The Group management report prepared for the first time in 1997 and the management report of ELSA AG have been combined pursuant to § 315 (3) of the German Commercial Code (HGB). If not stated otherwise the statements apply both to the position of the Group and that of ELSA AG.

GROUP MANAGEMENT REPORT

Markets

The high demand for PC products continued in 1997. Demand was created by the continuation of investment activities on the part of industry and the steadily increasing importance of the computer in the consumer sector. The growing expansion of the Internet also contributed to maintaining the boom in the PC market.

ELSA

ELSA has emerged from the intense competition taking place in Germany over the last few years as the clear market leader. With its divisions of Computer Graphics and Data Communications ELSA now competes first and foremost with international suppliers, predominantly from the United States and Canada. In order to be successful in global competition ELSA is planning to go public. In preparation for this step the Company was converted to the legal form of a stock corporation (AG) in November 1997.

Products

The high product quality and the wide-spread popularity and utilization of the Windows NT operating systems have enabled ELSA to tap new sales markets for high-end 3D Computer Graphics products. Good growth rates in the Internet are an excellent prerequisite for the activities in the business segment of Data Communications.

Exports

The internationalization which has begun in 1996 was continued successfully in 1997. The Group export rate rose to 27 % in comparison with the AG export rate of 13 % in the prior year. This development was also supported by the American subsidiary for the first time. In order to further expand international business the establishment of branches in Japan and Taiwan has begun in 1997.

Development of sales

The net sales of the Group were increased by 26,8 % to DM 287 million in 1997, for ELSA AG by 22 % to DM 275 million (prior year DM 228 million). Both divisions contributed to this growth. In the division of Computer Graphics ELSA achieved the highest growth rates at 36 %.

Result of operations

The result from ordinary activities calculated for the first time on a consolidated basis amounted to DM 13.9 million. The temporary weakness of the German consumer market had a negative effect on this result with the AG result of DM 12.1 million DM 2.0 million lower than the prior year. Development projects and expenses that cannot be 2.7 million capitalized in connection with the conversion into a stock corporation (AG) and the planned initial public offering also had a negative impact on the result. These negative influences were largely compensated by the positive result from ELSA Inc., so that 1997 also yielded a good result.

Employees

In 1997 ELSA increased the number of employees in the Group from 344 to 489. Consequently 133 new jobs were created at ELSA AG and 12 new jobs at the Group subsidiaries or at the sales outlets.

Research & development

In order to maintain the Company's leading market position product development is still of decisive importance. In the last fiscal year ELSA invested 28 % (DM 9.3 million) of direct expenses incurred in the Research and Development division. These expenses related to the development of new products and the maintenance and expansion of existing product lines. For 1998 an even greater increase in development activities is planned.

Further business prospects

In the first few months of 1998 sales and income increased again. The orders on hand, which remain high, and additional OEM orders are expected to lead to further increases in sales and income in 1998.

Aachen, March 1998

ELSA AG
The Management Board

Assets

			1997 DM
A.	**FIXED ASSETS**		
	I. Intangible assets		
		concessions, industrial and simular rights and licenses in such rights and assets	**521,039.34**
	II. Property, plant and equipment		
		1. Land and buildings including buildings on third-party land	9,351,710.08
		2. Other equipment, operational and office equipment	4,759,648.35
		3. Advance payments and construction in progress	342,553.18
			14,453,911.61
	III. Financial assets		
		1. Shares in affiliated companies	1.00
		2. Other loans	525,853.87
		3. Advance payments on financial assets	744,342.43
			1,270,197.30
			16,245,148.25
B.	**CURRENT ASSETS**		
	I. Inventories		
		1. Raw materials and supplies	25,459,544.74
		2. Work-in-process	10,680,528.73
		3. Finished goods and merchandise	18,338,358.66
		4. Advance payments	8,118.37
			54,486,550.50
	II. Receivable and other assets		
		1. Trade receivables	21,723,680.03
		2. Other assets	3,532,403.26
			25,256,083.29
	III. Checks, cash-on-hand, postal giro balances, balances at bank		**4,023,370.26**
			83,766,004.05
C.	**DEFERRED TAX ASSETS**		**513,624.60**
D.	**PREPAID EXPENSES**		**406,902.47**
			100,931,679.37

Liabilities and equity

			1997 DM
A.	**EQUITY**		
	I. Subscribed capital		5,800,000.00
	II. Capital surplus		1,500,000.00
	III. Earned surplus		
		Other earned surplus	735.11
	IV. Consolidated retained earnings		7,000,195.45
	V. Difference from capital consolidation		98,332.66
	VI. Currency translation adjustment		40,656.00
	VII. Minority interest		541,684.89
			14,981,604.11
B.	**CAPITAL OF DORMANT PARTNERS**		**11,500,000.00**
C.	**ACCRUALS**		
	1. Accruals for pensions and reserves for similar obligations		508,951.00
	2. Accrued taxes		2,793,730.83
	3. Other accruals		3,820,366.68
			7,123,048.51
D.	**LIABILITIES**		
	1. Liabilities due to banks		41,631,987.91
	2. Trade payables		22,580,291.23
	3. Other liabilities		3,114,747.61
	• *thereof for taxes: DM 1.418.454,11*		
	• *thereof for social security and similar obligations: DM 728.449,89*		
			67,327,026.75
			100,931,679.37

	DM	1997 DM
1. Sales		286,565,103.07
2. Increase in finished goods inventories and work-in-process		5,026,124.51
3. Production for own plant and equipment capitalized		104,.884.97
4. Other operating income		4,377,250.35
5. Cost of materials		
a) Cost of raw materials, supplies and trading stock	211,143,525.77	
b) Cost of purchased services	1,796,292.00	
		212,939,817.77
6. Personnel expenses		
a) Wages and salaries	29,540,560.24	
b) Social security, pension and other benefit costs		
• thereof for pensions: DM 179.336,25	4,928,989.12	
		34,469,549.36
7. Depreciation on intangible assets and property, plant and equipment		3,298,008.52
8. Other operating expenses		29,515,621.63
9. Income from long-term loans		31,552.83
10. Other interest and similar income		15,416.48
11. Interest and similar expenses		2,044,137.83
12. Result from ordinary activities		13,853,197.10
13. Taxes on income		6,468,906.78
14. Other taxes		31,113.14
15. Profit share of dormant partners		805,381.95
16. **Consolidated net income for the year**		**6,547,795.23**
17. Profit carried forward from the prior year		452,400.22
18. **Consolidated retained earnings**		**7,000,195.45**

CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED DECEMBER 31, 1997

STATEMENT OF FIXED MOVEMENTS DURING THE YEAR 1997

ACQUISITION AND PRODUCTION COST

	Jan 1, 1997 DM	Currency diff. DM	Additions DM	Disposals DM	Transfer DM	Dec 31, 1997 DM
I. INTANGIBLE ASSETS						
Concessions, industrial and similar rights and assets and licenses in such rights and assets	617,390.81	0.00	512,208.08	0.00	0.00	1,129,598.89
II. PROPERTY, PLANT AND EQUIPMENT						
1. Land and buildings including buildings on third-party land	9,970,015.20	0.00	648,389.62	6,501.44	33,955.19	10,645,858.57
2. Other equipment, factory and office equipment	8,418,898.80	52,509.46	4,083,370.85	605,902.28	17,448.48	11,966,325.31
3. Advance payments and construction in progress	51,403.67	0.00	342,553.18	0.00	-51,403.67	342,553.18
	18,440,317.67	**52,509.46**	**5,074,313.65**	**612,403.72**	**0.00**	**22,954,737.06**
III. FINANCIAL ASSETS						
1. Shares in affiliated companies	252,115.44	0.00	0.00	0.00	0,00	252,115.44
2. Other loans	546,059.45	0.00	30,000.00	50,205.58	0.00	525,853.87
3. Advance payments	0.00	0.00	744,342.43	0.00	0.00	744,342.43
	798,174.89	**0.00**	**774,342.43**	**50,205.58**	**0.00**	**1,522,311.74**
	19,855,883.37	**52,509.46**	**6,360,864.16**	**662,609.30**	**0.00**	**25,606,647.69**

ELSA GROUP, AACHEN

ACCUMULATED DEPRECIATION					NET BOOK VALUES
Jan 1, 1997 DM	Currency diff. DM	Additions DM	Disposals DM	Dec 31, 1997 DM	Dec 31, 1997 DM
459,049.81	0.00	149,509.74	0.00	608,559.55	521,039.34
882,869.12	0.00	412,581.81	1,302.44	1,294,148.49	9,351,710.08
5,046,652.92	15,662.36	2,735,916.97	591,555.28	7,206,676.97	4,759,648.34
0.00	0.00	0.00	0.00	0.00	342,553.18
5,929,522.04	**15,662.36**	**3,148,498.78**	**592,857.72**	**8.500.825,46**	**14,453,911.60**
252,114.44	0.00	0.00	0.00	252,114.44	1.00
0.00	0.00	0.00	0.00	0.00	525,853.87
0.00	0.00	0.00	0.00	0.00	744,342.43
252,114.44	**0.00**	**0.00**	**0.00**	**252,114.44**	**1,270,197.30**
6,640,686.29	**15,662.36**	**3,298,008.52**	**592,857.72**	**9,361,499.45**	**16,245,148.24**

Assets

		1997 DM	1996 DM
A.	**FIXED ASSETS**		
	I. Intangible assets		
	Concessions, industrial and similar rights and licenses in such rights and assets	**487,229.00**	**158,341.00**
	II. Property, plant and equipment		
	1. Land, land rights and buildings including buildings on third-party land	9,351,710.08	9,087,146.08
	2. Other equipment, operational and office equipment	4,232,876.00	3,146,536.00
	3. Advance payments and construction in progress	342,553.18	51,403.67
		13,927,139.26	**12,285,085.75**
	III. Financial assets		
	1. Shares in affiliated companies	4,169,765.86	3,397,301.86
	2. Other loans	525,853.87	546,059.45
	3. Advance payments on financial assets	744,342.43	0.00
		5,439,962.16	**3,943,361.31**
		19,854,330.42	**16,386,788.06**
B.	**CURRENTS ASSETS**		
	I. Inventories		
	1. Raw materials and supplies	25,459,544.74	5,826,581.35
	2. Work-in-process	10,680,528.73	15,246,699.53
	3. Finished products and merchandise	14,772,328.94	8,186,046.65
	4. Advance payments	8,118.37	21,467.50
		50,920,520.78	**29,280,795.03**
	II. Receivable and other assets		
	1. Trade receivables	14,572,774.13	19,684,414.51
	2. Receivables from affiliated enterprises	6,153,999.86	3,692,541.82
	3. Other assets	3,453,489.06	223,158.26
		24,180,263.05	**23,600,114.59**
	III. Checks, cash-on-hand, postal giro balances, balances at banks	2,173,410.30	1,640,461.04
		77,274,194.13	**54,521,370.66**
C.	**PREPAID EXPENSES**	271,555.48	255,723.52
	• thereof for discount: DM 0,00 (prior year: DM 416,00)		
		97,400,080.03	**71,163,882.24**

Liabilities and equity

		1997 DM	1996 DM
A.	**EQUITY**		
	I. Subscribed capital	5,800,000.00	5.300.000.00
	II. Capital surplus	1,500,000.00	0.00
	III. Earned surplus		
	Other earned surplus	735.11	735.11
	IV. Retained earnings	6,977,860.19	7,312,377.22
		14,278,595.30	**12,613,112.33**
B.	**CAPITAL OF DORMANT PARTNERS**	**11,500,000.00**	**6,000,000.00**
C.	**ACCRUALS**		
	I. Accruals for pensions and reserves for similar obligations	508,951.00	424,207.00
	II. Accrued taxes	470,849.46	5,440,702.28
	III. Other accruals	3,586,177.38	3,681,032.75
		4,565,977.84	**9,545,942.03**
D.	**LIABILITIES**		
	I. Liabilities due to banks	41,631,987.91	18,597,986.55
	II. Trade payables	22,320,525.07	20,810,397.25
	III. Other liabilities	3,102,993.91	3,596,444.08
	• thereof for taxes: DM 1.406.700,41 (prior year: DM 2.139.601,28)		
	• thereof relating to social security and similar obligations: DM 728.449,89 (prior year: DM 551.994,30)		
		67,055,506.89	**43,004,827.88**
		97,400,080.03	**71,163,882.24**

	DM	1997 DM	1996 DM
1. Sales		275,279,848.41	226,163,578.99
2. Increase in finished goods and work-in-process		2,231,638.48	13,435,604.01
3. Production for own plant and equipment capitalized		104,884.97	95,196.80
4. Other operating income		3,715,319.44	1,529,752.86
5. Cost of materials			
a) Cost of raw materials, supplies and trading stock	210,915,533.19		181,661,536.54
b) Cost of purchased services	1,796,292.00		975,085.89
		212,711,825.19	182,636,622.43
6. Personnel expenses			
a) Wages and salaries	26,760,411.92		18,920,547.53
b) Social security, pension and other benefit costs, • thereof for pensions: DM 179.336,25 (prior year: DM 510.170,25)	4,928,989.12		3,745,828.57
		31,689,401.04	22,666,376.10
7. Depreciation on intangible assets and property, plant and equipment		3,189,708.67	2,454,763.42
8. Other operating expenses		23,864,671.34	18,174,360.57
9. Income from investments • thereof from affiliated enterprises: DM 4.276.005,55 (prior year: DM 0,00)		4,276,005.55	0.00
10. Income from long-term loans		31,552.83	32,219.22
11. Other interest and similar income • thereof from affiliated enterprises: DM 38.351,17 (prior year: DM 0,00)		52,098.52	20,171.24
11. Interest and similar expenses • thereof to affiliated enterprises: DM 77.264,93 (prior year: DM 0,00)		2,113,699.38	1,223,205.83
13. **Result from ordinary activities**		**12,122,042.58**	**14,121,194.77**
14. Taxes on income		4,320,064.52	6,089,738.44
15. Other taxes		31,113.14	78,205.02
16. Profit share of dormant partners		805,381.95	641,666.97
17. **Net income for the year**		**6,965,482.97**	**7,311,584.34**
18. Profit carried forward from the prior year		12,377.22	792.88
19. **Retained earnings**		**6,977,860.19**	**7,312,377.22**

AG-INCOME STATEMENT
FOR THE FISCAL YEAR 1997

Development of fixed assets in 1997

	ACQUISITION AND PRODUCTION COST				
	Jan 1, 1997 DM	Additions DM	Disposals DM	Transfer DM	Dec 31, 1997 DM
I. INTANGIBLE ASSETS					
Concessions, industrial and similar rights and licenses in such rights and assets	617,390.81	470,472.88	0.00	0.00	1,087,863.69
II. PROPERTY, PLANT AND EQUIPMENT					
1. Land and buildings including buildings on third-party land	9,970,015.20	648,389.62	6,501.44	33,955.19	10,645,858.57
2. Other equipment, factory and office equipment	8,088,808.97	3,718,780.50	605,902.28	17,448.48	11,219,135.67
3. Advance payments and construction in progress	51,403.67	342,553.18	0.00	-51,403.67	342,553.187
	18,110,227.84	**4,709,723.30**	**612,403.72**	**0.00**	**22,207,547.42**
III. FINANCIAL ASSETS					
1. Shares in affiliated companies	3,649,416.30	772,464.00	0.00	0.00	4,421,880.30
2. Other loans	546,059.45	30,000.00	50,205.58	0.00	525,853.87
3. Advance payments	0.00	744,342.43	0.00	0.00	744,342.43
	4,195,475.75	**1,546,806.43**	**50,205.58**	**0.00**	**5,692,076.60**
	22,923,094.40	**6,727,002.61**	**662,609.30**	**0.00**	**28,987,487.71**

ELSA AG, parent company

ACCUMULATED DEPRECIATION				NET BOOK VALUES	
Jan 1, 1997 DM	Additions DM	Disposals DM	Dec 31, 1997 DM	Dec 31, 1997 DM	Dec 31, 1996 DM
459,049.81	141,584.88	0.00	600,634.69	487,229.00	158,341.00
882,869.12	412,581.81	1,302.44	1,294,148.49	9,351,710.08	9,087,146.08
4,942,272.97	2,635,541.98	591,555.28	6,986,259.67	4,232,876.00	3,146,536.00
0.00	0.00	0.00	0.00	342,553.18	51,403.67
5,825,142.09	**3,048,123.79**	**592,857.72**	**8,280,408.16**	**13,927,139.26**	**12,285,085.75**
252,114.44	0.00	0.00	252,114.44	4,169,765.86	3,397,301.86
0.00	0.00	0.00	0.00	525,853.87	546,059.45
0.00	0.00	0.00	0.00	744,342.43	0.00
252,114.44	**0.00**	**0.00**	**252,114.44**	**5,439,962.16**	**3,943,361.31**
6,536,306.34	**3,189,708.67**	**592,857.72**	**9,133,157.29**	**19,854,330.42**	**16,386,788.06**

A Introductory remarks

The consolidated financial statements and the financial statements of ELSA AG shall be explained together as stated below; if not otherwise specified the statements made refer to both financial statements.

ELSA AG is a large corporation within the meaning of § 267 of the German Commercial Code (HGB).

The balance sheet and the income statement have been prepared in accordance with the format of §§ 266, 275 HGB and § 158 (1) of the Corporation Law (AktG); for the income statement the cost summary method has been used as in prior years.

B Companies included in consolidation

All companies in Germany and abroad for which ELSA AG is directly or indirectly entitled to the majority of the voting rights of the shareholders are included in consolidation. An exception applies for ELSA America, Inc., Santa Clara, which has not been consolidated pursuant to § 296 (2) HGB.

The following companies are included in consolidation:

Name, Headquarter	Share	Subscribed capital Dec 31, 1997 DM	Shareholders equity Dec 31, 1997 DM	Result 1997 DM	Date of initial consolidation
ELSA AG, Aachen	100%	5,800,000.00	14,278,595.30	6,965,482.97[2)]	Jan 1st, 1997
ELSA, Inc., San Jose, California, USA	100%	77,740.00	7,331,616.07[1)]	3,835,982.55	Jan 1st, 1997
ELSA Japan, Inc., Tokyo, Japan	95%	813,120.00	813,120.00[1)]	0.00	Dec 15, 1997

1) Excluding item for currency translation adjustment amounting to a total of KDM 542.

2) The result of ELSA AG includes the simultaneous collection of the result of ELSA, Inc.

C Principles of consolidation

Capital consolidation is performed according to the book value method according to § 301 (1) sentence 2 no. 1 HGB. In this context the book values of the participations are compared to the prorated capital that must be consolidated at the time of the initial consolidation. Differences arising in this connection, if they relate to hidden reserves, are allocated to the appropriate assets. Any remaining differences are shown as differences from capital consolidation.

Intercompany results, sales, expenses and income as well as receivables and liabilities between the companies included in full consolidation are eliminated.

For the translation of shareholders' equity the historical average rate of exchange, for asset and liability items the exchange rate on the balance sheet date and for items of the income statement the annual average rate of exchange are used.

D Accounting and valuation principles

The assets and liabilities included in the consolidated financial statements are stated and valued uniformly on the basis of the accounting and valuation principles which are applicable and applied for the financial statements of ELSA AG. Valuation options pursuant to the German Commercial Code are used uniformly and the values stated in the individual financial statements of the Group companies adjusted in this respect.

The accounting and valuation principles applied to date have been retained with the exception of the valuation of inventories. In detail, the procedure was as follows:

■ *Intangible fixed assets*

Intangible fixed assets are valued at acquisition cost less depreciation. Depreciation is calculated according to the expected useful life of the assets, applying the straight-line method in accordance with tax regulations.

Property, plant and equipment

Property, plant and equipment is valued at acquisition or production cost and—if depreciable—less accumulated depreciation. Depreciation is based on the expected useful life of the assets; the straight-line or declining balance method is used in accordance with the tax regulations. In the case of the declining balance method, the transition to straight-line depreciation takes place as soon as the latter leads to higher depreciation. The simplification rule of R 44 (2) sentence 3 of the Income Tax Directive (EStR) for the calculation of the depreciation of movable assets acquired during a fiscal year is applied. Low-value assets are fully depreciated in the year of acquisition. For these fully depreciated low-value assets a disposal of the same amount is shown in the fixed assets movement schedule in addition to the depreciation.

Financial assets

Shares in affiliated companies are shown at acquisition cost or at the lower value attributable on the balance sheet date.

Other loans include loans to employees, which are stated at nominal value.
The item prepayments for financial assets contains the future share in the capital stock of ELSA Asia, Inc. in Taiwan. It has been valued at acquisition cost.

Inventories

Raw materials and supplies are valued according to the FIFO method, goods at the average acquisition cost or, if lower actual values were to be taken according to the lower of cost or market principle, at these values. Products and services are valued at production cost or at the lower actual value. The production costs of finished goods and services and work-in-process contain necessary overhead costs in addition to the directly allocable costs.

Cost components that do not have to be capitalized pursuant to tax regulations are not included in the production cost.

■ *Receivables and other assets*

Receivables and other assets are stated at nominal value. Sufficient individual bad debt allowances are set up for doubtful accounts. In addition trade receivables are reduced by an appropriate lump-sum reserve to cover the general collectibility risk.

■ *Cash on hand, balances at banks, prepaid expenses*

Cash, cash equivalents and prepaid expenses are stated at nominal value.

■ *Accruals*

Pension reserves are calculated actuarially on the basis of an interest rate of 6 % and valued according to the "Teilwertmethode" (a method similar to the "entry age method") according to § 6 a of the Income Tax Law (EstG).

The accrued taxes relate to the taxes not yet assessed for the fiscal year and the prior year.

The other accruals are set up for all other uncertain liabilities and potential losses. The accruals are set up in the amount necessary under prudent business judgment; they correspond to the expected expenditure and potential losses. All recognizable risks are accounted for.

■ *Liabilities*

Liabilities are stated at their repayment amount.

■ *Currency translation*

Receivables and liabilities in foreign currency are translated at the exchange rate at the time of occurrence; if the exchange rate as of the balance sheet date is lower for receivables or higher for liabilities, valuation is based on the exchange rate of the balance sheet date.

E Explanations to the balance sheet and the consolidated balance sheet

I Fixed assets

The development of fixed assets in the individual financial statements and in the consolidated financial statements can be seen in the following fixed assets movement schedule:

Shares in affiliated companies

As of December 31, 1997 ELSA AG has at least a 20 % share in the following companies:

	Book values as of 31.12.1997 DM
***ELSA, Inc.**, San Jose, California, U.S.A.*	3,397,300.86
***ELSA Japan, Inc.**, Tokyo, Japan*	772,464.00
***ELSA America, Inc.**, Santa Clara, California, U.S.A.*	1.00
	4,169,765.86

ELSA, Inc. has prepared its financial statements as of December 31, 1997. The shareholders' equity stated therein amounts to US $ 2,248,285 excluding the net income for the year 1997. The net income for fiscal year 1997 amounts to US $ 2,145,284.

ELSA Japan, Inc. did not start operations in 1997. Its shareholders' equity amounts to Yen 60,000,000.00.

The financial statements of **ELSA America, Inc.** as of September 30, 1997 show a negative shareholders' equity of US $ 36,030.80. The net income for the year shown for fiscal year 96/97 amounts to US $ 191,760.20.

For the sake of correct presentation the item "Prepayments for financial assets" has been included in the balance sheet, showing the future share in the capital stock of **ELSA Asia, Inc.** in Taiwan.

Moreover we refer to our information given on the companies included in consolidation.

III Inventories

Raw materials and supplies have been valued in the fiscal year according to the FIFO order of consumption method (prior year: weighted average price). The change in the valuation method leads to a reduction in result of approx. *KDM 651*.

IV Receivables and other assets

There are no receivables and other assets with a residual term of more than one year at ELSA AG or the ELSA Group.

V Receivables from affiliated enterprises

As in the prior year, there are no receivables with a residual term of more than one year at ELSA AG or the ELSA Group.

VI Deferred taxes

KDM 234 of the deferred tax assets of the ELSA Group amounting to approx. *KDM 514* result from the individual financial statements of the companies included in consolidation. Deferred tax assets of approx. *KDM 278* contrast with deferred taxes on the liability side of *KDM 44*. Moreover deferred tax assets of approx. *KDM 280* were shown in the balance sheet due to consolidation measures with effect on result pursuant to § *306 HGB*.

VII Subscribed capital

The subscribed capital was increased by KDM 500 by a capital contribution by the shareholders' resolution of August 20, 1997.
In the context of the conversion of August 25, 1997 the Company issued 1,160,000 fully paid-in bearer shares with a nominal value of DM 5.00 each.

VIII *Capital reserve*

The capital reserve of *KDM 1,500* results from the premium paid in the context of the capital increase.

IX *Difference from capital consolidation*

The credit difference from capital consolidation amounting to KDM 98 results from exchange rate fluctuations between the time of the acquisition of the participation and the initial consolidation.

X *Other accruals*

Other accruals split up as follows:

ELSA Group		ELSA AG	
	12/31/1997 DM		**12/31/1997 DM**
Warranties	1,355,000.00	*Warranties*	1,355,000.00
Vacation claims	640,237.63	*Vacation claims*	563,371.00
Outstanding invoices	548,750.11	*Outstanding invoices*	526,540.12
Reimbursement of storage costs	480,000.00	*Reimbursement of storage costs*	480,000.00
Costs for advertising expenses	163,752.20	*Costs for advertising expenses*	163,752.20
Costs of financial statements	156,000.00	*Costs of financial statements*	156,000.00
Employer's liability insurance	150,000.00	*Employer's liability insurance*	150,000.00
Other	326,626.74	*Other*	191,514.06
	3,820,366.68		**3,586,177.38**

XI Liabilities

Liabilities of the **ELSA Group** as of December 31, 1997:

	Residual term				
	Less than 1 year DM	**2-5 years DM**	**More than 5 years DM**	**Total DM**	**Secured by land charges DM**
Liabilities due to banks	33,846,485.39	1,385,942.00	6,399,560.52	41,631,987.91	8,291,569.52
Trade payables	22,580,291.23	0.00	0.00	22,580,291.23	0.00
Other liabilities	3,114,747.61	0.00	0.00	3,114,747.61	0.00
Total liabilities	**59,541,524.23**	**1,385,942.00**	**6,399,560.52**	**67,327,026.75**	**8,291,569.52**

Liabilities of **ELSA AG** as of December 31,1997:

	Residual term				
	Less than 1 year DM	**2-5 years DM**	**More than 5 years DM**	**Total DM**	**Secured by land charges DM**
Liabilities due to banks	33,846,485.39	1,385,942.00	6,399,560.52	41,631,987.91	8,291,569.52
Trade payables	22,320,525.07	0.00	0.00	22,320,525.07	0.00
Other liabilities	3,102,993.91	0.00	0.00	3,102,993.91	0.00
Total liabilities	**59,270,004.37**	**1,385,942.00**	**6,399,560.52**	**67,055,506.89**	**8,291,569.52**

The usual retention of ownership for the delivery of raw materials, consumables and supplies and goods applies for the trade receivables.

F Explanation to the income statement and the consolidated income statement

I Sales

The sales of the fiscal year split up as follows:

ELSA Group

	1997 KDM
a)	
According to business divisions:	
• *Computer Graphics*	196,692
• *Data Communications*	89,873
	286,565

	1997 KDM
b)	
According to geographical markets:	
• *Germany*	209,038
• *EU and bordering countries*	34,676
• *North America*	40,539
• *Asia*	2,202
• *Others*	110
	286,565

ELSA AG

	1997 KDM
a)	
According to business divisions:	
• *Computer Graphics*	188,966
• *Data Communications*	86,314
	275,280

	1997 KDM
b)	
According to geographical markets:	
• *Germany*	209,038
• *EU and bordering countries*	34,676
• *North America*	29,254
• *Asia*	2,202
• *Others*	110
	275,280

II *Expenses or income not relating to the period*

There were no significant expenses or income not relating to the period in the fiscal year.

III *Income from long-term loans*

For the sake of correct presentation the item "Income from long-term loans" has been included in the income statement. In this case the prior year figures have been adjusted to the figures stated in 1997.

IV *Extraordinary expenses and income*

The net result for the year results exclusively from the result of ordinary activities. Therefore it is not necessary to divide up the tax expense amongst the partial results of ordinary and extraordinary activities.

G Other disclosures

Contingent liabilities and other financial obligations

Other than the liabilities and accruals listed in the balance sheet there are no other significant contingent liabilities.

The other financial obligations of **ELSA AG** amount to KDM 2,.405 and mainly relate to the purchase agreement for the land and buildings of the Fuehren fabric factory.

Moreover, at the foreign Group companies the following obligations from rent, leasing and similar continuous obligations exist:

ELSA Group			
1998 TDM	1999 TDM	2000 and later TDM	Total TDM
479	366	13	858

Therefore the **ELSA Group** has other financial obligations amounting to approx. *KDM 3,263*.

II *Number of employees*

The number of employees developed as follows during fiscal year 1997:

ELSA Group

	03/31/97	06/30/97	09/30/97	12/31/97	ø1997
White-collar workers	307	339	347	365	340
Blue-collar workers	62	60	66	72	65
Temporary workers and students	103	87	73	74	84
	472	486	486	511	489

ELSA AG

	03/31/97	06/30/97	09/30/97	12/31/97	ø1997	ø1996
White-collar workers	290	315	319	337	315	204
Blue-collar workers	62	60	66	72	65	51
Temporary workers and students	103	87	73	74	84	76
	455	462	458	483	464	331

III *Appropriation of profit*

The Management Board suggests that the retained earnings are to be reinvested in full and transferred to the revenue reserve for the purpose of an increase in capital.

IV *Bodies*

a) **Management Board/Management**

Until the conversion of ELSA GmbH into a stock corporation Mr. Theo Beisch, Aachen, was the sole general manager of the Company.

On August 25, 1997 the Supervisory Board appointed the following Management Board :

Chairman:	Deputies:
Theo Beisch, Aachen	*Peter Gueldenberg, Eschweiler*
	Josef Beisch, Aachen

In 1997 the entire total remuneration of the management/Management Board amounted to *KDM 1,700*

b) **Supervisory Board**

The Supervisory Board of ELSA AG has the following members:

Chairman:

Max Beisch, Melsbach (until December 18,1997)

Dipl.-Ing. Wolfgang Dondorf, Marienheide (from December 18, 1997 on)

Deputies:

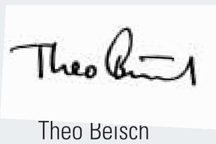
Friedhelm Hammer, attourney, Aachen (until December 18,1997)

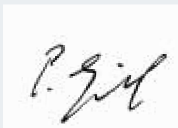
Theodor Ludger Lieven, Thinnister-Clermont, Belgium (from December 18, 1997)

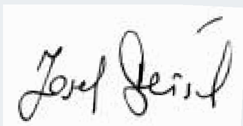
Dipl.-Kfm. Dr. Hanno Schmitz-Hüser, Certified Public Accountant/Tax Advisor, Stolberg

The total remuneration of the Supervisory Board amounts to *DM 17,000.00* in 1997.

Aachen, March 12, 1998


Theo Beisch


Peter Gueldenberg


Josef Beisch

Auditor's opinion

Based upon our audit, we herewith render the following unqualified opinion on the financial statements and the consolidated financial statements of ELSA Aktiengesellschaft, Aachen, as of December 31, 1997 and on the combined management report and Group management report for fiscal year 1997:

*"The accounting, the financial statements and consolidated financial statements, which we have audited in accordance with professional standards, comply with the German legal provisions. The financial statements and the consolidated financial statements present, in compliance with generally accepted accounting principles, a true and fair view of the net worth, financial position and results of **ELSA** Aktiengesellschaft and of the Group. The combined management report and Group management report is in agreement with the financial statements and with the consolidated financial statements."*

Hamburg, March 13, 1998

ARTHUR ANDERSEN
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft mbH

Jäckel
Wirtschaftsprüfer

Ludwig
Wirtschaftsprüfer

	1997 DM
ASSETS	
CURRENT ASSETS	
Cash and cash equivalents	4,023,370.26
Accounts receivable trade	21,780,238.73
Other receivables	3,241,092.91
Inventories	54,779,017.66
Prepaid expenses	1,501,916.45
Other current assets	291,310.35
	85,616,946.36
PROPERTY, PLANT AND EQUIPMENT	
Land, land improvements and buildings	9,693,398.08
Machinery and equipment	6,101,829.35
	15,795,227.43
LONG TERM INVESTMENTS	**525,854.87**
INTANGIBLE ASSETS	
Licenses and similar rights	521,039.34
Software costs	2,839,992.86
	3,361,032.20
TOTAL ASSETS	**105,299,060.86**

The accompanying Notes are an integral part of these Consolidated Financial Statements.

	1997 DM
LIABILITIES AND SHAREHOLDERS' EQUITY	
CURRENT LIABILITIES	
Short-term borrowings incl. current portion of long-term debt	33,846,485.39
Accounts payable trade	22,580,291.23
Accounts payable other	3,114,747.61
Accrued liabilities	6,614,097.51
	66,155,621.74
NON-CURRENT LIABILITIES	
Long-term debt	7,785,502.52
Provision for pensions	478,647.00
Deferred tax liability	2,227,972.38
	10,492,121.90
	76,647,743.64
DORMANT PARTNER	**11,500,000.00**
MINORITY INTERESTS	**40,656.00**
SHAREHOLDERS' EQUITY	
Capital stock	5,800,000.00
Capital reserve	1,500,000.00
Retained earnings	9,066,681.92
Cumulative translation adjustment	743,979.30
	17,110,661.22
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	**105,299,060.86**

3D engineering workstation	Construction design workstation with CAD environment
ATM	Asynchronous Transfer Mode High-speed data transfer between computer networks.
Bandwith	The bandwidth determines the data transfer capacity of a data line. The corresponding measurement unit is "bits per second", abbreviated as bps. ISDN systems can reach a transfer capacity of 128 kbps, exceeding the bandwidth of conventional copper lines used in the telephone system.
Cable Modem	Special modem technology for transferring data on the TV cable network.
CAD	Computer Aided Design Modern workstations in all areas of the construction business employ computers as time and cost-saving construction tools. CAD workstations require particularly powerful computer systems, demanding both pro cessor performance and a fast graphics system. High demands are made of the graphics system, particularly in the area of three-dimensional visualisation.
Digital Video	Just as for sound recording – where digital technology has superseded analogue technology – digital recordings are revolutionising the way moving pictures are recorded. Digital video will gain popularity with DVD technology and the further spread of these drives, and the computer is an ideal tool for post-processing digital videos.
Graphics Board	Plug-in expansion board for the PC which prepares, processes and transfers graphics data (images) onto a graphics output unit (e.g. a monitor or projector). One or more special processors on the graphics board perform the intensive computational work required to display moving images on the computer monitor.
Grahics Card/Graphics Controller	Alternative terms for a graphics board.
Graphic System	A graphics system is a combination of a graphics board and a monitor.
IEEE1394	New standard for higher data transfer rates at the serial port of a computer.
Intranet	Internal company network based on the same protocols and graphical user interfaces as the Internet. Used for distributing information within a company.
ISDN	Integrated Services Digital Network Europe-wide standardised digital network for the use of voice and data services. Apart from its many convenience features, ISDN enables high-speed and secure data transfers.
ISDN Adapter	An external device or plug-in board for connecting a PC to the ISDN network. Thus the ISDN network can be used for transferring data to and from remote computers.
ISDN Router	A device that connects networks, in order to exchange data via the ISDN network. ISDN routers are mainly used for accessing remote systems and networks, such as the Internet.
LCD	Liquid Crystal Display Flat monitors using technology based on the physical behaviour of liquid crystals under the influence of variable currents and polarised light. LCDs offer the advantages of low space and energy requirements in comparison to conventional monitors.

Multi-screen Technology	Graphics information from one computer are displayed on multiple monitors. Multi-screen technology is applied, for example, at stock exchanges where different international stock exchanges can be monitored simultaneously at a multi-screen workstation.
Modem	Device for exchanging data between computers over analogue telephone lines.
OEM	Original Equipment Manufacturer Licensees of OEM products incorporate products from OEM licensors into their own range under their own brand name or use it as a component of an overall solution developed by them.
Operating System	The operating system can be viewed as the computer working environment and as the command interface between the user and the computer itself. Examples of operating systems are Windows and Unix.
Online Service	Service providers, such as CompuServe and AOL, furnish their members with access to online information sources and also to theInternet.
PC Cards	Credit-card sized cards for insertion into Laptops or Notebooks. PC cards enable the easy and flexible expansion of a computer's functionality. This means that, for example, a modem PC card can be used to connect a notebook to telephone networks for data exchange.
Remote Access	Access to the hardware and software of a remote system via a network connection. Unlike remote maintenance (remote control), the remote computer cannot be controlled, but its resources are made available. Typical remote access tasks are Internet access or the connection of staff in the field to the computer at their base.
Remote Control	Control of a remote computer from another PC via a network connection, for example, via telephone, ISDN, or a LAN (Local Area Network). Typical applications are performing maintenance and diagnostic activities on the remote system.
SOHO	Small Office/Home Office Describes the target market of small to medium-sized office environments and home workers.
Terminal Adapter	External ISDN desktop device for connecting a computer to the ISDN network (also ISDN adapter).
UNIX	An operating system that has been highly regarded among the various operating systems for about the last 30 years.
Video Input and Output Ports	Interface to graphics boards for processing analogue video signals and outputting digital images from computers in video signal format.
Videoconferencing System	Enables visual communication over large distances by transferring images, speech and data.
Virtual Reality	Representation of environments through three-dimensional computer modelling. In a near-perfect animated 3D surrounding, an observer can move freely in virtual space and experience views and perspectives in 3D.
xDSL	Digital Subscriber Line New, high-speed method of transferring data via the existing copper cabling of the analogue telephone network. xDSL includes four different protocols: ADSL, SDSL, HDSL and VDSL. The protocols differ primarily in terms of the transfer rates available for transmission and reception, and their maximum possible cable lengths.

1998

IPO – Neuer Markt in Frankfurt, Germany
Global expansion of manufacturing

1997

ELSA Japan, Inc., Tokyo, incorporated
ELSA Asia, Inc., Taipei, incorporated as sales and marketing organisation
ELSA converted from GmbH to ELSA AG, a stock corporation

1996

First international **OEM customer: Compaq**

1995

DIN EN ISO 9001 certification

1993

Strengthened U.S. entry: **ELSA, Inc.**, Santa Clara

1991

ELSA Asia, Inc. established as procurement office

1989

First overseas subsidiary: **ELSA America, Inc.**

1986

Computer Graphics at **ELSA**

1980

ELSA incorporated: first activity in industrial electronics

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Sonnenweg 11
52070 Aachen
Germany
Internet www.elsa.de

Subsidiaries:
ELSA, Inc.
2231 Calle De Luna
Santa Clara, CA 95054
USA
Internet www.elsa.com

ELSA Asia, Inc.
7F-11, No.188, Sec. 5
Nanking East Road
Taipei 105
Taiwan, R.O.C.
Internet www.elsa.com

ELSA Japan, Inc.
Mita Suzuki Building 3F
5-20-14 Shiba, Minato-ku
Tokyo 108-0014
Japan
Internet www.elsa.com