REG-Meggitt PLC Preliminary Results - Part 2

Released : 03 Mar 2009 07:00

Part 2 : For preceding part double click [nRn1C1776O]

c) Profit for the year	99.1	89.3
Adjustments to profit before tax per above	124.0	73.6
Tax effect of adjustments to profit before tax	(47.9)	(33.1)
Adjustments to profit for the year	76.1	40.5
Underlying profit for the year	175.2	129.8

a. Exceptional items relate to the integration of significant acquisitions and items which by virtue of their size and nature are considered to be non-recurring (note 4).

b. The Group excludes from its underlying profit the amortisation of intangible assets acquired in business combinations (note 11).

c. IFRS 3 requires finished goods acquired through a business combination to be valued at estimated selling price less costs of disposal and a reasonable profit allowance for the selling effort. Work in progress acquired in a business combination is valued at estimated selling price less costs to complete, costs of disposal and a reasonable profit allowance for the work not yet completed. The fair value of acquired inventory is thus significantly higher than the same items built post acquisition, the value of which includes no profit element. This increase arising from the revalued inventory is charged to the income statement as the inventory is consumed and is excluded from the Group's underlying profit figures.

d. 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 required 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

e. 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

3. Reconciliations between profit and underlying profit (continued)

values of the derivatives and in the fair value of fixed rate borrowings is excluded from underlying profit. Any gains or losses arising from the requirement to continue to measure fixedrate borrowingsat fair value after the associated interest rate derivatives have matured or have been cancelled are also excluded from underlying profit (note 5).

e The goodwill adjustment arises from the recognition of tax losses during the year in respect of businesses acquired in earlier years. These tax losses existed when the businesses were acquired but a deferred tax asset was not recognised at the time as the recoverability of those losses was not probable at the time the fair values were finalised. IFRS requires that goodwill is adjusted in the year the recoverability becomes probable with a corresponding charge recorded in profit before tax.

4. Exceptional items

	Notes	2008 £m	2007 £m
Integration of K&F Industries Holdings Inc ("K&F")	a	10.2	4.7
Integration of Firearms Training Systems Inc ("FATS")	b	2.9	0.7
Integration of other businesses	c	4.6	-
Profit on sale of S-Tec Corporation ("S-Tec")	d	(1.9)	-
Exceptional operating costs		15.8	5.4
Rights issue			
- Interest on bank deposits	e	-	(2.0)
- Reduced interest payable net of costs of new facilities	e	-	(1.6)
Redemption of K&F 7.75% senior subordinated notes	f	-	3.6
Exceptional net finance costs		-	-
Analysed as:			
Exceptional finance income		-	(2.0)
Exceptional finance costs		-	2.0
Exceptional net finance costs		-	-

a. Costs incurred during the year include the rationalisation of repair and overhaul centres with the relocation of the Slough and Liege facilities to Coventry in the UK and the relocation of the Atlanta facility to Akron in the US. Costs were also incurred in rationalising and restructuring R&D and engineering capabilities and in moving steel brake and structural manufacturing from Akron to Mexico. Further exceptional operating costs of £14.1 million are expected to arise over the next two years as the integration is completed.

b. During the year the consolidation of Caswell with FATS US at a new site in Atlanta was completed.

c. During the year other business integration costs were also incurred, principally the integration of the Avery Hardoll business into other businesses in the Group.

. Cash expenditure on all exceptional operating costs above was £16.5 million (2007: £4.2 million), including £9.5 million in respect of K&F (2007: £1.9million) and £3.3 million (2007: £1.3 million) in respect of FATS

d. In January 2008 the Group completed the disposal of S-Tec and recorded a profit of £1.9 million which has been treated as an exceptional operating item (note 10).

e. The Group announced on 6 March 2007 the proposed acquisition of K&F for an enterprise value of USD 1.8 billion funded in part by a rights issue with the balance financed by a new debt facility.

4. Exceptional items (continued)

The reduction in net finance costs arising from the cash raised by the rights issue and finance costs associated with the new debt facilities was treated as exceptional net finance income in respect of the period between completion of the rights issue on 18 April 2007 and completion of the acquisition on 22 June 2007.

f Following the acquisition of K&F the Group commenced a cash tender offer for K&F's USD 315 million aggregate principal amount of 7.75% senior subordinated notes which were due in 2014. This tender offer successfully completed on 3 August 2007. The premium payable on redemption, being the difference between the total consideration paid and the book value of the notes at the date the offer completed, was treated as exceptional finance costs.

The reduction in net finance costs arising from the cash raised by the rights issue and finance

5. Financial instruments

	2008 £m	2007 £m
Movement in the fair value of foreign currency forward contracts	49.6	5.8
Impact of retranslating net foreign currency assets and liabilities at spot rate	(4.2)	(0.7)
Movement in the fair value of interest rate derivatives	2.9	0.2
Movement in the fair value of fixed rate borrowings	(2.2)	-
Financial instruments - loss	46.1	5.3

6. Net finance costs

	2008 £m	2007 £m
Interest on bank deposits	0.6	3.6
Unwinding of interest on other receivables	1.0	0.9
Expected return on retirement benefit scheme assets	31.3	27.0
Other finance income	1.0	1.2
Finance income	33.9	32.7
Interest on bank borrowings	(39.0)	(27.1)
Interest on USD 250 million senior notes	(7.4)	(6.7)
Interest on 7.75% senior subordinated notes	-	(1.7)
Premium on redemption of 7.75% senior subordinated notes (note 4)	-	(3.6)
Interest on finance lease obligations	(0.3)	(0.2)
Unwinding of interest on provisions (note 13)	(1.9)	(1.1)
Unwinding of discount on retirement benefit scheme liabilities	(36.0)	(28.2)
Other finance costs	(2.4)	(1.4)
Finance costs	(87.0)	(70.0)
Net finance costs	(53.1)	(37.3)
Analysed as:		
Exceptional finance income	-	2.0
Exceptional finance costs	-	(2.0)
Interest related to retirement benefit schemes (note 14)	(4.7)	(1.2)
Other trading interest	(48.4)	(36.1)
	(53.1)	(37.3)

7. Earnings per share

The calculation of earnings per ordinary share is based on profits of £99.1 million (2007: £89.3 million) and on the weighted average of 661.9 million (2007: 612.6 million) ordinary shares in issue during the year ended 31 December 2008.

The calculation of diluted earnings per ordinary share is based on the same profits as used in the calculation of basic earnings per ordinary share. The weighted average number of ordinary shares of 663.0 million (2007: 615.9 million) used in the calculation is based on the weighted average number used in the calculation of basic earnings per share adjusted for the effect of options.

Underlying earnings per share is based on underlying profit (note 3) and is calculated below:

	2008 Pence	2007 Pence
Basic earnings per share	15.0	14.6
Add back effects of:		
Exceptional operating costs	1.8	0.6
Amortisation of intangibles acquired in business combinations	4.7	3.3
Disposal of inventory revalued in business combinations	-	2.1

Financial instruments	5.0	0.6
Exceptional finance income	-	(0.5)
Exceptional finance costs	-	0.4
Rights issue *	-	1.0
Underlying earnings per share	26.5	22.1

* As referred to in note 4 the Group excluded exceptional finance income arising from the rights issue, for the period from when the rights issue proceeds were received on 18 April 2007 to 22 June 2007, the date when the acquisition of K&F was completed. For the purposes of underlying earnings per share for 2007 the Group also adjusted the weighted average number of shares used to exclude the effect of the new shares for this same period. The weighted average number of shares used for underlying earnings per share in 2007 was 586.9 million.

8. Dividends

The Board is recommending a final dividend of 5.75p per ordinary share (2007: 5.75p). Taken with the interim dividend of 2.70p (2007: 2.45p) paid in the year this gives a total dividend of 8.45p (2007: 8.20p) representing an increase of 3%. Subject to approval at the Annual General Meeting to be held on 23 April 2009, the proposed dividend will be paid on 8 May 2009 to shareholders on the register at close of business on 13 March 2009. In continuation of recent practice, shareholders will be offered the opportunity to elect for shares in lieu of cash for the final dividend.

9. Business combinations

On 7 January 2008 Meggitt acquired 100% of the share capital of Ferroperm Piezoceramics A/S ("Ferroperm") for £9.8 million. Ferroperm is located in Kvistgaard, Denmark and is a world leader in the manufacture of advanced piezo-electric ceramic materials for a range of specialist sensor applications, such as vibration, dynamic pressure, underwater acoustics and medical ultrasound. The acquisition has been accounted for using the purchase method of accounting.

9. Business combinations (continued)

The assets and liabilities arising from the acquisitions are as follows:

	Book value £m	Fair value £m
Goodwill (note 11)	-	5.6
Development costs	0.3	-
Other intangible assets (note 11)	-	4.3
Property, plant and equipment (note 12)	0.7	0.7
Inventories	0.9	1.1
Trade and other receivables - current	0.6	0.7
Trade and other payables - current	(0.3)	(0.4)
Current tax liabilities	(0.2)	(0.2)
Bank and other borrowings - current (note 18)	(0.8)	(0.8)
Provisions - current (note 13)	(0.1)	(0.1)
Deferred tax liabilities	-	(1.1)
Total	1.1	9.8
Consideration satisfied in cash (including costs)		7.8
Deferred consideration		2.0
Total consideration payable		9.8

Total cash consideration paid in respect of acquisitions totalled £9.2 million, of which, £7.8 million was paid in respect of Ferroperm and £1.4 million in respect of deferred consideration relating to acquisitions completed in earlier years.

10. Disposals

On 3 January 2008, Meggitt completed the disposal of S-Tec to Cobham plc for a net consideration of £17.2 million. S-Tec designs, certifies and manufactures general aviation autopilots, supplying original equipment manufacturers and the aftermarket. The business was no longer considered core to Meggitt's current operations. The assets and liabilities disposed are summarised below.

	2008 £m
Goodwill	9.2

Development costs	1.1
Other intangible assets	0.2
Property, plant and equipment	1.3
Inventory	2.2
Trade and other receivables - current	1.8
Trade and other payables - current	(1.3)
Provisions - current	(0.2)
Net assets disposed	14.3
Currency translation loss transferred from equity	1.0
Total	15.3
Net consideration	17.2
Profit on disposal (note 4)	1.9

11. Intangible assets

	Goodwill	Development costs	Programme participation costs	Other intangible assets
	£m	£m	£m	£m
Balance at 1 January 2008:				
As previously reported	1,071.2	57.7	121.8	742.2
Restatement (note 21)	(3.4)	-	-	(0.5)
As restated	1,067.8	57.7	121.8	741.7
Exchange rate adjustments	309.3	19.9	37.0	214.8
Businesses acquired (note 9)	5.6	-	-	4.3
Additions	-	23.7	35.7	5.8
Disposals	-	-	-	(0.4)
Amortisation charge *	-	(3.5)	(14.1)	(64.6)
Balance at 31 December2008	1,382.7	97.8	180.4	901.6

* Of the £64.6 million amortisation of other intangible assets £61.8 million relates to the amortisation of intangible assets arising in business combinations and has been excluded from underlying profit (note 3).

12. Property, plant and equipment

	2008	2007 Restated
	£m	£m
Balance at 1 January:		
As previously reported	195.4	127.6
Restatement (note 21)	(4.2)	-
As restated	191.2	127.6
Exchange rate adjustments	44.9	1.6
Businesses acquired (note 9)	0.7	43.1
Additions	35.9	41.0
Transfer to assets available for sale	-	(1.2)
Disposals	(0.9)	(2.1)
Depreciation charge	(26.6)	(18.8)
Balance at 31 December	245.2	191.2

13. Provisions

	Environmental legal & regulatory	Onerous contracts	Warranty costs	Total
	£m	£m	£m	£m
Balance at 1 January 2008:				
As previously reported	61.2	10.3	19.0	90.5
Restatement (note 21)	1.5	-	-	1.5
As restated	62.7	10.3	19.0	92.0
Exchange rate adjustments	20.5	1.4	3.8	25.7
Businesses acquired (note 9)	-	-	0.1	0.1
Transfer from/(to) trade and other payables	-	4.3	(4.6)	(0.3)
Charge/(credit) to income statement:-				
- net operating costs	15.2	(1.5)	2.7	16.4
- net finance costs (note 6)	1.4	0.5	-	1.9
Utilised	(18.8)	(2.1)	(5.6)	(26.5)
Balance at 31 December2008	81.0	12.9	15.4	

109.3

	2008	2007
		Restated
	£m	£m
Current	45.3	18.0
Non-current	64.0	74.0
Balance at 31 December	109.3	92.0

14. Retirement benefit obligations

	2008	2007
	£m	£m
Balance at 1 January	(153.3)	(97.2)
Exchange rate adjustments	(44.8)	(0.1)
Businesses acquired	-	(82.0)
Charge to income statement:		
- net operating costs	(13.3)	(12.1)
- net finance costs (note 6)	(4.7)	(1.2)
Contributions	35.8	14.5
Actuarial (losses)/gains	(60.9)	24.8
Balance at 31 December	(241.2)	(153.3)
Comprising:		
Fair value of scheme assets	451.9	471.4
Fair value of scheme liabilities	(693.1)	(624.7)
Balance at 31 December	(241.2)	(153.3)

14. Retirement benefit obligations (continued)

Principal financial assumptions

	2008	2007
UK schemes:		
Discount rate	6.30%	5.65%
Inflation rate	3.00%	3.25%
Current life expectancy in years: Member aged 65 (Male)	20.1 to 21.5	20.1 to 21.5
Overseas schemes:		
Discount rate	6.50%	6.40%
Salary increases	4.00%	4.00%
Healthcare cost increases	*	*
Current life expectancy in years: Member aged 65 (Male)	18.8	18.8

* Healthcare cost increases are assumed to be 8.5% for 2009 trending down to 5.0% by 2016. (2007: 9.5% for 2008 trending down to 5.0% by 2013).

Regulations in the UK and US require repayment of pension deficits over a period of time. This will require cash payments into the respective schemes in addition to normal contributions. These additional cash payments, which will not be a charge to the income statement, continue to be discussed with the relevant schemes' trustees and we estimate they will be approximately £25 million (pre-tax) in 2009.

15. Share capital

	2008	2007
	No. m	No. m
Number of shares outstanding at start of year	658.3	436.1
Rights issue	-	218.2
Issued on exercise of sharesave and executive share options	1.3	1.9
Scrip dividend	6.0	2.1
Number of shares outstanding at end of year	665.6	658.3

16. Summary of movements in equity

		2008	2007
		£m	£m
At 1 January		1,063.4	559.4
Total recognised income for the year		259.4	105.3
Employee share schemes:			
	Value of services provided	3.1	4.3
	Proceeds from shares issued	2.1	3.4
	Purchase of own shares	(1.3)	-
Dividends		(40.3)	(35.6)
Rights issue		-	426.6
At 31 December		1,286.4	1,063.4

17. Cash inflow from operations

	2008	2007
	£m	£m
Profit for the year	99.1	89.3
Adjustments for:		
Tax	20.2	16.1
Depreciation and amortisation	108.8	71.8
Loss/(profit) on disposal of property, plant and equipment	0.5	(0.5)
Loss on disposal of intangibles	0.4	-
Profit on disposal of subsidiaries (note 10)	(1.9)	-
Net finance costs (note 6)	53.1	37.3
Financial instruments (note 5)	46.1	5.3
Adjustment to goodwill on recognition of tax losses (note 3)	-	3.2
Retirement benefit obligation deficit payments	(22.5)	(2.4)
Changes in working capital	(24.9)	(10.0)
Cash inflow from operations	278.9	210.1

18. Reconciliation of net cash flow to movement in net debt

	2008	2007
	£m	£m
Movement in the year in:		
Cash and cash equivalents	1.0	26.6
Bank and other borrowings	74.0	(111.1)
Change in net debt resulting from cash flows	75.0	(84.5)
Arising on acquisition of businesses (note 9)	(0.8)	(368.0)
Other non-cash movements	5.3	(5.9)
Exchange differences	(312.0)	(3.3)
Movement in net debt in the year	(232.5)	(461.7)
Net debt at 1 January	(815.4)	(353.7)
Net debt at 31 December	(1,047.9)	(815.4)
Disclosed as:		
Cash and cash equivalents	67.3	64.9
Obligations under finance leases - current	(1.0)	(0.5)
Bank and other borrowings -current	(13.5)	(16.7)
Obligations under finance leases - non-current	(6.2)	(5.0)
Bank and other borrowings - non-current	(1,094.5)	(858.1)
Net debt at 31 December	(1,047.9)	(815.4)

19. Net debt

In addition to cash and cash equivalents of £67.3 million (2007: £64.9 million) the Group also has headroom against its committed facilities of £345.4 million (2007: £174.6 million). The weighted average maturity profile of our committed facilities is 3.6 years (2007: 3.8 years). The maturity profile of the Group's committed facilities at the year end is shown below:

	2008	2007
	£m	£m
In 2010	125.2	341.6
In 2012	813.8	587.7
In 2013	472.9	90.4
In 2015	48.7	35.2
Committed facilities	1,460.6	1,054.9

The Group's banking covenants are still measured under frozen UK GAAP and, on this basis, interest cover for the year ended 31 December 2008 was 6.6 times (covenant requirement: >3.0x). Net debt to EBITDA as at 31 December 2008 was 2.4 times (covenant requirement: â _3.5x). Interest cover (based on underlying operating profit) was 5.6 times (2007: 5.8 times).

20. Assets and liabilities held for sale

The disposal of S-Tec was announced on 21 November 2008 and subsequently completed on 3 January 2008 for a net consideration of £17.2 million (note 10). Accordingly at 31 December 2007 the related assets and liabilities were classified as a disposal group held for sale and were presented separately in the balance sheet.

21. Restatement of prior year comparatives

IFRS 3 requires fair values of assets and liabilities acquired to be finalised within 12 months of the acquisition date with the exception of certain deferred tax balances. All fair value adjustments are required to be recorded with effect from the date of acquisition and consequently result in the restatement of previously reported financial results. During 2008 the Group finalised the fair values of K&F completed in 2007 and this resulted in adjustments to the balance sheet at that date. These amendments primarily relate to revisions to the fair value of property and recognition of future tax benefits. The impact of the restatements is shown below:

	2007 As reported £m	2007 Fair value adjustments £m	2007 As restated £m
Goodwill (note 11)	1,071.2	(3.4)	1,067.8
Other intangible assets (note 11)	742.2	(0.5)	741.7
Property, plant and equipment (note 12)	195.4	(4.2)	191.2
Trade and other payables - current	(226.8)	(0.3)	(227.1)
Current tax liabilities	(43.1)	(1.1)	(44.2)
Deferred tax liabilities - non-current	(276.5)	11.0	(265.5)
Provisions - non-current (note 13)	(72.5)	(1.5)	(74.0)
Other net liabilities - not affected by restatement	(326.5)	-	(326.5)
Net assets	1,063.4	-	1,063.4

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