



**During another difficult year with most of our markets remaining very challenging, the Group has reduced its debt and continued to work on operational improvements in all respects.**

The improvement strategy, adopted in 2000 and pursued during 2001, continued unabated during 2002. We worked on improving operational performance in all respects and irrespective of the generally lower level of customer demand. We kept our central costs low and delivered lower costs and reduced working capital in the subsidiaries. We continued to effect disposals amongst the European industrial businesses and most importantly, we again reduced the Group net debt which ended the year at £87.4m, a reduction of 29% in the year and a reduction of nearly 50% from when the debt reduction programme started in May 2000.

Gross capital expenditure in the year was reduced to 74% of depreciation. However, necessary and justifiable investment was maintained. Indeed, two new factories were opened in the year to relocate Senior Aerospace BWT and Senior Aerospace Ermeto into modern efficient factories.

During the course of the year, manufacturing recessionary influences became more obvious in most of the developed, industrialised world. Economic conditions in Germany were particularly weak throughout 2002 with those in the rest of continental Europe and the USA weakening during the period. Canada and, to a lesser extent, the UK were relatively buoyant.

The global airline industry continued to react adversely to the economic slowdown and the threat of international terrorism. Whilst there was some recovery in traffic volumes during 2002, airline profitability, particularly in the USA, remains very poor. As a consequence, the major suppliers to the airlines – the aircraft and engine builders who are our customers – continued to adjust their production schedules downwards throughout 2002. Hopefully 2003 will see more settled levels of demand.

Senior Automotive encountered mixed market conditions. In Europe, the overall demand for vehicles fell by about 3% but the proportion of diesel engine vehicles continued to climb. In the USA, demand remained higher than we had originally expected primarily because of dealer incentives and cheap financing. As a result vehicle sales remained at healthy levels (16.8m cars and light trucks) and, importantly, dealer stocks of vehicles were at the same level in December 2002 as they were in December 2001 – 59 days. Destocking in 2003 should not, therefore, be a significant issue although demand levels are expected to show declines over 2002.

In the industrial markets in which we participate, UK construction was satisfactory, semi-conductor equipment continued to be severely depressed, oil and gas was slightly better than expected, power generation started well but finished weaker and process plant (e.g. chemicals and steel) remained tough.

### **Prospects**

We enter 2003 with many business opportunities. In aerospace, the joint strike fighter programme (JSF) at Lockheed Martin is gathering momentum with many of our operations being involved, as they are with the new large Airbus A380. In automotive, volume increases are being seen in our South Africa facility and, in the longer term, diesel engine performance is beginning to attract more interest in the USA, the common rail system having transformed the diesel engine's fortunes in Europe.

Throughout the operations, we continue to seek operational performance and management improvements in all areas – lean production, more effective design and rigorous financial routines. Whilst we plan to continue our existing policies and strategies throughout 2003, now the debt level is much lower, we can look forward to being able to review these in the medium term in order to take better advantage of the economic upturn when it comes.

Our employees have made valuable contributions during another period of challenge and change and, as an acknowledgement of the part they have played, the Annual Report features a small selection of the men and women of our organisation, in addition to the hardware traditionally highlighted.



- 1 Graham Menzies with Sylvio Deveau, Dino Pettiford and Peter Fontecchio who have all completed 40 years' service with Senior Aerospace Metal Bellows.
- 2 John Williams and Tony Shannon at Senior Aerospace Jet Products.
- 3 The management team of Senior Aerospace Ermeto outside their new factory.
- 4 Greg Frye presents Cessna's recognition award to Wade Bailey at Senior Aerospace Composites.

Senior Aerospace had to adjust capacity almost monthly throughout 2002 as the industry reduced demand. We squeezed out cost and working capital and ended the year with an improving performance.

Demand continued to slow during the year and all operations experienced rescheduling by customers resulting, almost without exception, in lower volumes. Consequently, many capacity adjustments needed to be made. The operations responded well to these circumstances.

Metal Bellows, which specialises in edge-welded bellows applications, primarily for infinite-life low-maintenance pumps, accumulators and reservoirs, performed exceptionally well despite the semi-conductor industry failing to recover. They were helped by an increase in defence and military spending. During the year, medical application volumes increased, installation of a new business computer system began and design engineering proposals were made for substantial work on JSF.

In San Diego, California, Senior Aerospace has two machine shops making structural parts for civil and military jet engines as well as the engine mountings into the nacelles on the aeroplanes. At Ketema, the two main customers both adjusted schedules downwards and the company suffered considerable disruption as a result. By the last quarter of the year, however, a degree of stability had returned. At Jet Products, volumes came down significantly, primarily as a result of the Boeing 737 build-rate being halved. As a result of the need to reduce capacity, its small feeder factory was closed and the operations moved into the main facility. Towards the end of the year, the managements of Ketema and Jet Products were amalgamated, not only as a cost reduction measure, but also to instil the very highest standards of manufacturing excellence necessary to profitably meet the demands of this sector of the market. These two operations enter 2003 in good operational shape and with demand slightly ahead of plan.

In France, Ermeto moved out of five old buildings into one new modern facility. The prospects for the company continue to be encouraging and it was one of the few operations to grow its sales during the year. At Calorstat, an unsatisfactory loss in 2001 was replaced by a breakeven trading result in 2002 as a result of the cost reduction measures taken. 2003 has an improved outlook as new business from Airbus is in production.

Bosman, in Holland, had an eventful year with the rebuilding of the main assembly hall (following the roof collapse in 2001), reductions in customer schedules and a major reduction in its airline repair business. To counter this the company successfully developed aftermarket business for the industrial gas turbine sector. The company ended the year with an encouraging order book for 2003.

Senior Aerospace has two composite ducting businesses, BWT in the UK and Composites in the USA. BWT suffered a substantial schedule downturn from its main customer, Bombardier, which coincided with BWT moving into a new facility. Together with Composites, BWT is working on the design and development of the cockpit ducting system for the A380, the costs of which are being expensed as incurred. It is expected that this work will be finished early in 2003. As a result of the relationship on this programme, additional work with Airbus may be secured. Composites had a solid order book throughout 2002 and despite a small reduction in sales over 2001, increased its profit. The key to this was a full year deployment of lean manufacturing techniques. However, their biggest customer, Cessna, recently reduced its schedules for 2003.

At Bird Bellows, in the UK, a modest reduction in sales for the year was accompanied by a similarly modest reduction in profitability. This company is the sole supplier to Airbus for the flexible wing duct joints and has been nominated for the A380 programme.

At SSP, in Los Angeles, schedules strengthened helped by the ramp up of the Rolls-Royce Trent 500 programme and the higher levels of spending on military programmes by the US Government. The financial performance of the company improved and is expected to improve further in 2003. This company is an industry leader in high temperature ducting system design. Modernisation of the existing leasehold facility is anticipated to begin during 2003.

Throughout Senior Aerospace, improvements in on-time delivery and inventory turns have been delivered as a result of the strategy to improve operational effectiveness. Further improvements are expected. Capital expenditure for the Division is likely to be significantly less than depreciation in 2003 because, with the industry in the doldrums, the Division needs little additional capacity. However, few programmes in the industry have been cancelled and the sales and engineering staff have remained busy. The principal exception to this was Fairchild Dornier's receivership, when the FD728 development was halted and we had to write off £0.3m. Due to our continued engineering activity we do not expect to lose market share whilst the industry awaits an upturn. Instead, we expect to win additional future programmes to allow us to grow again when confidence returns to the aerospace industry.