

1 March 2011

## Recovery firmly under way

Meggitt PLC (“Meggitt” or “the Group”), a leading international company specialising in high performance components and sub-systems for the aerospace, defence and energy markets, today announces preliminary audited results for the year ended 31 December 2010.

### FINANCIAL HIGHLIGHTS

£m	2010	2009	% change
Revenue	<b>1,162.0</b>	1,150.5	+1%
Underlying <sup>1</sup> :			
EBITDA	<b>364.4</b>	343.4	+6%
Operating profit	<b>303.7</b>	286.2	+6%
Profit before tax	<b>256.1</b>	234.2	+9%
Earnings per share	<b>27.8p</b>	25.3p	+10%
Statutory:			
Operating profit	<b>220.1</b>	232.8	-5%
Profit before tax	<b>172.5</b>	180.8	-5%
Earnings per share	<b>20.1p</b>	20.5p	-2%
Net debt	<b>721.4</b>	808.6	-11%
Dividend	<b>9.20p</b>	8.45p	+9%

(1) Underlying profit and EPS are used by the Board to measure the trading performance of the Group and exclude certain items, principally amortisation of acquired intangibles, operating exceptional items and the marking to market of financial instruments, as set out in notes 3 and 9.

- Recovery in the Group’s markets took hold during second half of 2010:
  - Order intake in civil and energy up by more than 20% compared with second half of 2009; military up 9%.
  - Civil revenues up 18% year-on-year in second half, energy up 19%, military up 1%.
  - As expected, revenue growth of 9% in second half resulted in modest growth for year as a whole.
  - Good momentum going into 2011 with closing order book in excess of £750m; orders for 2011 delivery up 12%.
- Operating margin increased from 24.9% to 26.1% with cost reductions continuing to flow through. In-year transformation savings of £54m exceeded target.
- Excellent net cash generation of £137.1m (2009: £126.0m).
- Net debt reduced by 11% to £721.4m (2009: £808.6m), 1.9x EBITDA (covenant basis).
- Recommended dividend increased by 9% to 9.20p.

- Through our Transformation programme we are positioning the business for future growth – strengthening our organisation, increasing our customer focus, more effectively investing in R&D and driving operations excellence.
- Group expects organic growth of 6-7% on average over next five years assuming continuing economic recovery. Similar growth rates are expected from Pacific Scientific Aerospace (PSA).
- In January 2011 the Group announced its proposed acquisition of PSA for \$685m, which is subject to normal completion requirements. The deal, which is expected to close in April, will be funded through a combination of a placing of 69.8m shares (which was completed successfully on 21 January) and existing debt facilities and is expected to be earnings enhancing immediately.

**Terry Twigger, Chief Executive, commented:**

*"As expected, our civil and energy markets recovered strongly in the second half, and this momentum is continuing into 2011, whilst our military markets also improved. Our cost cutting and Transformation programmes have ensured that the Group has come through the downturn with not only higher margins but also stronger and better able to generate organic revenue growth going forward. In a challenging year, the Group grew underlying profit before tax by 9% and we anticipate further growth in 2011 and beyond, enhanced by the proposed acquisition of PSA. We also maintained our focus on cash, delivering a second consecutive year of record net cash generation underlining the robustness of Meggitt's business.*

*As a sign of our confidence in the prospects for the Group, we are recommending an increase in the full year dividend of 9%."*

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## **STRATEGIC POSITIONING**

Meggitt has made major changes over the last two years to reshape and position our business for growth. Between mid-2008 and mid-2010 we have seen considerable economic turmoil and an unprecedented downturn in our civil markets. Our response to this downturn was to cut costs fast and hard, to focus even more on cash generation and to accelerate our Transformation programme. The results of these measures, and a stronger US dollar, can be seen in our 2010 performance – record margins, underlying profits ahead of the last pre-downturn year, 2008, and record net cash.

More importantly, the Transformation programme has left us better placed to drive future organic growth. We have a new, capability based, divisional structure with resources, such as engineering, marketing and central services organised in the most effective way. This new structure, together with continuing economic recovery, should drive organic growth of 6-7% over the medium term, led by our civil and energy markets, with military growing more slowly.

### **Acquisition of PSA**

Since the year-end the Group has announced its intention to acquire the PSA businesses from Danaher, which is subject to normal completion requirements. PSA fits well into Meggitt's business model, with strong technology positions, a significant level of sole source content and aftermarket sales representing over one third of total revenue. The acquisition adds fire and smoke suppression capabilities to Meggitt's product portfolio, creating a leading integrated fire and smoke detection and suppression offering, and will enhance Meggitt's electric solutions offering as aircraft of the future shift away from hydraulic/pneumatic technology and towards electric power. It will also strengthen Meggitt's portfolio of sensors and anti-icing products, and enhance the Group's low cost manufacturing capability with the addition of factories in Mexico and Vietnam. The business had revenues of \$378m in 2010, delivering EBITDA of \$79m, and has significant positions on growth programmes which will drive revenue growth into the future. The transaction is expected to complete at the end of April at a price of \$685m, representing a multiple of 8.7x 2010 EBITDA (7.9x after a negotiated tax benefit) and is expected to be earnings enhancing immediately.

With its intellectual property, balanced portfolio, sole source positions, significant installed base a healthy, growing order book, and the acquisition of PSA, Meggitt is well positioned for 2011 and beyond.

## **MARKET BACKGROUND**

### **Civil Aerospace**

Meggitt operates in three main segments of the civil aerospace market: large jets, regional aircraft and business jets. The large jet fleet includes approximately 16,000 aircraft, the regional aircraft fleet about 6,000, and business jets over 16,000. The Group has products on most of these aircraft and hence a very large, and growing, installed base. The split of civil revenues, which account for 42% of the Group total, is circa two thirds aftermarket and one third original equipment (OE).

The economic factors which weighed heavily on civil OE deliveries and air traffic throughout 2009 and into 2010 started to ease during the year. Manufacturers of large jets have been able to maintain deliveries at 2009 levels in 2010, and have announced increases to production rates in 2011 and 2012, demonstrating the resilience of their order book. Business jet and regional aircraft manufacturers reduced production levels in 2009 and 2010 and we expect deliveries in 2011 to be broadly flat followed by a recovery in both segments from 2012. Over the five years to 2015 we expect our revenues from civil OE to grow at an average rate of around 7-8% per annum, helped by strong growth in business jets and new platform introductions including the Boeing 787, Airbus A350 and Bombardier C Series. Our growth assumptions assume there will be no further economic downturn.

International and US Domestic Available Seat Kilometres (ASKs), a proxy for air traffic which is a key driver of the demand from airlines for spares on large and regional aircraft, declined by around 5% in 2009 before returning to growth in 2010, with the growth becoming more broad based as the year progressed. Full year ASK growth was just under 4% in 2010, although monthly growth rates in the latter months of the year were around 7% (excluding December which was impacted by adverse weather in the US and Europe). We expect 2011 ASK growth to be around 5%, the long term trend rate.

US business jet usage, which decreased 17% in 2009, rebounded strongly in 2010, and growth for the year as a whole was 12%, in line with our expectations. Continued growth is expected in 2011, albeit against progressively tougher comparatives.

In the civil aftermarket, we expect our revenues to grow around 8-9% per annum over the five years to 2015. This is based on ASK growth of 5% per year, with business jets expected to grow aftermarket revenues at a double digit rate per annum based on a continuing recovery in utilisation, growing international demand, and on-going mix change from steel brakes to carbon brakes which have a higher unit shipset price.

### **Military**

The requirement for governments around the world to tackle their budget deficits is leading to increased pressure on military spending in most western countries, albeit tempered by the continuing requirement to provide troops for Afghanistan and other conflict areas. For the US, which is by far the most important military market for Meggitt, the debate between the Administration and Congress on current and future year budgets at a macro and programme level makes for an uncertain environment. Some growth in base budget spending over the next couple of years looks likely, followed by reductions in the out years. The precise impacts of these future spending reductions are still being determined, but Secretary Gates is looking to use efficiency savings to protect key programmes as far as possible, and to adapt the tools, equipment and training to meet the increasingly asymmetric threats of international terrorism. We believe that the focus on modernising and extending the life of existing platforms where Meggitt has an established aftermarket as well as new platforms to address the new threats will create opportunities for the Group. The new products and technologies Meggitt is developing for new platforms can also be retrofitted onto existing platforms, which could potentially accelerate revenue streams for the Group given the significant existing fleet sizes involved.

This market is therefore expected to remain robust over coming years. Our revenues are generated from a broad range of platforms for all branches of the military, with a healthy split between OE and aftermarket. We are well positioned on the current growth platforms such as Eurofighter Typhoon, V22, F35 (JSF), E/F-18 Super Hornet and Black Hawk, but are not overly exposed to any single one. Although impacted by the US Government's continuing negotiations over its fiscal year 2011 budget, our expectation is that our military revenues should continue to grow by around 2% compound over the next few years, even with a substantial reduction in utilisation of certain aircraft types (rotary wing and transport aircraft) following the planned drawdown of troops from Afghanistan.

### **Energy and Other**

Other revenues (14% of Group total) come from various end markets such as energy (approximately 50%), automotive, test, consumer goods and medical.

Within the energy market, demand for new power generation equipment was subdued, but existing operators continued to spend money maintaining and upgrading their plants. We expect the OE energy market to return to growth in 2011, with aftermarket demand likely to continue to grow faster. In the offshore gas segment there has been growing bid and proposal

activity during the year which will drive market growth in 2011 and beyond for our compact printed circuit heat exchangers. We expect our energy revenues to grow at double digit percentages in the medium term. Demand in automotive, test equipment and consumer goods in 2010 was weak and the outlook is expected to continue to be mixed in the short term.

## REVENUES AND ORDERS

The challenging trading conditions of 2009 persisted into the first half of 2010 when revenues were down 6% year on year. As the recovery took hold in the second half, revenues increased by 9% on the prior year, to give an overall increase of 1% for the year as a whole (2010: £1,162.0m; 2009: £1,150.5m). The split of revenue growth between first (H1) and second (H2) half by segment is shown below:

	2010 Revenues £m	2010 Growth	H1 Growth	H2 Growth
Civil OE	150.3	2%	(6%)	12%
Civil AM	343.9	6%	(6%)	21%
Total Civil	494.2	5%	(6%)	18%
Military	507.5	(2%)	(6%)	1%
Energy	84.5	2%	(14%)	19%
Other	75.8	(2%)	(6%)	1%
Total	1,162.0	1%	(6%)	9%

Civil aerospace revenues grew 5%, heavily skewed towards the second half when growth was 18% as a result of the recovery in air traffic. The recovery in the aftermarket, particularly for business jets where utilisation started to recover in late 2009, was a key driver of this revenue growth.

Military revenues returned to growth in the second half although full year revenues were 2% below last year. The year on year decline arose mainly in our Braking Systems and Equipment divisions, both of which recorded significant non-recurring revenue in 2009 related to the re-supply of products for the B1 Bomber and the Abrams tank, respectively. Excluding these items, military revenues from our other platforms increased year on year albeit at a slower rate than we had expected. In Europe, the Eurofighter programme revenues grew through a combination of OE deliveries and growing aftermarket revenues.

Energy revenues increased 2%. Within this, industrial revenues grew healthily, particularly sales to end users, but this was partly offset, as expected, by reduced revenues from our compact printed circuit heat exchangers. Encouragingly order intake for printed circuit heat exchangers was more than 3 times the level in 2009 and this product range returned to good growth in the second half of 2010.

Meggitt's other specialist markets had a mixed year reflecting the general economic climate. Revenue for this segment was down 2%.

Our order book grew by 8% during the year, with orders for 2011 delivery up 12%. Our closing order book is over £750m, giving a solid base for our expected revenue growth in 2011.

## **PROFIT AND DIVIDENDS**

The Board's preferred measure of the Group's trading performance is underlying profit. Underlying operating profit for the year grew 6% to £303.7m (2009: £286.2m) and underlying operating margin increased to 26.1% (2009: 24.9%), driven by cost reductions.

Net finance costs decreased to £47.6m (2009: £52.0m) as a result of our strong cash generation and lower interest rates. Within this, post-retirement finance charges decreased to £9.8m (2009: £12.2m). Underlying profit before tax increased by 9% to £256.1m (2009: £234.2m).

With a tax charge of 25.0% (2009: 27.0%) and, after taking account of the increased share count due to strong take up of scrip dividends during the year, underlying earnings per share increased by 10% to 27.8 pence (2009: 25.3 pence).

On a statutory basis, profit before tax decreased by 5% to £172.5m (2009: £180.8m) and earnings per share decreased by 2% to 20.1p (2009: 20.5p). The adjustments between underlying profit and statutory profit are described in notes 3 and 9.

The recommended final dividend is increased by 10% to 6.35p (2009: 5.75p) and represents a total dividend for the year of 9.20p (2009: 8.45p), an increase of 9%.

## **CASH FLOW AND BORROWINGS**

Cash inflow from operations before exceptional operating items was a very healthy £331.3m, which was 109% of underlying operating profit (2009: £341.7m and 119%).

The business generated £137.1m of net cash, an £11.1m increase on the record 2009 performance, whilst continuing to invest significant amounts in our development programmes and the deployment of our common ERP solution. As a result, net debt decreased from £808.6m at 31 December 2009 to £721.4m at 31 December 2010, despite an adverse translation impact of £36.3m on our mainly US dollar denominated debt.

There are two main financial covenants in our banking agreements. The net debt/EBITDA ratio, which must not exceed 3.5x, was 1.9x at 31 December 2010 (2009: 2.4x) and interest cover, which must be not less than 3.0x, was 9.1x (2009: 8.0x). The Group therefore has significant headroom against both key covenant ratios and, at 31 December 2010, had £728.4m of undrawn headroom, net of cash, against committed bank facilities. The Group received strong support for its \$600m private placement which was completed in June 2010.

The proposed PSA acquisition, including costs, will be financed by a placing of 69.8m shares and debt from existing committed facilities. The equity placing was successfully completed on 21 January 2011 and raised £246.2 million. Had the acquisition occurred at the end of December 2010 our pro-forma headroom and net debt/EBITDA ratio would have been £531.2m and 2.1x respectively.

## **TRANSFORMATION PROGRAMME**

In addition to its ongoing procurement and low cost manufacturing programmes, the Group responded to the economic downturn by accelerating our initiative to position the business for the future. We targeted £50m per annum of incremental cost savings as a run rate by the end of 2010. This target has now been raised to £57m by the end of 2011. Approximately half of these savings are expected to be permanent. The balance are volume related and will come

back as volumes return. Savings in the year were £54m and although we expect to increase resources in 2011 in engineering, sales & marketing and programme management, we are confident of achieving the £57m run rate by the end of 2011. The operating exceptional cost of achieving the additional savings in 2010 was £13.2m (2009: £16.9m).

Positioning the business for the future is not primarily about cost saving, it is about strengthening the organisation and increasing our customer focus, as well as embedding common processes and systems across the Group. Concentrating key resources such as engineering and sales & marketing teams at a divisional level, and enhancing the cooperation between divisions will improve customer responsiveness and help us to win incremental new business going forward. We are already seeing positive results from this and expect to see more going forward.

During the year we appointed Dr Richard Greaves, formerly President of Sensing Systems, as Group Technology & Engineering Director, giving him a broad remit to focus on emerging technology trends as well as providing Group-wide support to our divisional engineering teams. It goes without saying that we have not neglected our factories either, increasing their focus on delivering high quality product on time and at a competitive cost. Our strategic sourcing and low cost manufacturing initiatives have supported the factories in their quest to become more cost effective.

## **INVESTING FOR THE FUTURE**

Developing and owning intellectual property is a critical part of Meggitt's successful strategy. Total product development expenditure in 2010 was £84.2m (2009: £85.2m), of which 20% was funded by customers. The largest relative investment was in Sensing Systems at around 15% of segment revenues.

Strategic technology investment continues to add exciting capabilities to our offering. For example we have developed our tip clearance measurement technology which is capable of measuring the gap between the tip of a rotating blade in an engine and the engine casing. Gas turbine manufacturers (whether for land based turbines or aircraft engines) can use this data to adjust the gap between the blade and the casing to improve fuel efficiency (preliminary tests showed a 2% reduction in fuel burn was possible). This technology reached Technical Readiness Level 6 during the year, signifying a model which has been tested in an operational environment – a significant milestone in proving the capability of the product. Another example is our particle smoke detection capability which enhances our fire and smoke detection system by helping to filter out dust and other contaminants which can provide false positive indications in the cargo bay. This significantly increases reliability for aircraft operators, and has received significant attention from a key OEM. These and other similar investments help to maintain our strong position in our chosen markets and to win incremental positions on new programmes.

Meggitt also invested £28.4m (2009: £23.9m) in supplying free of charge equipment to new aircraft coming into the fleet and in making programme participation contributions, mostly in the braking systems business.

Capital expenditure on property, plant and equipment and other intangible assets increased to £27.7m (2009: £25.6m), including investment in the deployment of our common ERP system across the Group.

As part of the Group's low cost manufacturing strategy, Meggitt continued to expand the range of products manufactured at its facility in Xiamen, China. We also opened and began to transfer certain production activities to our second Mexican factory at Queretaro. This is part of a continuing process of seeking out opportunities to reduce our cost base and win new business.

## RETIREMENT BENEFIT SCHEMES

We experienced strong asset performances during the year, particularly in equity markets, which, together with cash contributions, resulted in scheme assets increasing by £63.7m to £567.9m. Assets are now at levels 20% higher than those prior to the market crash in 2008. However, a further tightening of the yields on AA corporate bonds, the rates used to discount scheme liabilities, offset much of the asset gains and overall the scheme deficits reduced modestly to £265.1m (2009: £280.5m). The Group made deficit reduction payments in the year of £23.1m (2009: £21.8m).

## OPERATIONAL HIGHLIGHTS

The financial performance of the individual divisions is highlighted in the table below:

£m				Underlying			Return on Sales	
Revenue				Operating Profit				
2010	2009			2010	2009		2010	2009
309.7	318.8	-3%	Aircraft Braking Systems	120.7	116.2	4%	39.0%	36.4%
182.8	181.9	0%	Control Systems	44.7	43.4	3%	24.5%	23.9%
156.0	147.9	5%	Polymers & Composites	28.4	30.0	-5%	18.2%	20.3%
208.4	192.6	8%	Sensing Systems	39.5	32.5	22%	19.0%	16.9%
305.1	309.3	-1%	Equipment Group	70.4	64.1	10%	23.1%	20.7%
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1,162.0	1,150.5	1%	Total	303.7	286.2	6%	26.1%	24.9%
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**Meggitt Aircraft Braking Systems (MABS)** provides wheels, brakes and brake control systems for over 30,000 in-service aircraft, and continues to develop innovative technology for new programmes such as the all-electric braking system on Bombardier's CSeries aircraft. The division targets sole source programmes, and is particularly strong in regional aircraft, business jets and military platforms. The division represents 27% of total Group revenue, generating 88% of its revenues from the aftermarket and 12% from the OE market.

MABS' profitable civil aftermarket (circa 67% of revenues) has recovered well from the downturn, growing 8% in 2010. The recovery has been strongest in business jets, following on from the increase in utilisation which began to be reported in the second half of 2009. Business jet OE deliveries (which generate little upfront revenue but add to our installed fleet for future aftermarket sales) bucked the overall market trend with deliveries of jets equipped with MABS wheels & brakes increasing by 4% in 2010. Military revenues were down 20%, largely due to the completion of a substantial resupply campaign on the B1 bomber which generated strong revenues in 2009. Operating margins strengthened further during the year, reflecting continued cost reduction efforts and final K&F integration savings as well as an unusually favourable mix.

**Meggitt Control Systems (MCS)** designs and manufactures products which either manage the flow of liquids and gases around turbine engines (both aerospace and industrial) or control the temperature of oil, fuel and air around aircraft engines. Its valve business is also involved in the supply of airport ground fuelling products and it supplies cabin air conditioning for smaller aircraft. The division represents 16% of total Group revenue and generated 54% of its revenues from the OE market and 46% from the aftermarket.

For MCS, civil aerospace and energy revenues were broadly flat whilst growing military sales, particularly parts for aircraft in service in Afghanistan, were largely offset by a small decline in other specialist markets. Despite almost flat revenue, continued progress in cost reductions helped to improve operating margins from 23.9% to 24.5%.



**Meggitt Polymers & Composites (MPC)** has a strong military focus, representing approximately two thirds of its sales. It supplies flexible bladder fuel tanks, ice protection products and composite assemblies for a range of fixed wing and rotorcraft platforms, as well as complex seals packages for civil and military platforms. These market segments are linked by their dependence on similar materials technology and manufacturing processes. We supply over 70% of the US military requirements for fuel bladders and ballistically tolerant or crashworthy fuel tanks. MPC represents 13% of total Group revenue and generated approximately two thirds of its revenues from the OE market and one third from the aftermarket.

Revenues in MPC were up 5% in the year on the back of continued growth in military sales, in particular the contract to supply ballistically resistant fuel tanks for the Bradley Fighting Vehicle. Civil aerospace sales showed modest growth, mainly in large jets reflecting additional packages of seals which went into production during the year. Operating margins declined from 20.3% to 18.2%, as a result of a combination of poor mix and one-off rework costs incurred on one of our long-standing military contracts.

**Meggitt Sensing Systems (MSS)** designs and manufactures highly engineered sensors to measure a variety of parameters such as vibration, temperature, pressure, fluid level and flow. Its products are designed to operate effectively in the extreme conditions of temperature, vibration and contamination that exist in an aircraft or ground based turbine engine. They combine these sensors into broader electronics packages which take data from the sensors and other systems around the engine to provide condition data to operators and maintainers of engines, contributing to improved safety and a reduced cost of operating the engine. As well as migrating these products into other specialist markets which require similar capabilities, such as test and measurement, automotive crash test and medical pacemakers, MSS has teamed with MABS to apply their engine condition monitoring capability onto the undercarriage where we see a considerable market opportunity. MSS represents 18% of total Group revenue and generated 77% of its revenues from the OE market and 23% from the aftermarket.

MSS reported good growth in civil, military and energy revenues partly offset by weakness in its other specialist markets which continued to experience difficult market conditions. Growth in civil markets included continuing healthy demand for the retrofit of its advanced vibration monitoring equipment on the Boeing 737 aircraft. Military sales grew on the back of continued strong demand for our military helicopter health and usage monitoring products, particularly the Black Hawk platform, and energy revenues grew as we improved our penetration of end user customers through our expanding office network in target countries. The improvement in operating margins reflects incremental cost reduction activity as well as favourable exchange rate benefits.

**Meggitt Equipment Group (MEG)** comprises a technologically diverse range of businesses, each of which has differentiated capabilities and a specific focus, ranging from high speed electromechanical devices through to sophisticated electronics and electromechanical components and sub-systems. Products include fire protection, military training and combat systems, secondary flight displays, printed circuit heat exchangers (PCHes) and industrial sensors. The division represents 26% of total Group revenue and generates approximately two thirds of its revenues from the OE market and one third from the aftermarket.

Revenues in MEG were down 1% on last year as a result of the expected weak sales of our PCHes at Heatric and the completion of certain military contracts, combined with delays in receiving follow-on orders. Although Heatric's PCH business declined in the first half, strong order intake helped it to return to growth in the second half, a trend which we expect to continue into 2011. The military business is experiencing some delays in new contracts, particularly at the Irvine, California facility, which have persisted into 2011, not helped by the delay in approving the DoD's FY 2011 budget. Operating margins improved to 23.1%, helped by a favourable mix of product sales in the second half.

## CONTRACT WINS

Overall Group order intake improved markedly during the period, and particularly in the second half. In addition to booked orders, the Group continued its solid track record of contract wins in the period, which will typically drive order intake in this, or more often future, periods. Examples of significant contract wins, either because of their scale or strategic significance for the Group include:

**Tyre Pressure Monitoring System (TPMS)** – Our first extension of our condition monitoring capability onto the undercarriage;

**Integrated Secondary Flight Display** – The most up-to-date, low risk, standby instrument on the international market was approved by the FAA and EASA and selected by a number of customers;

**Blast resistant fuel tanks** for military ground vehicle – Our first contract to apply our life-saving helicopter technology to a ground vehicle;

**Military contracts** – A variety of military contracts were awarded including helicopter fuel cell, ice protection, composites and interiors for the Black Hawk and V22 programmes, a linkless feed ammunition handing system for the Future Rapid Effects System (FRES) scout variant, and a modernisation programme for the Ministry of Defence's premier live-fire range for operational pre-deployment training at the British Army Training Unit Suffield in Alberta, Canada;

**VibroSight®** - Our upgraded condition monitoring product for land based turbines launched in 2010 won multiple contracts in Europe and Asia;

**Printed Circuit Heat Exchangers (PCHEs)** – Heatric's order intake trebled in 2010 as demand recovered across the globe.

## BOARD OF DIRECTORS

Sir Alan Cox retired from the Board in February 2011 having served as a non-executive director for nearly 15 years. During this time the Group has expanded significantly and Sir Alan's advice and counsel during this period of rapid growth has been invaluable.

Paul Heiden joined the Board as a non-executive director in June 2010. Paul is also Chairman of Talaris Topco Limited and a non-executive director of The London Stock Exchange Group and UU Plc. He was previously Chief Executive of FKI Plc.

## GROUP OUTLOOK

The outlook for our civil markets continues to improve in line with our expectations. Production of large jets is likely to remain strong in 2011, helped by the entry into service of the Boeing 787. Growth in air traffic and business jet utilisation is expected to continue on the back of the recovery in 2010, providing good momentum for our civil aftermarket revenues.

In military markets, the delay in approving the DoD's FY 2011 budget is likely to impact new programme awards, but should have little effect on existing delivery contracts and regular aftermarket demand which are the heart of our military revenues. We therefore continue to expect modest growth in military revenues in 2011.

Our energy market is expected to be a source of healthy growth as PCHE sales recover and sales to power generation customers continue to grow on the back of new product launches and our expanded sales network. Other specialist markets are expected to be broadly flat for the year.

We expect to complete the acquisition of PSA by the end of April this year, subject to the normal completion requirements. PSA is a great fit with Meggitt and will enhance growth and earnings going forward. We look forward to welcoming the PSA employees into the Meggitt organisation and working with them to integrate their businesses into the enlarged Meggitt group. We expect to achieve \$5m of synergies from the integration of PSA in 2011 at a one-off cost of approximately \$9m. Total 2011 operating exceptional costs related to PSA are expected to be c\$17m including transaction costs. The acquisition is expected to be earnings enhancing immediately.

Based on current market indicators and at constant exchange rates, the Group expects to deliver good organic revenue growth in 2011 and is well positioned for the longer term. As a consequence the Board has recommended increasing the final dividend by 10% to 6.35p, making 9.20p for the year, a 9% increase on 2009.

## CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2010

	Notes	2010 £m	2009 £m
<b>Continuing operations</b>			
<b>Revenue</b>	2	<b>1,162.0</b>	1,150.5
Cost of sales		<u>(639.8)</u>	<u>(656.3)</u>
<b>Gross profit</b>		<b>522.2</b>	494.2
Net operating costs		<u>(302.1)</u>	<u>(261.4)</u>
<b>Operating profit*</b>	3	<b>220.1</b>	232.8
Finance income	6	<b>33.6</b>	28.1
Finance costs	7	<b>(81.2)</b>	(80.1)
Net finance costs		<u>(47.6)</u>	<u>(52.0)</u>
<b>Profit before tax **</b>		<b>172.5</b>	180.8
Tax		<b>(33.7)</b>	(42.0)
<b>Profit for the year from continuing operations attributable to equity holders</b>		<u><b>138.8</b></u>	<u>138.8</u>
Earnings per share:			
Basic	9	<b>20.1p</b>	20.5p
Diluted	9	<b>19.9p</b>	20.5p
* Underlying operating profit	3	<b>303.7</b>	286.2
** Underlying profit before tax	3	<b>256.1</b>	234.2

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2010

	2010 £m	2009 £m
<b>Profit for the year</b>	<b>138.8</b>	138.8
<b>Other comprehensive income/(expense) for the year:</b>		
Actuarial losses	(1.5)	(67.6)
Currency translation differences	29.3	(81.4)
Cash flow hedge movements	20.6	10.7
Other comprehensive income/(expense) before tax	48.4	(138.3)
Related tax movements	(7.5)	11.2
<b>Other comprehensive income/(expense) for the year</b>	<b>40.9</b>	(127.1)
<b>Total comprehensive income for the year attributable to equity holders</b>	<b>179.7</b>	11.7

## CONSOLIDATED BALANCE SHEET

As at 31 December 2010

	Notes	2010 £m	2009 £m
<b>Non-current assets</b>			
Goodwill	12	1,295.5	1,261.9
Development costs	12	151.3	119.0
Programme participation costs	12	183.8	174.9
Other intangible assets	12	722.1	754.5
Property, plant and equipment	13	207.1	215.9
Trade and other receivables		88.6	36.2
Derivative financial instruments		12.0	1.9
Deferred tax assets		105.0	170.6
		<b>2,765.4</b>	<b>2,734.9</b>
<b>Current assets</b>			
Inventories		239.1	236.5
Trade and other receivables		238.4	211.3
Derivative financial instruments		6.2	4.5
Current tax recoverable		0.8	0.2
Cash and cash equivalents	20	51.9	62.9
		<b>536.4</b>	<b>515.4</b>
<b>Total assets</b>	2	<b>3,301.8</b>	<b>3,250.3</b>
<b>Current liabilities</b>			
Trade and other payables		(249.9)	(239.2)
Derivative financial instruments		(4.0)	(17.2)
Current tax liabilities		(60.8)	(34.6)
Obligations under finance leases	20	(0.8)	(0.8)
Bank and other borrowings	20	(12.7)	(9.7)
Provisions	14	(40.7)	(35.8)
		<b>(368.9)</b>	<b>(337.3)</b>
<b>Net current assets</b>		<b>167.5</b>	<b>178.1</b>
<b>Non-current liabilities</b>			
Trade and other payables		(7.8)	(9.2)
Derivative financial instruments		(17.1)	(24.5)
Deferred tax liabilities		(329.6)	(393.2)
Obligations under finance leases	20	(3.9)	(4.6)
Bank and other borrowings	20	(755.9)	(856.4)
Provisions	14	(115.3)	(71.0)
Retirement benefit obligations	15	(265.1)	(280.5)
		<b>(1,494.7)</b>	<b>(1,639.4)</b>
<b>Total liabilities</b>		<b>(1,863.6)</b>	<b>(1,976.7)</b>
<b>Net assets</b>		<b>1,438.2</b>	<b>1,273.6</b>
<b>Equity</b>			
Share capital		34.9	34.3
Share premium		859.4	825.9
Other reserves		14.1	14.1
Hedging and translation reserves		159.1	117.3
Retained earnings		370.7	282.0
<b>Total equity attributable to equity holders</b>		<b>1,438.2</b>	<b>1,273.6</b>

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2010

	Share capital	Share premium	Other reserves	Hedging and translation reserves	Retained earnings	Total equity
	£m	£m	£m	£m	£m	£m
<b>At 1 January 2009</b>	33.3	798.8	14.1	195.7	244.5	1,286.4
Profit for the year	-	-	-	-	138.8	138.8
Other comprehensive income/(expense) for the year:						
Actuarial losses	-	-	-	-	(67.6)	(67.6)
Currency translation differences:						
Arising in the year	-	-	-	(81.4)	-	(81.4)
Cash flow hedge movements:						
Movement in fair value	-	-	-	(5.6)	-	(5.6)
Transferred to income statement	-	-	-	16.3	-	16.3
Other comprehensive expense before tax	-	-	-	(70.7)	(67.6)	(138.3)
Related tax movements	-	-	-	(7.7)	18.9	11.2
Other comprehensive expense for the year	-	-	-	(78.4)	(48.7)	(127.1)
Total comprehensive (expense)/income for the year	-	-	-	(78.4)	90.1	11.7
Employee share option schemes:						
Value of services provided	-	-	-	-	4.0	4.0
Shares issued	0.1	1.2	-	-	-	1.3
Dividends	0.9	25.9	-	-	(56.6)	(29.8)
<b>At 31 December 2009</b>	<b>34.3</b>	<b>825.9</b>	<b>14.1</b>	<b>117.3</b>	<b>282.0</b>	<b>1,273.6</b>
<b>Profit for the year</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>138.8</b>	<b>138.8</b>
<b>Other comprehensive income/(expense) for the year:</b>						
Actuarial losses	-	-	-	-	(1.5)	(1.5)
Currency translation differences:						
Arising in the year	-	-	-	29.3	-	29.3
Cash flow hedge movements:						
Movement in fair value	-	-	-	(3.0)	-	(3.0)
Transferred to income statement	-	-	-	23.6	-	23.6
Other comprehensive income/(expense) before tax	-	-	-	49.9	(1.5)	48.4
Related tax movements	-	-	-	(8.1)	0.6	(7.5)
<b>Other comprehensive income/(expense) for the year</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>41.8</b>	<b>(0.9)</b>	<b>40.9</b>
<b>Total comprehensive income for the year</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>41.8</b>	<b>137.9</b>	<b>179.7</b>
Employee share option schemes:						
Value of services provided	-	-	-	-	10.4	10.4
Shares issued	0.1	4.5	-	-	(0.4)	4.2
Dividends	0.5	29.0	-	-	(59.2)	(29.7)
<b>At 31 December 2010</b>	<b>34.9</b>	<b>859.4</b>	<b>14.1</b>	<b>159.1</b>	<b>370.7</b>	<b>1,438.2</b>

## CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2010

	Notes	2010 £m	2009 £m
Cash inflow from operations before exceptional operating items		<b>331.3</b>	341.7
Cash outflow from exceptional operating items	4	<b>(15.5)</b>	(21.9)
<b>Cash inflow from operations</b>	19	<b>315.8</b>	319.8
Interest received		0.4	0.9
Interest paid		<b>(38.5)</b>	(42.9)
Tax paid		<b>(29.9)</b>	(27.1)
Tax equalisation swap received/(paid)*		4.2	(11.8)
<b>Cash inflow from operating activities</b>		<b>252.0</b>	238.9
Purchase of subsidiaries		-	(1.0)
Proceeds from disposal of subsidiaries		-	0.3
Capitalised development costs	12	<b>(33.5)</b>	(35.1)
Capitalised programme participation costs		<b>(28.4)</b>	(23.9)
Purchase of other intangible assets		<b>(13.7)</b>	(7.1)
Purchase of property, plant and equipment		<b>(14.0)</b>	(18.5)
Proceeds from disposal of property, plant and equipment		0.2	0.7
<b>Cash outflow from investing activities</b>		<b>(89.4)</b>	(84.6)
Dividends paid to Company's shareholders		<b>(29.7)</b>	(29.6)
Issue of equity share capital		4.2	1.3
Proceeds from borrowings		<b>395.4</b>	256.2
Debt issue costs		<b>(1.7)</b>	-
Repayments of borrowings		<b>(542.3)</b>	(382.4)
<b>Cash outflow from financing activities</b>		<b>(174.1)</b>	(154.5)
<b>Net decrease in cash and cash equivalents</b>	20	<b>(11.5)</b>	(0.2)
Cash and cash equivalents at start of year		<b>62.9</b>	67.3
Exchange gains/(losses) on cash and cash equivalents		0.5	(4.2)
<b>Cash and cash equivalents at end of year</b>	20	<b>51.9</b>	62.9

\* Represents settlements under tax equalisation swaps designed to hedge the Group's tax exposure on foreign exchange movements.



## NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2010

### 1. Basis of preparation

This document contains abridged preliminary financial information for the year ended 31 December 2010 together with comparatives.

The information presented has been prepared in accordance with those parts of the Companies Act 2006 applicable to companies reporting under International Financial Reporting Standards as adopted by the European Union ("IFRSs") and in accordance with the FSA Listing Rules. It has been prepared under the historical cost convention as modified by the revaluation of certain financial assets and financial liabilities (including derivative instruments) at fair value.

The financial information contained in this document does not constitute Group statutory accounts as defined in Sections 404 and 435 of the Companies Act 2006. It is based on, and is consistent with, that in the Group's statutory accounts for the year ended 31 December 2010 and those financial statements will be delivered to the Registrar of Companies following the Company's Annual General Meeting. The auditors' report on those accounts is unqualified and does not contain a statement under Section 498(2) or (3) of the Companies Act 2006.

Group statutory accounts for the year ended 31 December 2009 have been filed with the Registrar of Companies. The auditors' report on those accounts is unqualified and does not contain a statement under Section 498(2) or (3) of the Companies Act 2006.

### 2. Segmental analysis

As part of the transformation programme (see note 4), the Group has created five new divisions. Results are reported in 2010 under this new segmental structure, in line with the format now reviewed by the Group's Chief Operating Decision Maker, which has been identified as the Board. Comparative segmental information for 2009 has been restated in line with the new segmental structure.

#### Year ended 31 December 2010

	Aircraft Braking Systems £m	Control Systems £m	Polymers & Composites £m	Sensing Systems £m	Equipment Group £m	Total £m
Gross revenue	309.7	183.3	156.9	213.7	305.4	1,169.0
Inter-segment revenue	-	(0.5)	(0.9)	(5.3)	(0.3)	(7.0)
<b>Revenue</b>	<b>309.7</b>	<b>182.8</b>	<b>156.0</b>	<b>208.4</b>	<b>305.1</b>	<b>1,162.0</b>
<b>Underlying operating profit*</b>	<b>120.7</b>	<b>44.7</b>	<b>28.4</b>	<b>39.5</b>	<b>70.4</b>	<b>303.7</b>

#### Year ended 31 December 2009 (Restated)

	Aircraft Braking Systems £m	Control Systems £m	Polymers & Composites £m	Sensing Systems £m	Equipment Group £m	Total £m
Gross revenue	319.0	184.0	147.9	196.7	309.7	1,157.3
Inter-segment revenue	(0.2)	(2.1)	-	(4.1)	(0.4)	(6.8)
<b>Revenue</b>	<b>318.8</b>	<b>181.9</b>	<b>147.9</b>	<b>192.6</b>	<b>309.3</b>	<b>1,150.5</b>
<b>Underlying operating profit*</b>	<b>116.2</b>	<b>43.4</b>	<b>30.0</b>	<b>32.5</b>	<b>64.1</b>	<b>286.2</b>

\* A reconciliation of underlying operating profit to operating profit is shown in note 3.

## 2. Segmental analysis (continued)

	31 December 2010	31 December 2009 (Restated)
	£m	£m
Aircraft Braking Systems	454.6	434.8
Control Systems	114.5	114.3
Polymers & Composites	69.4	71.7
Sensing Systems	176.4	151.2
Equipment Group	179.6	165.2
<b>Total segmental trading assets</b>	<b>994.5</b>	<b>937.2</b>
Centrally managed trading assets*	113.8	56.6
Goodwill	1,295.5	1,261.9
Other intangible assets	722.1	754.5
Derivative financial instruments – non-current	12.0	1.9
Deferred tax assets	105.0	170.6
Derivative financial instruments - current	6.2	4.5
Current tax recoverable	0.8	0.2
Cash and cash equivalents	51.9	62.9
<b>Total assets</b>	<b>3,301.8</b>	<b>3,250.3</b>

\* Centrally managed trading assets principally include amounts recoverable from insurers in respect of environmental issues relating to former sites and amounts recoverable under tax equalisation swaps, trade and other receivables and property, plant and equipment of central companies.

## 3. Reconciliations between profit and underlying profit

Underlying profit is used by the Board to measure and monitor the underlying trading performance of the Group. It excludes certain items as described below:

	2010 £m	2009 £m
<b>Operating profit</b>	<b>220.1</b>	<b>232.8</b>
Exceptional operating items (note 4)	15.7	20.8
Amortisation of intangibles acquired in business combinations (note 12)	64.7	69.2
Financial instruments (note 5)	3.2	(36.6)
Adjustments to operating profit*	83.6	53.4
<b>Underlying operating profit</b>	<b>303.7</b>	<b>286.2</b>
<b>Profit before tax</b>	<b>172.5</b>	<b>180.8</b>
Adjustments to operating profit per above	83.6	53.4
<b>Underlying profit before tax</b>	<b>256.1</b>	<b>234.2</b>
<b>Profit for the year</b>	<b>138.8</b>	<b>138.8</b>
Adjustments to operating profit per above	83.6	53.4
Tax effect of adjustments to operating profit	(30.3)	(21.2)
Adjustments to profit for the year	53.3	32.2
<b>Underlying profit for the year</b>	<b>192.1</b>	<b>171.0</b>

Underlying earnings per ordinary share ("EPS") for the year is 27.8p (2009: 25.3p). See note 9 for the definition of underlying EPS and its reconciliation to basic EPS.

\* Of the adjustments to operating profit, £4.9 million (2009: £10.0 million) relating to exceptional operating items has been charged to cost of sales with the balance of £78.7 million (2009: £43.4 million) included within net operating costs.

#### 4. Exceptional operating items

Items which are significant by virtue of their size or nature and which are considered non-recurring are classified as exceptional items.

	Notes	2010 £m	2009 £m
Transformation programme	a	13.2	16.9
Integration of K&F Industries Holdings, Inc. ("K&F")	b	1.2	3.7
Acquisition costs incurred	c	1.3	-
Integration of other businesses		-	0.3
Profit on disposal of businesses		-	(0.1)
<b>Exceptional operating items</b>		<b>15.7</b>	<b>20.8</b>

- In 2009, in response to the economic downturn, the Group commenced a transformation programme involving reductions in factory direct and indirect headcount and related costs arising from volume reductions, transforming the way the business is managed, effectively removing a layer of management, freezing executive pay and reducing pension and other benefits. The programme continued to make good progress during 2010 exceeding the targeted annual run-rate savings of £50.0 million by the end of the year. Further savings have been identified in 2011 with an increased annual run-rate target of £57.0 million set for the end of 2011. Total costs of achieving the £57.0 million savings are expected to be approximately £35.0 million. Costs associated with the programme are treated as an exceptional operating item.
- Costs were incurred during 2010 in completing the integration of K&F, with final savings of £22.1 million delivered.
- Costs were incurred during 2010 in respect of the proposed acquisition of Pacific Scientific Aerospace which was announced on 18 January 2011 (see note 22).

Cash expenditure on exceptional operating items was £15.5 million (2009: £21.9 million), including £13.7 million in respect of the transformation programme (2009: £14.6 million), £1.1 million in respect of K&F (2009: £6.4 million) and £0.7 million in respect of acquisition costs (2009: £Nil).

#### 5. Financial instruments

Although the Group uses foreign currency forward contracts to hedge against foreign currency exposures, it has decided that the costs of meeting the extensive documentation requirements to be able to apply hedge accounting under IAS 39 ("Financial Instruments: Recognition and Measurement") are not merited. The Group's underlying profit figures exclude amounts which would not have been recorded if hedge accounting had been applied.

Where interest rate derivatives do not qualify to be hedge accounted, movements in the fair value of these derivatives are excluded from underlying profit. Where interest rate derivatives do qualify to be accounted for as fair value hedges, any difference between the movement in the fair values of the derivatives and in the fair value of fixed rate borrowings is excluded from underlying profit (see note 3).

	2010 £m	2009 £m
Movement in the fair value of foreign currency forward contracts	(0.3)	(41.1)
Impact of retranslating net foreign currency assets and liabilities at spot rate	0.7	3.7
Movement in the fair value of interest rate derivatives	(6.1)	(2.9)
Movement in the fair value of fixed rate borrowings	8.9	3.7
<b>Financial instruments – loss/(gain)</b>	<b>3.2</b>	<b>(36.6)</b>

## 6. Finance income

	2010 £m	2009 £m
Interest on bank deposits	0.2	0.4
Unwinding of interest on other receivables	1.2	1.1
Expected return on retirement benefit scheme assets	32.0	26.1
Other finance income	0.2	0.5
<b>Finance income</b>	<b>33.6</b>	<b>28.1</b>

## 7. Finance costs

	2010 £m	2009 £m
Interest on bank borrowings	24.6	30.5
Interest on senior notes	12.2	8.6
Interest on finance lease obligations	0.3	0.3
Unwinding of interest on provisions (note 14)	1.3	1.2
Unwinding of interest on retirement benefit scheme liabilities	41.8	38.3
Amortisation of debt issue costs	1.5	1.5
Less: amounts included in the cost of qualifying assets	(0.5)	(0.3)
<b>Finance costs</b>	<b>81.2</b>	<b>80.1</b>

## 8. Tax

The Finance (No. 2) Act 2010 included legislation to reduce the main rate of corporation tax in the UK from 28% to 27% with effect from 1 April 2011. Further reductions are proposed to reduce the main rate by 1% per annum to 24% by 1 April 2014.

The legislation to reduce the main tax rate to 27% is reflected in the financial statements for the year ended 31 December 2010. The impact on net deferred tax liabilities as at 31 December 2010, profit for the year (underlying and statutory) and other comprehensive income for the year has not been significant. As the further reductions to the main rate of UK corporation tax have not been substantially enacted at the balance sheet date, their impact is not reflected in the financial statements.

## 9. Earnings per ordinary share

Earnings per ordinary share ("EPS") is calculated by dividing the profit attributable to equity holders of £138.8 million (2009: £138.8 million) by the weighted average number of shares in issue during the year of 691.5 million (2009: 676.4 million). The weighted average number of shares used excludes 0.6 million shares (2009: Nil) being the weighted average number of own shares bought by the Group and held during the year by an independently managed Employee Share Ownership Plan Trust.

The calculation of diluted EPS is based on the same profits as used in the calculation of basic EPS. The weighted average number of ordinary shares of 699.4 million (2009: 676.9 million) used in the calculation is based on the weighted average number used in the calculation of basic EPS adjusted to reflect the assumption that all potentially dilutive ordinary shares convert. For the Group this means assuming all share options and equity-settled share appreciation rights in issue are exercised.

## 9. Earnings per ordinary share (continued)

Underlying EPS is based on underlying profit (see note 3) and is calculated below:

	<b>2010</b>	2009
	<b>Pence</b>	Pence
<b>Basic EPS</b>	<b>20.1</b>	20.5
Add back effects of:		
Exceptional operating items	<b>1.6</b>	2.1
Amortisation of intangibles acquired in business combinations	<b>5.8</b>	6.5
Financial instruments	<b>0.3</b>	(3.8)
<b>Underlying EPS</b>	<b>27.8</b>	25.3

## 10. Dividends

The Board is recommending a final dividend of 6.35p per share (2009: 5.75p). Taken with the interim dividend of 2.85p (2009: 2.70p) paid in the year this gives a total dividend of 9.20p (2009: 8.45p). Subject to approval at the Annual General Meeting to be held on 20 April 2011, the proposed dividend will be paid on 6 May 2011 to shareholders on the register at close of business on 11 March 2011. In continuation of recent practice, shareholders will be offered the opportunity to elect for shares in lieu of cash for the final dividend.

## 11. Related party transactions

The remuneration of the key management personnel of the Group including executive directors is set out below:

	<b>2010</b>	2009
	<b>£m</b>	£m
Wages and salaries	<b>7.1</b>	7.4
Social security costs	<b>0.8</b>	0.9
Pension costs and other post-retirement benefit costs	<b>0.5</b>	0.5
Share-based payment expense	<b>4.8</b>	1.6
<b>Total</b>	<b>13.2</b>	10.4

## 12. Intangible assets

	Goodwill	Development costs	Programme participation costs	Other intangible assets
	£m	£m	£m	£m
At 1 January 2009	1,382.7	97.8	180.4	901.6
Exchange rate adjustments	(120.8)	(7.5)	(15.3)	(81.6)
Additions	-	35.1	27.6	7.1
Interest capitalised	-	0.1	-	0.1
Disposals	-	-	-	(0.1)
Amortisation	-	(6.5)	(17.8)	(72.6)*
<b>At 31 December 2009</b>	<b>1,261.9</b>	<b>119.0</b>	<b>174.9</b>	<b>754.5</b>
At 1 January 2010	1,261.9	119.0	174.9	754.5
Exchange rate adjustments	33.6	6.7	4.0	20.3
Additions	-	33.5	24.6	15.8
Interest capitalised	-	0.3	-	0.2
Amortisation	-	(8.2)	(19.7)	(68.7)*
<b>At 31 December 2010</b>	<b>1,295.5</b>	<b>151.3</b>	<b>183.8</b>	<b>722.1</b>

- \* Of the £68.7 million amortisation (2009: £72.6 million) of other intangible assets, £64.7 million (2009: £69.2 million) relates to the amortisation of intangible assets arising in business combinations and has been excluded from underlying profit (see note 3).

Goodwill is tested for impairment annually or more frequently if there is any indication of impairment. A full impairment review was conducted for the year ended 31 December 2010 and no impairment charge was required.

## 13. Property, plant and equipment

	2010	2009
	£m	£m
At 1 January	215.9	245.2
Exchange rate adjustments	6.4	(16.4)
Additions	14.2	17.4
Interest capitalised	-	0.1
Disposals	(0.6)	(0.9)
Depreciation	(28.8)	(29.5)
<b>At 31 December</b>	<b>207.1</b>	<b>215.9</b>

#### 14. Provisions

	2010 £m	2009 £m
At 1 January	106.8	109.3
Exchange rate adjustments	2.7	(9.6)
Transfers (to)/from trade and other payables – non-current	(0.1)	0.5
Charge to income statement – cost of sales	2.3	0.5
Charge to income statement – net operating costs*	65.7	20.7
Charge to income statement – finance costs (note 7)	1.3	1.2
Utilised	(22.7)	(15.8)
<b>At 31 December</b>	<b>156.0</b>	<b>106.8</b>
<b>Disclosed as:</b>		
Current	40.7	35.8
Non-current	115.3	71.0
<b>At 31 December</b>	<b>156.0</b>	<b>106.8</b>

\* During the year an increase of £66.3 million (2009: £19.6 million) in amounts recoverable under the Group's environmental insurance policies was recognised within other receivables and credited to operating profit.

#### 15. Retirement benefit obligations

	2010 £m	2009 £m
The amounts recognised in the balance sheet are as follows:		
Fair value of scheme assets	567.9	504.2
Present value of scheme liabilities	(833.0)	(784.7)
<b>At 31 December</b>	<b>(265.1)</b>	<b>(280.5)</b>

#### Key financial assumptions

UK scheme:		
Discount rate	5.40%	5.70%
Inflation rate	3.30%	3.50%
Salary inflation rate	4.30%	4.50%
Life expectancy in years at age 65: Member currently aged 45 (Male)	23.8 to 26.3	23.7 to 26.2
Overseas schemes:		
Discount rate	5.25%	5.65 to 5.85%
Salary increases	4.00%	4.00%
Life expectancy in years at age 65: Member currently aged 45 (Male)	19.0	18.9

#### 16. Share capital

	2010 No. m	2009 No. m
Allotted and fully paid:		
At 1 January	685.3	665.6
Issued on exercise of executive share options	1.7	0.5
Issued on exercise of sharesave options	0.6	0.3
Scrip dividends	10.4	18.9
<b>At 31 December</b>	<b>698.0</b>	<b>685.3</b>

## 17. Contingent liabilities

The Company has given guarantees in respect of uncommitted credit facilities for certain of its subsidiaries, some property leases, other leasing arrangements and the performance by some current and former subsidiaries of certain contracts. Also, there are similar guarantees given by certain other Group companies. The fair value of these guarantees is not considered to be significant.

The Company and various of its subsidiaries are, from time to time, parties to legal proceedings and claims which arise in the ordinary course of business. The directors do not anticipate that the outcome of these proceedings, actions and claims, either individually or in aggregate, will have a material adverse effect upon the Group's financial position.

## 18. Capital commitments

	2010 £m	2009 £m
Contracted for but not incurred:		
Intangible assets	0.5	1.2
Property, plant and equipment	4.3	3.4
<b>Total</b>	<b>4.8</b>	<b>4.6</b>

## 19. Cash inflow from operations

	2010 £m	2009 £m
Profit for the year	138.8	138.8
Adjustments for:		
Tax	33.7	42.0
Depreciation (note 13)	28.8	29.5
Amortisation (note 12)	96.6	96.9
Loss on disposal of property, plant and equipment	0.2	0.1
Loss on disposal of intangible assets	-	0.1
Profit on disposal of businesses (note 4)	-	(0.1)
Finance income (note 6)	(33.6)	(28.1)
Finance costs (note 7)	81.2	80.1
Financial instruments (note 5)	3.2	(36.6)
Retirement benefit obligation deficit payments	(23.1)	(21.8)
Share-based payment expense	14.3	5.4
Change in working capital	(24.3)	13.5
<b>Cash inflow from operations</b>	<b>315.8</b>	<b>319.8</b>



## 20. Net debt

	2010 £m	2009 £m
Movement in the year in:		
Cash and cash equivalents	(11.5)	(0.2)
Bank and other borrowings	148.6	126.2
<b>Change in net debt resulting from cash flows</b>	<b>137.1</b>	<b>126.0</b>
Exchange differences	(36.3)	115.5
Other non-cash movements	(13.6)	(2.2)
<b>Movement in net debt in the year</b>	<b>87.2</b>	<b>239.3</b>
Net debt at 1 January	(808.6)	(1,047.9)
<b>Net debt at 31 December</b>	<b>(721.4)</b>	<b>(808.6)</b>
Disclosed as:		
Cash and cash equivalents	51.9	62.9
Obligations under finance leases – current	(0.8)	(0.8)
Bank and other borrowings – current	(12.7)	(9.7)
Obligations under finance leases – non-current	(3.9)	(4.6)
Bank and other borrowings – non-current	(755.9)	(856.4)
<b>Net debt at 31 December</b>	<b>(721.4)</b>	<b>(808.6)</b>

## 21. Restatement of prior year comparatives

As part of the transformation programme (see note 4), the Group has created five new divisions. Results are reported in 2010 under this new segmental structure, in line with the format now reviewed by the Group's Chief Operating Decision Maker. Comparative segmental information for 2009 has been restated in line with the new segmental structure (see note 2).

## 22. Post balance sheet events

On 18 January 2011, the Company announced the proposed acquisition of Pacific Scientific Aerospace ("PSA") from Danaher Corporation for a total cash consideration of \$685.0 million. PSA is a leading supplier of components to the global civil aerospace and military markets. Organised in six businesses, PSA offers fire suppression, sensing, electric power, electric actuation and security products, with a balanced presence between civil aerospace (57% of revenues) and military (43% of revenues) markets. The proposed acquisition, which is subject to normal completion requirements, will be funded in part by an equity placing of 69.8 million new ordinary shares (representing less than 10% of Meggitt's current issued share capital) with the balance being funded from existing debt facilities. The equity placing was successfully completed on 21 January 2011 and raised £246.2 million.

## **PRINCIPAL RISKS AND UNCERTAINTIES**

### **Markets - Competition**

#### *Potential impact*

We operate in a highly competitive global market that has experienced significant consolidation in recent years. Losing contracts to competitors, many of whom have greater financial, technological and marketing resources, or being forced to accept lower margins, would have an adverse effect on Meggitt's results.

The group's competitive position would suffer were it unable to meet future investment requirements, continue research and development or provide cash and equipment incentives to original equipment manufacturers. Such investments, which decrease our cash flow in the short-term, need to be recovered through future revenues.

Losing key intellectual property or failing to enforce its rights could hinder our development and provide competitor advantage.

#### *Mitigation action*

- Protecting our positions by maintaining a broad customer base.
- Maintaining diverse products and operations to reduce the effect of action by any single competitor.
- Maintaining a competitive manufacturing base.
- Maintaining the highest manufacturing and quality standards and attending to individual customer certification requirements.
- Developing proprietary intellectual property and products in markets that demand high levels of technology, quality and service and strong, long-term relationships with customers.
- Maintaining a robust intellectual property protection programme.
- Ensuring good operational cash flow and available finance.

### **Markets - Product demand**

#### *Potential impact*

Military markets currently account for 44% of group revenues. Any reduction in military spending or reordering of priorities, particularly by the US government (Meggitt's largest customer), could adversely affect our revenues.

A significant or prolonged downturn due to recession, commodity prices, terrorist attack or aerospace regulations would decrease demand for the group's products from civil aerospace customers which account for 42% of group revenues.

#### *Mitigation action*

- Spreading our activities across the civil aerospace, military and energy markets.
- Generating revenues from original equipment manufacturers and aftermarket services.
- Operating across different geographical regions.
- Maintaining, where practical, a flexible cost base.

### **IT Security**

#### *Potential impact*

Intellectual property and other business data is stored and transmitted electronically. Accordingly, the group is exposed to the risk of data loss either through third-party breach of our systems or the unintentional loss of data by employees.

#### *Mitigation action*

- Established a senior management IT security committee to monitor risks and prioritise mitigation actions.
- Appointed a group head of IT security.
- Enhancing IT security policies and continually upgrading and standardising security tools.

## **Operations – Acquisitions**

### *Potential impact*

Meggitt continues to pursue acquisitions as part of our growth strategy. Such acquisitions may not realise expected benefits.

### *Mitigation action*

- Undertaking due diligence.
- Obtaining representations, warranties and indemnities from vendors where possible.
- Implementing comprehensive business integration processes.

## **Operations – Contracts**

### *Potential impact*

Multi-year, fixed price contracts with original equipment manufacturing customers expose us to variations in production costs.

The group is subject to the contracting regulations of our government customers, particularly those of the US government, our largest customer, which can impose a range of sanctions in response to violations.

### *Mitigation action*

- Ensuring estimates of cost are based on reliable historic data, future productivity improvements and, where possible, by entry into multi-year, fixed price contracts with major suppliers.
- Maintaining a comprehensive ethics and business conduct programme, including guidelines for doing business with the US Government and an anti-corruption policy.

## **Operations – Equipment fault**

### *Potential impact*

Meggitt's products generally operate in extreme environments where a serious incident arising from failure could result in liabilities for personal injury or death and damage to our reputation. The group may also be subject to material product warranty obligations to third parties for equipment it manufactures and services.

### *Mitigation action*

- Designing manufacturing processes that ensure stringent quality and reliability standards.
- Protecting the group from future product liability claims subject to coverage limits with liability insurance.

## **Operations – Supply chain**

### *Potential impact*

We rely on our own manufacturing operations and independent suppliers for key raw materials and components, some of which may be available from a limited number of suppliers. Any disruption to the supply chain could have an impact on our ability to meet customer requirements and adversely affect the group's results.

### *Mitigation action*

- Maintaining significant investment in modernising facilities and improving production processes to develop leading manufacturing operations.
- Maintaining a supplier risk assessment programme.
- Subjecting robust business continuity plans to regular testing to manage the risk of a loss of a major facility or supplier.

## **Operations – Transformation programme**

### *Potential impact*

The group is well-advanced in a major reorganisation to ensure it emerges from the recession leaner, more competitive and better placed to respond to customers' requirements. This is being achieved by adjusting headcount in line with volumes, removing a layer of management, implementing common IT solutions to enable shared services, streamlining other back office and administrative activity and reviewing discretionary expenditure.

Risks associated with such reorganisations include changes being adversely received by customers, new internal processes, including common IT solutions, not being implemented effectively and anticipated costs savings not being realised.

### *Mitigation action*

- Monitoring and responding to feedback from customers which has been positive to date.
- Implementing proven programme management processes and resourcing the programme effectively, helping to deliver savings in excess of original estimates to date.
- Phasing in systems changes and introducing shared services in a controlled manner.

## **Finance - Credit**

### *Potential impact*

Credit risk exists in relation to customers, banks and insurers.

### *Mitigation action*

- Maintaining a wide customer base and rigorous credit control procedures.
- Maintaining a wide bank group and monitoring relationships with banks and other counterparty risks through our treasury function.
- Diversifying funding through US private placement issues.
- Selecting insurers with good credit ratings.

## **Finance – Exchange rates**

### *Potential impact*

We operate in, and sell products to, a range of countries with different currencies, resulting in exchange rate exposure.

Transaction risk arises where revenues are denominated in currencies different from those of the costs of manufacture.

Risk arises on the translation into sterling of income statements and net assets of overseas subsidiaries.

### *Mitigation action*

- Addressing longer-term risk of exposure to exchange rate fluctuations by sourcing goods and services in currencies matching the revenue exposure where cost-effective.
- Hedging short-term transaction risk.
- Managing translation risk where possible by the currency matching of borrowings with the net assets of overseas subsidiaries.

## **Finance – Financing**

### *Potential impact*

Meggitt's long-term financing is provided by shareholders in the form of equity and by banks and other institutions in the form of debt.

The ability to raise additional equity finance is dependent on general market conditions and being able to convince potential investors of the strategic case for investing in Meggitt.

Debt facilities are provided for finite periods of time and need to be renewed periodically, unless repaid from cash generated. Such renewal could be affected by any structural issues in the credit markets.

Debt facilities contain covenants which, if breached, could result in the facilities being withdrawn.

#### *Mitigation action*

- Maintaining good relationships with major shareholders as evidenced by the successful raising of £246 million through an equity placing in January 2011 to support the proposed acquisition of Pacific Scientific Aerospace.
- Negotiating debt facility extensions. During the year the group successfully negotiated the raising of an additional USD600 million funds through a private placement.
- Basing covenant calculations on frozen GAAP to reduce volatility arising from certain fair value measurements and any future accounting standard changes.
- Including covenant clauses that enable net debt and EBITDA to be retranslated to sterling at similar exchange rates to reduce exchange movement volatility.
- Monitoring actual and forecast results against covenant ratios regularly.

### **Finance – Interest rates**

#### *Potential impact*

Fluctuations in rates affect the interest the group pays on its external borrowings.

#### *Mitigation action*

- Using the underlying character of the debt instruments and interest rate derivatives such as interest rate swaps.

### **Finance – Retirement benefits funding**

#### *Potential impact*

The group's post-retirement benefit schemes are currently in deficit (£265.1m at 31 December 2010). The level of future funding may be adversely affected by poor investment performance, changes in corporate bond yields and inflation rates, greater than anticipated improvements in life expectancy and changes in the regulatory environment. This in turn would have an adverse affect on amounts recorded in the income statement and the level of future cash contributions required to be made.

#### *Mitigation action*

- Closed all defined benefit pension schemes in the UK and USA to new members.
- Agreeing deficit recovery plans with the trustees based on actuarial advice and the results of scheme valuations.
- Reducing future service benefits to contain cost.

### **Corporate – Environmental**

#### *Potential impact*

Meggitt's operations and facilities are subject to laws and regulations that govern the discharge of pollutants and hazardous substances into air and water, the handling, storage and disposal of such materials, and other environmental matters. Failing to comply with our obligations potentially exposes the group to serious consequences, including fines, other sanctions and operational limitations.

We are involved in the investigation and remediation of current and former sites for which we have been identified as a potentially responsible party under US law.

#### *Mitigation action*

- Designing processes that minimise the effect of the group's operations on the environment.
- Commissioning independent third-party audits of our sites.
- Carrying out extensive environmental due diligence on potential acquisitions and purchasing environmental insurance for all new sites.
- Providing for the expected costs arising from these sites based on available information and establishing a receivable to the extent these costs are recoverable under the group's environmental insurance policies.

## **Corporate – Legal and regulatory**

### *Potential impact*

We are subject to litigation in the ordinary course of business and provide for such costs. However, there is a risk that successful claims or costs could exceed the provisions made. For example, a number of asbestos-related claims have been made against subsidiary companies. To date, the amount connected with such claims in any year has not been material and many claims are covered fully or partly by existing insurance and indemnities.

The group is subject to the laws and regulations of the countries in which it operates, including health and safety, environmental, export compliance and government contracting regulations. In the US, there is a system of voluntary disclosure to the relevant authorities to deal with any breach of export laws. Any reported or unreported breach may be investigated and, depending upon its seriousness, result in criminal, civil or administrative penalties, including suspension or debarment. The US authorities are investigating alleged violations of US export control laws by four US Meggitt subsidiaries and a UK business. These investigations are likely to lead to financial penalties for which provision has been made and the imposition of corrective measures. Suspension or debarment and denial of export privileges are also possible.

The aerospace industry is highly regulated so the group would be adversely affected if a material certification, authorisation or approval were revoked or suspended.

### *Mitigation action*

- Maintaining a legal and compliance function to oversee the management of these risks and the appropriate response to any issues as they arise.
- Providing for claims which cannot be recovered from insurers.
- Maintaining a health and safety programme across all of our businesses.
- Investing significant resources in implementing best practice trade compliance and ethics programmes which are reviewed quarterly by the Board's Ethics and Trade Compliance Committee.

## **Corporate – People**

### *Potential impact*

Meggitt's success depends upon the efforts, abilities, experience and expertise of certain senior and specialist employees. Failure to retain them or recruit alternatives would have an adverse effect.

The group would be adversely affected by work stoppages or slowdowns at its facilities and those of key customers or suppliers.

### *Mitigation action*

- Maintaining development and succession programmes, competitive remuneration packages and good communications at all levels.

## **DIRECTORS' RESPONSIBILITIES STATEMENT**

Each of the persons who is a director at the date of the approval of this report confirm that, to the best of their knowledge:

- the Group financial statements, which have been prepared in accordance with IFRSs adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group; and
- the Directors' Report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

By order of the Board:

T Twigger  
Chief Executive  
28 February 2011

S Young  
Group Finance Director  
28 February 2011

**– E N D S –**