# Senior plc Interim Report 2006

## Senior plc corporate profile

**Senior is an international manufacturing group with operations in 11 countries.** Senior designs, manufactures and markets high technology components and systems for the principal original equipment producers in the worldwide aerospace, diesel engine, exhaust system and energy markets.

# Financial Highlights

| | Half-year to 30 June | | |
|---|---|---|---|
| | **2006** | 2005 | |
| Revenue | **£195.6m** | £166.9m | +17.2% |
| Operating profit | **£11.6m** | £9.5m | +22.1% |
| Profit before taxation | **£8.7m** | £7.2m | +20.8% |
| Basic earnings per share | **2.24p** | 1.92p | +16.7% |
| Adjusted profit before taxation(1) | **£9.1m** | £7.4m | +23.0% |
| Adjusted earnings per share(1) | **2.33p** | 1.99p | +17.1% |
| Proposed interim dividend per share | **0.65p** | 0.65p | |
| Free cash flow(2) | **(£2.4m)** | £1.4m | |
| Net borrowings | **£75.6m** | £59.1m | |

(1) Adjusted profit before taxation and adjusted earnings per share arise before a £nil loss on disposal of fixed assets (2005 – £0.2m) and a £0.4m charge for amortisation of intangible assets acquired on acquisition (2005 – £nil).

(2) See Note 9(b) for derivation of free cash flow.

## The Group had an excellent first half of the year with adjusted profit before taxation increasing 23% over the prior year.

In Aerospace, revenue grew strongly as commercial aircraft and engine manufacturers increased build rates at a fast pace and Sterling Machine began to contribute following its acquisition in January 2006. In the Flexonics Division, energy markets were strong and automotive markets were flat, but still healthy. Production of the new heavy duty diesel engine products is on schedule to commence in the final quarter of this year. Prospects for the Group remain very encouraging.

### Financial Results

Senior, in common with all companies listed on security exchanges within the European Union, now prepares its financial statements according to International Financial Reporting Standards (IFRS). All figures, including comparatives (which unless otherwise stated are for the first six months of 2005), have been prepared in accordance with IFRS.

In the six months to 30 June 2006, Group revenues were £195.6m, an increase of 17.2% over the prior year (2005 – £166.9m). Operating profit was £11.6m and represented a 22.1% increase over the £9.5m reported for the first half of 2005. When compared to the first six months of 2005, the effect of currency movements on translating overseas revenues and earnings into sterling was to increase revenue by £5.6m and operating profit by £0.4m.

In addition to the statutory information, the Group has consistently reported adjusted figures to better reflect the underlying performance of the business. These are calculated before: (i) profit/loss on disposal of fixed assets; (ii) profit/loss on disposal of operations; and (iii) amortisation of intangible assets arising from acquisitions. In the first half of 2006, the loss on disposal of fixed assets was £nil (2005 – £0.2m) and amortisation of intangible assets arising from acquisitions was £0.4m (2005 – £nil). Adjusted operating profit was, therefore, £12.0m (2005 – £9.7m).

Finance costs consist of interest payable on borrowings of £3.0m (2005 – £2.5m) and interest on defined benefit pension obligations of £0.4m (2005 – £0.5m). The increase was due to higher levels of both borrowings and interest rates. Investment income fell from £0.7m in the first half of 2005 to £0.5m as the interest rate differential between the US$ and sterling narrowed.

Profit before tax was £8.7m (2005 – £7.2m). Adjusted profit before tax, at £9.1m, was 23.0% above the prior year (£7.4m). With an effective tax rate of 17.6% (2005 – 17.6%) and an increase in the number of shares in issue, adjusted earnings per share was 2.33p. This was 17.1% above the 1.99p adjusted earnings per share reported for the first half of 2005.

### Acquisition

On 27 January 2006 the Group completed the acquisition of Sterling Machine Co. Inc., a US manufacturer of transmission and rotor-head helicopter components for military platforms, principally to Sikorsky Aircraft Corporation. The consideration for the business, including assumed net debt, was US$37.6m (£21.4m) which was funded by the placing of 15 million new Senior plc shares at 60p each (raising £8.8m) and utilisation of the Group's existing borrowing facilities.

During the five-month period from the date of acquisition to 30 June 2006, Sterling Machine reported revenue of £5.2m and trading profit of £0.6m. Further details of the acquisition can be found in Note 8 of these Interim Financial Statements.

## Cash Flow and Borrowings

Free cash flow (net cash flow from operating activities after net capital expenditure, interest and tax but before acquisitions, disposals, share issues and dividend payments) was an outflow of £2.4m (2005 – £1.4m inflow). Note 9(b) sets out its calculation. The reduction was mainly due to the ongoing investment in production equipment, for the new heavy duty diesel products and increased aerospace capacity, together with increased working capital requirements arising from higher sales volumes.

Net debt increased by £13.2m in the six-month period to be £75.6m at 30 June 2006. The increase was due to the free cash outflow of £2.4m, dividend payments of £4.4m and the acquisition of Sterling Machine (consideration £21.4m). These outflows were partially offset by proceeds of £8.9m from the issue of new shares, a non-cash movement of £0.1m and a beneficial currency movement of £6.0m. The Group has most of its borrowings denominated in US$, as a match against its US$ assets, and the weakening US$ (from $1.72: £1 at the end of December 2005 to $1.85: £1 at the end of June 2006) caused the reported sterling net debt to decrease by £6.0m in the six-month period.

## Dividend

The Board has declared an unchanged interim dividend of 0.65p per share. This will be paid on 30 November 2006 to shareholders on the share register at 3 November 2006.

## Aerospace Division

Revenue for the first six months of 2006 increased by 27.9% to £95.3m (2005 – £74.5m) and adjusted operating profit by 28.6% to £8.1m (2005 – £6.3m). Adjusted operating margins remained at 8.5% as the impact of higher raw material prices was offset by increased volumes.

The wide-bodied and business jet industries continued to increase build rates of aircraft and engines. Boeing and Airbus collectively delivered 414 aircraft in the six month period, up 20% from the 344 delivered in the first half of 2005. Their combined order intake was again ahead of deliveries. Business jet manufacturers reported similar increases whereas Bombardier and Embraer both reduced deliveries of their regional jets. The delay in deliveries of the new Airbus A380 is having only a negligible impact on the performance of the Division. Overall, the commercial aircraft market is very healthy with all the Group's aerospace operations benefiting.

The increase in volumes has, however, led to significant increases in the prices of metals, such as aluminium and titanium, as well as lengthening supplier lead times. The price increases have largely been passed onto customers thereby contributing to revenue growth albeit with a detrimental effect on operating margins.

Sterling Machine made a good start within the Group, despite the six-week strike at its major customer, Sikorsky, which ended in April. Sterling's future prospects are encouraging with a number of new programmes being won and the capacity of the factory is currently being expanded by 50%.

Capital expenditure for the Division increased to £3.2m (2005 – £1.7m) as new machining capacity and capability was installed at Jet Products and Ketema, notably for production of parts for Rolls Royce's Trent 700, 800 and 1000 engines.

### Flexonics Division

Revenue for the Flexonics Division rose by 8.5% to £100.6m (2005 – £92.7m) and adjusted operating profit by 10.9% to £6.1m (2005 – £5.5m). Adjusted operating margins increased to 6.1% (2005 – 5.9%).

Demand for passenger vehicles in North America and Europe was broadly flat, whereas that for commercial trucks increased by around 10% when compared to the first half of 2005. The petrochemical and power generation markets were strong, driven by high oil prices, GDP growth, particularly in Asia, and tightening emission regulations.

Against this backdrop, Pathway, with its global reach, saw strong revenue growth. The Group's North America automotive company increased sales, despite the flat markets, with a number of new programmes going into production.

Elsewhere, Senior Automotive Blois, in France, returned to profitability as planned and the Group's Brazilian operation benefited from stronger automotive volumes. Hargreaves' order book strengthened at the same time as activity on the new Wembley Stadium winds down.

As anticipated, the second quarter of the year saw the arrival of the majority of the plant and machinery required to put the new heavy duty diesel products into production in North America. Capital expenditure, at £8.0m for the Division, was consequently higher, representing 2.3x depreciation. Start-up costs were also incurred and expensed. These products are scheduled to go into production in the final quarter of the year and by the time they reach full run-rate are expected to generate over $50m of sales per annum. Additional enquiries continue to be received on a regular basis.

### Outlook

The large commercial aircraft and engine manufacturers have strong order books and their markets are forecast to continue to grow. Boeing and Airbus have indicated that they will continue to increase their build rates over the coming years, with the availability and prices of metals, such as aluminium and titanium, potentially dictating the rate of increase. The regional jet and military markets are anticipated to be stable whilst volumes of business jets are forecast to increase. Following its recent acquisition, prospects for Sterling Machine are encouraging as its main customer, Sikorsky, is in the process of substantially increasing the build rate of its helicopters. The development of new aircraft, such as the Boeing 787 ("Dreamliner"), Airbus 350X and Airbus 400M also offer significant opportunities for Senior.

Sales of the new heavy duty diesel engine products, which go into production shortly, are expected to provide a significant improvement to the Flexonics Division's turnover. Prospects for being awarded additional programmes for these products remain very good. Elsewhere, automotive markets are expected to remain stable, but competitive, and the power generation and energy markets are anticipated to remain healthy, aided by tightening emission standards and the high price of oil.

Overall, the Group is well placed to deliver healthy future growth.

**James Kerr-Muir** Chairman

**Graham Menzies** Chief Executive

2 August 2006

# Consolidated income statement

## for the half-year ended 30 June 2006 (unaudited)

| | Notes | **Half-year ended 30 June 2006 £m** | Half-year ended 30 June 2005 £m | Year ended 31 Dec 2005 (restated) £m |
|---|---|---|---|---|
| **Continuing operations** | | | | |
| **Revenue** | 3 | **195.6** | 166.9 | 338.6 |
| Trading profit | | **11.6** | 9.7 | 19.8 |
| Loss on sale of fixed assets | | **–** | (0.2) | (0.2) |
| Operating profit(1) | 3 | **11.6** | 9.5 | 19.6 |
| Investment income | | **0.5** | 0.7 | 1.3 |
| Finance costs | | **(3.4)** | (3.0) | (6.3) |
| Profit before tax(2) | | **8.7** | 7.2 | 14.6 |
| Tax | 5 | **(1.5)** | (1.3) | (2.5) |
| **Profit for the period** | | **7.2** | 5.9 | 12.1 |
| Attributable to: | | | | |
| Equity holders of the parent | | **7.2** | 5.9 | 12.1 |
| Earnings per share | | | | |
| Basic | 7 | **2.24p** | 1.92p | 3.94p |
| Diluted | 7 | **2.19p** | 1.89p | 3.87p |
| | | | | |
| (1) Adjusted operating profit | 4 | **12.0** | 9.7 | 19.8 |
| (2) Adjusted profit before tax | 4 | **9.1** | 7.4 | 14.8 |

The comparative figures for the year ended 31 December 2005 have been restated to reflect the early adoption of the amendment to International Accounting Standard 21 'The Effects of Changes in Foreign Exchange Rates' issued in December 2005, which was endorsed by the EU in May 2006. See Note 2 for details.

# Consolidated statement of recognised income and expense

for the half-year ended 30 June 2006 (unaudited)

| | **Half-year ended 30 June 2006** | Half-year ended 30 June 2005 | Year ended 31 Dec 2005 (restated) |
|---|---|---|---|
| | **£m** | £m | £m |
| Initial recognition of financial instruments | **–** | (0.2) | (0.2) |
| (Losses)/gains on cash flow hedges | **(1.4)** | (0.7) | 0.5 |
| Gains/(losses) on revaluation of financial investments | **1.9** | – | (1.8) |
| Exchange differences on translation of foreign operations | **(5.3)** | 0.9 | 4.2 |
| Actuarial gains/(losses) on defined benefit pension schemes | **1.6** | (0.3) | 0.2 |
| Tax on items taken directly to equity | **0.5** | (0.9) | (0.7) |
| **Net (loss)/income recognised directly in equity** | **(2.7)** | (1.2) | 2.2 |
| Amounts transferred to profit or loss on cash flow hedges | **(0.1)** | (0.1) | (0.3) |
| **Profit for the period** | **7.2** | 5.9 | 12.1 |
| **Total recognised income and expense for the period** | **4.4** | 4.6 | 14.0 |
| Attributable to: | | | |
| Equity holders of the parent | **4.4** | 4.6 | 14.0 |

The comparative figures for the year ended 31 December 2005 have been restated to reflect the early adoption of the amendment to International Accounting Standard 21 'The Effects of Changes in Foreign Exchange Rates' issued in December 2005, which was endorsed by the EU in May 2006. See Note 2 for details.

# Consolidated balance sheet

as at 30 June 2006 (unaudited)

| | Notes | **30 June 2006** | 30 June 2005 | 31 Dec 2005 (restated) |
|---|---|---|---|---|
| | | **£m** | £m | £m |
| **Non-current assets** | | | | |
| Goodwill | | **85.6** | 76.1 | 77.1 |
| Other intangible assets | | **3.1** | 1.1 | 1.1 |
| Property, plant and equipment | | **80.1** | 72.7 | 76.1 |
| Deferred tax assets | | **0.1** | 0.1 | 0.1 |
| Trade and other receivables | | **3.4** | 3.9 | 3.8 |
| Total non-current assets | | **172.3** | 153.9 | 158.2 |
| **Current assets** | | | | |
| Inventories | | **53.9** | 44.9 | 47.7 |
| Construction contracts | | **4.3** | 5.1 | 3.4 |
| Trade and other receivables | | **65.7** | 62.9 | 64.9 |
| Cash and cash equivalents | | **6.5** | 8.2 | 8.5 |
| Total current assets | | **130.4** | 121.1 | 124.5 |
| **Total assets** | | **302.7** | 275.0 | 282.7 |
| **Current liabilities** | | | | |
| Trade and other payables | | **70.1** | 70.8 | 69.7 |
| Tax liabilities | | **10.3** | 10.0 | 10.0 |
| Obligations under finance leases | | **0.2** | 0.2 | 0.2 |
| Bank overdrafts and loans | | **13.7** | 2.3 | 0.2 |
| Total current liabilities | | **94.3** | 83.3 | 80.1 |
| **Non-current liabilities** | | | | |
| Bank and other loans | | **66.7** | 62.1 | 66.3 |
| Retirement benefit obligations | 10 | **37.0** | 41.2 | 39.9 |
| Deferred tax liabilities | | **1.4** | 1.9 | 2.1 |
| Obligations under finance leases | | **1.5** | 1.7 | 1.6 |
| Others | | **0.3** | 0.2 | 0.4 |
| Total non-current liabilities | | **106.9** | 107.1 | 110.3 |
| **Total liabilities** | | **201.2** | 190.4 | 190.4 |
| **Net assets** | | **101.5** | 84.6 | 92.3 |
| | | | | |
| **Equity** | | | | |
| Issued share capital | | **32.5** | 30.8 | 30.9 |
| Share premium account | | **11.1** | 3.5 | 3.8 |
| Equity reserve | | **0.6** | 0.3 | 0.4 |
| Other reserve | | **–** | 17.0 | – |
| Hedging and translation reserve | | **(1.9)** | (0.3) | 2.4 |
| Retained earnings | | **60.5** | 34.6 | 56.1 |
| Own shares | | **(1.3)** | (1.3) | (1.3) |
| **Equity attributable to equity holders of the parent** | | **101.5** | 84.6 | 92.3 |
| **Total equity** | | **101.5** | 84.6 | 92.3 |

The comparative figures for the year ended 31 December 2005 have been restated to reflect the early adoption of the amendment to International Accounting Standard 21 'The Effects of Changes in Foreign Exchange Rates' issued in December 2005, which was endorsed by the EU in May 2006. See Note 2 for details.

# Consolidated cash flow statement

for the half-year ended 30 June 2006 (unaudited)

| | Notes | **Half-year ended 30 June 2006 £m** | Half-year ended 30 June 2005 £m | Year ended 31 Dec 2005 £m |
|---|---|---|---|---|
| **Net cash from operating activities** | 9a) | **8.4** | 9.0 | 16.5 |
| **Investing activities** | | | | |
| Interest received | | **0.6** | 0.8 | 1.4 |
| Proceeds on disposal of property, plant and equipment | | **–** | 0.7 | 0.9 |
| Purchases of property, plant and equipment | | **(11.3)** | (9.0) | (16.3) |
| Purchases of intangible assets | | **(0.1)** | (0.1) | (0.3) |
| Acquisition of subsidiaries | 8 | **(21.4)** | (0.1) | (0.1) |
| **Net cash used in investing activities** | | **(32.2)** | (7.7) | (14.4) |
| **Financing activities** | | | | |
| Dividends paid | | **(4.4)** | (4.1) | (6.1) |
| Repayment of borrowings | | **(1.7)** | (0.1) | (1.0) |
| Repayments of obligations under finance leases | | **(0.1)** | (0.1) | (0.3) |
| Share issues | | **8.9** | 0.1 | 0.5 |
| New loans raised | | **20.5** | 5.4 | 7.1 |
| Net cash outflow on forward contracts | | **(0.9)** | (0.4) | (0.2) |
| **Net cash from financing activities** | | **22.3** | 0.8 | – |
| **Net (decrease)/increase in cash and cash equivalents** | | **(1.5)** | 2.1 | 2.1 |
| **Cash and cash equivalents at beginning of period** | | **8.5** | 5.9 | 5.9 |
| Effect of foreign exchange rate changes | | **(0.5)** | – | 0.5 |
| **Cash and cash equivalents at end of period** | 9c) | **6.5** | 8.0 | 8.5 |

# Notes to the consolidated interim financial statements

for the half-year ended 30 June 2006 (unaudited)

### 1. General information

The information for the year ended 31 December 2005 does not constitute the Group's statutory accounts for 2005 as defined in Section 240 of the Companies Act 1985. Statutory accounts for 2005 have been delivered to the Registrar of Companies. The Auditors' report on those accounts was unqualified and did not contain statements under Sections 237(2) or (3) of the Companies Act 1985.

These interim financial statements, which were approved by the Board of Directors on 2 August 2006, have not been audited or reviewed by the Auditors.

### 2. Accounting policies

These interim financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS).

The accounting policies adopted are consistent with those followed in the preparation of the Group's annual financial statements for the year ended 31 December 2005, with the exception of the accounting policy, under IAS 21, for exchange differences that arise on re-translation of inter-company loans in a currency different to that of either counterparty. At the time of preparation of the Group's annual financial statements for 2005 the EU had not endorsed an amendment to IAS 21 which required such exchange differences to be taken to reserves and consequently a gain of £2.0m was recognised in the income statement in respect of such loans, under IAS 21 as then endorsed. In May 2006 the EU endorsed the amendment to IAS 21 and consequently these interim financial statements have been prepared in accordance with the revised Standard and the December 2005 comparatives have been adjusted to recognise the gain of £2.0m in the translation reserve.

### 3. Business segments

For management purposes, the Group is organised into two operating divisions according to the market segments that they serve. These divisions are the basis on which the Group reports its primary segment information. The two divisions are Aerospace and Flexonics, the latter incorporating both the automotive and industrial operations previously reported as separate divisions.

**3. Business segments** continued

Segment information for revenue, operating profit and a reconciliation to entity net profit is presented below.

| | **Aerospace Half-year ended 30 June 2006 £m** | **Flexonics Half-year ended 30 June 2006 £m** | **Eliminations/ Central costs Half-year ended 30 June 2006 £m** | **Total Half-year ended 30 June 2006 £m** | Aerospace Half-year ended 30 June 2005 £m | Flexonics Half-year ended 30 June 2005 £m | Eliminations/ Central costs Half-year ended 30 June 2005 £m | Total Half-year ended 30 June 2005 £m |
|---|---|---|---|---|---|---|---|---|
| External revenue | **95.2** | **100.4** | **–** | **195.6** | 74.3 | 92.6 | – | 166.9 |
| Inter segment revenue | **0.1** | **0.2** | **(0.3)** | **–** | 0.2 | 0.1 | (0.3) | – |
| Total revenue | **95.3** | **100.6** | **(0.3)** | **195.6** | 74.5 | 92.7 | (0.3) | 166.9 |
| Adjusted operating profit (see Note 4) | **8.1** | **6.1** | **(2.2)** | **12.0** | 6.3 | 5.5 | (2.1) | 9.7 |
| Loss on sale of fixed assets | **–** | **–** | **–** | **–** | (0.2) | – | – | (0.2) |
| Amortisation of intangible assets from acquisition | **(0.4)** | **–** | **–** | **(0.4)** | – | – | – | – |
| | **7.7** | **6.1** | **(2.2)** | **11.6** | 6.1 | 5.5 | (2.1) | 9.5 |
| Investment income | | | | **0.5** | | | | 0.7 |
| Finance costs | | | | **(3.4)** | | | | (3.0) |
| Profit before tax | | | | **8.7** | | | | 7.2 |
| Tax | | | | **(1.5)** | | | | (1.3) |
| Profit after tax | | | | **7.2** | | | | 5.9 |

## 4. Adjusted operating profit and profit before tax

The provision of adjusted operating profit and profit before tax, derived in accordance with the table below, has been included to identify the performance of operations, from the time of acquisition or until the time of disposal, prior to the impact of gains or losses arising from the disposal of fixed assets and amortisation of intangible assets acquired on acquisitions.

| | **Half-year ended 30 June 2006 £m** | Half-year ended 30 June 2005 £m | Year ended 31 Dec 2005 (restated) £m |
|---|---|---|---|
| Operating profit | **11.6** | 9.5 | 19.6 |
| Loss on sale of fixed assets | **–** | 0.2 | 0.2 |
| Amortisation of intangible assets from acquisition | **0.4** | – | – |
| Adjustments to operating profit | **0.4** | 0.2 | 0.2 |
| Adjusted operating profit | **12.0** | 9.7 | 19.8 |
| Profit before tax | **8.7** | 7.2 | 14.6 |
| Adjustments to profit as above before tax | **0.4** | 0.2 | 0.2 |
| Adjusted profit before tax | **9.1** | 7.4 | 14.8 |

## 5. Tax charge

| | **Half-year ended 30 June 2006 £m** | Half-year ended 30 June 2005 £m |
|---|---|---|
| Current tax: | | |
| UK corporation tax | **–** | – |
| Foreign tax | **1.5** | 1.2 |
| | **1.5** | 1.2 |
| Deferred tax: | | |
| Current year | **–** | 0.1 |
| | **1.5** | 1.3 |

Corporation tax for the interim period is charged at 17.2% (2005 – 18.1%), representing the best estimate of the weighted average annual corporation tax rate expected for the full financial year.

## 6. Dividends

| | **Half-year ended 30 June 2006 £m** | Half-year ended 30 June 2005 £m |
|---|---|---|
| Amounts recognised as distributions to equity holders in the period: | | |
| Final dividend for the year ended 31 December 2005 of 1.35p (2004 – 1.35p) per share | **4.4** | 4.1 |
| Proposed interim dividend for the year ended 31 December 2006 of 0.65p (2005 – 0.65p) per share | **2.1** | 2.0 |

The proposed interim dividend was approved by the Board of Directors on 2 August 2006. This proposed dividend has not been included as a liability in these financial statements.

## 7. Earnings per share

The calculation of the basic and diluted earnings per share is based on the following data:

| Number of shares | **Half-year ended 30 June 2006 m** | Half-year ended 30 June 2005 m |
|---|---|---|
| Weighted average number of ordinary shares for the purposes of basic earnings per share | **321.4** | 306.7 |
| Effect of dilutive potential ordinary shares: | | |
| Share options | **6.7** | 4.8 |
| Weighted average number of ordinary shares for the purposes of diluted earnings per share | **328.1** | 311.5 |

| | **Half-year ended 30 June 2006** | | Half-year ended 30 June 2005 | |
|---|---|---|---|---|
| **Earnings and earnings per share** | **Earnings £m** | **EPS pence** | Earnings £m | EPS pence |
| Profit for the period | **7.2** | **2.24** | 5.9 | 1.92 |
| Adjust: | | | | |
| Loss on sale of fixed assets net of tax of £nil (2005 – £nil) | **–** | **–** | 0.2 | 0.07 |
| Amortisation of intangible assets from acquisition net of tax of £0.1m | **0.3** | **0.09** | – | – |
| Adjusted earnings after tax | **7.5** | **2.33** | 6.1 | 1.99 |
| Earnings per share | | | | |
| – basic | | **2.24p** | | 1.92p |
| – diluted | | **2.19p** | | 1.89p |
| – adjusted | | **2.33p** | | 1.99p |
| – adjusted and diluted | | **2.29p** | | 1.96p |

The effect of dilutive shares on the earnings for the purposes of diluted earnings per share is £nil (2005 – £nil).

The denominators used for all basic, diluted and adjusted earnings per share are as detailed in the 'Number of shares' table above.

The provision of an adjusted earnings per share, derived in accordance with the table above, has been included to identify the performance of operations, from the time of acquisition or until the time of disposal, prior to the impact of the following items:

– gains or losses arising from the disposal of fixed assets
– amortisation of intangible assets acquired on acquisitions

## 8. Acquisitions

On 27 January 2006, the Group acquired 100% of the issued share capital of Sterling Machine Co., Inc., a manufacturer of precision machined parts for the aerospace industry, based in Enfield, Connecticut, USA. The cash consideration was £21.4m, including costs, of which £1.2m related to the purchase of property. The acquisition was funded in part by the placing of 15m ordinary shares generating net proceeds of £8.8m, the balance being funded by the Group's existing revolving credit facilities.

Set out below is a summary of the net assets acquired and details of the fair value adjustments:

| | Carrying values pre-acquisition £m | Provisional fair value £m |
|---|---|---|
| Intangible assets | – | 2.7 |
| Property, plant and equipment | 2.1 | 2.1 |
| Inventories | 3.8 | 3.4 |
| Trade and other receivables | 2.4 | 2.1 |
| Trade and other payables | (0.5) | (0.5) |
| Net assets acquired | 7.8 | 9.8 |
| Goodwill | | 11.6 |
| Total consideration | | 21.4 |
| Consideration satisfied by: | | |
| Cash | | 21.3 |
| Directly attributable costs | | 0.1 |
| Net cash outflow arising on acquisition | | 21.4 |

The fair value adjustments contain some provisional amounts which will be finalised in the financial statements for the year ended 31 December 2006, by which time the closing balance sheet will have been agreed with the vendors.

The intangible assets acquired as part of the acquisition relate to customer contracts. Goodwill represents the value of the assembled workforce and its contribution to anticipated future profitability arising from additional capital investment.

Sterling Machine contributed £5.2m revenue and £0.6m to the Group's operating profit from the date of acquisition to 30 June 2006. If the acquisition had been completed on 1 January 2006, Group revenue for the half-year ended 30 June 2006 would have been £196.1m and Group operating profit would have been £11.6m.

The amounts shown in the consolidated cash flow statement for acquisition of subsidiaries include £nil (2005 half-year – £0.1m; 2005 year – £0.1m) relating to deferred consideration payable in respect of previous acquisitions.

## 9. Notes to the cash flow statement

a) Reconciliation of operating profit to net cash from operating activities

| | Half-year ended 30 June 2006 £m | Half-year ended 30 June 2005 £m |
|---|---|---|
| Operating profit | **11.6** | 9.5 |
| Adjustments for: | | |
| Depreciation of property, plant and equipment | **6.0** | 5.7 |
| Amortisation of intangible assets from acquisition | **0.4** | – |
| Amortisation of other intangible assets | **0.3** | 0.3 |
| Share options | **0.2** | 0.2 |
| Loss on disposal of property, plant and equipment | **–** | 0.2 |
| Pension payments in excess of service cost | **(1.4)** | (1.2) |
| Operating cash flows before movements in working capital | **17.1** | 14.7 |
| Increase in working capital | **(4.5)** | (3.5) |
| Cash generated by operations | **12.6** | 11.2 |
| Income taxes paid | **(1.1)** | (0.1) |
| Interest paid | **(3.1)** | (2.1) |
| Net cash from operating activities | **8.4** | 9.0 |

b) Free cash flow

Free cash flow, a non-statutory item, highlights the total net cash generated by the Group prior to corporate activity such as acquisitions and disposals and transactions with shareholders. It is derived as follows:

| | Half-year ended 30 June 2006 £m | Half-year ended 30 June 2005 £m |
|---|---|---|
| Net cash from operating activities | **8.4** | 9.0 |
| Interest received | **0.6** | 0.8 |
| Proceeds on disposal of property, plant and equipment | **–** | 0.7 |
| Purchases of property, plant and equipment | **(11.3)** | (9.0) |
| Purchases of intangible assets | **(0.1)** | (0.1) |
| Free cash flow | **(2.4)** | 1.4 |

## 9. Notes to the cash flow statement continued

c) Analysis of net debt

| | At 1 January 2006 £m | Cash flow £m | Non-cash items £m | Exchange movement £m | At 30 June 2006 £m |
|---|---|---|---|---|---|
| Cash and cash equivalents | 8.5 | (1.5) | – | (0.5) | 6.5 |
| Debt due within one year | (0.2) | – | (13.5) | – | (13.7) |
| Debt due after one year | (66.3) | (18.8) | 13.6 | 4.8 | (66.7) |
| Finance leases | (1.8) | 0.1 | – | – | (1.7) |
| Forward exchange contract (losses)/gains | (2.6) | 0.9 | – | 1.7 | – |
| Total | (62.4) | (19.3) | 0.1 | 6.0 | (75.6) |

The forward exchange contract losses shown above are reported as £nil (1 January 2006 – £2.8m) in current liabilities within trade and other payables and £nil (1 January 2006 – £0.2m) in current assets within trade and other receivables.

Non-cash items shown above relate to the recognition of financial instruments under IAS 39.

## 10. Retirement benefit schemes

**Defined benefit schemes**

Aggregate post-retirement benefit liabilities are £37.0m (30 June 2005 – £41.2m; 31 December 2005 – £39.9m). The primary components of this liability are the Group's UK pension plan and US pension plans, with deficits of £28.8m (30 June 2005 – £32.9m; 31 December 2005 – £31.3m) and £4.5m (30 June 2005 – £5.0m; 31 December 2005 – £4.9m) respectively. These values have been assessed by an independent actuary using current market values and discount rates.

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**Senior plc**
59/61 High Street
Rickmansworth
Hertfordshire
WD3 1RH
United Kingdom

**T** +44 (0)1923 775547
**F** +44 (0)1923 896027
**E** info@seniorplc.com
**W** www.seniorplc.com