026,464)
All other, net, including amortization of patents and other product development costs	10,932,423	16,411,761
Funds provided from operations	$181,058,730	$201,307,922
Retirements of property, plant and equipment, less accumulated depreciation and amortization	15,486,810	7,678,675
Common Stock issued in connection with an acquisition, net	3,404,543	—
Proceeds from exercise of stock options	527,694	—
Total source of funds	$200,477,777	$208,986,597
Application of Funds:		
Additions to property, plant and equipment, including $54,222,322 with respect to Basic Incorporated in 1979	$146,741,462	$ 71,900,656
Cash dividends declared	35,892,028	29,105,495
Reduction of long-term debt, net	4,253,380	7,630,133
Redemption of Series A Convertible Preferred Stock	—	724,095
Increase in investments, net, including Yara Engineering in 1979 and 1978	12,613,294	19,987,264
Acquisition of Basic Incorporated—		
Noncurrent assets other than property, plant and equipment	3,203,937	—
Long-term debt	(9,000,000)	—
All other, net	(3,933,953)	(4,237,935)
Total application of funds	$189,770,148	$128,109,708
Net Increase in Working Capital	$ 10,707,629	$ 80,876,889
Details of Increase (Decrease) in Working Capital:		
Cash	$ 39,428,158	$137,415,855
Accounts receivable	63,429,937	3,361,449
Inventories	69,729,082	22,700,110
Notes payable and current portion of long-term debt	(7,109,746)	10,431,831
Accounts payable and accrued liabilities	(51,888,136)	(42,005,614)
Federal, state and foreign income taxes	(53,036,843)	5,073,954
Advance payments on contracts	(51,670,427)	(56,591,681)
Other, net	1,825,604	490,925
	$ 10,707,629	$ 80,876,889

References are to the accompanying notes to financial statements.

Notes to Financial Statements

1. Accounting Policies and Supplementary Information

(a) Principles of Consolidation

The financial statements of all but certain minor domestic and foreign subsidiaries have been included in the consolidated financial statements. In consolidating the financial statements of the parent company and its consolidated subsidiaries, all significant income and expense amounts and all significant balance sheet amounts of an intercompany nature, including unrealized intercompany profits, have been eliminated.

Investments in unconsolidated subsidiaries, associated companies (those having license agreements with the Company) and other companies which are 20% or more owned are recorded at cost adjusted for the Company's equity in undistributed earnings or losses. Dividends received from such companies aggregated $706,000 in 1979 and $370,000 in 1978. Retained earnings at December 31, 1979, include $3,126,000 with respect to the undistributed earnings of unconsolidated subsidiaries and other associated companies which are 20% or more owned.

The aggregate investment (including the equity in undistributed earnings or losses) in companies which are 20% or more owned exceeds the equity in the net assets of such companies as shown in their financial statements by $5,338,000. Such excess is considered to be allocable to the underlying assets, primarily fixed assets including mineral deposits, and is being amortized over their estimated useful lives.

Investments in associated and other companies which are less than 20% owned are carried at the lower of aggregate cost or market value. Such investments included securities which are traded in foreign markets having an aggregate cost of $14,107,000 at December 31, 1979 and $13,951,000 at December 31, 1978. The aggregate market value of these marketable securities was $40,645,000 at December 31, 1979 and $31,160,000 at December 31, 1978. At December 31, 1979, there were gross unrealized gains of $25,538,000.

(b) Cash and Short-term Investments

Cash included temporary investments and time deposits amounting to $396,721,000 and $364,729,000 at December 31, 1979 and 1978, respectively.

(c) Reserves for Doubtful Accounts and Allowances

Accounts receivable are shown in the Consolidated Balance Sheet net of reserves for doubtful accounts and allowances of $13,829,000 at December 31, 1979, and $14,332,000 at December 31, 1978.

(d) Long-term Contracts

Costs associated with long-term contracts are accumulated in work in process inventory and include both direct and indirect costs. Direct costs include, among other things, direct labor, field labor, drafting, subcontracting and direct materials. Indirect costs consist primarily of manufacturing overhead. General and administrative expenses are not inventoried. Inventoried costs relating to long-term contracts, less amounts attributed to earned billings or sales, aggregated $171,726,000 at December 31, 1979 and $152,036,000 at December 31, 1978 (Note 1e).

Profits on long-term contracts for financial reporting purposes are recorded principally on the basis of the estimated stage of completion. However, no profits are recorded on contracts for equipment manufactured in the Company's plants prior to billing the customer and in most cases prior to shipment of the equipment. These contracts extend over a period of several months to four or more years. Revisions in cost estimates during the progress of work under long-term contracts have the effect of including in subsequent accounting periods adjustments necessary to reflect the results indicated by the revised estimates of final cost. Projected or realized losses under long-term contracts, if any, are provided for in the period when first determined.

At December 31, 1979 and 1978, accounts receivable included (a) balances billed but not paid by customers under retainage provisions in long-term contracts and (b) receivables under long-term contracts which were not billable (primarily retainages which will be billed upon completion and acceptance of the equipment). The approximate amounts involved in these categories are shown below:

December 31	1979	1978
Billed but unpaid retainage	$ 14,171,000	$ 15,870,000
Unbilled receivables (primarily retainages)	91,606,000	82,628,000
	$105,777,000	$ 98,498,000
Less — amounts included in unearned billings	(75,323,000)	(72,413,000)
	$ 30,454,000	$ 26,085,000

Approximately $20,309,000 of the $30,454,000 shown above at December 31, 1979 is expected to be collected during 1980.

(e) Inventories

Inventories at December 31, 19[illegible] aggregated $436,840,000. Inventories at December 31, 1979 and 1978, are summarized below:

December 31	1979	1978
Inventoried costs relating to long-term contracts		
[illegible]	$[illegible]	$152,936,000
Raw materials and supplies	69,770,000	76,062,000
Other work in process	185,236,000	150,807,000
Finished goods	101,637,000	79,735,000
	$528,369,000	$458,640,000

Inventoried costs relating to long-term contracts are priced at the lower of cost (average or actual) or market. Reference should be made to Note 1d regarding accounting for long-term contracts.

Inventories of raw materials and supplies, other work in process and finished goods are priced at the lower of cost or market. Such inventories include, among other things, material costs, direct labor and indirect costs (primarily manufacturing overhead). Costs were determined using the average cost-in, first-out (FIFO) and last-in, first-out (LIFO) methods of pricing. In general, domestic inventories other than [illegible] at locations involved in long-term [illegible] are priced at cost, basically using the LIFO method.

[illegible] of current cost over the carrying [illegible] of inventories valued on a LIFO method basis was $50,900,000 at December 31, 1979 and $42,400,000 at December 31, 1978.

(f) Translation of Foreign Currencies

The foreign currency amounts with respect to subsidiary companies and companies which are carried at equity in net assets are translated in terms of United States dollars as follows: assets (other than inventories and net fixed assets) and liabilities at the rates of exchange at the respective year-ends; inventories and net fixed assets at historical rates of exchange; and income and expenses at the average rates of exchange during the years.

Gains or losses from foreign currency translation and from exchange transactions are credited or charged to income currently. Such exchange adjustments are included in the Consolidated Statement of Income (primarily charged to cost of sales in 1978 and interest income in 1979) and aggregated a net loss of $2,966,000 and $4,952,000 in 1979 and 1978, respectively.

(g) Property, Plant and Equipment

Land, buildings, machinery and equipment are carried at cost. Depreciation expense generally is calculated on the straight-line basis for financial reporting purposes and on accelerated methods for income tax purposes; annual rates for major items being from 5% to 10% for machinery and equipment and from 2% to 4% for buildings.

Expenditures for maintenance, repairs, renewals and betterments which do not materially prolong the useful life of the asset or are of a minor nature are generally charged to costs and expenses. When an item or unit of property is retired or substantial betterments result from major repair or renewal, the cost of the replaced property is retired and the cost of the replacing property is capitalized. At the time properties are retired or otherwise disposed of, the reserves for depreciation are charged with accumulated depreciation applicable to such assets. The difference between the amounts at which such assets are carried (less accumulated depreciation) and the proceeds, in the case of sales of property, is charged or credited to income.

(h) Research and Development Costs and Intangible Assets

Company sponsored research and development expense relating to the development of new products or services or the improvement of existing products or services aggregated $37,700,000 in 1979 and $32,000,000 in 1978.

Costs incurred in connection with research and development work generally are expensed as incurred. However, patents and other costs of product development which arise from acquisitions are amortized over their estimated lives. Goodwill arising from certain prior year acquisitions accounted for as purchase transactions (Vetco Inc., Gray Tool Company and National Tank Company) is being amortized over forty years.

(i) Accrued Liabilities

Accrued liabilities included the following:

December 31	1979	1978
Payroll, salaries and commissions	$ 71,185,000	$ 56,262,000
Advances on long-term contracts	164,468,000	167,260,000
Other	183,257,000	147,653,000
	$418,910,000	$371,175,000

(j) Pension Costs

The Company and its subsidiaries have retirement plans or make contributions to union pension plans which cover substantially all their employees. Certain of the plans are entirely non-contributory and others permit or require employee contributions toward the cost of current service benefits. The benefits for employees are determined under the terms of the plans which take into consideration, among other things, years of credited service and, in certain cases, earnings of employees. Generally, pensions are covered by funds invested by trustees and by policies issued by insurance companies. The unfunded cost of past service benefits at December 31, 1979 is estimated at $171,483,000. At December 31, 1979, the actuarially computed value of vested benefits exceeds the fund assets and balance sheet accruals by approximately $102,943,000. The increases in the foregoing amounts during 1979 of $41,179,000 and $25,193,000, respectively, were due primarily to increased benefit levels for a significant portion of the covered salaried and hourly employees and to the acquisition of Basic Incorporated.

Amounts accrued and charged to costs and expenses with respect to such plans aggregated $41,710,000 in 1979, and $32,995,000 in 1978, which include, as to certain of the plans, amortization of the past service costs generally over a thirty-year period. It is the policy of the Company and its subsidiaries to fund their accrued pension costs.

(k) Income Taxes

The provision for Federal, state and foreign taxes on income is summarized below:

	1979	1978
United States	$63,267,000	$54,240,000
Foreign*	17,510,000	19,516,000
State	8,163,000	4,944,000
	$88,940,000	$78,700,000

*Includes foreign taxes payable by United States subsidiaries doing business in foreign countries.

The provision consists of:

	1979	1978
Provision for income taxes estimated to be currently payable	$47,658,000	$ 6,520,000
Provision for deferred income taxes resulting from timing differences	38,213,000	71,145,000
Provision for deferred investment tax credit, less amortization	3,069,000	1,035,000
	$88,940,000	$78,700,000

The effective income tax rate was 47.7% in 1979 and 49.5% in 1978. The effective tax rate differed from the United States income tax rate of 46% (48% in 1978) primarily because of amortization of the investment tax credit, percentage depletion allowance in excess of cost depletion, state and foreign income taxes, equity in earnings and losses of associated and other companies and foreign currency translation losses.

Deferred income taxes result from timing differences in reporting the following items for tax and financial statement purposes:

	1979	1978
Profit recognized on long-term contracts on percentage of completion basis for financial statement purposes and on completed contract basis for income tax purposes	$31,000,000	$65,000,000
Excess of depreciation using accelerated methods for tax purposes over straight-line basis for financial reporting purposes	6,114,000	7,148,000
Other	1,099,000	(1,003,000)
	$38,213,000	$71,145,000

The Company follows the practice of amortizing the investment tax credit over the estimated lives of the applicable property additions, rather than in the year the additions are placed in service. At December 31, 1979, the unamortized balance of the investment tax credit was $17,016,000.

Provision has been made for United States income taxes that may be due on the portion of the earnings of consolidated foreign subsidiaries which is expected to be remitted. Undistributed earnings intended to be reinvested indefinitely in foreign subsidiaries totaled $45,500,000 at December 31, 1979.

2. Acquisitions

In early 1979, the Company acquired substantially all of the outstanding common and 5% convertible preference shares of Basic Incorporated for approximately $74,000,000. Basic Incorporated is an integrated producer of refractory materials, specialized chemicals and a manufacturer of electronic products.

The Company's investment in Basic Incorporated has been allocated to the various tangible and intangible assets acquired. Property, plant and equipment acquired in this transaction are being amortized based on their fair market values and estimated useful lives.

The operations of Basic Incorporated have been included in the accompanying Consolidated Statement of Income beginning with the month of February 1979. If the operations of the Company for 1978 had been consolidated with those of Basic Incorporated, the pro-forma consolidated net sales would have been $2,418,077,000. After giving effect to pro-forma adjustments for interest expense, depreciation expense, amortization of intangibles and income taxes, the pro-forma consolidated net income would have been $83,153,000 ($5.12 per share) in 1978. The Company's operating results for 1979 have not been restated on a pro-forma basis because the amounts involved are not significant.

In January 1979, the Company acquired two other companies, issuing 166,497 shares of common stock (net of escrow shares returned to Treasury) for one and paying $3,175,000 in cash for the other company. Since these acquisitions have also been treated as purchases for accounting purposes, results of their operations from the dates of acquisition have been included in the accompanying Consolidated Statement of Income. Also during 1979, the Company purchased additional shares of Yara Engineering common stock for $9,323,000 which increased its equity to approximately 44%.

3. Joint Venture

During 1976, The Lummus Company, a wholly owned subsidiary, entered into a Joint Venture Agreement with Thyssen Rheinstahl Technik G.m.b.H., a member of the Thyssen A.G. Group, for the purpose of performing a $1,100,000,000 lump sum turnkey contract awarded to them by the Ministry of Industry and Minerals of the Government of Iraq. The contract requires the partners to perform engineering, design, procurement, construction, training and initial operations for a petrochemical plant in Iraq. The Joint Venture Agreement provides for certain limits of Lummus' financial responsibility for the project.

Engineering and other services being performed by The Lummus Company in connection with the Joint Venture are not included in sales for 1979 or 1978 as the Company's interest in the Joint Venture operating results will be accounted for by means of the equity method of accounting. As of December 31, 1979, engineering, procurement and material deliveries are substantially completed, with construction expected to be completed in stages during 1980. Upon completion of the plant, the Joint Venture will be responsible for start-up, final training of personnel and initial operations. The Company anticipates that recognition of its share of Joint Venture profits will commence as mechanical construction nears completion.

The Joint Venture's total assets of $1,000,000,000 as of December 31, 1979, which are not consolidated with those of the Company, consist primarily of costs expended to date and the balance of cash received under the terms of the contract.

4. Short-term Borrowings

Notes payable and current portion of long-term debt included the following:

December 31	1979	1978
Notes payable to banks	$ 6,274,000	$1,139,000
Current portion of long-term debt	5,339,000	3,364,000
	$11,613,000	$4,503,000

The weighted average interest rate for notes payable to banks was approximately 15% at December 31, 1979, and 10% at December 31, 1978. The maximum amount of notes payable to banks outstanding at any month-end was $6,274,000 in 1979, and $10,834,000 in 1978.

Lines of credit established at various banks in the United States aggregated $95,000,000 at December 31, 1979. The amounts borrowed are generally repayable on a short-term basis with interest at the prevailing prime rate.

5. Long-term Debt

Long-term debt consisted of the following:

December 31,	1979	1978
7.45% Sinking Fund Debentures due 1996, sinking fund requirement of $3,335,000 annually from 1982 to 1995	$ 50,000,000	$ 50,000,000
6⅜% (as amended in January, 1980) Sinking Fund Debentures due 1992, less debentures held in treasury of $2,511,000 in 1979 and $2,742,000 in 1978; sinking fund requirement of $2,222,000 annually to 1980 and thereafter $2,750,000 annually to 1991	34,157,000	36,148,000
Capitalized lease obligations, payable through 2001 (Note 6)	23,172,000	19,594,000
9½% Note payable, $1,000,000 annually from 1980 to 1983 and $2,000,000 annually thereafter	20,000,000	20,000,000
Notes and other term payables	22,396,000	17,261,000
	$149,725,000	$143,003,000
Less-Current portion	5,339,000	3,364,000
	$144,386,000	$139,639,000

The Sinking Fund Debentures are direct unsecured obligations of the Company and are redeemable at the option of the Company, as a whole or in part, at any time prior to maturity at redemption prices as set forth in the respective Indentures, plus accrued interest to the redemption date.

In January 1980, the Company received the required consents from holders of its 5⅞% Sinking Fund Debentures due 1992 to amend the Indenture under which these debentures were issued in 1967. In general, the amendments conform certain covenants contained in the Indenture to those of the Indenture under which the 7.45% Sinking Fund Debentures due 1996 were issued in 1971. In addition, the amendments increased the interest rate from 5⅞% to 6⅜%, effective from January 15, 1980, and increased the mandatory annual sinking fund payment from $2,222,000 to $2,750,000 beginning with the July 15, 1981 sinking fund payment.

Certain of the Indentures under which the long-term debt was issued provide, among other things, for restrictions on the payment of cash dividends and the incurrence of funded debt. Under the most restrictive condition, as amended pursuant to consents received in January, 1980, the amount of consolidated retained earnings not restricted as to payment of cash dividends at December 31, 1979, was $363,420,000. Under the most restrictive condition, as amended, neither the Company nor any restricted subsidiary may become liable for any Senior Funded Debt, with certain exceptions, unless immediately thereafter Consolidated Net Tangible Assets will aggregate at least 200% of Consolidated Senior Funded Debt.

Annual maturities of total long-term debt, other than capitalized lease obligations, approximate $4,015,000, $6,080,000, $9,710,000, $9,448,000 and $10,539,000 for the years 1980 through 1984, respectively.

Notes and other term payables consisted of loans and mortgages payable by the Company and its subsidiaries. The weighted average interest rate on such payables is approximately 9.4% per annum. Certain fixed assets were pledged to secure $4,721,000 of term payables at December 31, 1979.

6. Long-term Leases

Total rent, other than on capital leases, charged to expense was $43,355,000 in 1979, and $37,280,000 in 1978.

At December 31, 1979, the approximate minimum future payments under capital leases and noncancelable operating leases are as follows:

	Capital Leases	Noncancelable Operating Leases
1980	$ 2,989,000	$ 24,416,000
1981	3,207,000	19,343,000
1982	2,909,000	15,152,000
1983	2,864,000	11,385,000
1984	2,877,000	8,120,000
After 1984	22,033,000	30,976,000
Total minimum lease payments	$36,879,000	$109,392,000
Less—Estimated executory costs	1,065,000	
Net minimum lease payments	$35,814,000	
Less—Amount representing interest	12,642,000	
Present value of net minimum lease payments	$23,172,000	

7. Stock Option Plan

The "1970 Stock Option Plan", as amended, provides for the granting, to officers and other salaried employees of the Company and its subsidiaries and employees of operations acquired by the Company, of options to purchase shares of its common stock at the market price of the stock on the dates of grant. Amendments to the "1970 Stock Option Plan", in 1979, extended the expiration date to April 24, 1989 (formerly April 28, 1980), increased the number of shares authorized for options from 600,000 to 1,200,000 and provided for the granting of stock appreciation rights.

Options granted in 1972 under the "1970 Stock Option Plan" were five-year qualified options and ten-year tandem options, and those granted in 1979 and 1978 were ten-year non-qualified options.

In 1979 and 1978, stock appreciation rights relating to 14,500 and 241,750 shares, respectively, were granted and are outstanding at December 31, 1979. Stock appreciation rights entitle the optionee to receive an amount equal to the difference between the option price and the fair market value on the exercise date for the number of shares for which the stock appreciation right is exercised. The payment may be made in shares, cash, or a combination of both, at the discretion of the Compensation Committee of the Board of Directors. The stock appreciation rights become exercisable on the date that the related stock options become exercisable. However, as to rights granted in 1978 in connection with existing non-qualified options, such rights became exercisable six months from the date of stockholder approval. Appreciation of outstanding rights resulted in charges against earnings of $6,000,000 in 1979.

The stock options granted in 1979 and 1978 are exercisable twelve months from date of grant. A summary of option transactions during the years 1978 and 1979 is shown below:

	Number of Shares	Option Price Per Share	Option Price Total	Market Price*
Year ended December 31, 1978:				
Granted	440,248	$34.00	$14,968,432	$14,968,432
Expired	(118,236)	36.88-39.00	4,374,536	
Year ended December 31, 1979:				
Granted	12,500	$37.75	$ 471,875	$ 471,875
Became exercisable	434,748	34.00	14,781,432	25,432,758
Exercised	(13,866)	34.00-39.00	527,694	714,223
Cancelled	(9,250)	34.00-39.00	333,250	
At December 31, 1979:				
Outstanding	54[illegible],382	$34.00-39.00	$19,171,613	
Available for future grants	59[illegible],023			

*At the dates options were granted, became exercisable or were exercised.

8. Capital Stock

(a) Series A Convertible Preferred Stock

The Series A Convertible Preferred Stock was redeemed on July 24, 1978, at the redemption price of $45 per share. Changes during 1978 in the Series A Convertible Preferred Stock issued and in the treasury were as follows:

	Preferred Stock			
	Issued		Treasury Stock	
	Shares	Amount	Shares	Amount
Balance at December 31, 1977	240,248	$ 1,490,618	54,930	$48,293
Conversion into common stock	(224,157)	(1,390,784)	(54,930)	(48,293)
Redeemed	(16,091)	(99,834)	—	—
Balance at December 31, 1978	—	—	—	—

(b) Common Stock

Changes during 1978 and 1979 in common stock issued and in the treasury, as included in the accompanying Consolidated Balance Sheet, were as follows:

	Common Stock			
	Issued		Treasury Stock	
	Shares	Amount	Shares	Amount
Balance at December 31, 1977	15,978,112	$60,919,295	110,580	$11,474
Conversion of Series A Convertible Preferred Stock	302,499	1,395,272	74,155	48,293
Transfer from retained earnings in connection with redemption of Series A Convertible Preferred Stock	—	99,834	—	—
Transfers in connection with a pooling of interests in:				
1978	—	70,000	(69,371)	—
a prior year	—	—	8,491	—
Balance at December 31, 1978	16,280,611	$62,484,401	123,855	$59,767
Issued in connection with an acquisition	199,995	4,539,287	—	—
Return to treasury of escrow shares	—	(1,134,744)	33,498	—
Exercise of stock options	—	527,694	(13,866)	—
Balance at December 31, 1979	16,480,606	$66,416,638	143,487	$59,767

9. Incentive Compensation Plan

The Company's Incentive Compensation Plan was approved by the stockholders in 1941 and, as amended, in 1968. The Plan provides that in any fiscal year there may be allocated an amount for use in the Plan determined by a formula, but subject to certain limitations. The Compensation Committee of the Board of Directors, comprised of non-participants in the Plan, subject to the approval of the Board of Directors, allocates the amount to be used for the purpose of the Plan in any one year and determines the participants from among the officers and other key salaried employees and the amount of their participation. The amounts allocated to the Incentive Account aggregated $6,000,000 in 1979 and $4,500,000 in 1978.

10. Quarterly Financial Data (Unaudited)

Summarized unaudited quarterly financial data for the years 1979 and 1978 is as follows

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
1979				
Net sales	$582,789,000	$675,781,000	$684,881,000	$814,053,000
Operating income	$ 32,110,000	$ 42,345,000	$ 35,186,000	$ 61,104,000
Net income	$ 18,096,000	$ 23,036,000	$ 21,494,000	$ 35,012,000
Net income per share	$ 1.11	$ 1.42	$ 1.30	$ 2.13
1978				
Net sales	$491,923,000	$623,709,000	$559,072,000	$657,047,000
Operating income	$ 27,080,000	$ 37,411,000	$ 30,279,000	$ 52,674,000
Net income	$ 14,985,000	$ 19,726,000	$ 17,278,000	$ 28,327,000
Net income per share	$ .93	$ 1.22	$ 1.08	$ 1.74

11. Net Income per Share

Net income per share was based on the average number of common shares outstanding, including, in 1979, the assumed exercise of outstanding stock options, and, for the period prior to redemption in 1978, common shares issuable on conversion of the Series A Convertible Preferred Stock.

12. Pending Litigation

In May 1975 three utility companies filed a complaint against the Company and certain other defendants alleging that the Company is liable for breach of contract, breach of warranties, negligence and other claims in connection with the supply and erection of a fossil fueled electric generating plant in New York known as the Roseton Plant. Damages are claimed against all defendants in an unspecific amount alleged to be in excess of $125 million, the major part of which appears to be for consequential damages. The case continues to be in the pretrial discovery phase.

In the past several years, several thousand claimants have brought suit against industrial corporations for serious personal and fatal injuries allegedly resulting from exposure to insulation products containing asbestos. The Company has not manufactured such products for a number of years. The Company has been included as a defendant in approximately 1,900 of such claims, of which approximately 1,000 were asserted in 1979. It can be expected that a substantial number of additional asbestos related claims will continue to be asserted against the Company.

Although the amount of liability, if any, at December 31, 1979, with respect to the actions then pending to which the Company and its subsidiaries are party cannot be ascertained, in the opinion of the Company, any resulting liability will not materially affect the Company's consolidated financial statements.

13. Contingent Liabilities and Commitments

The Company and certain subsidiaries are contingently liable under guarantees and on discounted notes receivable arising in the ordinary course of business. The financial risk involved is not material in relation to the consolidated financial position.

14. Estimated Replacement Cost (Unaudited)

The Company's 1979 annual report on Form 10-K filed with the Securities and Exchange Commission includes additional information (required by the SEC) with respect to the estimated current replacement cost of plant and equipment and certain inventories at December 31, 1979 and 1978, and the related estimated effect of such costs on cost of sales and depreciation and amortization for the years then ended. This data differs from the historical cost/constant dollar information which is required to be furnished in the Company's annual report to shareholders for 1979.

15. Financial Reporting by Business Segments

The Company's equipment, products and services are classified into the following business segments: (a) design, manufacture, installation and service of steam generating systems and equipment for the electric utility industry including nuclear steam supply systems; (b) design, engineering and construction services (principally through a subsidiary, The Lummus Company), primarily for the chemical, petrochemical and petroleum industries; (c) equipment supplied to industrial markets and (d) products and services supplied to industrial markets.

(a) The following tables present financial data by business segment:

	1979	1978	1977
Sales (1)—			
Steam generating systems, equipment and services for the electric utility industry	$ 926,220,000	$ 815,767,000	$ 747,808,000
Design, engineering and construction services	351,719,000	308,438,000	300,698,000
Equipment for industrial markets	815,563,000	688,815,000	605,338,000
Products and services for industrial markets	664,002,000	518,731,000	389,920,000
Total	$2,757,504,000	$2,331,751,000	$2,044,764,000
Operating Profit—			
Steam generating systems, equipment and services for the electric utility industry	$ 65,166,000	$ 56,985,000	$ 46,451,000
Design, engineering and construction services	27,979,000	27,663,000	24,664,000
Equipment for industrial markets	81,167,000	62,823,000	53,477,000
Products and services for industrial markets	25,948,000	20,819,000	13,147,000
Total	$ 200,260,000	$ 168,290,000	$ 137,739,000
Equity in Net Earnings of Associated and Other Companies (2)	4,340,000	1,397,000	1,775,000
Interest Expense	(15,663,000)	(18,400,000)	(11,563,000)
Unallocated—			
Corporate expense	(16,356,000)	(14,443,000)	(12,141,000)
Miscellaneous, net	15,000,000	22,172,000	17,199,000
Consolidated income before income taxes	$ 186,581,000	$ 159,016,000	$ 133,009,000

December 31,	1979	1978	1977
Identifiable Assets—			
Steam generating systems, equipment and services for the electric utility industry	$ 432,133,000	$ 385,962,000	$ 358,021,000
Design, engineering and construction services	151,989,000	135,746,000	135,230,000
Equipment for industrial markets	548,756,000	515,815,000	550,387,000
Products and services for industrial markets	451,069,000	349,927,000	334,883,000
Total	$1,583,947,000	$1,387,450,000	$1,378,521,000
Investments in Associated and Other Companies (Equity Basis) (2)	50,713,000	33,172,000	20,988,000
Corporate and Unallocated Assets, net (3)	448,300,000	416,325,000	254,765,000
Consolidated	$2,082,960,000	$1,936,947,000	$1,654,274,000

1. Includes only sales to unaffiliated customers (intersegment sales are not significant) and no single customer accounts for 10% or more of the consolidated sales.

2. Companies accounted for under the equity method of accounting (20% or more owned) are located principally in the United States, Europe and other foreign areas. The principal companies included in this category are not vertically integrated with the operations of the Company and its consolidated subsidiaries. Such companies are engaged in the manufacture and sale of steam generating equipment for utility and industrial use and other equipment, products and services for industrial markets.

3. Includes primarily cash, marketable securities and corporate facilities.

Depreciation and amortization by business segment for the years 1979, 1978 and 1977 were as follows: (a) steam generating systems, equipment and services for the electric utility industry $18.0 million, $12.2 million and $11.8 million; (b) design, engineering and construction services $3.3 million, $3.7 million and $2.9 million; (c) equipment for industrial markets $22.3 million, $20.1 million and $12.2 million and (d) products and services for industrial markets $21.6 million, $16.0 million and $12.2 million. Similar amounts charged to corporate and unallocated assets were $.9 million in the year 1979, $.6 million in the year 1978 and $.5 million in the year 1977.

Capital additions by business segment for the years 1979, 1978 and 1977 were as follows: (a) steam generating systems, equipment and services for the electric utility industry $20.7 million, $13.9 million and $17.0 million; (b) design, engineering and construction services $9.2 million, $5.3 million and $4.3 million; (c) equipment for industrial markets $22.4 million, $23.2 million and $85.8 million and (d) products and services for industrial markets $94.5 million, $32.5 million and $15.0 million.

(b) Significant financial data by geographic area follows (1)

	1979	1978	1977
Sales (2)—			
United States	$2,234,650,000(3)	$1,851,973,000(4)	$1,646,731,000(5)
Canada	191,107,000	163,706,000	169,860,000
Europe	259,950,000	234,134,000	181,419,000
Other Foreign	71,797,000	81,938,000	46,754,000
Total	$2,757,504,000	$2,331,751,000	$2,044,764,000
Net Income—			
United States	$ 71,867,000	$ 60,356,000	$ 52,762,000
Canada	13,552,000	9,639,000	5,670,000
Europe	7,357,000	7,538,000	6,309,000
Other Foreign	4,845,000	2,783,000	2,448,000
Total	$ 97,641,000	$ 80,316,000	$ 67,189,000

December 31	1979	1978	1977
Identifiable Assets—			
United States	$1,213,796,000	$1,022,587,000	$ 991,094,000
Canada	118,962,000	121,426,000	112,174,000
Europe	200,418,000	177,390,000	211,609,000
Other Foreign	50,771,000	66,047,000	63,644,000
Total	$1,583,947,000	$1,387,450,000	$1,378,521,000

1. Data presented for geographic areas outside of the United States includes operations of foreign subsidiaries and operations of domestic subsidiaries located in foreign areas.

2. Includes only sales to unaffiliated customers (intergeographic sales are not material).

3. Includes export sales of $258,901,000 of which $19,989,000, $47,703,000 and $191,209,000 represent sales to customers in Canada, Europe and other foreign countries, respectively.

4. Includes export sales of $193,052,000 of which $11,686,000, $50,228,000 and $131,138,000 represent sales to customers in Canada, Europe and other foreign countries, respectively.

5. Includes export sales of $189,630,000 of which $9,041,000, $50,842,000 and $129,747,000 represent sales to customers in Canada, Europe and other foreign countries, respectively.

Auditors' Report

To the Board of Directors and Stockholders of Combustion Engineering, Inc.:

We have examined the consolidated balance sheets of Combustion Engineering, Inc. (a Delaware corporation) and subsidiary companies as of December 31, 1979 and 1978, and the related consolidated statements of income, retained earnings and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated balance sheets and consolidated statements of income, retained earnings and changes in financial position present fairly the financial position of Combustion Engineering, Inc. and subsidiary companies as of December 31, 1979 and 1978, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

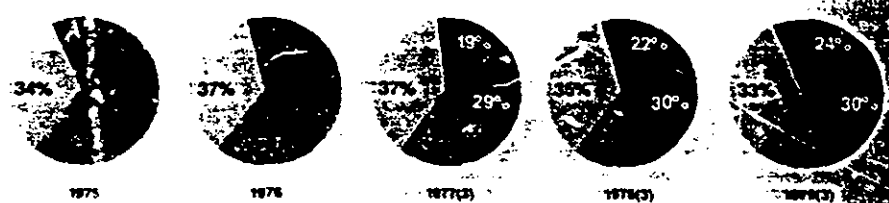
Arthur Andersen & Co.

Stamford, Connecticut
February 13, 1980

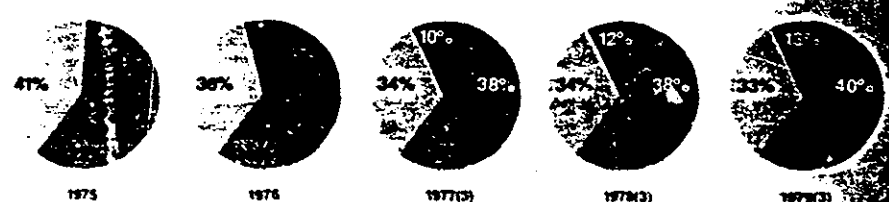
Lines of Business and Brief Description of the Business

The Company's products and services are classified in the following categories according to general markets served: (a) design, manufacture, installation and service of steam generating systems and equipment for the electric utility industry, including nuclear steam supply systems; (b) design, engineering and construction services (principally through its subsidiary, The Lummus Company), primarily for the chemical, petrochemical and petroleum industries; and (c) equipment, products and services supplied to industrial markets. The relative contributions to consolidated net sales and to income from operations before income taxes and extraordinary items by lines of business for the years 1975 through 1979 are shown in the following charts:

Relative Contribution to Net Sales



Relative Contribution to Earnings from Operations(1)



Steam generating systems, equipment and services for the electric utility industry supplied by the Power Systems Group.

Design, engineering and construction services provided by the Engineering Group.

Equipment, products and services supplied to industrial markets by the Industrial Products, Process Equipment and Power Systems Groups and C-E Glass (see Notes 2 and 3).

(1) Before taking into consideration the following: interest expense; interest earned on marketable securities; equity in earnings (losses) of associated and other companies; minority interests in earnings (losses) of subsidiaries; Corporate unallocated expenses and other income and (deductions); and income taxes.

(2) None of the Company's equipment, products or services supplied to industrial markets contributed 10% or more to the Company's consolidated net sales.

(3) See Note 15 of the Notes to Financial Statements. For 1977, 1978 and 1979, the equipment, products and services category is shown as:

- Equipment for industrial markets, and
- Products and services for industrial markets.

Steam Generating Systems, Equipment and Services for the Electric Utility Industry

Power Systems Group supplies steam generating systems, equipment and services for the electric utility industry. In the fossil field, the Company designs, manufactures and installs systems and equipment fueled by coal, natural gas or oil; including natural circulation, controlled circulation and combined circulation types. In the nuclear field, the Company designs, manufactures and supplies complete pressurized water nuclear steam supply systems, including the fabrication of nuclear fuel. The foregoing systems and equipment are sold principally to electric utilities and to prime contractors for electric utilities.

Design, Engineering and Construction Services

Engineering Group designs, engineers and constructs chemical process plants, petroleum refineries and other industrial facilities for the petrochemical, metallurgical, pulp and paper and other process industries. This Group also provides engineering, design and project management technology related to the development and production of crude oil and natural gas; and designs, manufactures and installs gas processing and conditioning plants.

Equipment, Products and Services for Industrial Markets

Several Groups and C-E Glass supply equipment, products and services for industrial markets, the most significant of which are shown below.

Equipment

Industrial Products Group—

- Equipment for the metal casting industry
- Screening equipment for general industrial applications

Process Equipment Group—

- Field production processing equipment for the oil and natural gas industries
- Oilfield equipment, primarily wellhead assemblies and high pressure pipe connections
- Subsea oil and gas field drilling and production equipment, and specialized equipment for use on mobile drilling rigs
- Gas-to-gas heat exchangers sold to manufacturers of steam generating equipment and others
- Equipment for the pulp and paper industry
- Grinding equipment and pulverizers for general industrial applications

Power Systems Group—

- Steam generating equipment and services for general industrial applications
- Nuclear reactor vessels and other nuclear components sold to manufacturers of steam generating equipment and for use in research projects

Products and Services

Industrial Products Group—

- Wood doors, windows and other building products
- Electronic assemblies for the communications industry
- Specialty refractories and refractory products for the steel, aluminum, glass and other industries
- Wire cloth and screening for general industrial applications and for paper mills
- Industrial minerals mined and processed by the Company for itself and others
- Foundry chemicals, washes and supplies

Process Equipment Group—

- Erection, retrofit and general contracting in oil and gas field production and processing plants
- Specialty chemicals for use in oil and gas production processing
- Carbon, alloy and stainless steel forgings
- Coating, inspection and other services primarily for the oil and gas industry

C-E Glass—

- Automotive and architectural glass



Supplementary Information Concerning the Impact of the Changes in the General Level of the Purchasing Power of the Dollar (Unaudited)

Introduction

In September, 1979, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 33, Financial Reporting and Changing Prices (FAS 33). The Statement requires large, publicly held companies to include certain information concerning the impact of inflation as a supplement to the customary financial information in the annual report. This Statement acknowledges the need for experimentation in providing information on the effects of inflation, as well it might.

FAS 33 requires the calculation and statement of an adjusted net income amount (presumably for comparison with net income as reported in the accompanying Consolidated Financial Statements). It is to be noted that the predecessor to FAS 33, namely, the Securities and Exchange Commission Accounting Series Release No. 190, issued in March, 1976, dealing with the same general subject of inflation-adjusted amounts, made no attempt to determine an adjusted net income and actually cautioned against simplistic use for this purpose of the data presented.

The objectives of FAS 33 are to be accomplished in a two-step approach: a general indexing approach called constant dollar accounting, and a specific pricing method called current cost accounting. Only constant dollar accounting information is being presented herein. Current cost calculations will be furnished beginning with the year 1980.

FAS 33 Requirements

FAS 33 requires certain historical cost dollar amounts to be adjusted to amounts which have purchasing power equivalent to that of the average dollar for 1979. This is to be accomplished by indexing certain historical cost amounts using the Consumer Price Index for All Urban Consumers (CPI). It should be noted that the CPI is not necessarily representative of the actual impact of inflation on the Company's costs. In addition, the constant dollar information does not purport to represent appraised value, current cost value or replacement cost of the related assets.

In determining "income from continuing operations on a historical cost/constant dollar" basis, adjustments are to be made for the effects of depreciation and amortization and cost of sales that result from applying the indexing process to property, plant and equipment and certain inventory. Also, the related required disclosure of "net assets at end of year on a historical cost/constant dollar" basis is similarly only to be adjusted by the effects of indexing net property, plant and equipment and inventory.

FAS 33 requires the estimation of the "purchasing power gain (loss) on net monetary items." Monetary items are those assets or liabilities which are stated in dollars that are fixed or determinable without reference to future prices. All other assets and liabilities are considered to be non-monetary. Monetary assets and liabilities depend heavily on the general purchasing power of the dollar and its decrease in value during periods of inflation. Holders of net monetary assets lose purchasing power during inflationary periods since these assets will purchase fewer goods and services in the future; conversely, a person with net monetary liabilities will benefit during periods of inflation because payment of the net liabilities will be in dollars having a lesser value.

Inflation Adjusted Data for 1979

The following table presents a reconciliation between net income as shown in the accompanying Consolidated Financial Statements and net income adjusted to a historical cost/constant dollar basis, and sets forth the purchasing power gain on net monetary liabilities for the year, all as prescribed by FAS 33.

	1979
(Dollars in Thousands)	
Net Income as Shown in the Accompanying Consolidated Financial Statements	$97,641
Adjustments Required by FAS 33 to Restate to Average 1979 Dollars—	
Cost of sales (excluding depreciation and amortization)	(8,692)
Depreciation and amortization	(16,598)
Net Income Adjusted for General Inflation (stated in average 1979 dollars)	$72,351
Purchasing Power Gain on Net Monetary Liabilities	$25,802

As can be seen above, the only adjustments made to net income as reported in the accompanying Consolidated Financial Statements are increases to cost of sales and depreciation and amortization as a result of applying the indexing process to property, plant and equipment and certain inventory. No adjustment to sales has been made.

Nor has adjustment been made to the provision for income taxes included in the adjusted income from continuing operations, as current tax laws do not permit the deduction of the additional costs resulting from inflation. As a result, although the effective income tax rate based on historical cost financial data is 47.7%, after the above adjustments to cost of sales and depreciation and amortization, the effective tax rate would be 55.1%. This higher effective tax rate is indicative of the result of inclusion of inflation adjustments.

The purchasing power gain on net monetary liabilities has not been recognized in the adjusted income from continuing operations. Since the Company is in a net monetary liability position, a significant gain is generated and shown separately. Had such gain been reflected in net income adjusted for general inflation, it would have offset the increased depreciation and amortization and cost of sales resulting from the indexing process.

The following table presents a summary of selected financial data for the years 1975 to 1979 adjusted to average 1979 dollars as measured by the required CPI index.

	1979	1978	1977	1976	1975
(Dollars in Thousands, Except per Share Amounts)					
Net Sales	$2,757,504	$2,595,475	$2,450,337	$2,335,637	$2,308,780
Historical Cost Information Adjusted in Accordance with FAS 33					
Net Income	$ 72,354				
Net Income per Share	4.42				
Net Assets at End of Year	721,688				
Purchasing Power Gain on Net Monetary Liabilities	25,802				
Cash Dividends Declared per Common Share	$ 2.20	$ 2.00	$ 1.80	$ 1.68	$ 1.69
Market Price per Common Share at Year-end	$ 55.98	$ 34.97	$ 43.39	$ 41.80	$ 28.34
Average Consumer Price Index	217.4	195.4	181.5	170.5	161.2

[redacted] Data not required

The Company does not regard the foregoing adjusted net income as a proper reflection of the impact of inflation on its operations or as an indication of the effects of inflation on future cash flows for several reasons:

1. Much of the business of the Company and its subsidiaries results from meeting customer requirements specified under contracts. Such contracts are both long and short-term. The contract price, particularly in the case of long-term contracts, either includes an amount for the estimated increase in the cost of labor, materials and services over the period required for performance of the contract or is subject to adjustment based on a price escalation clause in the contract.

2. With respect to other products and services, the Company and its subsidiaries attempt to recover cost increases by increasing selling prices. Their ability to do so is subject to the limitation of competitive factors, customer demand and the Company's voluntary compliance with federal price guidelines.

3. The use of constant dollar depreciation as required by FAS 33 is a theoretical concept intended to focus attention on the effect of inflation. Depreciation is normally intended only to allocate the original purchase cost over the useful life of the related fixed asset and not to provide for the eventual replacement of property, plant and equipment.

4. Although the cumulative impact of inflation over a number of years has resulted in higher costs for replacement of existing plant and equipment, such inflationary increases have partially been offset by technological improvements and design changes.

5. In the normal course of business, the Company will replace its property, plant and equipment over an extended period of time. Decisions concerning replacement will be made in the light of economic, regulatory and competitive conditions existing on the dates such determinations are made. Therefore, the indexed amounts given effect to herein in accordance with FAS 33 are not meaningful as a measure of future replacement costs.

The underlying concepts of accounting methods which adjust for inflation are not radically new. Management considers relevant economic factors in making basic business decisions. Investors also recognize that inflation affects future cash flows and the capability of a company to continue its operations at the levels it has attained in the past. Interpretation of data such as is required by FAS 33, however, is very much dependent on the facts and circumstances in each case, as well as uncontrollable future events. Therefore, any interpretation of such data without the knowledge of the particular facts and circumstances can be misleading.

Comparative Financial Statistics 1970-1979

	(Dollars in Thousands Except per Share Amounts)	1979(5)	1978
Summary of Operations	Net Sales	$2,757,504	$2,331,375
	Costs and Expenses—		
	Cost of sales	$2,373,357	$2,006,26
	Selling, general and administrative expenses	213,402	178,04
		$2,586,759	$2,184,30
	Operating Income	$ 170,745	$ 147,44
	Other Income and (Deductions)—		
	Interest expense	(16,663)	(18,400
	Miscellaneous, net	32,499	29,972
	Income Before Income Taxes and Extraordinary Items	$ 186,581	$ 159,016
	Taxes on Income	88,940	78,700
	Income Before Extraordinary Items	$ 97,641	$ 80,316
	Extraordinary Items (3)	—	—
	Net Income	$ 97,641	$ 80,316
	Net Income per Share (2)—		
	Income before extraordinary items	$ 5.96	$ 4.97
	Extraordinary items (3)	—	—
	Net income	$ 5.96	$ 4.97
	Average Shares Outstanding (2)	16,371,638	16,171,110
	Cash Dividends Declared—		
	Total	$ 35,892	$ 29,105
	Per share—		
	Common	2.20	1.80
	Preferred	—	.85
Other Financial Statistics	Current Assets	$1,428,639	$1,252,542
	Current Liabilities	1,144,337	978,948
	Working Capital	284,302	273,594
	Property, Plant and Equipment, net	515,983	450,866
	Investments and Other Assets	136,756	132,171
	Deferred Income Taxes and Investment Tax Credit	232,981	222,999
	Long-term Debt	144,386	139,639
	Shareholders' Equity		
	Amount	559,674	493,993
	Per share (4)	34.26	30.58
	Capital Expenditures	$ 146,741	$ 74,901
	Depreciation and Amortization	66,138	52,567
	Orders Received	$2,897,763	$2,298,490
	Unfilled Orders	2,986,465	2,879,929
	Employees	43,286	45,729
	Shareholders of Record	26,742	26,451

See pages 24-26 for Management Discussion and Analysis of the Summary of Operations for the years 1979 and 1978

1. In 1974, the Company changed to the last-in, first-out (LIFO) method of inventory valuation with respect to certain domestic inventories (generally inventories other than those involved in long-term contract work). The LIFO method was adopted because the rapid increase in prices would have resulted in an overstatement of profits if use of the average, or first-in, first-out (FIFO) method were continued, since inventories sold were replaced at substantially higher prices. The effect of this change was to reduce net income for the year 1974 by $5,887,919 equal to $3.32 per share.

2. Net income per share was based on the average number of shares outstanding. Average shares outstanding include (a) the average number of common shares outstanding, (b) common shares issuable on the conversion of the Series A Convertible Preferred Stock, prior to redemption in July, 1972, (c) in the years 1970 through 1974, estimated shares to be released from escrow based on earnings of certain companies subsequent to acquisition and (d) in the years 1971, 1972, 1973 and 1979, the assumed exercise of all outstanding stock options. The average number of shares outstanding in each period has been adjusted where necessary to give effect retroactively to a 2-for-1 stock split in 1970, a 3-for-2 stock split in 1977, and shares issued in connection with significant poolings of interest.

	1977(5)	1976(5)	1975	1974	1973	1972	1971	1970
	$2,044,764	$1,830,925	$1,711,151	$1,428,028	$1,168,578	$1,054,532	$ 960,910	$ 879,204
	$1,776,518	$1,601,773	$1,513,297	$1,253,616	$ 998,987	$ 902,596	$ 819,794	$ 747,439
	145,742	122,117	109,317	94,336	87,484	77,181	69,857	65,984
	$1,922,260	$1,723,890	$1,622,614	$1,347,952	$1,086,471	$ 979,777	$ 899,651	$ 813,423
	$ 122,504	$ 107,035	$ 88,537	$ 80,076	$ 82,107	$ 74,755	$ 71,259	$ 65,781
	(11,563)	(9,989)	(10,119)	(11,704)	(9,561)	(8,643)	(6,273)	(5,964)
	22,068	8,147	5,024	5,472	6,885	6,387	3,845	3,135
	$ 133,009	$ 105,193	$ 83,442	$ 73,844	$ 79,431	$ 72,499	$ 68,831	$ 62,952
	65,820	50,990	38,850	33,660	36,340	32,980	32,100	30,630
	$ 67,189	$ 54,203	$ 44,592	$ 40,184	$ 43,091	$ 39,519	$ 36,731	$ 32,322
	—	—	—	(2,700)	—	(16,000)	—	—
	$ 67,189	$ 54,203	$ 44,592	$ 37,484(1)	$ 43,091	$ 23,519	$ 36,731	$ 32,322
	$ 4.17	$ 3.36	$ 2.77	$ 2.50	$ 2.70	$ 2.48	$ 2.34	$ 2.09
	—	—	—	(.17)	—	(1.00)	—	—
	$ 4.17	$ 3.36	$ 2.77	$ 2.33(1)	$ 2.70	$ 1.48	$ 2.34	$ 2.09
	16,117,125	16,121,660	16,083,514	16,080,781	15,952,219	15,930,967	15,722,697	15,467,769
	$ 24,098	$ 21,188	$ 20,137	$ 18,617	$ 16,320	$ 15,160	$ 14,195	$ 13,237
	1.50	1.316	1.25	1.152	.997	.958	.917	.85
	1.70	1.70	1.70	1.70	1.70	1.70	1.70	1.70
	$1,086,841	$ 876,259	$ 717,029	$ 662,049	$ 523,588	$ 484,278	$ 458,427	$ 388,275
	894,123	663,412	529,623	494,088	373,170	329,435	315,977	281,544
	192,718	212,847	187,406	167,961	150,418	154,843	142,450	106,731
	437,145	358,741	315,850	297,339	266,536	219,096	203,145	182,731
	128,948	54,643	35,977	38,111	40,622	39,976	64,820	65,215
	169,960	99,638	57,802	41,669	14,946	9,557	20,931	19,104
	147,270	128,176	116,497	121,242	121,490	107,116	103,193	75,348
	441,581	398,417	364,934	340,500	321,140	297,242	286,291	260,225
	27.30	24.31	22.12	20.49	19.15	17.64	17.15	15.47
	$ 122,055	$ 81,446	$ 50,621	$ 61,796	$ 57,330	$ 38,747	$ 42,336	$ 35,370
	39,630	33,030	29,653	27,744	23,868	19,765	17,972	15,723
	$2,111,246	$1,738,626	$1,527,288	$2,515,965	$1,999,142	$1,220,497	$ 979,133	$1,130,262
	2,968,556	2,980,098	3,132,481	3,347,114	2,288,011	1,477,500	1,350,050	1,337,121
	44,770	42,843	45,938	40,765	35,316	34,950	33,374	32,645
	26,596	25,536	25,212	24,758	21,305	21,549	21,390	19,252

1. Represents, in 1972 and 1974, a provision for loss on the disposition of the holding in United Nuclear Corporation, less in each case the effect of applicable income taxes ($15,000,000 in 1972 and $2,500,000 in 1974).

2. Based on net assets and common shares outstanding at year-end.

3. Includes Gray Tool Company for periods subsequent to October, 1976, Vetco Inc. for the periods subsequent to November, 1977, and Basic Incorporated for the period subsequent to January, 1979.

The Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission may be obtained after March 31, 1980, by writing to: Secretary, Combustion Engineering, Inc., 900 Long Ridge Road, Stamford, Connecticut 06902.

Management Discussion and Analysis of the Summary of Operations

The following comments are intended to present an overview of the more important matters affecting operating results for the years 1977, 1978 and 1979 as shown on pages 22 and 23, and to provide a comparative summary of the backlog for each of the last three years. Other statistics on Business Segments are contained in Note 15 to the December 31, 1979, Financial Statements and under the caption Lines of Business and Brief Description of the Business on page 18.

1979 Compared to 1978

On a consolidated basis, net sales increased 18% over those in 1978. Sales increases by business segment were as follows: Products and services for industrial markets by 28%; equipment for industrial markets by 18%; steam generating systems, equipment and services for the electric utility industry by 14% and design, engineering and construction services by 14%.

Comments on the principal factors affecting sales in 1979 follow:

(a) Products and services for industrial markets—
The increase in this segment was attributable primarily to increased shipments of refractory and mineral products (including those of Basic Incorporated, which was acquired early in 1979), increased shipments of forgings and other products and services to the oil and gas industry including those furnished by companies acquired in the final quarter of 1978, and increased shipments of automotive and architectural glass. These favorable factors were offset in part by a decline in sales and services caused by the disposition of several companies previously included in this segment.

(b) Equipment for industrial markets—
The increase in this segment was due mainly to increased shipments of oil field equipment (primarily wellhead assemblies, subsea drilling and production equipment, and field production processing equipment), gas-to-gas heat exchangers and pulverizing equipment for general industrial applications, and a higher level of field construction work on industrial steam generating equipment. Sales in 1978 were adversely affected by work interruptions at several major plants due to contract negotiations.

(c) Steam generating systems, equipment and services for the electric utility industry—
The increase in this segment was due mainly to a higher level of activity on nuclear steam supply systems and fuel, higher shipments of air quality control equipment and maintenance parts and increased field construction work on fossil steam generating equipment. Sales in 1978 were adversely affected by work interruptions at several major plants due to contract negotiations.

(d) Design, engineering and construction services—
The increase in this segment was primarily attributable to sales of natural gas processing and conditioning equipment by a company acquired early in 1979. It should be noted that engineering, construction and other services being performed by The Lummus Company in connection with the Joint Venture with Thyssen Rheinstahl Technik G.m.b.H. for the supply of a petrochemical complex to the Government of Iraq are not included in sales (see Note 3 to the Financial Statements).

Cost of sales increased by 18% over that in 1978 primarily as a result of the increase in sales volume and higher costs of material, labor and services. Other significant factors affecting cost of sales and profitability in 1979 were as follows:

(a) Profits from equipment for industrial markets increased over the year 1978 due primarily to increased shipments of oil field production and processing equipment and the lesser effect of acquisition adjustments (primarily with respect to Vetco Inc.) in 1979. These favorable trends were offset in part by lower profits realized in 1979 from shipments of steam generating equipment and equipment for the pulp and paper industry and the metal casting industry caused by various factors in each case, including higher research and development costs, lower profit margins and work interruptions caused by contract negotiations.

(b) Profits from steam generating systems equipment and services for the electric utility industry were higher in 1979 than in 1978 due mainly to reduced losses on overall nuclear activities resulting from an increase in work on nuclear fuel and a decline in provisions for cost and other adjustments to nuclear steam supply system contracts. Adjustments were made in 1979 to recognize the declining level of production in certain nuclear facilities. Profits from fossil steam generating equipment, including construction services, were moderately below the 1978 level due to higher operating expenses.

(c) Profits from products and services for industrial markets increased in 1979 over those in 1978 due principally to the increased shipments of refractory and mineral products, forgings and other products and increased services to the oil and gas industry.

Amortization of the upward adjustment of Basic Incorporated assets to reflect fair market value at the date of acquisition adversely affected the profits of this business segment in 1979. Acquisition adjustments with respect to Vetco coating and inspection services in 1979 were at a lower rate than in 1978.

Profit in 1979 from the distribution of wood building products was below the level of 1978 due in part to competitive market conditions.

(d) Profit on design, engineering and construction services increased slightly over the year 1978. Higher profits on engineering and construction services, primarily on work performed by domestic offices for overseas projects, were offset substantially by unfavorable cost and other adjustments including acquisition adjustments with respect to a company acquired in January, 1979.

Selling, General and Administrative Expenses increased 20% over those in 1978 due primarily to expenses of companies acquired in the latter part of 1978 and the beginning of 1979, and in general, higher staffing, payroll related expenses and other expenses.

Interest Expense declined 9% from that in 1978 due mainly to a reduction in the provision for interest on proposed federal income tax assessments; offset in part by interest on the indebtedness of Basic Incorporated.

Miscellaneous, net increased $2,527,000 in 1979 due mainly to the increase of $2,944,000 in the equity in earnings of associated and other companies. This increase was due largely to the equity interest in Yara Engineering Corporation acquired in 1978 and 1979.

Taxes on Income increased 13% over those in 1978 due to the increase in income before taxes, offset in part by a decline in the statutory United States Federal income tax rate from 48% to 46%.

Unfilled Orders

A summary showing the backlog of unfilled orders by business segment is set forth below:

December 31	1979	1978	1977
Steam generating systems, equipment and services for the electric utility industry	$2,113,591,000	$2,143,242,000	$2,247,887,000
Design, engineering and construction services	270,938,000*	200,329,000*	237,529,000*
Equipment for industrial markets	528,261,000	457,331,000	413,160,000
Products and services for industrial markets	73,675,000	79,027,000	69,980,000
	$2,986,465,000*	$2,879,929,000*	$2,968,556,000*

*The backlog at December 31, 1979, 1978 and 1977, does not include the supply of a $1.1 billion petrochemical complex for the Government of Iraq being performed by the Joint Venture comprised of The Lummus Company and Thyssen Heinstahl Technik, G m b H.

1978 Compared to 1977

On a consolidated basis, net sales increased 14% over those in 1977. Sales increases by business segment were as follows: Products and services for industrial markets by 33%; equipment for industrial markets by 14%; steam generating systems, equipment and services for the electric utility industry by 9% and design, engineering and construction services by 3%.

Comments on the principal factors affecting sales in 1978 follow:

Sales were adversely affected in the year 1978 by work interruptions at several major plants due to strikes related to contract negotiations. The segments most significantly affected by the strikes were steam generating systems, equipment and services for the electric utility industry and equipment for industrial markets. Other comments by business segment follow.

(a) Products and services for industrial markets—
The increase in this segment was attributable primarily to including for a full year the oil field pipe inspection and coating services and other services provided by Vetco Inc. which was acquired in December, 1977, and to increased shipments of wood doors, windows and other building products, refractory and mineral products, foundry materials and supplies and architectural glass.

(b) Equipment for industrial markets—
The increase in this segment was due mainly to shipments of oil field exploration and production equipment (including those of Vetco Inc.) and increased shipments of equipment for the pulp and paper industry. These favorable trends were offset in part by lower shipments of equipment for the metal casting industry and steam generating equipment for industrial use.

(c) Steam generating systems, equipment and services for the electric utility industry—
The increase in this segment was due mainly to higher shipments of fossil fueled steam generating equipment and increased construction services on boiler erection work and maintenance projects. Activity on contracts for nuclear steam supply systems and fuel was approximately the same in both years.

(d) Design, engineering and construction services—
The moderate increase in this segment was primarily attributable to higher activity in domestic offices on process plants, including petrochemical, pharmaceutical and energy-related projects; offset by a general decline in sales of heat transfer equipment. While engineering and procurement services furnished in connection with the Lummus Joint Venture with Thyssen Rheinstahl Technik, G.m.b.H. for the supply of a petrochemical complex to the Government of Iraq were at a lower level in 1978, material deliveries and construction activities increased during the year. It should be noted that engineering and other services furnished in connection with the Lummus Joint Venture are not included in sales as the 50% interest in the Joint Venture will be accounted for by means of the equity method of accounting (see Note 3 to the Financial Statements).

Cost of Sales increased by 13% over that in 1977 primarily as a result of the increase in sales volume, higher costs of material, labor and services and the effect of work stoppages related to contract negotiations. Other significant factors affecting cost of sales and profitability in 1978 were as follows:

(a) Amortization of the adjustment of Vetco Inc. and Gray Tool Company assets to reflect fair market value at the dates of acquisition (Vetco Inc., November, 1977 and Gray Tool Company, October, 1975), particularly the upward valuation of inventories and intangible assets, adversely affected operating results in 1977 and 1978. Amortization of these adjustments in future years will be at a reduced rate.

(b) Profits from the manufacture and distribution of architectural glass, wood doors, windows and other building products improved in 1978 as a result of the increase in housing starts and a strong home improvement market.

(c) Losses on overall nuclear activities decreased in 1978. This was due primarily to provisions in 1977 for cost adjustments and repairs on certain nuclear steam supply system contracts.

Selling, General and Administrative Expenses increased 22% over those in 1977 due primarily to (a) the inclusion of Vetco Inc. expenses for a full year in 1978, (b) higher selling expenses in all business segments and (c) in general, higher staffing, payroll related expenses and occupancy expenses.

Interest Expense increased 59% over that in 1977 due mainly to interest on proposed federal income tax assessments and interest on the indebtedness of Vetco Inc.

Miscellaneous, net increased in 1978 due mainly to higher interest earned as a result of a higher average level of investable funds and higher interest rates.

Taxes on Income increased 20% over those in 1977 due to the increase in income before taxes.

Market Price Range Per Share

	1979		1978	
Common Stock (1)	High	Low	High	Low
First Quarter	$39½	$32⅛	$37¼	$31
Second Quarter	45½	35¼	43¾	33½
Third Quarter	54	44⅜	44⅛	37⅞
Fourth Quarter	59½	43⅛	39¼	31⅜
Preferred Stock (1,2)	High	Low	High	Low
First Quarter	$ —	$ —	$46½	$42½
Second Quarter	—	—	56½	51
Third Quarter	—	—	—	—
Fourth Quarter	—	—	—	—

Quarterly Dividends Declared Per Share

	1979	1978
Common Stock		
First Quarter	$ .50	$ .40
Second Quarter	.55	.45
Third Quarter	.55	.45
Fourth Quarter	.60	.50
Preferred Stock (2)		
First Quarter	$ —	$ .425
Second Quarter	—	.425
Third Quarter	—	—
Fourth Quarter	—	—

1 Traded on the New York Stock Exchange

2 Redeemed on July 24, 1978

Transfer Agents and Registrars

The Chase Manhattan Bank, N.A.
Chase Manhattan Plaza, New York, N.Y. 10015

The Connecticut Bank and Trust Company
Constitution Plaza, Hartford, Conn. 06115

Securities Listing

The Common Stock and 7.45% Sinking Fund Debentures Due 1996 are listed on the New York Stock Exchange

Combustion Engineering, Inc.

Corporate Headquarters:
900 Long Ridge Road, Stamford, Conn. 06902
Telephone (203) 329-8771

12/31/79

Combustion Engineering, Inc.
900 Long Ridge Road
Stamford, Connecticut 06902

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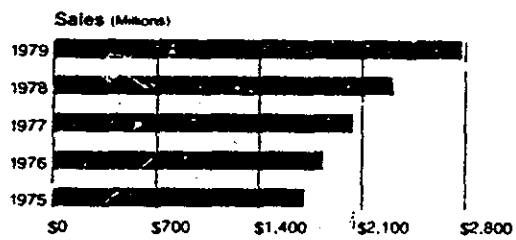
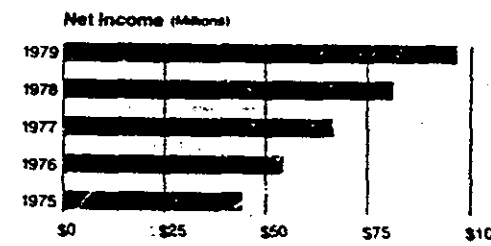
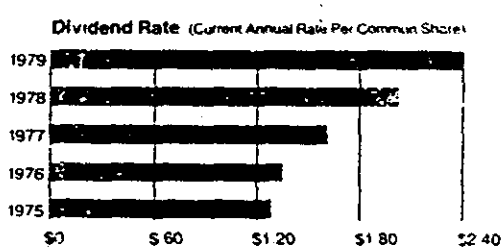
COMBUSTION ENGINEERING

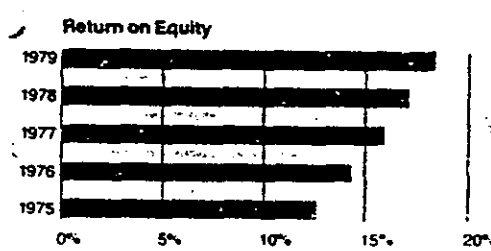
COMBUSTION ENGINEERING ANNUAL REPORT 1979

Five-Year Summary









1980

Combustion Engineering provides equipment, products and services for a wide variety of industrial uses.

Major markets served include:

- Oil and gas exploration and production;
- Petroleum and petrochemical processing;
- Environmental control and energy conservation;
- Electric power generation; and
- Steel production, pulp and paper manufacturing, minerals production and handling, and commercial and residential construction.

The Company, with 43,286 employees has facilities and offices in 84 countries throughout the world. The names Combustion Engineering, or C-E, or the Company, as used in this Annual Report, refer to Combustion Engineering, Inc. and/or one or more of its subsidiaries.

TO THE SHAREHOLDERS

Combustion Engineering's sales and earnings again reached record levels in 1979.

Net sales, including those of Basic Incorporated acquired early in the year, increased to $2.76 billion, up 18 percent from $2.33 billion in 1978.

Net income in 1979 was $97.6 million, compared with $80.3 million in 1978, an increase of 21.6 percent. Net income per share rose to $5.96 from $4.97 per share in 1978.

The backlog of unfilled orders at year-end totaled $2.99 billion, compared with $2.88 billion on December 31, 1978.

Oil and Gas Operations Led Growth

Operations serving oil and gas equipment markets made an important contribution to the Company's overall record performance in 1979. The outlook for this part of our business remains favorable for the foreseeable future.

The Company has continued to strengthen its position in this growing worldwide market. Of the $700 million spent or committed for growth in the past five years, nearly half has gone into this area. Last year alone, facilities additions included:

- Expansion of Gray Tool's manufacturing capacity in Houston;
- A new facility for inspection and coating of oil field tubular goods for C-E Vetco in West Germany;
- Completion of C-E Natco's new plant for manufacture of chemical intermediates for use in oil and gas production;
- Expansion of Beaumont Well Works' facilities to include a new 11,000-ton, multi-ram forge which will be used to produce large forgings and high-performance parts for well control and other oil field equipment.

These and other capital improvements and acquisitions have been undertaken without adding significantly to the Company's long-term debt.

Customer acceptance of C-E Vetco's well control equipment for offshore use has been demonstrated by subsea installations of advanced design now in operation in the North Sea, the Gulf of Mexico and off the coasts of California and Brazil.

Engineering and construction services, principally for the petroleum and petrochemical processing industries, continue to be in demand. Included in recent awards to C-E Lummus are:

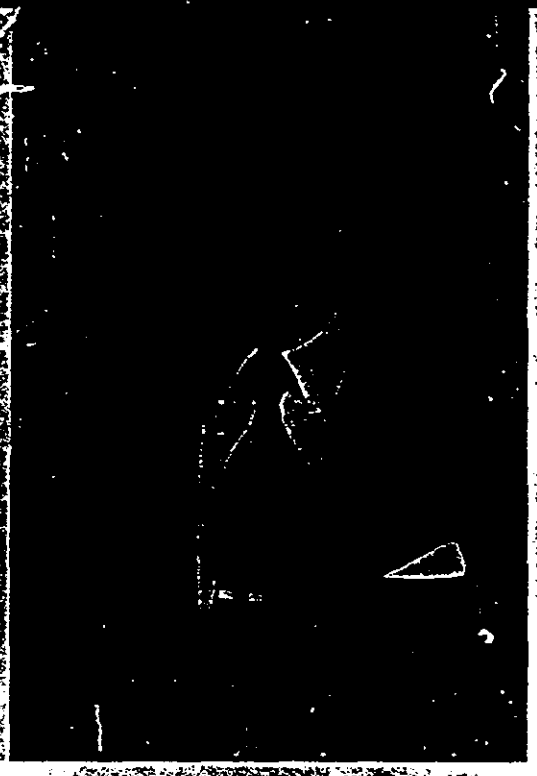
- Design of three separate ethylene plants for The People's Republic of China awarded through prime contractor Toyo Engineering Corporation of Tokyo;
- Contracts for new ethylene plants in Scotland and Taiwan, and a polyethylene plant in Brazil;
- Refinery revamping in Trinidad and West Germany, and chemical plant upgradings in England and at Exxon's Bayway complex in New Jersey;
- Engineering and construction management for a $300 million fertilizer plant in Indonesia, and prime contract responsibility for a $100 million uranium refinery in Hope Township, Ontario, Canada;
- Continuation of engineering and project management responsibility for an extensive network of crude oil desalting facilities in Saudi Arabia.

Work on the $1.1 billion petroleum and petrochemical plant in Basrah, Iraq, being carried out by a joint-venture of Lummus and Thyssen Rheinstahl Technik, G.m.b.H. of West Germany, continues on schedule with construction planned for completion this year.

Synfuels Activity Intensified

C-E Lummus is now engineering the first commercial-scale coal gasification plant to be built in the United States, a project sponsored by American Natural Resources Company and others, to be located near Beulah, North Dakota.

Immediately adjacent to that site, C-E Power Systems is building two of the nation's largest lignite-fired utility steam supply systems for Basin Electric Power Cooperative. The synthetic fuel plant and the 860-Mw fossil-fired utility station, both important C-E projects, will be fueled from the same North Dakota lignite fields.



The coal gasification demonstration plant at Windsor, Connecticut passed the 2000-hour operating mark in 1979. It has demonstrated the ability of the C-E-designed process to handle a variety of coals, and could be the forerunner of plants used to convert oil- or gas-fired utility boilers to clean-burning coal.

C-E Power Systems has delivered a prototype fluidized bed boiler to the Great Lakes Naval Training Center, a further step in a five-year program to demonstrate whether or not high-sulfur coal can be burned in an environmentally acceptable manner without the use of scrubbers and precipitators.

Among the important utility awards received by C-E Power Systems this past year is a $150 million project for Cajun Electric Power Company which includes two lignite-fired, 600-Mw steam generators, associated pulverizers and other equipment.

C-E's Nuclear Power Systems operations are continuing work on 19 nuclear steam supply systems, including 13 standardized System 80™ 1300-Mw units, although delivery dates have been extended in several instances.

It continues to be our firm belief that the key to reaching a realistic solution to the world's energy problems is effective use of all the primary resources—oil and gas, coal and nuclear. Conservation and the search for economically viable alternative energy sources must be aggressively pursued.

Sales of Industrial Equipment, Products Up
Increased shipments of environmental equipment principally for electric utilities, pulverizers for industrial use, and screening and related equipment contributed to last year's record performance.

Sales of refractories, and special-purpose industrial minerals, another area targeted for growth, advanced last year. New facilities are under way or planned for fused silica—widely used in electronic applications—and for ceramic fibers, and magnesium oxide.

Dividend Increased Twice in 1979
Reflecting confidence in the Company's continued growth, the Board of Directors voted to increase the dividend twice in 1979, making it the 15th consecutive year of dividend increases. There have been six dividend increases in the past three years. The current annual rate is $2.40 per share, compared with $2.00 at this time a year ago.

In January 1980, Paul W. MacAvoy was elected a director of the Company. Dr. MacAvoy is professor of economics and a member of the Governing Board of the School of Organization and Management at Yale University. He is a national authority on energy and economics.

My thanks go to our employees, officers and directors for their continuing efforts, loyalty and interest. On behalf of everyone at C-E, I wish to express appreciation to our shareholders for their confidence and support. I am confident that C-E is well positioned to continue its growth in the decade ahead.

Arthur J. Santry, Jr.
President

February 14, 1980



Increased Demand: Industrial development and economic growth will require increased energy use in all regions of the world in the 1980s.



The Worldwide Energy Challenge

Providing adequate supplies of energy is a vital challenge throughout the world. Fuels of all types have become increasingly more difficult to provide and more costly for industries, utilities and consumers, alike.

The most accessible reserves of oil and gas are steadily being consumed. Yet energy-related industries are being called upon not only to maintain the world's existing level of supply, but even to increase it.

Meeting this challenge requires getting the most from proven oil reserves through enhanced recovery methods. It requires finding additional reserves of oil and gas by drilling deeper and deeper wells, probing offshore, and exploring remote areas. It means finding better ways to burn coal efficiently and cleanly. And it means developing efficient and affordable new energy technologies.

Combustion Engineering, the Energy Systems Company, is a world leader in this effort. No other company has C-E's broad combination of capabilities to help energy-related industries meet this worldwide challenge.

Worldwide Growth in Energy: Hong Kong's energy intensity characterizes rising demand expected in all parts of the world to satisfy basic human needs.

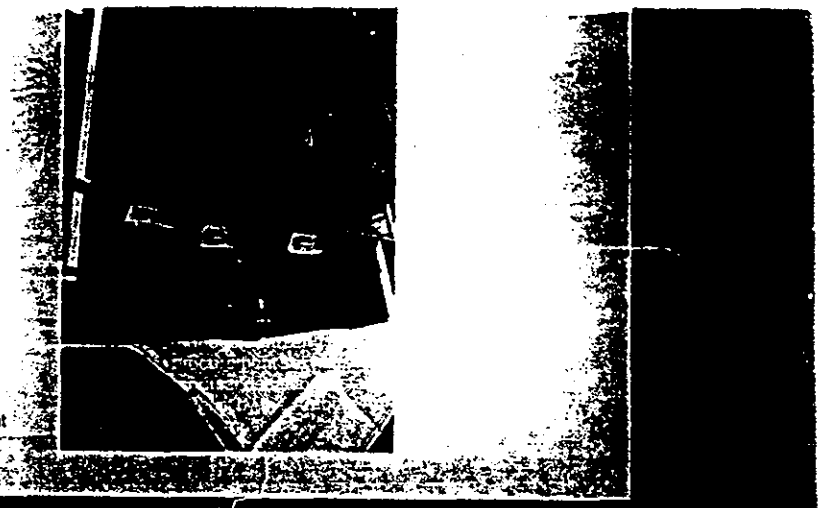


C-E continues to meet the worldwide energy challenge by supplying equipment, products and services to help produce energy, conserve it, and even to create new energy forms. The Company has been deeply involved in energy-related technologies for well over half a century.

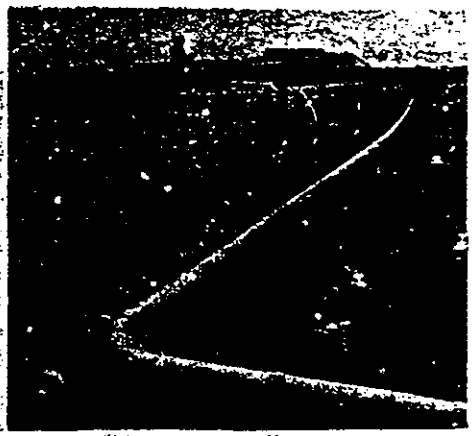
Today, C-E has intensified and broadened its ability to help make the most effective use of the world's primary energy resources: helping to find, treat and process oil and gas, upgrading and building refineries and petrochemical plants, advancing technologies for coal and nuclear steam generation, and leading the way in development of alternative fuels.

Whatever form the energy challenge takes, and wherever in the world it leads, C-E people are there, on the job, helping.

Oil and Gas Production Processing: The largest electrically-powered production platform in the Gulf of Mexico is equipped with C-E Natco processing systems. This unusual offshore installation can handle up to 120 million cubic feet of gas and 25,000 barrels of oil per day.



C-E People on the Energy Scene: Offshore and onshore, C-E is at work around the globe helping to maintain and increase the supply of critically needed energy. Far left—Installing a 20,000-pound-per-square-inch Christmas tree in an oil field: Left—Supervising installation of a production processing system on an offshore platform: Right—Conducting research at a coal gasification demonstration unit.



Saudi Arabian Desalting Network: In the remote eastern desert region of Saudi Arabia, C-E Lummus is providing project management, engineering and procurement services for 22 modular desalting installations to be built by the Arabian American Oil Company.



)il Field Pipe Inspection: Right—
eicolog® mobile equipment by
-E Vetco Services provides one of
ne most advanced testing systems
ow available for inspection
f oil field tubular goods.

)ffshore Innovations: Far right—
ompact Grayloc® connectors by
ray Tool are used throughout
eparator manifolding on Centex
il & Gas Incorporated's offshore
oduction platform in the Gulf of
exico. The high-strength platform
as designed by C-E Crest. It
cludes a C-E Natco production
ocessing system.

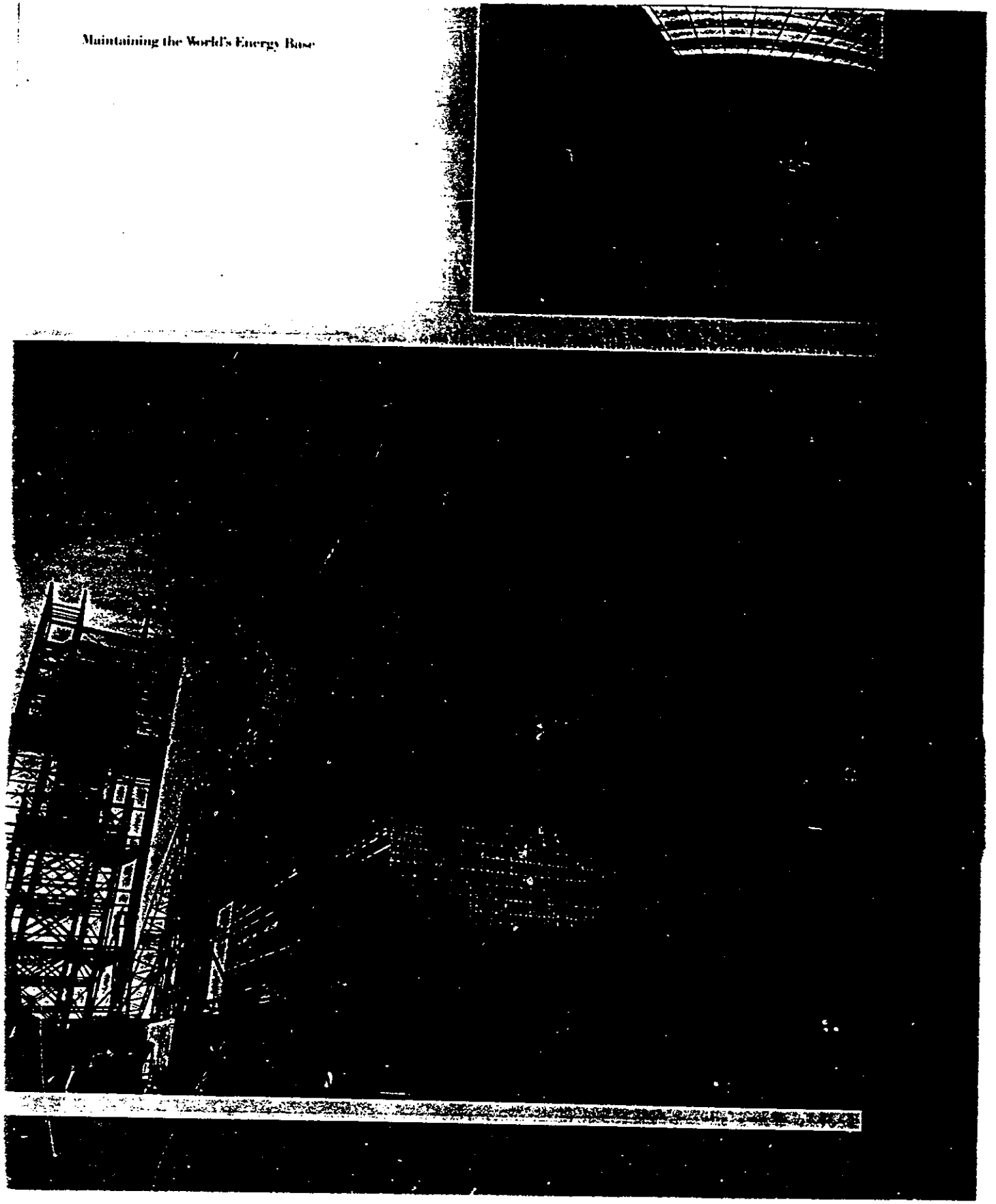


Maintaining the World's Energy Base

The world must achieve a balanced use of existing energy sources to improve living standards and to provide for economic growth. The greatest contribution to assuring adequate supplies through the end of this century must come largely from the primary energy sources: oil and gas, coal and nuclear.

To meet the demand for petroleum and petrochemical products alone, each year the world must add to its oil and gas reserves an amount at least equal to that found on the Alaskan North Slope—just one indication that the need for oil and gas equipment and services will continue to increase. In response to this opportunity, nearly half of the approximately $700 million spent or committed by C-E for growth in the past five years has gone into businesses serving the oil and gas exploration and production industries.

$1 Billion Project in Iraq: C-E Lummus is project manager with Thyssen Rheinstahl Technik, G.m.b.H. for a $1.1 billion petrochemical complex being built in Iraq. The project, one of the largest in C-E Lummus' history, will provide Iraq with its first world-scale facility. Completion of construction is scheduled for 1980.





Nuclear Plant Operator Training: Left—Operating conditions in the control room of an 800-Mw pressurized water nuclear plant are duplicated at C-E Power Systems' simulator in Windsor, Connecticut.

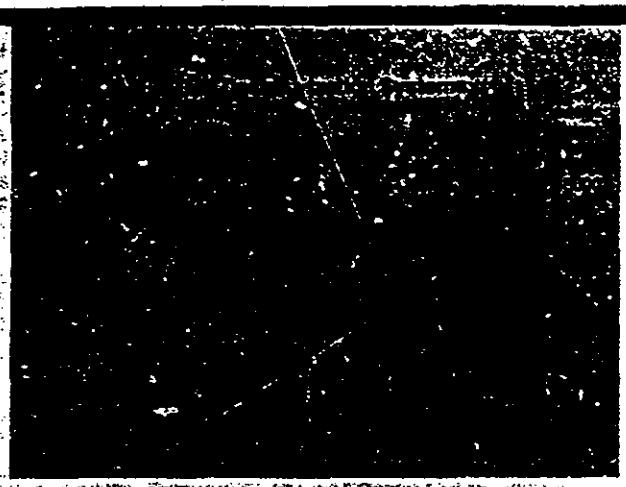
Worldwide Technical Assistance: Right—Mechanical engineers from Hyundai Heavy Industries Co., Ltd., of Korea undergo training as part of C-E Power Systems' program to insure that licensees maintain high standards of quality in the design and manufacture of fossil-fueled steam generating systems.

It is likely that electricity will assume an even larger role as an energy source in the years to come. Focus is on coal and nuclear as the fuels that are environmentally and economically viable for power generation.

C-E is a leading supplier of both coal-fired and nuclear steam supply systems, and of related equipment and services. Steam generators of C-E design account for about 40 percent of the world's thermal electric power. The Company has significantly expanded its scope of supply to meet the operating needs of the electric utilities.

Petroleum and petrochemical processing also are key elements in the energy supply-and-demand equation. Plants are being built throughout the world to help satisfy demand. C-E is one of a handful of international organizations experienced to manage the engineering and construction of today's refineries and petrochemical plants, which continue to grow in size, complexity and cost.

Major Lignite-Fired Boiler Installation: One of the tallest fossil-fired boilers in the world is being installed in a 35-story structure by C-E Power Systems at Unit 1 of the Antelope Valley Power Station of Basin Electric Power Cooperative. A second unit has been ordered from C-E with construction to start in 1981. Both units, totaling 860 Mw, will burn North Dakota lignite from adjacent fields.



Environmental Protection: Left—U.S. utilities' increased experience with operation of flue gas desulfurizers places C-E among the leading firms in this new technology.

Industrial Furnace Efficiency: Right—At Basic Incorporated's Bettsville, Ohio, research facility, refractory materials used in the installation and maintenance of industrial furnace linings undergo testing for heat resistance and energy conservation characteristics.

Chemical Plant Emissions Control: Far right—Cor-Pak® thermal oxidizer by C-E Air Preheater cleans stack gas emissions while its built-in heat exchanger, combined with a C-E waste heat boiler, saves nearly $1 million in fuel annually in a major chemical-plant installation.



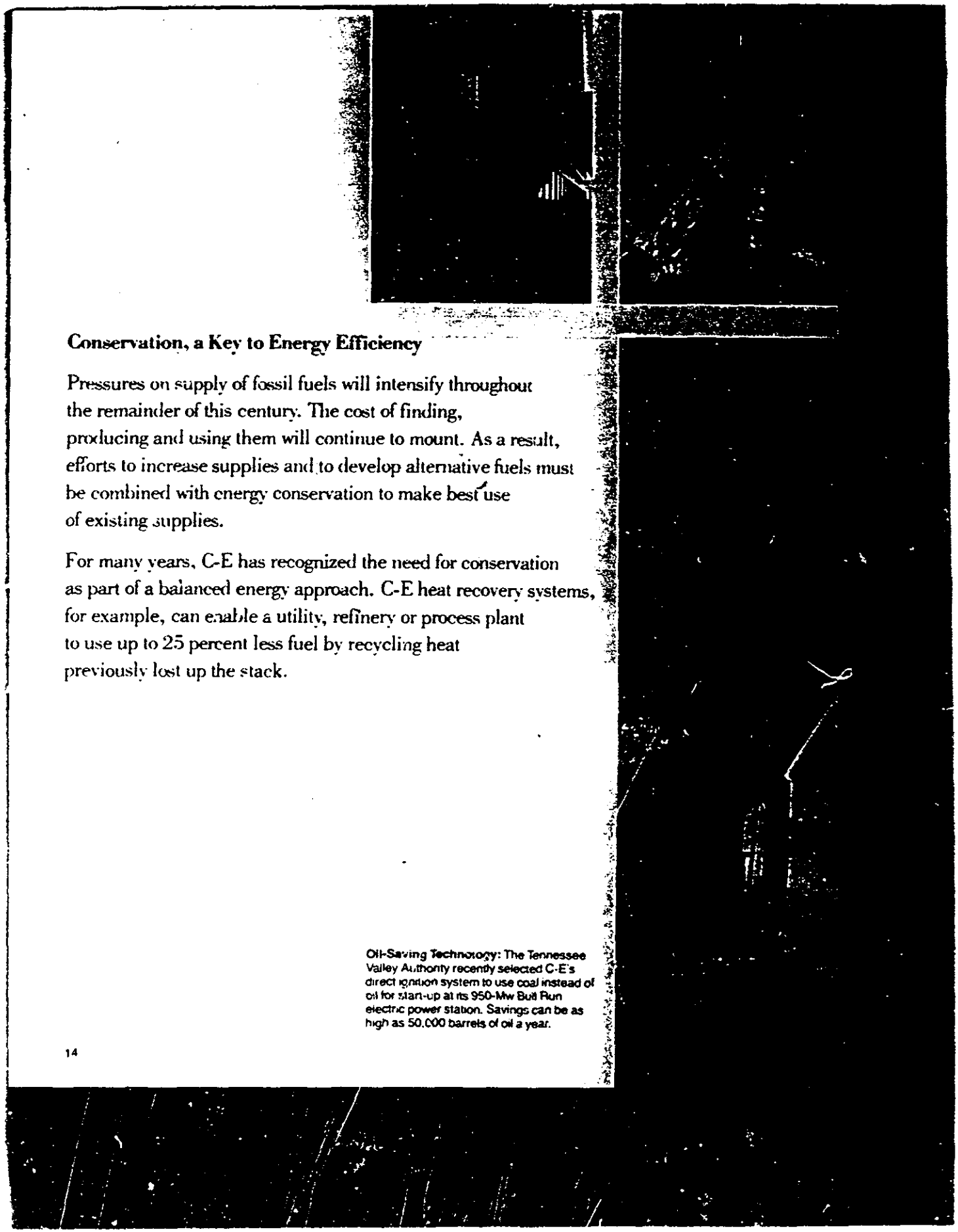
Burning Coal Cleanly, More Efficiently

Burning coal in a steam supply system is a complex process. For more than 65 years, C-E has been in the business of helping utilities and industry get the highest possible energy output from every ton consumed.

C-E knows as much about the combustion of coal as any company in the world. Equipment, products and services are being expanded to enable electric utilities and industry to keep pace with new requirements for processing coal efficiently and cleanly.

Within its increased scope of supply, C-E now has more experience with equipment for flue gas desulfurization than any other utility supplier. In industry, C-E special-purpose materials, such as refractories, help make intensive fuel-burning processes operate more economically.

Expanded Scope of Supply: Members of C-E construction crew install scrubber system in Jeffrey Energy Center's Unit 2 in St. Marys, Kansas. For Units 1 and 2, C-E will have provided over $174 million in equipment and services, including steam generators, pulverizers, heat recovery systems and field construction.

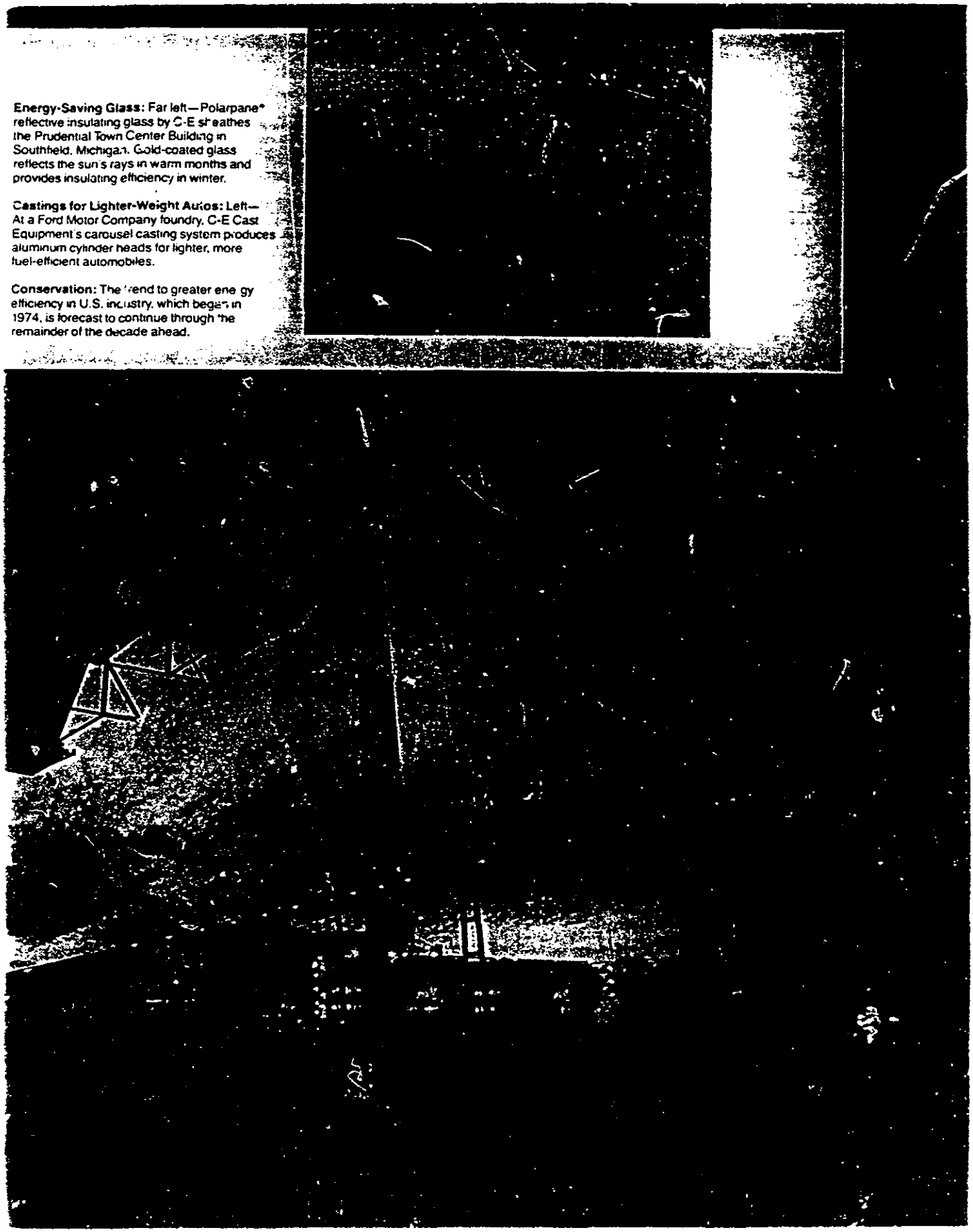


Conservation, a Key to Energy Efficiency

Pressures on supply of fossil fuels will intensify throughout the remainder of this century. The cost of finding, producing and using them will continue to mount. As a result, efforts to increase supplies and to develop alternative fuels must be combined with energy conservation to make best use of existing supplies.

For many years, C-E has recognized the need for conservation as part of a balanced energy approach. C-E heat recovery systems, for example, can enable a utility, refinery or process plant to use up to 25 percent less fuel by recycling heat previously lost up the stack.

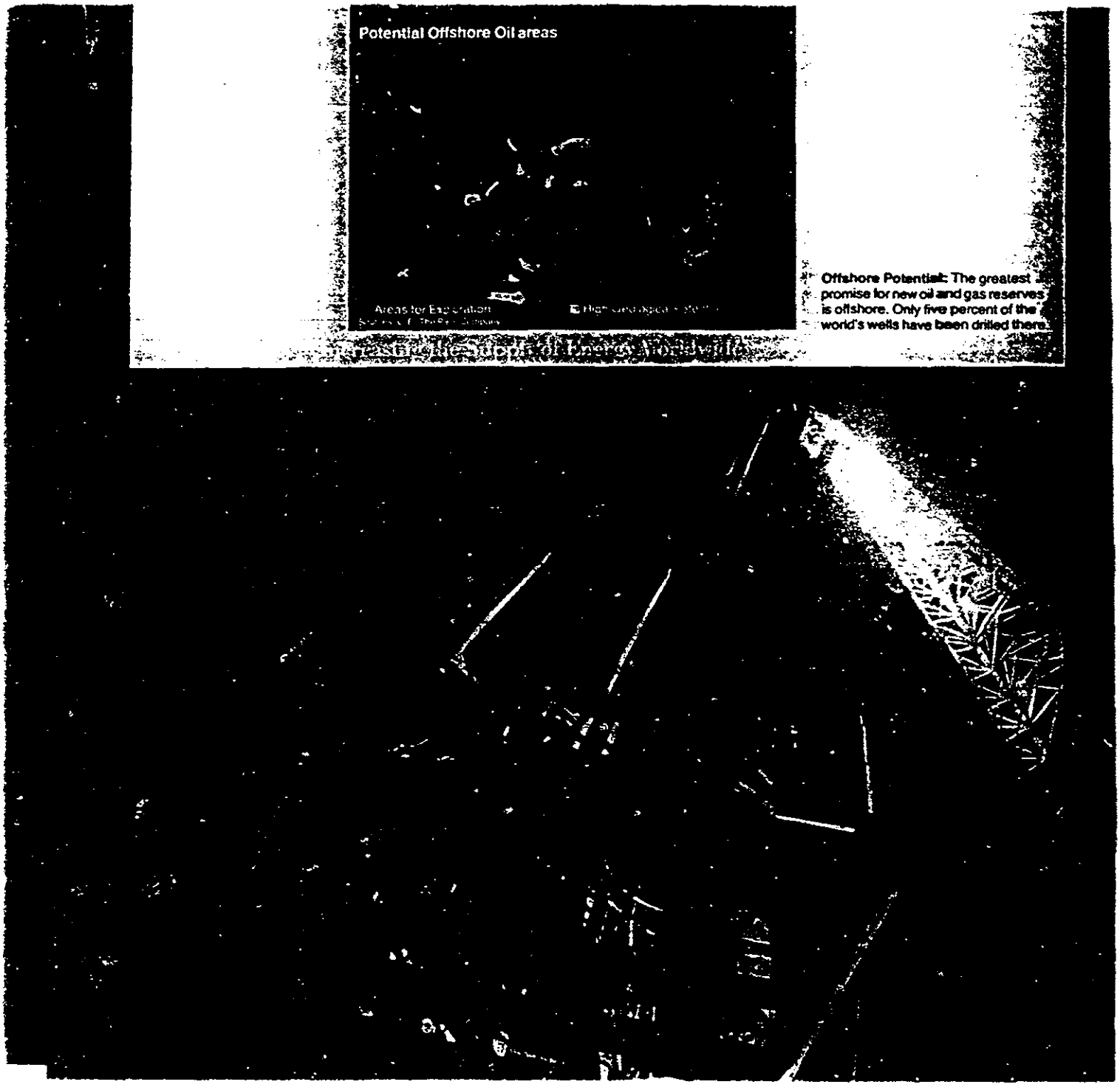
Oil-Saving Technology: The Tennessee Valley Authority recently selected C-E's direct ignition system to use coal instead of oil for start-up at its 950-Mw Bull Run electric power station. Savings can be as high as 50,000 barrels of oil a year.



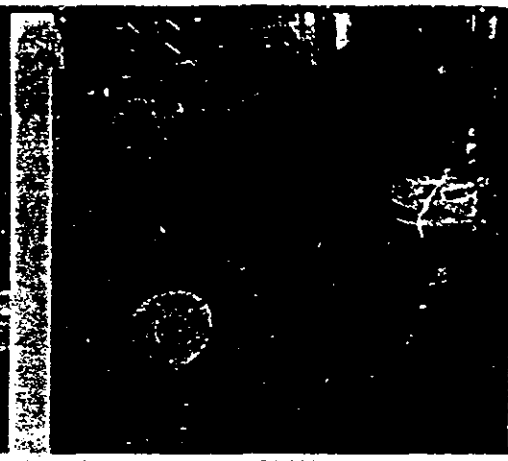
Energy-Saving Glass: Far left—Polarpane® reflective insulating glass by C-E sheathes the Prudential Town Center Building in Southfield, Michigan. Gold-coated glass reflects the sun's rays in warm months and provides insulating efficiency in winter.

Castings for Lighter-Weight Autos: Left—At a Ford Motor Company foundry, C-E Cast Equipment's carousel casting system produces aluminum cylinder heads for lighter, more fuel-efficient automobiles.

Conservation: The trend to greater energy efficiency in U.S. industry, which began in 1974, is forecast to continue through the remainder of the decade ahead.


Potential Offshore Oil areas
Areas for Exploration
Offshore Potential: The greatest promise for new oil and gas reserves is offshore. Only five percent of the world's wells have been drilled there.





Advanced Well Control Technology: Far left—Specialists from Gray Tool and The Louisiana Land and Exploration Company install a surface well control system to handle natural gas pressures up to 20,000 pounds-per-square-inch. Left—Capabilities of C-E's Beaumont Well Works include special forgings such as those used in advanced well control systems and seamless rolled rings for gearing on heavy machinery.

Increasing the Supply of Energy Worldwide

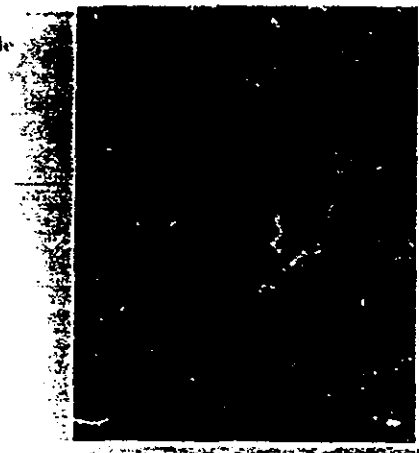
Coping with the energy challenge means increasing the world's supply of primary resources. It means research in advanced technologies. It means developing existing equipment, products and services to handle tougher requirements in oil fields, in factories and in power plants.

Oil and natural gas will continue to play a major role in meeting the world demand for energy. Onshore development will accelerate. But the greatest potential is offshore, where vast reserves are just beginning to be tapped.

Wherever oil and gas are located, no matter how difficult to develop, C-E equipment, products and services are helping to find, recover and process them.



Brazilian Offshore Oil Project: C-E Vetco subsea production template is loaded on a barge for a 50-mile journey off the coast of Brazil, where it was lowered 600 feet to the ocean floor. C-E Vetco's unique production system can handle six wells on the template and four additional satellite wells.



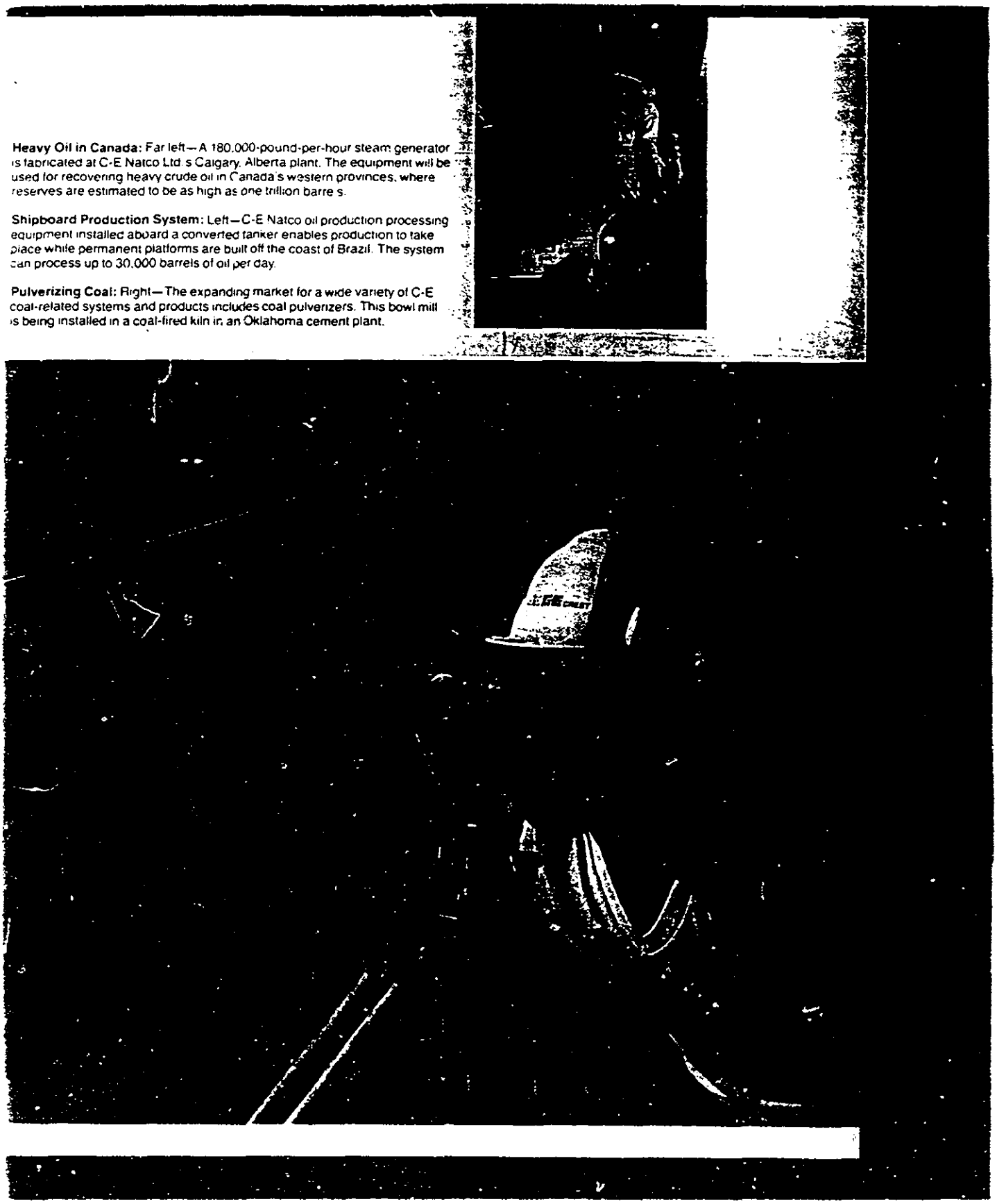


Petroleum supplies can be increased by recovering and processing heavy oil and tar sands, and by enhancing recovery of oil reserves in existing fields which until now have been too expensive to produce.
Heavier crude oil feedstocks can now be processed by refineries of advanced design.

Special-purpose chemicals used for oil and gas production processing are also helping to increase supplies. A new generation of well control and production treating and processing equipment is handling raw crude oil and natural gas flowing at extremely high pressures and under severe operating conditions.

C-E equipment and services are extensively involved in these frontier areas, helping to increase the world's energy base.

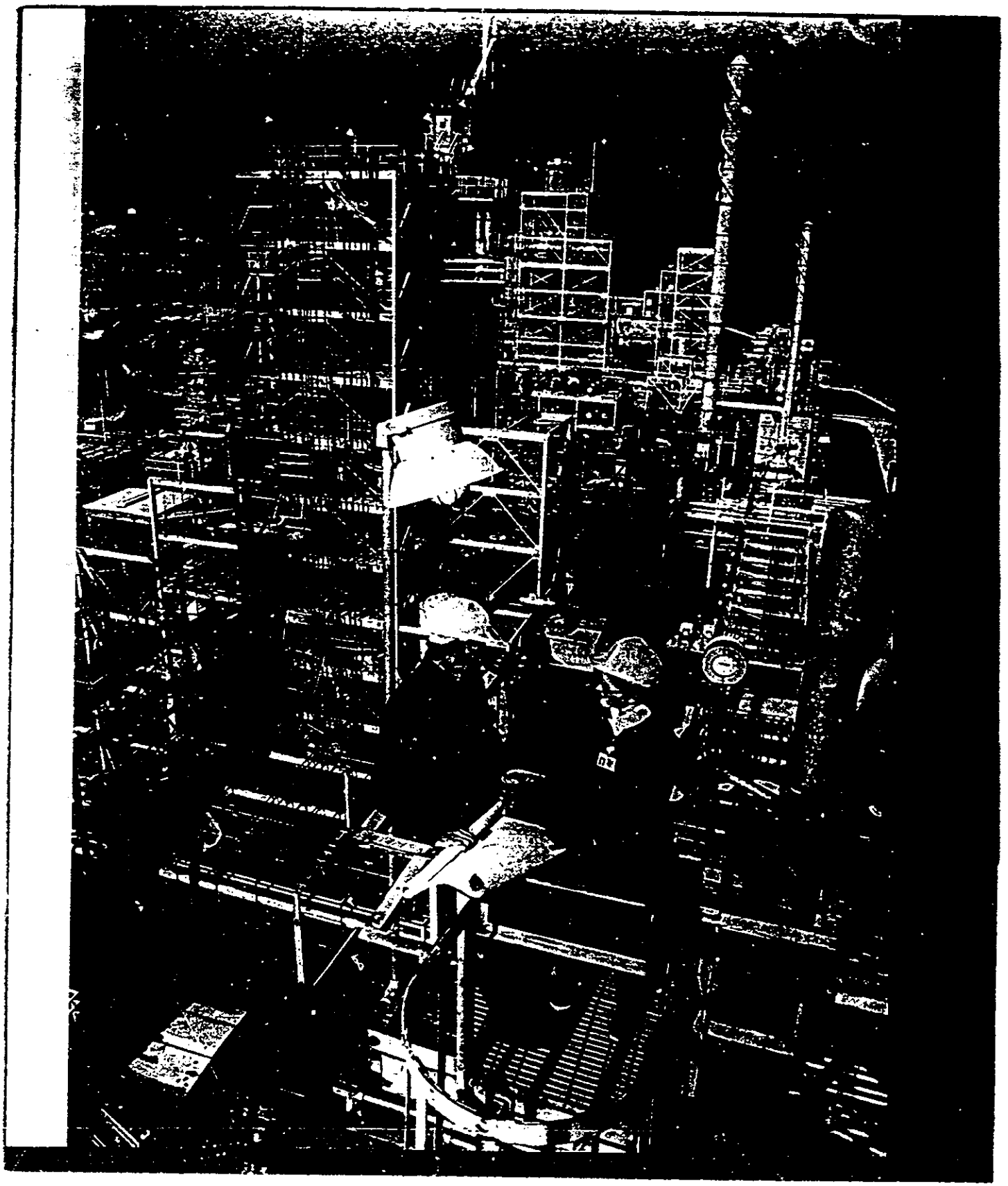
Oil Recovery in Peru: C-E Crest is project manager and designer of Occidental Petroleum Co.'s secondary recovery system on Peru's northern coast. The system will inject filtered seawater from the Pacific Ocean into the oldest producing oil field in South America to recover more oil.

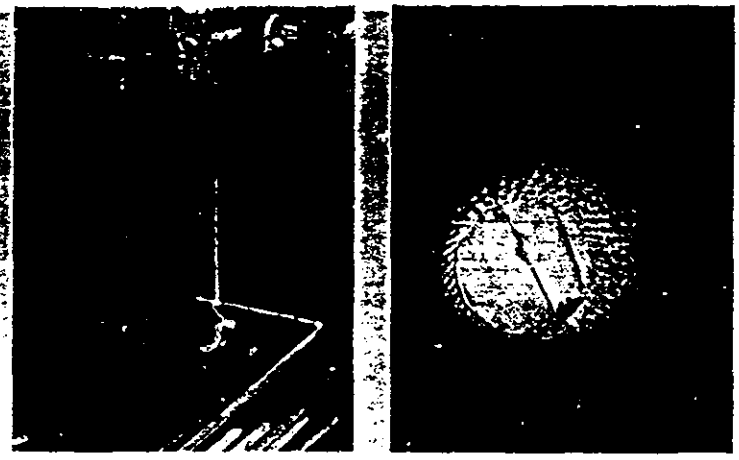


Heavy Oil in Canada: Far left—A 180,000-pound-per-hour steam generator is fabricated at C-E Natco Ltd.'s Calgary, Alberta plant. The equipment will be used for recovering heavy crude oil in Canada's western provinces, where reserves are estimated to be as high as one trillion barrels.

Shipboard Production System: Left—C-E Natco oil production processing equipment installed aboard a converted tanker enables production to take place while permanent platforms are built off the coast of Brazil. The system can process up to 30,000 barrels of oil per day.

Pulverizing Coal: Right—The expanding market for a wide variety of C-E coal-related systems and products includes coal pulverizers. This bowl mill is being installed in a coal-fired kiln in an Oklahoma cement plant.





Synthetic Fuel: Right—The U.S. Department of Energy's Solvent Refined Coal pilot plant at Fort Lewis, Washington, utilizes a C-E Lummus system that features proprietary antisolvent coal deashing technology.

C-E Refractories: Far right—Industrial furnaces are being relined with CER-Wool™ ceramic fiber to take advantage of the new material's energy-saving qualities.

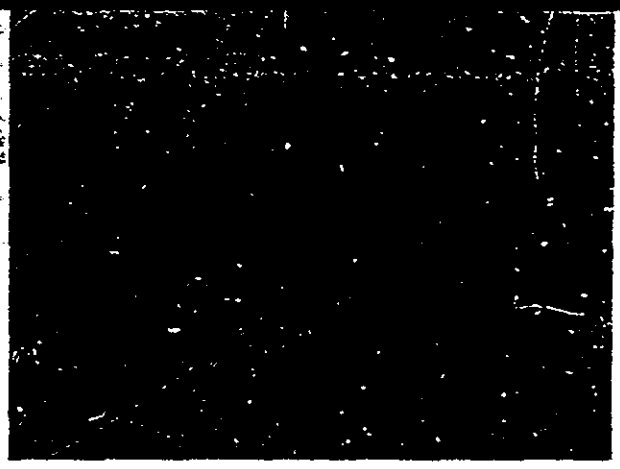
Creating New Technology

For more than a decade, C-E has been a leader in developing synthetic fuels from coal. Today, a C-E deashing process is on line in one of the nation's first coal liquefaction pilot plants. The process also will be used in an additional pilot plant coming on stream later this year.

Also in operation is the nation's largest demonstration plant for transforming coal into a clean-burning gas for electric power generation. It has been designed, built and operated by C-E in a program jointly sponsored by the Company, the U.S. Department of Energy, and the Electric Power Research Institute.

The size and complexity of commercial-scale synthetic fuel plants will require assigning project management responsibility to companies with extensive engineering and construction experience. C-E Lummus is currently engineering the nation's first commercial-size coal gasification plant, a $1.5 billion project in North Dakota.

Coal Liquefaction: Complexity of synthetic fuels development is evident at Ashland Synthetic Fuels Inc.'s test facility under construction in Catlettsburg, Kentucky. When this plant goes on stream in 1980, using a system that includes C-E Lummus proprietary deashing technology, it will be the largest DOE-sponsored coal liquefaction pilot plant in operation.



Energy Alternatives: Timely decisions are required in planning energy-supply alternatives in view of long lead times required for commercial development.

Looking into the 1980s and beyond, C-E has research and development programs under way in a variety of energy-related areas, including:

- Advanced systems for subsea oil and gas well-completion and production,
- High-temperature, high-pressure wellheads,
- Special-purpose materials, such as new refractories and oil field chemicals,
- Clean utilization of coal through fluidized bed combustion and magnetohydrodynamics, and
- Advanced nuclear reactor designs.

C-E's work in advanced technologies also includes equipment and processes for recovery and upgrading of heavy oils, including oil from tar sands.

No matter what the resource mix, C-E is well positioned to help meet energy requirements head-on. For more than 65 years, C-E's businesses have been principally related to energy. The Company's proven technology and experience are ready to help meet this worldwide challenge.

Coal Gasification: The coal gasification demonstration unit at C-E's Windsor, Connecticut facility is the largest of its kind in the nation. The test unit converts coal into a clean-burning gas for possible use in utility and industrial boilers.

COMBUSTION ENGINEERING PRODUCTS AND SERVICES

Electric Power Generation Air Heaters Ash Handling Systems Coal Mills Construction and Maintenance Services Control Rods and Drive Mechanisms Design and Engineering Ducts Economizers Fabricated Products Fans Fuel Additives Fuel Conversion Heat Exchangers Inspection Services Nuclear Fuel Nuclear Reactor Components Nuclear Steam Systems (standardized) Operator Training Preheaters (Ljungstrom®) Pressure Vessels Reactor Coolant Pumps Reactor Internals Reactor Vessels Reheaters Solar Collector Glass Steam Condensers Steam Generators Structural Fabrication Superheaters Tubing Transmission Structures

Environmental Control and Waste Disposal Ash Handling Systems Air Classifiers Air Diffusers Air Separators Baghouse Filter Systems Construction and Supply Services Desulfurization Networks Design and Engineering Services Detectors Dewatering Equipment Dust Collectors Electrostatic Precipitators Filters Flue Gas Desulfurization Systems (FGD) Fume Incineration Systems Liquid Cyclones Odor Control Equipment Pressure Static Screens Resource Recovery Systems and Services Seawater Treating Units Sewage Sludge Dryers and Incinerators Single and Double Shakers Solid Waste Boiler Firing Systems Solid Waste Incineration Systems

Foundry Binders Chip Dryers Coated and High-temperature Sands Field Supervision Services Melt Shop Engineering Mixers Molding Machines Phenolic Urethane Binders Pouring Systems Refractories Refractory Coatings Sand Handling Equipment Scrap Metal Preheaters SPO² Molding

Oil and Gas Drilling, Exploration and Production Actuators Adjustable Drilling Chokes Blowout Preventer Assemblies and Stacks Clamp and Pipe Connectors Deaerators Drilling Manifolds Drilling Mud Additives and Screening Driveable Connectors Feasibility Studies Fluids Separation Forgings Gas Processing Units and Scrubbers Glycol Dehydrators Heaters Hydrocarbon Recovery Units Pipeline Inspection Liquid Dehydration and Low-temperature Extraction Units Marine Riser and Motion Compensators Muldine Suspension Systems Pipe Coating and Inspection Services Precipitators Pressure Vessels Production Systems and Chemicals Rupture Discs and Safety Heads Secondary Recovery Equipment Separators Specialty Connectors Steam Flooding Storage Tanks Subsea Drilling and Production Systems Swivels Tensioning Systems Training Courses Valves, Instruments and Controls Water Conditioning Well-completion Systems and Related Equipment

Petroleum, Petrochemical, Minerals and Related Industries Design Engineering Plant Construction Project Management Procurement Operations and Maintenance Services Construction Equipment Rental Supply of Fired Heaters, Heat Exchangers, and Air Cooled Equipment and Gas Processing Plants

Process Industries Air Classifiers Air Diffusers Air Preheaters Bark Burning Boilers Calciners Chemical Recovery Units Continuous Digestors Coolers Dewatering Equipment Digestors Disc Mills Disc Refiners Drums Dust Collectors Evaporators Flash Dryers Heat Exchangers Heaters Hydrators Incinerators Instrumentation Kilns Pelletizers Presses Pulverizers Refiners Rotary Dryers and Kilns Screens and Screening Machines Mechanical Air Separators Stainless Steel Tubing Thermo-mechanical Pulping Systems Valves Wallboard Manufacturing Equipment Woven Wire

Refractories, Ceramics, and Special-Purpose Minerals Abrasion Resistant Ceramic Shapes Aluminum Silicates Bauxite Boiler Treatment Chemicals Bonding Mortars Bricks Castables Celestite Ceramic Fiber Products Chromites Clays Cristobalite Custom Grinding Services Dolomite Drying and Blending Services Fused Magnesia Fused Silica Shapes Fused Spinel Glass Furnace Refractories Gunning Mixes Iron Pyrites and Iron Oxides Kyanite Magnetite Mullite and Mullite Shapes Plastic Refractories Pouring Pit Refractories Pyrites Ramming Mixes Refractory Washes Speculite Strontium Sulfate Sand Zircon

Residential and Commercial Construction Amber Glass Bath, Shower Enclosure Glass Clear Glass Curtainwall Glass Entrances and Entrance Systems Figured Glass Float Glass Glare-reducing Glass Heat-absorbing Glass Heat-treated and -strengthened Glass Insulating Glass Lighting Fixture Glass Louvers Mantels Posts Reflective Glass Rolled Glass Safety Glass Spandrels Stairways and Stair Parts Windows Woven Metal

COMBUSTION ENGINEERING, INC.

Board of Directors

Harry J. Bolwell (1978)
Chairman and Chief Executive Officer
Midland-Ross Corporation, Cleveland, Ohio,
manufacturer of steel products and controls

James F. Calvert (1975)
Vice President, Combustion Engineering, Inc

W. Van Alan Clark, Jr. (1971)*†
Chairman, The Sippican Corporation,
Marion, Mass., consulting engineers and
manufacturers and developers of diverse equipment

Thomas A. Ennis (1960)
Vice President, Combustion Engineering, Inc

Lambert J. Gross (1963)
Vice President, Combustion Engineering, Inc

Robert M. Jenney (1963)*†
President, Jenney Oil Company Incorporated, Boston, Mass

Paul W. MacAvoy (1980)
Milton Steinbach Professor of Organization
and Management and Economics, Yale University

Scott L. Probasco, Jr. (1960)†
President and Chief Executive Officer, Ancorp Bancshares, Inc
Chattanooga, Tenn., a multi-bank holding company

George Putnam (1974)*†
Chairman, The Putnam Management Company, Inc
Boston, Mass., investment advisor to investment companies

Arthur J. Santry, Jr. (1957)*
President, Combustion Engineering, Inc

Robert C. Seamans, Jr. (1977)†
Dean, School of Engineering, Massachusetts Institute
of Technology

Robert G. Stone, Jr. (1963)*†
Chairman, West India Shipping Company, Inc.,
New York, N.Y., owners and operators of specialized vessels

James F. Thornton (1958)
Consultant to Combustion Engineering, Inc

Howard M. Winterson (1968)
Vice President, Combustion Engineering, Inc

Directors Emeriti

Hubert G. Ebdon
Douglas B. Steimle
Walter H. Zinn

*Member of the Executive Committee, Robert G. Stone, Jr., Chairman
†Member of the Audit Committee, W. Van Alan Clark, Jr., Chairman
Date following the name indicates the year first elected Director

Officers

Arthur J. Santry, Jr.
President

James F. Calvert
Vice President-Operations

Joseph F. Condon
Vice President-International

William J. Connolly
Vice President-Marketing and Communications

Thomas A. Ennis
Vice President-Administration

Lambert J. Gross
Vice President-Finance

Richard J. Halkman
Vice President, Secretary and General Counsel

James B. Kelly
Vice President in charge of Industrial Products Group

Mitchell Kiamie
Vice President and Controller

George S. Kimmel
Vice President and Treasurer

Charles K. Leeper
Vice President Corporate Technology

William P. Orr
Vice President in charge of Engineering Group

George R. Parkin
Vice President-Development and Planning

John H. Slack
Vice President in charge of Process Equipment Group

Howard M. Winterson
Vice President in charge of Power Systems Group

Combustion Engineering, Inc.
900 Long Ridge Road
Stamford, Connecticut 06902



Offshore Brazil: Petrobras, the national oil and gas company of Brazil, prepares a C-E Vetco subsea template for use in exploratory drilling off the coast of Rio de Janiero.

COMBUSTION ENGINEERING

The Energy Systems Company

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