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News release

London, Wednesday 25 March 2009
For immediate release

Interim results for the six months ended 31 January 2009

	Headline*				Statutory	
	2009 £m	2008 £m	Growth	Underlying#	**2009 £m**	2008 £m
Continuing activities						
Sales	**1,292**	1,088	19%	(3)%	**1,292**	1,088
Operating profit	**185**	158	17%	(10)%	**160**	170
Operating margin	**14.3%**	14.5%	–	–	**12.4%**	15.6%
Pre-tax profit	**167**	159	5%	(17)%	**135**	165
Basic EPS	**32.5p**	30.8p	6%		**28.0p**	34.3p
Free cash flow	**104**	26				
Dividend	**10.5p**	10.5p			**10.5p**	10.5p

*In addition to statutory reporting, Smiths Group reports its continuing operations on a headline basis. Headline profit is before exceptional items, amortisation of acquired intangible assets, profit/loss on disposal of businesses and financing gains/losses from currency hedging. Free cash flow is described in the Financial review.

#Organic growth at constant currency.

Our reported results are ahead of last year driven by a strong organic performance from John Crane, the benefit of recent acquisitions, significantly improved cash generation and favourable exchange rates.

Clear opportunities remain to improve the business. Divisional restructuring is well underway to cut costs and enhance customer service while the rationalisation of the corporate HQ has already delivered £3m of cost savings. We have strengthened the Group portfolio and increased our exposure to faster growing markets through two acquisitions in China, subject to regulatory approvals.

The business environment has changed dramatically since last September when we announced our preliminary results. Smiths Group has not been immune to the economic challenges but our half-year performance demonstrates a resilience that augurs well for the longer term in markets with inherently strong secular growth prospects. Our focus remains to deliver our cost saving initiatives, generate cash and deliver long-term value for shareholders. A solid balance sheet underpins these plans. Absent further deterioration in world economies and assuming current exchange rates, we remain on track to deliver full year results in line with expectations.

Philip Bowman
Chief Executive
Smiths Group plc

Highlights

Key developments*

- Divisional restructuring programmes underway to reduce costs and improve customer service
- Rationalisation of the corporate HQ completed and greater divisional focus on delivering returns – total restructuring savings to date of £8m
- Upgrade of business systems including ERP for Detection, John Crane and Medical on track
- Underlying increase in Group R&D investment of 11% to £49m (reported increase of 29%)
- Extended our product portfolio and presence through two acquisitions, subject to regulatory approvals
- US$175m of additional long-term debt capital raised in February to extend our maturity profile
- Strong free cash flow generation

Business highlights*

Smiths Detection: Reported sales up 5%; underlying sales down 11%

- As previously guided, revenue was distorted by variable order flow – particularly in ports and borders
- Strong sales of airport equipment to US and good military growth with orders for JCAD
- Margins adversely affected by currency transaction (£5m) and adverse cost absorption due to reduced volumes

John Crane: Reported sales up 39%; underlying sales up 6%

- Growth driven by ongoing demand from the oil and gas sector and robust aftermarket
- Restructuring initiatives delivered £3m savings
- Upstream energy services business created with CDI and Fiberod

Smiths Medical: Reported sales up 16%; underlying sales down 3%

- Single-use consumables proving more robust than hardware
- Operational improvements have reduced customer backorders to a five year low
- Decision to exit diabetes business informed by SKU and customer profitability review

Smiths Interconnect: Reported sales up 25%; underlying sales down 2%

- Several long-term military programmes have delivered revenue growth
- Offset by lower sales to wireless operators following a large contract last year
- First half margins constrained by restructuring costs

Flex-Tek: Reported sales up 12%; underlying sales down 11%

- Performance affected by deepening recession in US housing and household appliances although market share increased
- Continued growth in sales of components to the aircraft industry
- Rationalisation programme and other cost initiatives helping preserve margins

*Underlying figures are at constant currency and exclude the impact of acquisitions and disposals

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Presentation

The presentation slides and a live webcast of the presentation to analysts are available at www.smiths.com/results at 09.00 (UK time) on Wednesday 25 March. A recording of the webcast is available later that day. A live audio broadcast of the presentation is also available by dialling:

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Photography

Original high-resolution photography is available to the media, please contact:

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Statutory reporting

Statutory reporting takes account of all items excluded from headline performance. On a statutory basis, pre-tax profit from continuing operations was £135m (2008: £165m) and earnings per share were 28.0p (2008: 34.3p). The items excluded from headline performance comprise amortisation of acquired intangible assets of £15m (2008: £7m), £8m in respect of restructuring corporate and divisional headquarters, profit on disposal of businesses of £1m (2008: £27m), profit on disposal of property of £14m (2008: nil), financing losses of £3m (2008: £3m) and £20m (2008: £8m) in connection with John Crane, Inc. asbestos litigation.

Chief Executive's review

Since we announced our results in September, global markets have been in unprecedented turmoil. While the Group's performance has not been immune from the repercussions, many parts of the business continue to show resilience in markets that are underpinned by long-term secular growth trends. John Crane delivered strong organic growth and continues to benefit from a robust aftermarket in sales and servicing which represents around two thirds of revenue. Demand for healthcare expands as populations age and become more prosperous. While tighter hospital capital budgets curtailed Smith Medical's hardware revenues, most of its sales derive from single-use consumable items for which sales have proven to be more robust. Smiths Detection is driven by a risk environment that demands increased security and protection. As previously announced, its order flow was lower in the first half – particularly in the ports and borders segment – as a result of large contract wins last year. Smiths Interconnect's largest end market is serving several long-term military programmes which have seen continued growth. However, investment by telecom wireless infrastructure providers has slowed. Although Flex-Tek is exposed to more cyclical markets such as US housing and domestic appliances, it has benefited from sales of high-performance products to the aerospace market. It has also made good progress in preserving margins through cost management and tactical pricing.

There continue to be significant opportunities to improve performance progressively over a three-year period and through this generate value for shareholders. In the first six months of the year, we have made good progress towards these objectives:

- Restructuring initiatives announced last year are well under way with savings to date of £8m following the opening of a much reduced corporate HQ and good progress made in John Crane, Flex-Tek and Smiths Medical;
- We are strengthening the product portfolio and extending our geographic presence through two acquisitions, subject to regulatory approvals;
- Improvement of our business systems to support better data-driven decision-making is on track with ERP programmes progressing well in Smiths Detection, John Crane and Smiths Medical;
- A product portfolio review is underway in Smiths Medical to examine the opportunities of enhancing its profitability. An early conclusion is the decision in March 2009 to discontinue the diabetes business;
- We have also increased significantly our investment in R&D to drive future growth through new product initiatives; and
- Our plans are supported by a strong balance sheet and in February 2009 we raised additional long-term debt capital from the issue of US$175m of Senior Notes.

Last year we launched a major restructuring programme across the Group and during this period we have made further progress. Reorganisation of the corporate HQ is now complete and, as a result, we have delivered savings of £3m compared with last year. Details of the restructuring programmes are given in the divisional reviews but to date we have delivered savings of £8m and have spent £13m, with £8m in the period. Together, the programmes are expected to produce annual cost savings of £47m when completed in three years time. The total cost of delivering these programmes will be £48m which is being treated as an exceptional item.

There are valuable opportunities to build Smiths through bolt-on acquisitions which can bring complementary technologies, support geographic expansion or leverage existing infrastructure. In the first half, Smiths Medical acquired Zhejiang Zheda Medical Instrument Co. Ltd ("ZDMI"). A manufacturer of syringe pumps and enteral feeding devices primarily for the fast-growing Chinese healthcare market. Smiths Interconnect agreed, subject to regulatory approvals, the purchase of Shenzhen Dowin Lightning Technologies ("Dowin"), a manufacturer of power and signal protection devices operating mainly in the wireless telecoms market.

Significant scope also exists to improve our information systems to enhance data-flow and speed up decision-making. For example, ERP systems are currently being deployed in Detection, John Crane and Medical. At a Group level, a new information platform is being introduced which will help capture operational data from the divisions. This creates opportunities to leverage the scale of the Group through group-wide procurement of travel, IT, logistics and other services.

During the period, we began a profitability review of the Smiths Medical portfolio – looking across customers and the portfolio of stock keeping units (SKUs). The analysis has already highlighted significant opportunities in pricing, minimum order quantities, customer management and complexity reduction. An early decision from this review is to exit the diabetes business. A considerable amount of intellectual property in the diabetes segment makes the development of next-generation products very costly and risky in terms of the potential for future patent disputes. As our only directly consumer-facing business, it shares few synergies with the rest of Smiths Medical's enterprises and requires a dedicated support infrastructure. We have concluded that our modest share, in an environment with two large and well-resourced competitors, will lead to a declining and increasingly less profitable business.

We are also driving higher levels of revenue growth organically through an increase in research and development (R&D) investment focused more tightly on growth areas that can deliver the most attractive returns. R&D investment for the Group increased by 11%, at constant currency, to £49m. In Detection, we launched an advanced people-screener which uses patented millimetre-wave technology to reveal a far wider range of threat items than currently possible with traditional non-ionising technologies. We are also beginning trials of a biological diagnostics tool that enable vets to carry out a rapid diagnosis of animal diseases in the field. In Medical, we have extended the launch of CADD-Solis to new markets.

We have a strong balance sheet and in February the Group successfully raised additional long term capital in the US private placement market through the issue of Senior Notes with a fixed 9 year maturity and fixed coupon of 7.37%. This flowed from a thorough review of the Group's financing strategy with the objective of extending the maturity of its debt and reducing its dependency on the banking market. We will continue to look for further opportunities to improve our financing profile.

Last September, we set out ranges for sales growth and margins for each of the divisions based on what we believed the businesses could achieve over the medium term in a financial and commercial environment consistent with that of recent years. Since then there has been a serious discontinuity in the economy and in financial markets. While our businesses are comparatively well placed, it will be harder to operate within these ranges in the near term. However, we remain committed to improving performance and delivering shareholder value consistent with achieving these ranges as the financial markets stabilise and world economies return to growth.

Outlook

Smiths Group has not been immune to the economic challenges but our half-year performance demonstrates a resilience that augurs well for the longer term in markets with inherently strong secular growth prospects. Smiths Detection will benefit from the global need for better security, although the scale and variability in the timing of order flow could affect short term results. John Crane's leadership position, strong aftermarket business and restructuring initiatives are expected to sustain margin improvements. The medical needs of an ageing population support long term growth for Smiths Medical but the pressure on healthcare budgets and the decision to exit the diabetes business will squeeze sales and profit expectations in the near term. Several long term military programmes support over a third of Smiths Interconnect's sales while the wireless telecoms and other industrial sectors are likely to be weaker. Flex-Tek will be held back by the recession in the US construction market but its restructuring initiatives are expected to preserve margins. Across the Group, our focus remains to deliver our cost saving initiatives, generate cash and deliver long-term value for shareholders. Absent further deterioration in world economies and assuming current exchange rates, we remain on track to deliver full year results in line with expectations.

Sales

Sales increased by £204m to £1,292m. Currency translation on overseas sales contributed £199m of this increase while the net impact of acquisitions and disposals increased sales by £40m. On an underlying basis, excluding the effects of currency translation and acquisitions and disposals, sales fell by £35m, or 3%. This £35m underlying decline in sales was driven by:

- John Crane (up £19m) as a result of ongoing projects, particularly from the oil and gas industry offset by;
- Smiths Detection (down £28m) reflecting the variable nature of the order flow, in particular with lower sales from the ports and borders market;
- Smiths Medical (down £11m) as a result of a slowdown in the healthcare market driven by lower hardware sales although disposables sales have held up better;
- Smiths Interconnect (down £2m) reflecting a slowdown in sales of components and subsystems to the wireless telecoms industry partially offset by continued growth in several military programmes; and
- Flex-Tek (down £13m) driven by the recession in US residential construction and domestic appliances, offset in part by growth in sales of fuel and hydraulic hoses to aerospace customers.

Profit

Headline operating profit rose £27m to £185m. Headline operating margin decreased by 20 basis points to 14.3% (2008: 14.5%). The increase in headline operating profit comprises £36m from favourable currency translation, £11m from the net impact of acquisitions and disposals made during the year, offset by a £20m, or 10%, decrease in underlying headline operating profit. The main drivers of this £20m underlying decline are:

- John Crane (up £8m) reflecting strong volume growth and price increases;
- Lower corporate centre costs (£4m benefit) offset by;
- Smiths Detection (down £19m) driven by lower volumes and adverse currency transaction;
- Smiths Medical (down £5m) reflecting lower hardware sales, increased ERP and R&D costs, and higher amortisation of capitalised R&D for newly launched products;
- Smiths Interconnect (down £6m) as a result of restructuring costs and adverse mix ; and
- Flex-Tek (down £2m) reflecting lower volumes.

Operating profit on a statutory basis, after taking account of the items excluded from the headline figures was £160m (2008: £170m).

The net interest charge increased to £21m (2008: £20m). There was a pensions financing gain of £2m (2008: £21m) which reflected the worsening funding position of the company's retirement benefit schemes.

Headline profit before tax increased by £8m to £167m. The Group's tax rate on headline profit for the period was 24% (2008: 25%). Headline earnings per share increased 6% to 32.5p (2008: 30.8p).

Cash generation

Headline operating cash flow totalled £154m, representing 83% of headline operating profit. Net debt has increased since July 2008 by £204m to £975m primarily as a result of foreign exchange translation (£118m), maturing net investment hedges (£45m) and acquisitions (£40m).

Dividend

In March 2008, the Board announced its intention to grow dividends consistent with increasing cover to around 2.5 times in the medium term. In line with previous guidance, the Board has declared an unchanged interim dividend of 10.5p per share. Looking ahead, our focus will remain on rebuilding dividend cover. This reflects the opportunities to invest in organic growth and acquisitions and the challenges in the financial markets which have affected the financing of corporates and defined benefit pension funds. The interim dividend will be paid on 24 April to shareholders registered at the close of business on 3 April. The ex-dividend date is 1 April.

Business review

Smiths Detection

	2009 £m	2008 £m	Reported growth	Underlying growth
Sales	**233**	222	5%	(11)%
Headline operating profit	**24**	35	(32)%	(45)%
Headline operating margin	**10.2%**	15.8%		
Statutory operating profit	**24**	35		

Reported sales grew 5%, or £11m, driven by currency translation. Excluding the currency translation benefit of £39m, sales declined 11% on an underlying basis. As previously signalled, this reflects the increasingly variable nature of the order flow of this largely government contracting business. The sales performance is driven primarily by declines in the ports and borders segment which benefited in the prior period from a large Russian contract. This decline has been partly offset by good growth in the military area, particularly from increased sales of JCAD, the advanced chemical point detector. The reduction in sales volumes (£14m) combined with adverse currency transaction (£5m) has squeezed margins with underlying headline operating profit down 45%, or £19m. Excluding the impact of currency transaction, underlying operating profit margins would have been 12.2%. We have continued to invest in the business with company-funded R&D investment increased to £15m and £6m of investment in a new ERP business system. This reflects our confidence in the long-term growth prospects of the business which continues to see a healthy level of tender activity and new business interest.

Underlying sales in transportation were in line with last year which reflects good growth in the US, while sales in EMEA were down. US sales have benefited from the introduction of a new generation of airport checkpoint explosive detection systems. Unlike conventional X-ray systems, this equipment captures multiple views of carry-on bags in a single sweep. The system also includes software algorithms that help the operator detect potential threats and it can easily be upgraded to meet future threats. Airports in Europe have been slower to adopt the new technology while trials are still underway and the current economic situation has caused governments to review the timing of some projects.

The ports and borders market has seen a decline in sales following a strong performance in the first six months of last year which benefited from a large contract in Russia. Average contract size has increased over recent years as governments have become more co-ordinated in their approach to border security and customs revenue protection. As a result, the sales profile in this business has become more variable and the working capital requirement has also increased. Our leading-edge technology leaves us well placed to benefit from long-term growth prospects. For instance, the US has mandated that 100% of arriving cargo be scanned by 2012. We continue to tender on some substantial projects in several markets. The European Commission has announced a full investigation into concerns about unfair competition from China in the EU market for advanced cargo-screening systems. This will examine whether the Chinese company, NucTech, has been dumping on the EC market and undercutting prices to a degree that precludes free and open competition.

Military sales delivered good organic growth through the ongoing JCAD programme. We received further orders from the US Department of Defense amounting to $65m during the period, taking the total orders to date to $122m. The lightweight JCAD is an advanced chemical point detector designed to help safeguard troops by automatically detecting, identifying and quantifying both chemical warfare agents and toxic industrial chemicals. We have also won a $19m contract from the US Army for Meteorological Measuring Set-Profiler (MMS-P) systems, which takes the total programme value to over $89m to date. The MMS-P gathers real-time meteorological data using satellites, ground sensors and weather balloons to assist with accuracy in military operations. The military production facility in Edgewood, Maryland, is being expanded by almost 50% to meet the demand created by several Department of Defense contract wins over the past two years.

We have also reorganised the business into Security & Inspection, which will focus on airports, ports and borders and critical infrastructure, and Military and Emergency Response. A new Chief Operating Officer post has been created and Chris Gane has joined us from Thales to drive improvements in operations management and efficiencies in manufacturing and logistics.

The implementation of a new ERP system began during 2008 following 18 months of planning and preparation. This single system will replace 14 legacy business software systems and provide a common information platform to support data-driven decision making. 14 sites representing 50% of sales have now gone live with the new system. The project is expected to conclude by the end of calendar year 2009. Investment to date has been £20m, with a total budget of £22m. We anticipate that once complete the project will generate efficiencies in working capital of £11m and annual cost savings of £8m.

Research and development

Smiths Detection has maintained its leadership in the sector through a consistent commitment to product innovation developed by in-house R&D, government-funded research and through partnerships and licences. Company-funded R&D increased by 2% to £15m or 6.5% of sales (2008: 5.9% of sales). This includes £5m of capitalised projects. Smiths Detection actively seeks customer and government support for R&D which totalled £7m in the period (2008: £4m). Total R&D spend was £22m (2008: £17m) or 9.4% of sales.

X-ray screening continues to be a focus for our investment, supporting the development of a new generation of cargo screening. We have also continued to invest in the development of our airport checkpoint explosive detectors particularly to address new threats. Trials are currently underway on the software that would allow automatic detection of suspect liquids in carry-on baggage. We have launched an advanced people-screener which for the first time uses electronic, real-time imaging in a standard checkpoint layout to detect weapons or explosives concealed under layers of clothing without physical contact. The new system, called 'eqo', is based on patented millimetre-wave technology which reveals a far wider range of weapons and hazards than is possible with traditional non-ionising technologies. The system offers a fast and efficient way of scanning people as they enter airport checkpoints, high profile buildings or other facilities that require protection.

Diagnostics continues to be an area of focus with development of a portable biological detection system that enables veterinarians to carry out rapid on-site diagnosis of animal diseases. Field trials will begin shortly for a foot and mouth test with the UN Food and Agriculture Organization while tests for bird flu are about to start laboratory validation with two government veterinary agencies. The same technology is now being developed for clinical applications such as the detection and identification of MRSA, *clostridium difficile* and other infectious diseases.

Outlook

The full year results are likely to be affected by the variable order profile although some improvement is expected in the second half, subject to our winning some of the large contracts currently under tender. At the same time, we have identified opportunities to reduce costs which will begin to support margin improvement. Looking beyond the next six months, we believe that the sector is set for sustained growth and Smiths Detection will benefit from its leadership position and the roll-out of new products.

John Crane

	2009 £m	2008 £m	Reported growth	Underlying growth
Sales	**393**	283	39%	6%
Headline operating profit	**66**	41	62%	18%
Headline operating margin	**16.8%**	14.4%		
Statutory operating profit	**40**	34		

John Crane's reported sales rose 39% and headline operating profit increased by 62%. Sales benefited from currency translation (£47m) and from acquisitions (£44m) giving underlying sales growth of 6%, or £19m. Similarly, headline operating profit benefited from currency translation (£8m) and from acquisitions (£9m), leaving an underlying growth rate of 18%. Margins increased by 240 basis points to 16.8%. The strong sales growth has been driven by continued demand for original equipment orders and aftermarket servicing. The petrochemical industry has remained the principal driver of growth with underlying demand continuing to be strong.

The provision of aftermarket maintenance and repair services to customers represents some two-thirds of John Crane's sales. The sale of original equipment for new production facilities is a third of sales and creates subsequent aftermarket service opportunities that are delivered via John Crane's industry-leading, global network of service centres. Some 132 local service centres are now sited in 54 countries worldwide and this number is expected to rise. These facilities provide a range of added value services including repair, root cause analysis, alignment and condition monitoring all designed to improve the performance of customers' rotating equipment and to reduce downtime. Current developments are focused on key growth markets. In the Middle East, we have opened four new facilities including a wet seal service centre in Bahrain and a service, sales, manufacturing and training facility in Damman, Saudi Arabia. In Asia Pacific, three service centres have been opened. We now have an expanded service capability in Rayong, Thailand to serve the petrochemical and oil & gas markets; a new facility in Darwin, Australia to service the oil & gas and minerals mining markets; and a new state-of-the-art wet and gas seal service facility in Tianjin, China, which is part of the recently opened John Crane China facility.

In end markets, underlying sales to the petrochemical/oil & gas sector were ahead of last year. Organic sales in other energy grew substantially, while commercial & refrigeration also grew well. The chemical, textile and pharmaceutical markets also saw good growth while industrial (power), pulp paper and mining decreased marginally.

At the start of this fiscal year, we launched a restructuring programme to create one global John Crane division by integrating the two existing regional organisations. Strategy and planning are now co-ordinated globally, while engineering, operations & supply chain strategy, finance, IT, human resources and legal operate globally. Sales and service functions have been kept close to our customers in regional organisations. These changes are facilitating improved customer focus, quicker decision-making, better delivery, and more effective communications. In the period, we spent £3m and delivered savings of £3m. Overall, the project was forecast to cost £24m and deliver annual savings of £25m.

Implementation of a new ERP system is underway across Europe with 10 markets now successfully online. The project has progressed into the Middle East and will proceed to Asia. Investment to date has been £20m out of a projected total of £24m. The project is expected to generate annual cost savings of £10m after completion in June 2010.

As part of an acquisition strategy to support growth, John Crane is expanding its product portfolio with complementary technologies for similar customers that can leverage the global sales and service network, and is building an upstream energy services business. The product portfolio has expanded with the acquisition of Indufil – a manufacturer of filtration systems for rotating equipment – and the creation of John Crane Bearing Technology from the acquired engineered bearings business of Sartorius. Indufil continued to see solid growth in the first half. Initial integration activities have focused on finance, IT, operations and developing the required skills in the John Crane sales force to promote Indufil's products through the global John Crane sales and service network. John Crane Bearing Technology saw good growth both in order intake and sales specifically for compressors and turbines. Integration activities are ongoing and have included migration to John Crane's ERP system. Training and development activity for the sales force is well underway to promote and sell the product range through John Crane's extensive network. General financial performance is ahead of expectations for this business.

In the upstream energy sector, John Crane Production Solutions business unit has been formed to capitalise on the synergies of the CDI Energy Services and Fiberod acquisitions. These businesses continue to perform well on a global basis. CDI has continued to grow at double digit rates, and has recently completed a major retrofit programme on pumping wells in Romania to improve the country's oil and gas production. Fiberod has also experienced high double digit growth. The success of these two companies is driven by their exceptional service capabilities and ability to offer customers reduced operating costs.

John Crane Production Solutions has launched a solar-powered low volume pumping system (LVPS) which minimises carbon emissions during gas extraction. The ECO2 pumping unit, which has been specifically developed for the LVPS, consumes less power than a handheld hair dryer and is being trialled by a major energy company at various sites in North America. ECO2 works by pumping water from the underground field – using Fiberod's lightweight sucker rods – allowing gas to travel to the surface where it is then collected and transported via pipelines. The system enables easier and more economical access to wells in remote areas than traditional artificial lift systems, which are powered by other methods and require miles of transmission cables and costly electricity to work.

Outlook

Two thirds of John Crane's sales is derived from the aftermarket where the oil & gas and power sectors remain relatively stable. It is anticipated that the chemical and industrial sectors will continue to be challenging. The order book for original equipment, which represents around one third of sales, remained strong in the first half and this is expected to underpin sales during the second half of this fiscal year. However, since January, orders for original equipment have softened as a result of lower capital investment by customers. The major restructuring programme which we began last year to deliver improved customer focus and operational efficiencies will help to underpin enhanced margins. This programme remains flexible to respond to the changing market conditions which we are monitoring closely with our customers.

Smiths Medical

	2009 £m	2008 £m	Reported growth	Underlying growth
Sales	**403**	346	16%	(3)%
Headline operating profit	**77**	67	15%	(6)%
Headline operating margin	**19.1%**	19.3%		
Statutory operating profit	**69**	59		

At reported exchange rates, Smiths Medical's sales grew 16% while headline operating profit increased by 15%. Reported sales benefited from currency translation (£66m) and acquisitions (£2m) which, if excluded, give an underlying sales decline of 3%. Headline operating profit benefited from currency translation (£14m) and acquisitions (£1m). Operating profit margins reduced slightly, by 20 basis points.

Looking at the medical device market as a whole, the economic downturn has adversely affected hospital capital budgets, which in turn is having a dramatic impact on hospital purchases of hardware or capital items. For example, most competitors in the infusion pump sector have reported significant sales declines in the latest reporting period. In parallel, elective procedures are being delayed as health insurance coverage reduces.

Some 80% of Smiths Medical sales are generated from single-use consumable items. This disposables market is considerably more stable and, in some segments, Smiths Medical has achieved market share growth. Hardware items, such as infusion pumps, comprise the remaining 20% of sales. This sales split is reflected in the underlying performances of the three product areas. Medication Delivery (which includes infusion pumps) declined by 3.8%, Vital Care (which includes temperature management and patient monitoring hardware) declined by 4.5%, while Safety Devices grew by 1.7%.

Underlying profit for the half declined by 6%. Though cost reduction actions in the first half successfully mitigated input price increases, the profit decline reflects increased costs for the accelerated roll-out of the new ERP system as well as increased expenditure on R&D.

Smiths Medical has made good progress in addressing the supply chain problems that have held back the business over the past two years. The 24-month performance improvement programme, which began last year, is delivering results with a further reduction in customer backorders since the year end. At £1.5m, total backorders now stand at their lowest level in more than five years. To date, the North American business has benefited most from these improvements and has held sales in line with last year. However, given the contracting cycle in some of our markets, the International business is taking longer to win back business lost during the earlier supply interruptions. As a result, sales in the International business have declined by 5.7%. Europe has been worst affected, down 6.3%

overall, while we have achieved double digit growth in developing markets such as China (15% organic growth) and India (55% organic growth).

The Medication Delivery business has been under pressure on two fronts. Firstly, the diabetes business has faced severe competitive pressure in the US and in other key markets. New pump sales are down significantly, partly offset by more resilient sales of the associated consumable items. Secondly, the delay in hospital capital purchases has directly impacted pump sales in our hospital and ambulatory infusion businesses. Our next generation ambulatory smart pump, CADD-Solis, has been extremely well received by prospective customers.

In Vital Care, our predominantly disposables-driven airway business was flat in the first half, with modest growth in North America offset by a small decline in the rest of the world. This product segment was the most severely affected by the supply problems in the last two years. With these issues behind us, and with a number of new products recently launched and in the pipeline, we expect to return to growth. The hardware businesses in our Vital Care segment, particularly patient monitoring and temperature management, declined in the period due partly to spending deferrals by customers as well as competitive pricing pressure.

Sales of our Safety Devices grew 1.7% in the first half. Recent new access product launches (which target the oncology market) have driven global growth in this business, and are coupled with good growth in our needle safety business. Solid growth in our US intravenous catheter business, which is almost entirely converted to safety products, was offset by a decline in our intravenous catheter business outside the US, where we are seeing competitive pressure from low featured, lower cost safety catheters.

During the period, we began a review of portfolio profitability, looking at margins by stock keeping units (SKUs), leading to decisions on the future shape of the portfolio. This analysis has already highlighted opportunities in terms of pricing, minimum order quantities, customer management and simplification. The initial focus has been on the rationalisation of our large number of SKUs, focusing particularly on our lower volume products which comprise some 13,000 SKUs from the total portfolio. We intend to eliminate at least 3,000 SKUs in an initial round. Furthermore, we have identified the opportunity for targeted price increases on our lower volume, lower margin SKUs. The next phase of the review will look at pricing opportunities across the portfolio including our spares business as well as driving improved customer profitability through enhanced key account management.

An early outcome from this portfolio review concerns our Diabetes business. A considerable amount of intellectual property in the diabetes segment makes the development of next-generation products very costly and risky in terms of the potential for future patent disputes. In addition, this market has evolved rapidly from a familiar hardware plus disposables model to an integrated diabetes disease management model requiring significant investments in continuous glucose monitoring electronically linked to insulin delivery systems. We have concluded that our modest share, in the face of two large well-resourced players, including the market leader in insulin-pump therapy, would result in a declining and increasingly less profitable business. As our only direct-to-consumer enterprise, this business also requires a significant and dedicated infrastructure. Therefore, we have decided to effect an early exit, which is now in the process of implementation. Throughout our involvement in the diabetes market, we have put customer care first, provided excellent customer support and maintained the integrity of our four-year warranty. We have been rewarded with a core group of very loyal customers, and we will continue to support this installed base although we will not sell any new pumps.

Our ongoing efforts to drive efficiency improvements and cost reduction are aimed at protecting business performance during the current downturn and positioning the business for greater margin growth as conditions improve. Overall, we have removed 300 posts since the year end. The North American restructuring programme, announced at the last full year results, is making good progress. The three former operational units in the US and Canada are now managed under a single management team. Though primarily intended to ensure a single face to the customer, we have been able simultaneously to drive business efficiencies, including the centralisation of complaints handling and the transition to a single US shared services centre.

The implementation of our ERP business systems continues to hit all the milestones. Business unit go-live dates are being achieved as planned, while total project costs are tightly controlled and running slightly favourable to expectations. Benelux, Japan, Spain and our manufacturing site at Southington, Connecticut, have gone live in the period. More than 60% of sales and sites are now operating with the new system, and over 90% of the products we make flow through the ERP at some point in the supply chain. The project, due for completion in March 2010, will improve the quality of management information and support inventory reductions, global sourcing and deliver savings. The total budget is £32m, of which £22m has been spent to date. Once complete, the project is expected to deliver annual cost savings of £15m.

Business developments

In November, we extended our presence and capabilities in China through the acquisition of Zhejiang Zheda Medical Instrument Co. Ltd ("ZDMI"). ZDMI manufactures syringe pumps and enteral feeding devices primarily for the Chinese healthcare market which is growing as the population ages and increases in prosperity. ZDMI has around 110 staff based in Hangzhou and posted sales of RMB 72.7m in the last calendar year. Integration is well underway. This acquisition consolidates our presence in a large and rapidly growing market and provides a low cost R&D base for the development of hospital infusion products for other international markets.

Research and development

Total R&D investment represented 3.4% of sales. We are now focusing our investment more tightly on product areas and segments which will deliver higher growth and improved profitability.

In our Vital Care segment, we launched several new products including the first wireless blood pressure monitoring device, SmartX; our percutaneous tracheostomy range, Uniperc, a range of silicone airway devices as well as some lower cost intubation devices.

During the first half of the year, we focused on the global rollout of new products with our CADD-Solis ambulatory smart pump now available in all English speaking markets and a multi language variant due to be launched in 2010. Our highly successful new products for our Access business are now available globally. We also introduced a 250ml cassette for our ambulatory infusion range which enables the pumps to be used for a wider range of therapies.

Outlook

Smiths Medical will continue to improve customer service and deliver on its performance improvement programme. The division will strive for growth in developing markets and globally through the launch of new products. The priority in the short term will be on margin improvement through restructuring and operating efficiencies. The review of portfolio profitability and the decision to exit the diabetes business will affect revenue growth in the near term but will support margin improvement.

Smiths Interconnect

	2009 £m	2008 £m	Reported growth	Underlying growth
Sales	**152**	121	25%	(2)%
Headline operating profit	**24**	23	3%	(20)%
Headline operating margin	**15.7%**	19.2%		
Statutory operating profit	**22**	22		

Reported sales for Smiths Interconnect increased by 25%, or £31m, driven by currency translation (£26m) and acquisitions (£7m). On an underlying basis, excluding the benefits of currency translation and acquisitions, sales fell 2% due to declines in sales of components to the wireless infrastructure market as well as the industrial markets in Europe. In particular, sales of our lightning and surge protection equipment declined against the same period last year which benefited from some significant short-term contracts. Sales to the military and aerospace markets have remained strong while the industrial and medical markets have become more challenging.

Headline operating profit increased by 3%. Excluding the benefit of currency translation (£6m) and acquisitions (£1m), headline profit declined by 20%, or £5m. Margins were adversely affected by one-off restructuring charges (£2m) and adverse currency transaction (£1m). Adjusting for these, the headline operating profit declined by 8% (£2m) mainly due an adverse mix effect on gross margins.

Smiths Interconnect manages its portfolio as five technology groups: Microwave Sub-Systems; Connectors; Protection; Interconnect Wireless Technologies and High Reliability Components,.

Microwave Sub-Systems has continued to see strong sales growth through several US military programmes. Demand for the delivery of Mobile Directional Antenna Systems (MDAS), which provides a three-frequency band data link to support multiple unmanned aircraft systems, remained high and the addition of a higher frequency capability enabled an existing telemetry system to be adopted by several new US and international UAV programmes. We continue to make good progress on satellite communications programmes for US forces including Satellite Communications On The Move (SOTM); Warfighter Information Network-Tactical (WIN T); and the Navy Multiband Terminal (NMT). NMT provides seamless assured connectivity between a ship's computer network and the US DoD Global Information Grid and will be installed in approximately 300 ships, submarines and shore locations over the next eight years. Additionally, demand for backhaul antennas remained robust despite the general weakening in wireless infrastructure.

Connectors sales reduced on an underlying basis reflecting some challenging end markets. The industrial rail traction and test & measurement markets in Europe have weakened considerably and there has also been a slowdown in the medical market and emerging geographies, particularly China. In the more robust military sector, we have seen some initial success with a new series of circular and rectangular harsh environment, high reliability connectors (SnapTac) particularly suited for 'future soldier' applications.

Sales of the Protection devices declined due to a general slowdown in the wireless infrastructure market and some significant contract wins last year in connection with the roll-out of the WiMAX broadband network within the US. Partially offsetting this, Protection has progressed well in diversifying its addressable markets with particular success in penetrating the defence sector. Margins were also affected by a shift in mix towards lower margin products compared with last year.

In the summer of 2008, Smiths Interconnect acquired Shanghai-based Allrizon Tongguang and Brisbane-based Triasx Pty Ltd. This led to the reorganisation of our microwave components businesses into two focused groups: Interconnect Wireless Technologies (IWT) providing microwave products and test solutions for the wireless telecommunications infrastructure market, and High Reliability Components (HRC) with more focus on the military and space markets. Both new acquisitions have been successfully integrated into the new IWT technology group. The combined trading performance is ahead of expectations due to a strong contribution from the sale of portable passive intermodulation analysers which are used by telecom operators to improve the signal quality and processing capabilities of mobile phone base stations. HRC has experienced mixed trading conditions with weaknesses in some sectors partially offset by continued strong demand for microwave filters used in counter-IED (Improvised Explosive Devices) systems.

Business developments

Smiths Interconnect initiated numerous restructuring projects in the first half that will yield direct, indirect and fixed cost savings and also increase the percentage of manufacturing in low cost economies. This included the combination of two Protection businesses with the majority of manufacturing transferring to our Mexico facility and the retention of a satellite engineering office. In addition, substantial reductions in work force were completed in Ireland, Scotland and Italy. All of these projects have already started to pay back and will be contributory factors to an improvement in operating margin in the second half of the year.

Smiths Interconnect has agreed, subject to regulatory approvals, the purchase of Dowin, a Chinese manufacturer of power and signal protection devices operating mainly in the wireless telecoms market. Based in Shenzhen, this move will complement our existing protection portfolio and provide a platform in Asia where we expect further investment in the roll-out of wireless infrastructure.

Outlook

With the exception of defence, all end markets are likely to remain challenging in the short term. In the longer term, the key focus for Smiths Interconnect will continue to be driving organic growth while seeking opportunities to add complementary technologies and extend its geographic reach through bolt-on acquisitions. Military communication is anticipated to be an area of continued investment by governments even if overall defence budgets plateau or decline. In the wireless communication infrastructure market, capital expenditure has slowed recently due to the current economic uncertainty, however growth is expected to return in 2010 as western operators plan to introduce higher speed next generation networks and new wireless networks are rolled out in developing markets.

Flex-Tek

	2009 £m	2008 £m	Reported growth	Underlying growth
Sales	**111**	100	12%	(11)%
Headline operating profit	**11**	11	3%	(17)%
Headline operating margin	**9.7%**	10.6%		
Statutory operating profit	**9**	11		

On a reported basis, Flex-Tek's sales increased 12%, or £11m, driven by currency translation (£22m) and the acquisition of Fast Heat (£2m). Excluding currency translation and acquisitions, underlying sales fell by 11%. This reflects the impact of the recession on the US residential construction markets and household appliances market. However, these declines were offset in part by the strong growth in sales of components and services to the aerospace market. Underlying headline profit declined by 17% and margins fell by 90 basis points.

Smiths Tubular Systems Aerospace delivered continued growth in sales and profit. This technology group benefited from the strong demand for fluid distribution components and services for commercial and military aircraft. The group has also benefited from production efficiency gains and, through a focus on careful cost control, has been able to improve margins.

Flexible Solutions provides flexible hose assemblies to domestic appliance manufacturers and ducting for the industrial market for a range of purposes from chemical transfer to grain handling. This group has experienced declines in sales and profit as a result of continued pressure in the household appliance and general industrial sectors. The domestic appliance market has seen significant declines over the past year while the general industrial markets remain challenging.

The Heat Solutions group supplies heating components for tumble dryers and HVAC ducting and related equipment to the US construction market, primarily to the residential sector. The recession in the US construction market has prompted a 36% fall in housing starts. Similarly, the US electric dryer appliance market has seen further declines. Against this background, sales fell although at a lower rate than the market, indicating that we have successfully gained share in a challenging trading environment. In addition, a focus on production efficiency, cost management and tactical pricing has helped to preserve margins.

Flex-Tek's new facilities in Asia continue to grow. We have expanded the range of products delivered from our Changshu, China facility to include gas delivery tubing and are in the process of gaining FAA approval for our Aerospace tubing overhaul and repair facility in the Clark Freeport Zone, Philippines. Our Aerospace tubing facility in Bangalore, India should be well positioned to benefit from recent announcements by the Indian government regarding increased defence spending.

Given the challenges in the end markets, Flex-Tek has also identified opportunities to rationalise its manufacturing portfolio to drive efficiency improvements. The programme is part of the wider Group restructuring and is expected to cost £5m in total and, once complete, deliver annualised savings of £7m. In the period to date, Flex-Tek has announced the closures of a factory near Glasgow, Scotland, and of a heating element facility in Elmhurst, Illinois. Savings to date total £2m. The restructuring programme will make Flex-Tek a stronger business and better positioned for a recovery in the US housing and appliance markets – when that occurs.

Outlook

Flex-Tek is facing continued uncertainty in the US residential construction, household appliance and industrial markets. It will rationalise its portfolio of sites and reduce costs in order to deliver future value when these markets improve. The growth opportunities in aerospace and developing markets will also be a focus.

Financial review

Earnings per share
Basic headline earnings per share from continuing activities were 32.5p (2008: 30.8p) a rise of 6%. On a statutory basis, the basic earnings per share from continuing activities were 28.0p (2008: 34.3p).

Exceptional and other items excluded from headline profit before tax
These items amounted to £31m, compared to a profit of £7m in 2008. They comprised:

- £8m in respect of restructuring corporate and divisional headquarters; this is part of a programme expected to cost approximately £48m over the next two years;
- £20m (2008: £8m) in connection with John Crane, Inc. asbestos litigation. Of this sum, £12m (2008: £8m) relates to discounting effects and £8m (2008: nil) was in respect of changes in the assumptions underlying the provision based on expert advice. The increase in balance sheet provision includes not only the charge to profit but also £53m arising from foreign exchange translation;
- Amortisation of intangible assets acquired in business combinations of £15m (2008: £7m). The amortisation relates principally to technology and customer relationships;
- Profit on disposal of businesses of £1m (2008: £27m); and
- Profit on disposal of property of £14m (2008: nil).
- Exceptional items in 2008 also included acquisition integration costs (£2m).

Financing losses totalled £3m (2008: £3m). These represent exchange gains and losses on financing which are not hedge accounted under IFRS.

Cash generation and net debt
Headline operating cash-flow was £154m, representing 83% of headline operating profit. This compares to £99m in the prior period and cash conversion of 63%. Cash expenditure on exceptional items was £7m (2008: £14m). On a statutory basis, net cash inflow from continuing operations was £132m (2008: £64m).

Free cash-flow from continuing operations (after interest and tax but before acquisitions, financing activities and dividends) was £104m (2008: £26m). Dividends paid on ordinary shares totalled £91m (2008: £91m). Net debt has increased since July 2008 by £204m to £975m primarily as a result of foreign exchange translation (£118m), maturing net investment hedges (£45m) and acquisitions (£40m).

Interest and other financing costs
Interest payable on debt, less interest on cash deposits, was £21m, compared with £20m in 2008. Net interest costs were 8.8 times covered by headline operating profits. The Group accounts for pensions using IAS19. As required by this standard, a finance credit is recognised reflecting the expected return on pension scheme assets and a finance charge is recognised reflecting the unwinding of the discount on the future pension liability. The net financing income for continuing operations was £2m in the period (2008: £21m).

Research and development
Investment in research and development (R&D) drives future performance and is a measure of the Group's commitment to the long-term organic growth of the business.

We invested a total of £49m in R&D on continuing operations, equivalent to 4% of sales. Of that total, £9m was funded by customers. The comparative figures for 2008 were £39m and £5m. Under IFRS, certain of these development costs are capitalised. The amount capitalised is shown as an intangible asset. Where customers contribute to the costs of development, the contribution is included as deferred income and disclosed within trade and other payables.

Taxation

The tax charge for the year represented an effective rate of 24% on the headline profit before taxation, compared to 25% in 2008. The rate reduced as a result of global tax incentives, the tax-efficient use of capital, active tax compliance management together with the impact of resolving certain open issues. On a statutory basis, the tax charge on continuing activities was £26m.

Retirement benefits

As required by IFRS the balance sheet reflects the net surplus or deficit in retirement benefit plans, taking assets at their market values at 31 January 2009 and evaluating liabilities at year-end AA corporate bond interest rates.

The period end retirement benefit position was:

	31 January 2009	31 July 2008
Funded plans:		
UK plans – funding status	**94%**	106%
US plans – funding status	**64%**	89%
Other plans – funding status	**77%**	81%

	31 January 2009	31 July 2008
Surplus/(deficit):		
Funded plans	**(330)**	102
Unfunded plans	**(134)**	(113)
Total liability	**(464)**	(11)

The increase in deficit is largely caused by the fall in global equity values. Company contributions to the funded pension plans were £13m (2008: £18m). A summary of the retirement benefit position is shown in note 8. The Bank of England's policy of quantitative easing has caused discount rates to fall which will have increased pension fund liabilities since the period end. The triennial review of the pension schemes will begin in April 2009 which will cause future contributions to increase.

Exchange rates

The results of overseas operations are translated into sterling at average exchange rates. The net assets are translated at period end rates. The principal exchange rates, expressed in terms of the value of sterling, are shown in the following table.

	31 January 2009	2 February 2008	
Average rates:			
US Dollar	**1.64**	2.02	Dollar strengthened 19%
Euro	**1.20**	1.41	Euro strengthened 15%
Period end rates:			
US Dollar	**1.45**	1.97	Dollar strengthened 26%
Euro	**1.13**	1.33	Euro strengthened 15%

Risks and uncertainties

The principal risks and uncertainties affecting the business activities of the Group were identified on pages 30 and 31 of the Annual Report for the year ended 31 July 2008, a copy of which is available at the Company's website at www.smiths.com. The key risks and uncertainties were summarised under the following headings:

- Competition, innovation and major projects
- Raw materials and inability to supply
- Global political and economic conditions
- Information technology
- Acquisitions and disposals
- Internal controls
- Legislative and regulatory
- Litigation and product liability
- Environmental and external events
- Financial
- Pension funding
- Human resources

In the view of the Board, the risks and uncertainties affecting the Group for the remaining six months of the financial year continue to be those set out in the above section of the Annual Report. In the last six months, the outlook for the global economy has deteriorated which is expected to affect adversely the Group's performance in the second half of the year relative to the same period last year. The downturn in financial markets since the year end has adversely affected the funding position of the Group's pension schemes which is likely to affect our results.

Consolidated income statement (unaudited)

	Notes	Period ended 31 January 2009 £m	Period ended 2 February 2008 £m	Year ended 31 July 2008 £m
Continuing operations				
Revenue	2	**1,291.6**	1,087.8	2,321.2
Cost of sales		**(705.0)**	(595.9)	(1,265.5)
Gross profit		**586.6**	491.9	1,055.7
Sales and distribution costs		**(186.1)**	(151.9)	(311.8)
Administrative expenses				
– normal activities		**(225.0)**	(191.5)	(396.4)
– provision for John Crane, Inc. litigation	4	**(16.2)**	(5.7)	(49.0)
Profit on disposal of businesses	4	**0.7**	27.0	27.2
Operating profit	2	**160.0**	169.8	325.7
Interest receivable		**8.0**	5.7	2.2
Interest payable		**(28.9)**	(25.5)	(43.2)
Other financing losses	3	**(6.3)**	(5.2)	(6.1)
Other finance income – retirement benefits		**2.4**	20.6	41.7
Finance costs		**(24.8)**	(4.4)	(5.4)
Share of post-tax losses of associated companies				(1.0)
Profit before taxation		**135.2**	165.4	319.3
Comprising				
– headline profit before taxation	3	**166.6**	158.9	380.3
– exceptional items	4			
• profit on disposal of businesses		**0.7**	27.0	27.2
• provision for John Crane, Inc. litigation		**(19.9)**	(8.2)	(53.7)
• other		**5.1**	(2.4)	(13.6)
– amortisation of acquired intangible assets		**(14.7)**	(7.2)	(19.2)
– other financing losses		**(2.6)**	(2.7)	(1.7)
		135.2	165.4	319.3
Taxation	5	**(26.2)**	(32.5)	(75.0)
Profit after taxation – continuing operations		**109.0**	132.9	244.3
(Loss)/profit after taxation – discontinued operations		**(0.1)**	8.5	24.5
Profit for the period		**108.9**	141.4	268.8
Attributable to				
Smiths Group shareholders		**108.6**	141.4	268.5
Minority interests		**0.3**		0.3
		108.9	141.4	268.8
Earnings per share	7			
Basic		**28.0p**	36.5p	69.3p
Basic – continuing operations		**28.0p**	34.3p	63.0p
Diluted		**27.7p**	36.0p	68.5p
Diluted – continuing operations		**27.7p**	33.8p	62.3p
Dividends per share (declared)	6			
– interim		**10.5p**	10.5p	10.5p
– final				23.5p
		10.5p	10.5p	34.0p

Consolidated statement of recognised income and expense (unaudited)

	Notes	**Period ended 31 January 2009 £m**	Period ended 2 February 2008 £m	Year ended 31 July 2008 £m
Exchange gain		**381.6**	78.7	89.5
Fair value gain on acquisition of former associate			0.2	0.4
Taxation recognised on share-based payment				
– current				5.2
– deferred		**(3.1)**	(3.6)	(3.8)
Actuarial losses on retirement benefits		**(412.3)**	(88.2)	(254.5)
Taxation recognised on actuarial losses – deferred		**84.0**	26.9	75.5
Fair value losses				
– on cash-flow hedges		**(15.9)**	(2.2)	(0.5)
– on net investment hedges		**(166.4)**	(40.1)	(47.5)
Net expense recognised directly in equity		**(132.1)**	(28.3)	(135.7)
Profit for the period		**108.9**	141.4	268.8
Total recognised income and expense		**(23.2)**	113.1	133.1
Attributable to				
Smiths Group shareholders	15	**(25.3)**	113.1	132.8
Minority interests		**2.1**		0.3
		(23.2)	113.1	133.1

Consolidated balance sheet (unaudited)

	Notes	31 January 2009 £m	2 February 2008 £m	31 July 2008 £m
Non-current assets				
Intangible assets	10	**1,614.1**	1,100.5	1,253.2
Property, plant and equipment	11	**358.4**	283.8	296.3
Investments accounted for using the equity method		**12.5**	10.3	9.1
Financial assets – other investments		**8.3**	0.2	3.6
Retirement benefit assets	8	**55.6**	306.6	174.2
Deferred tax assets		**163.7**	135.6	96.2
Trade and other receivables		**22.1**	17.3	14.6
Financial derivatives		**9.2**	3.7	1.4
		2,243.9	1,858.0	1,848.6
Current assets				
Inventories		**476.7**	382.2	380.3
Trade and other receivables		**650.4**	496.5	565.4
Cash and cash equivalents	12	**195.4**	142.6	132.5
Financial derivatives		**14.1**	6.8	6.5
		1,336.6	1,028.1	1,084.7
Total assets		**3,580.5**	2,886.1	2,933.3
Non-current liabilities				
Financial liabilities:				
– borrowings	12	**(978.6)**	(639.9)	(720.7)
– financial derivatives		**(0.7)**	(0.2)	(0.1)
Provisions for liabilities and charges	13	**(253.2)**	(166.7)	(200.6)
Retirement benefit obligations	8	**(519.8)**	(184.9)	(184.7)
Deferred tax liabilities		**(6.7)**	(130.3)	(64.3)
Trade and other payables		**(36.2)**	(23.0)	(27.5)
		(1,795.2)	(1,145.0)	(1,197.9)
Current liabilities				
Financial liabilities:				
– borrowings	12	**(191.9)**	(177.6)	(182.4)
– financial derivatives		**(100.3)**	(29.7)	(21.5)
Provisions for liabilities and charges	13	**(86.9)**	(88.0)	(70.0)
Trade and other payables		**(435.3)**	(375.8)	(420.7)
Current tax payable		**(153.0)**	(139.1)	(122.6)
		(967.4)	(810.2)	(817.2)
Total liabilities		**(2,762.6)**	(1,955.2)	(2,015.1)
Net assets		**817.9**	930.9	918.2
Shareholders' equity				
Share capital		**145.9**	145.5	145.5
Share premium account		**306.6**	302.9	303.6
Capital redemption reserve		**5.8**	5.7	5.8
Revaluation reserve		**1.7**	1.7	1.7
Merger reserve		**234.8**	234.8	234.8
Retained earnings		**330.7**	261.7	253.7
Hedge reserve		**(212.0)**	(23.5)	(29.2)
Total shareholders' equity	15	**813.5**	928.8	915.9
Minority interest equity		**4.4**	2.1	2.3
Total equity		**817.9**	930.9	918.2

Consolidated cash-flow statement (unaudited)

	Notes	Period ended 31 January 2009 £m	Period ended 2 February 2008 £m	Year ended 31 July 2008 £m
Net cash inflow from operating activities	16	**131.7**	64.3	198.1
Cash-flows from investing activities				
Expenditure on capitalised development		**(9.7)**	(8.4)	(19.8)
Expenditure on other intangible assets		**(7.3)**	(7.4)	(16.1)
Purchases of property, plant and equipment		**(28.9)**	(25.9)	(64.2)
Disposal of property, plant and equipment		**17.3**	2.0	2.7
Investment in financial assets		**(0.1)**		(3.4)
Proceeds from sale of financial assets			1.0	1.1
Acquisition of businesses		**(39.7)**	(18.8)	(149.7)
Disposal of Aerospace		**(0.1)**	(5.1)	(6.3)
Disposals of businesses		**(0.6)**	42.2	43.2
Net cash-flow used in investing activities		**(69.1)**	(20.4)	(212.5)
Cash-flows from financing activities				
Proceeds from exercise of share options		**3.6**	17.3	21.0
Purchase of own shares			(20.7)	(20.7)
Dividends paid to equity shareholders		**(91.1)**	(90.8)	(131.4)
Cash paid to shareholders under B share scheme				(16.4)
Cash outflow from matured derivative financial instruments		**(44.9)**		
Increase in new borrowings		**198.6**	99.3	135.9
Reduction and repayment of borrowings		**(65.0)**	(47.6)	(11.0)
Net cash-flow used in financing activities		**1.2**	(42.5)	(22.6)
Net increase in cash and cash equivalents		**63.8**	1.4	(37.0)
Cash and cash equivalents at beginning of period		**(40.0)**	3.1	3.1
Exchange differences		**(1.2)**	(0.4)	(6.1)
Cash and cash equivalents at end of period		**22.6**	4.1	(40.0)
Cash and cash equivalents at end of period comprise				
– cash at bank and in hand		**182.8**	124.4	122.5
– deposits		**12.6**	18.2	10.0
– bank overdrafts		**(172.8)**	(138.5)	(172.5)
		22.6	4.1	(40.0)

Notes to the Interim report (unaudited)

1 Basis of preparation

The condensed interim financial information covers the six month period ended 31 January 2009 and has been prepared under International Financial Reporting Standards (IFRS) as adopted by the European Union, in accordance with International Accounting Standard 34 'Interim Financial Reporting' and the Disclosure and Transparency Rules of the Financial Services Authority.

The interim financial information does not constitute statutory accounts within the meaning of Section 434 of the Companies Act 2006. It should be read in conjunction with the statutory accounts for the year ended 31 July 2008, which were prepared in accordance with IFRS as adopted by the European Union and have been filed with the Registrar of Companies. The auditors' report on these statutory accounts was unqualified and did not contain a statement under Section 237(2) or (3) of the Companies Act 1985.

Accounting policies

The condensed interim financial information has been prepared on the basis of the accounting policies applicable for the year ending 31 July 2009. These accounting policies are consistent with those applied in the preparation of the financial statements for the year ended 31 July 2008, except for the adoption of 'IFRS 8: Operating Segments'. Adoption of this standard has required changes to the segment information disclosures in note 2.

2 Analyses of revenue, operating profit and assets by business segment

Analysis by operating segment

From 1 August 2008 the Group has been organised into five divisions: Smiths Detection, John Crane, Smiths Medical, Smiths Interconnect and Flex-Tek. Prior period disclosures have been amended to conform to the new structure. The "Other" division comprises the Marine Systems business which was sold on 8 November 2007 and the Specialty Engineering divisional office which was disbanded on 31 July 2008.

Smiths divisions design and manufacture the following products:

- Smiths Detection – sensors that detect and identify explosives, weapons, chemical agents, biohazards, narcotics and contraband;
- John Crane – mechanical seals, seal support systems, engineered bearings, power transmission couplings and specialist filtration systems;
- Smiths Medical – drug delivery systems, vital care products and safety devices that prevent needlestick injuries and reduce cross infection;
- Smiths Interconnect – specialised electronic and radio frequency products;
- Flex-Tek – engineered components that heat and move fluids, flexible hosing and rigid tubing.

The position and performance of each division is reported monthly to the Board of Directors. This information is prepared using the same accounting policies as the consolidated financial information except that the Group uses headline operating profit to monitor divisional results and operating assets to monitor divisional position. See note 3 for an explanation of which items are excluded from headline measures.

Intersegment sales and transfers are charged at arms length prices.

	Period ended 31 January 2009						
	Smiths Detection £m	John Crane £m	Smiths Medical £m	Smiths Interconnect £m	Flex-Tek £m	Other £m	Total £m
Revenue	**233.3**	**392.7**	**402.5**	**152.0**	**111.1**		**1,291.6**
Divisional headline operating profit	**23.8**	**65.8**	**76.8**	**23.9**	**10.8**		**201.1**
Corporate headline operating costs							**(16.0)**
Headline operating profit	**23.8**	**65.8**	**76.8**	**23.9**	**10.8**		**185.1**
Divisional exceptional operating items (note 4)		**(19.6)**	**(0.7)**		**(1.8)**		**(22.1)**
Corporate exceptional operating items (note 4)							**11.7**
Amortisation of acquired intangible assets	**(0.3)**	**(5.9)**	**(6.7)**	**(1.8)**			**(14.7)**
Operating profit	**23.5**	**40.3**	**69.4**	**22.1**	**9.0**		**160.0**
Exceptional finance costs – adjustment to discounted provision (note 4)		**(3.7)**					**(3.7)**
Net finance costs – other							**(21.1)**
Share of post tax losses of associate companies							
Profit before taxation							**135.2**

2 Analyses of revenue, operating profit and assets by business segment continued

	Smiths Detection £m	John Crane £m	Smiths Medical £m	Smiths Interconnect £m	Flex-Tek £m	Other £m	Total £m
	Period ended 2 February 2008						
Revenue	222.0	282.8	346.3	121.1	99.6	16.0	1,087.8
Divisional headline operating profit	35.0	40.7	66.8	23.3	10.5	0.8	177.1
Corporate headline operating costs							(19.0)
Headline operating profit	35.0	40.7	66.8	23.3	10.5	0.8	158.1
Divisional exceptional operating items (note 4)	(0.1)	(6.1)	(2.4)	(0.1)		27.6	18.9
Amortisation of acquired intangible assets	(0.2)	(0.6)	(5.5)	(0.9)			(7.2)
Operating profit	34.7	34.0	58.9	22.3	10.5	28.4	169.8
Exceptional finance costs – adjustment to discounted provision (note 4)		(2.5)					(2.5)
Net finance costs – other							(1.9)
Share of post tax losses of associate companies	(0.4)	0.4					
Profit before taxation							165.4

	Smiths Detection £m	John Crane £m	Smiths Medical £m	Smiths Interconnect £m	Flex-Tek £m	Other £m	Total £m
	Year ended 31 July 2008						
Revenue	509.3	625.8	703.4	260.6	206.1	16.0	2,321.2
Divisional headline operating profit	93.3	103.8	139.6	54.0	24.3	0.8	415.8
Corporate headline operating costs							(35.2)
Headline operating profit	93.3	103.8	139.6	54.0	24.3	0.8	380.6
Divisional exceptional operating items (note 4)	0.1	(51.0)	(9.4)	(1.3)	(0.1)	28.3	(33.4)
Corporate exceptional operating items (note 4)							(2.0)
Amortisation of acquired intangible assets	(0.4)	(5.5)	(11.3)	(2.0)			(19.2)
Financing losses			(0.4)		0.1		(0.3)
Operating profit	93.0	47.3	118.5	50.7	24.3	29.1	325.7
Exceptional finance costs – adjustment to discounted provision (note 4)		(4.7)					(4.7)
Net finance costs – other							(0.7)
Share of post tax losses of associate companies	(1.4)	0.4					(1.0)
Profit before taxation							319.3

The net operating assets of the five divisions are set out below:

	Smiths Detection £m	**John Crane £m**	**Smiths Medical £m**	**Smiths Interconnect £m**	**Flex-Tek £m**	**Total £m**
	Period ended 31 January 2009					
Property, plant, equipment, development projects and other intangibles	**102.3**	**100.0**	**209.2**	**30.7**	**33.3**	**475.5**
Investments in associates	**12.5**					**12.5**
Working capital assets	**331.7**	**316.4**	**308.5**	**106.5**	**73.9**	**1,137.0**
Operating assets	**446.5**	**416.4**	**517.7**	**137.2**	**107.2**	**1,625.0**
Derivatives, tax and retirement benefit assets						**242.6**
Goodwill and acquired intangibles						**1,488.9**
Corporate assets						**28.6**
Cash						**195.4**
Total assets						**3,580.5**

2 Analyses of revenue, operating profit and assets by business segment continued

	Period ended 2 February 2008					
	Smiths Detection £m	John Crane £m	Smiths Medical £m	Smiths Interconnect £m	Flex-Tek £m	Total £m
Property, plant, equipment, development projects and other intangibles	71.7	71.1	155.3	24.8	25.2	348.1
Investments in associates	10.3					10.3
Working capital assets	263.2	216.3	270.9	77.7	57.2	885.3
Operating assets	345.2	287.4	426.2	102.5	82.4	1,243.7
Derivatives, tax and retirement benefit assets						452.7
Goodwill and acquired intangibles						1,013.4
Corporate assets						33.7
Cash						142.6
Total assets						2,886.1

	Year ended 31 July 2008					
	Smiths Detection £m	John Crane £m	Smiths Medical £m	Smiths Interconnect £m	Flex-Tek £m	Total £m
Property, plant, equipment, development projects and other intangibles	85.3	82.8	158.7	24.9	24.7	376.4
Investments in associates	9.1					9.1
Working capital assets	292.5	249.3	261.2	85.7	63.3	952.0
Operating assets	386.9	332.1	419.9	110.6	88.0	1,337.5
Derivatives, tax and retirement benefit assets						278.3
Goodwill and acquired intangibles						1,151.9
Corporate assets						33.1
Cash						132.5
Total assets						2,933.3

3 Headline profit measures

The Company seeks to present a measure of underlying performance which is not impacted by exceptional items or items considered non-operational in nature. This measure of profit is described as 'headline' and is used by management to measure and monitor performance. Normal restructuring costs are charged against profits.

The following items have been excluded from the headline measure:

- exceptional items, including income and expenditure relating to John Crane, Inc. asbestos litigation;
- amortisation of intangible assets acquired in a business combination – the amortisation charge is a non-cash item, and the directors believe that it should be added back to give a clearer picture of underlying performance; and
- other financing gains and losses which are not offset by exchange gains and losses on trading transactions.

	Period ended 31 January 2009 £m	Period ended 2 February 2008 £m	Year ended 31 July 2008 £m
Other financing gains and losses			
Financing gains and losses on financial instruments	**(2.6)**	(2.7)	(1.4)
Exceptional finance costs – adjustment to discounted provision (note 4)	**(3.7)**	(2.5)	(4.7)
Other financing gains/(losses)	**(6.3)**	(5.2)	(6.1)
Financing gains and losses in operating profit			
Financing gains and losses on financial instruments			(0.3)
	(6.3)	(5.2)	(6.4)

Financing gains and losses on financial instruments in other financing gains and losses represent the exchange gains and losses on intra-group financing and the results of derivatives and other financial instruments which are used to manage these exchange exposures.

4 Exceptional items

Items which are material either because of their size or their nature, or which are non-recurring, are presented within their relevant consolidated income statement category, but highlighted separately on the face of the income statement. The separate reporting of exceptional items helps provide a better picture of the Company's underlying performance. Items which may be included within the exceptional category include:

- profits/(losses) on disposal of businesses;
- spend on the integration of significant acquisitions;
- significant goodwill or other asset impairments;
- income and expenditure relating to John Crane, Inc. asbestos litigation; and
- other particularly significant or unusual items.

An analysis of the amounts presented as exceptional items in these financial statements is given below:

	Period ended 31 January 2009 £m	Period ended 2 February 2008 £m	Year ended 31 July 2008 £m
Operating items			
Restructuring of corporate and divisional headquarters	**(8.4)**		(4.5)
Integration of acquisitions		(2.4)	(9.1)
Profit on disposal of businesses	**0.7**	27.0	27.2
Profit on disposal of property	**13.5**		
Litigation			
– Provision for John Crane, Inc. litigation (note 13)	**(16.2)**	(5.7)	(49.0)
	(10.4)	18.9	(35.4)
Financing items			
Exceptional finance costs – adjustment to discounted provision (note 13)	**(3.7)**	(2.5)	(4.7)
	(14.1)	16.4	(40.1)

On 3 June 2008 the Company announced a number of changes to its corporate centre and divisional headquarters. The total cost of this restructuring including redundancy, relocation and consolidation of manufacturing, is considered exceptional by virtue of its size. It is now expected to amount to approximately £48m over the period to 2010, of which £8.4m has been charged in the current period.

The profit on disposal of businesses represents adjustments to provisions in respect of prior year disposals.

The profit on disposal of property relates to the sale of land in Basingstoke.

The operating charge in respect of John Crane, Inc. litigation comprises £8.6m arising from movements in discounting due to changes in US interest rates (period ended 2 February 2008: £5.7m), £6.5m in respect of increased provision for adverse legal judgments and £1.1m in respect of legal fees in connection with litigation against insurers.

5 Taxation

The interim tax charge of 19.4% is calculated by applying the estimated effective headline tax rate of 24.0% for the year ending 31 July 2009 to headline profit before tax and then taking into account the tax effect of non-headline items in the interim period.

A reconciliation of total and headline tax charge – continuing is as follows:

	Period ended 31 January 2009		Period ended 2 February 2008		Year ended 31 July 2008	
	Continuing operations £m	**Tax rate**	Continuing operations £m	Tax rate	Continuing operations £m	Tax rate
Profit before taxation	**135.2**		165.4		319.3	
Taxation	**(26.2)**	**19.4%**	(32.5)	19.6%	(75.0)	23.5%
Adjustments						
Non-headline items excluded from profit before taxation (note 7)	**31.4**		(6.5)		61.0	
Taxation on non-headline items	**(13.8)**		(7.2)		(16.3)	
Headline						
Headline profit before taxation	**166.6**		158.9		380.3	
Taxation on headline profit	**(40.0)**	**24.0%**	(39.7)	25.0%	(91.3)	24.0%

6 Dividends

The following dividends were declared and paid in the period:

	Period ended 31 January 2009 £m	Period ended 2 February 2008 £m	Year ended 31 July 2008 £m
Ordinary final dividend of 23.50p for 2008 (2007: 23.50p) paid 21 November 2008	**91.1**	90.8	90.8
Ordinary interim dividend 10.50p for 2008 paid 25 April 2008			40.6
	91.1	90.8	131.4

An interim dividend of 10.5p per share (2008: 10.5p) was declared by the Board on 24 March 2009 and will be paid to shareholders on 24 April 2009. This dividend has not been included as a liability in these accounts and is payable to all shareholders on the register of Members at the close of business on 3 April 2009.

7 Earnings per share

Basic earnings per share are calculated by dividing the profit for the period attributable to equity shareholders of the Parent Company by the average number of ordinary shares in issue during the period.

	Period ended 31 January 2009 £m	Period ended 2 February 2008 £m	Year ended 31 July 2008 £m
Profit/(loss) for the period			
– continuing	**108.7**	132.9	244.0
– total	**108.6**	141.4	268.5
Average number of shares in issue during the period	**388,556,061**	387,070,514	387,446,186

Diluted earnings per share are calculated by dividing the profit attributable to equity shareholders by 391,369,103 (period ended 2 February 2008: 393,138,707; period ended 31 July 2008: 391,851,712) ordinary shares, being the average number of ordinary shares in issue during the period, adjusted by the dilutive effect of share options.

A reconciliation of basic and headline earnings per share – continuing is as follows:

	Period ended 31 January 2009		Period ended 2 February 2008		Year ended 31 July 2008	
	Continuing operations £m	**EPS (p)**	Continuing operations £m	EPS (p)	Continuing operations £m	EPS (p)
Attributable to equity shareholders of the Parent Company	**108.7**	**28.0**	132.9	34.3	244.0	63.0
Exclude						
– exceptional operating items (note 4)	**10.4**		(18.9)		35.4	
– amortisation of acquired intangible assets	**14.7**		7.2		19.2	
– financing gains–charged to administrative expenses					0.3	
–exceptional finance cost – adjustment to discounted provision (note 4)	**3.7**		2.5		4.7	
– charged to financing	**2.6**		2.7		1.4	
	31.4		(6.5)		61.0	
less tax on non-headline items	**(13.8)**		(7.2)		(16.3)	
	17.6	**4.5**	(13.7)	(3.5)	44.7	11.5
Headline	**126.3**	**32.5**	119.2	30.8	288.7	74.5
Headline EPS – diluted (p)		**32.2**		30.3		73.7

8 Post-retirement benefits

Smiths operates a number of defined benefit plans throughout the world. The principal schemes are in the United Kingdom and in the United States and are of the defined benefit type, with assets held in separate trustee-administered funds. The principal changes to the assumptions used in updating the valuations for defined benefit pension plans are as follows:

	31 January 2009		2 February 2008		31 July 2008	
	UK	**US**	UK	US	UK	US
Rate of increase in salaries	**3.8%**	**3.8%**	4.3%	3.8%	4.1%	3.8%
Rate of increase in pensions in payment	**3.3%**	**n/a**	3.3%	n/a	3.6%	n/a
Rate of increase in deferred pensions	**3.3%**	**n/a**	3.3%	n/a	3.5%	n/a
Discount rate	**6.6%**	**6.4%**	6.2%	6.3%	6.6%	6.8%
Inflation rate	**3.3%**	**3.3%**	3.3%	2.8%	3.6%	3.3%

An operating charge of £11.7m and an interest credit of £2.4m have been recognised in the six month period to 31 January 2009 in respect of defined benefit pension and post-retirement healthcare plans.

Changes in the market value of post-retirement benefit scheme assets were largely due to a decline in global stock market values.

The amounts recognised in the balance sheet were as follows:

	31 January 2009 £m	2 February 2008 £m	31 July 2008 £m
Market value of funded plan assets	**2,637.1**	3,245.7	2,959.9
Present value of funded scheme liabilities	**(2,966.0)**	(3,000.9)	(2,856.5)
Unfunded pension plans	**(59.0)**	(55.8)	(54.4)
Post-retirement healthcare	**(74.8)**	(64.9)	(58.0)
Unrecognised asset due to surplus restriction	**(1.5)**	(2.4)	(1.5)
Net retirement benefit asset	**(464.2)**	121.7	(10.5)
Retirement benefit assets	**55.6**	306.6	174.2
Retirement benefit liabilities	**(519.8)**	(184.9)	(184.7)
Net retirement benefit asset	**(464.2)**	121.7	(10.5)

9 Acquisitions

On 10 November 2008 the Medical division acquired the entire share capital of Zhejiang Zheda Medical Instrument Co. Ltd a manufacturer of medical instruments based in Hangzhou, China. The acquisition will trade as Smiths Medical Zhejiang.

The values set out below are provisional pending finalisation of the fair values attributable, and will be finalised in subsequent periods.

	Book value £m	Fair value adjustments £m	Provisional fair value £m
Non-current assets			
– Intangible assets		**19.1**	**19.1**
– Property, plant and equipment	**0.6**		**0.6**
Current assets			
– Cash and cash equivalents	**6.6**		**6.6**
– Other current assets	**2.0**	**(0.1)**	**1.9**
Current liabilities			
– Other current liabilities	**(2.1)**		**(2.1)**
Net assets acquired	**7.1**	**19.0**	**26.1**
Goodwill on current year acquisitions			**18.3**
Goodwill adjustment on prior year acquisitions			**(0.4)**
			44.0

Cash paid during the period – current year acquisitions	**43.6**
Direct costs relating to current year acquisitions	**0.8**
Deferred consideration adjustments on prior year acquisitions	**(0.4)**
Total consideration	**44.0**

The fair value adjustments in respect of intangible assets are due to the recognition of £15.2m in respect of customer relationships and £3.9m in respect of technology. The fair value adjustments are provisional, based on management's best estimates.

The goodwill is attributable to the future growth opportunities which can be generated through Smiths Medical's global sales network.

From the date of acquisition to 31 January 2009 the acquisitions contributed £2.0m to revenue, £1.2m to headline profit before taxation and £1.2m to profit before taxation. If Smiths had acquired the assets at 1 August 2008, the acquisitions would have contributed £3.9m to revenue and £2.4m to profit for the period.

10 Intangible assets

	Goodwill £m	Development costs £m	Acquired intangibles £m	Other £m	Total £m
Cost					
At 31 July 2008	1,071.8	73.5	212.8	94.3	1,452.4
Exchange adjustments	283.1	21.3	69.4	13.5	387.3
Business combinations	18.3		19.1		37.4
Adjustments to prior year business combinations	(0.4)				(0.4)
Additions		9.7		7.3	17.0
At 31 January 2009	**1,372.8**	**104.5**	**301.3**	**115.1**	**1,893.7**
Amortisation					
At 31 July 2008	82.1	18.8	50.6	47.7	199.2
Exchange adjustments	20.7	5.6	17.1	13.1	56.5
Charge for the period		5.4	14.7	3.8	23.9
At 31 January 2009	**102.8**	**29.8**	**82.4**	**64.6**	**279.6**
Net book value at 31 January 2009	**1,270.0**	**74.7**	**218.9**	**50.5**	**1,614.1**
Net book value at 2 February 2008	907.9	46.2	105.5	40.9	1,100.5
Net book value at 31 July 2008	989.7	54.7	162.2	46.6	1,253.2

11 Property, plant and equipment

	Land and buildings £m	Plant and machinery £m	Fixtures, fittings, tools and equipment £m	Total £m
Cost				
At 31 July 2008	171.4	389.9	189.2	750.5
Exchange adjustments	36.3	101.6	35.9	173.8
Reclassification		4.9	(4.9)	
Business combinations	0.4	0.2		0.6
Additions	4.4	14.7	9.8	28.9
Disposals	(2.7)	(8.1)	(4.1)	(14.9)
At 31 January 2009	**209.8**	**503.2**	**225.9**	**938.9**
Depreciation				
At 31 July 2008	60.7	258.5	135.0	454.2
Exchange adjustments	15.6	65.8	25.8	107.2
Reclassification		3.8	(3.8)	
Charge for the period	3.1	16.7	10.5	30.3
Disposals	(0.3)	(7.5)	(3.4)	(11.2)
At 31 January 2009	**79.1**	**337.3**	**164.1**	**580.5**
Net book value at 31 January 2009	**130.7**	**165.9**	**61.8**	**358.4**
Net book value at 2 February 2008	104.2	130.9	48.7	283.8
Net book value at 31 July 2008	110.7	131.4	54.2	296.3

12 Cash and borrowings

The net debt figure includes accrued interest and the fair value adjustments relating to hedge accounting.

	31 January 2009 £m	2 February 2008 £m	31 July 2008 £m
Cash and cash equivalents			
Net cash and deposits	**195.4**	142.6	132.5
Short-term borrowings			
Bank overdrafts including impact of cash pooling gross up	**(172.8)**	(138.5)	(172.5)
Bank and other loans	**(3.8)**	(4.3)	(3.8)
B shares		(18.5)	(1.7)
Interest accrual	**(15.3)**	(16.3)	(4.4)
	(191.9)	(177.6)	(182.4)
Long-term borrowings			
7.875% Sterling Eurobond 2010	**(149.7)**	(149.6)	(149.6)
7.25% Sterling Eurobond 2016	**(148.9)**	(148.8)	(148.8)
5.45% US$ Private Placement 2013	**(181.5)**	(130.7)	(127.4)
Floating Rate Revolving Credit Facility 2012 (multi-currency)	**(411.4)**	(128.0)	(210.2)
EIB Sterling R. & D. Loan 2010	**(70.0)**	(70.0)	(70.0)
Bank and other loans	**(17.1)**	(12.8)	(14.7)
	(978.6)	(639.9)	(720.7)
Borrowings	**(1,170.5)**	(817.5)	(903.1)
Net debt	**(975.1)**	(674.9)	(770.6)

Cash and overdraft balances in interest compensation cash pooling systems are reported gross on the balance sheet. This gross up increased cash and overdrafts by £118.6m at 31 January 2009 (2 February 2008: £98.8m; 31 July 2008: £100.6m).

Movements in net debt

	31 July 2008 £m	Foreign exchange gains and losses £m	Repayments of borrowings and net cash inflow £m	Drawdown of borrowings and net cash outflow £m	Capitalisation, interest accruals and unwind of capitalised fees £m	Fair value movements from interest rate hedging £m	Change in maturity analysis £m	**31 January 2009 £m**
Net cash and cash equivalents	(40.0)	(1.2)	63.8					**22.6**
Other short-term borrowings	(9.9)	(0.1)	0.3		(9.2)		(0.2)	**(19.1)**
Long-term borrowings	(720.7)	(116.6)	64.7	(198.6)	(0.2)	(7.4)	0.2	**(978.6)**
Net debt	(770.6)	(117.9)	128.8	(198.6)	(9.4)	(7.4)		**(975.1)**

The net cash inflow includes £6.6m of cash acquired with new subsidiary undertakings.

Borrowing facilities

At the balance sheet date the Group had undrawn credit facilities of £248.6m which expire in 2012. In February the Group raised additional long term debt, increasing the undrawn credit facilities, see note 18.

13 Provisions for liabilities and charges

	At 31 July 2008 £m	Exchange adjustments £m	Provisions charged £m	Provisions released £m	Discounting £m	Utilisation £m	**At 31 January 2009 £m**
Warranty provision and product liability	46.2	7.4	10.8	(3.6)		(9.0)	**51.8**
Reorganisation	9.8	2.4	2.3			(3.1)	**11.4**
Property	3.5	0.1	0.6	(0.2)		(0.2)	**3.8**
Disposal	47.4						**47.4**
Litigation	163.7	57.6	16.9	(0.9)	3.7	(15.3)	**225.7**
	270.6	67.5	30.6	(4.7)	3.7	(27.6)	**340.1**

Analysed as:

	31 January 2009 £m	2 February 2008 £m	31 July 2008 £m
Current liabilities	**86.9**	88.0	70.0
Non-current liabilities	**253.2**	166.7	200.6
	340.1	254.7	270.6

Warranty provision and product liability

Warranties over the Group's products typically cover periods of between one and three years. Provision is made for the likely cost of after-sales support based on the recent past experience of individual businesses.

Reorganisation

Reorganisation provisions include £5.4m relating to the corporate and divisional headquarters restructuring (see note 4) and £6.0m costs relating to restructuring supply arrangements following the automotive seals disposal, which are expected to be spread over the next six years.

Litigation

John Crane, Inc.

John Crane, Inc. ("JCI") is one of many co-defendants in litigation relating to products previously manufactured which contained asbestos. Until 2006, the awards, the related interest and all material defence costs were met directly by insurers. In 2007, JCI secured the commutation of certain insurance policies in respect of product liability. While substantial excess liability insurance remains in place, the exact scope of the cover is currently the subject of litigation in the US. An adverse judgment at first instance from the Circuit Court of Cook County, Illinois is currently under appeal. In the meantime JCI is meeting defence costs directly, but intends to seek appropriate contribution from insurers in due course. Provision is made in respect of the expected costs of defending known and predicted future claims and of adverse judgments in relation thereto, to the extent that such costs can be reliably estimated. No account has been taken of recoveries from insurers as their nature and timing are not yet sufficiently certain to permit recognition as an asset for these purposes.

The JCI products generally referred to in these cases are ones in which the asbestos fibres were encapsulated in such a manner that, according to tests conducted on behalf of JCI, the products were safe. JCI ceased manufacturing products containing asbestos in 1985. JCI has resisted every case in which it has been named and will continue its robust defence of all asbestos-related claims based upon this 'safe product' defence. As a result of its defence policy, JCI has been dismissed before trial from cases involving approximately 165,000 claims over the last 30 years. JCI is currently a defendant in cases involving approximately 130,000 claims. JCI has had final judgments against it, after appeals, in only 74 cases, amounting to awards of some US$78m over the 30 year period.

The assumptions made in assessing the appropriate level of provision include:

- The periods over which the costs can be reliably estimated. Projections used range between 10 and 20 years.
- The future trend of legal costs allowing for 3% cost inflation.
- The rate of future claims.
- The rate of successful resolution of claims.
- The average level of judgments.

The provision is based on past history and allows for decreasing costs based on published tables of asbestos incidence projections. In the light of the significant uncertainty associated with asbestos claims, there can be no guarantee that the assumptions used to estimate the provision will be an accurate prediction of the actual costs that may be incurred and, as a result, the provision may be subject to revision from time to time as more information becomes available.

The provision shown in the table above is a discounted pre-tax provision using discount rates, being the risk-free rate on US debt instruments for the appropriate period. The deferred tax asset related to this provision is shown within the deferred tax balance. Set out below is the gross, discounted and post-tax information relating to this provision:

	31 January 2009 £m	2 February 2008 £m	31 July 2008 £m
Gross provision	**251.8**	142.2	185.9
Discount	**(50.5)**	(39.0)	(47.0)
Discounted pre-tax provision	**201.3**	103.2	138.9
Deferred tax	**(52.3)**	(39.2)	(37.5)
Discounted post-tax provision	**149.0**	64.0	101.4

The movement in discounting on this provision comprises £8.6m relating to the change in the discount rate, which is recognised in exceptional operating items (note 4), and £3.7m relating to the unwinding of the discounting, which is recognised in exceptional finance costs (note 3). Movements in exchange rates in the period have increased the gross provision by £68.7m and the discounted pre-tax provision by £52.7m.

Other litigation

The Group has on occasion been required to take legal action to protect its patents and other business intellectual property rights against infringement, and similarly to defend itself against proceedings brought by other parties. Provision is made for the expected fees and associated costs, based on professional advice as to the likely duration of each case. Most of the balance is expected to be utilised within the next five years.

Apart from that relating to John Crane, Inc., none of the other provisions is discounted.

14 Contingent liabilities

As stated in note 13, John Crane, Inc. ("JCI") is involved in numerous law suits pending in the United States in which plaintiffs are claiming damages arising from exposure to, or use of, products containing asbestos.

Provision has been made for the cost of adverse judgments expected to occur within the next ten years. The Group anticipates that asbestos litigation will continue beyond this period; however, because of the uncertainty surrounding the outcome of litigation beyond this period, the cost of adverse judgments cannot be reliably predicted.

In addition to the JCI asbestos law suits, other companies within the Group are also involved in product liability and other litigation for which no provision is made due to the inherent uncertainty of the outcome.

15 Changes in shareholders' equity

	Period ended 31 January 2009 £m	Period ended 2 February 2008 £m	Year ended 31 July 2008 £m
At beginning of period	**915.9**	903.3	903.3
Exercises of share options	**3.6**	17.3	21.0
Purchase of own shares		(20.7)	(20.7)
Conversion and redemption of B shares	**1.7**		
Total recognised income and expenses for the period	**(25.3)**	113.1	132.8
Dividends paid to equity shareholders	**(91.1)**	(90.8)	(131.4)
Dilution of interest in associated company			(0.9)
Share-based payment	**8.7**	6.6	11.8
At end of period	**813.5**	928.8	915.9

16 Cash-flows from operating activities

	Period ended 31 January 2009 £m	Period ended 2 February 2008 £m	Year ended 31 July 2008 £m
Profit before taxation – continuing operations	**135.2**	165.4	319.3
Profit before taxation – discontinued operations	**(0.1)**	8.9	26.8
	135.1	174.3	346.1
Net interest payable	**20.9**	19.8	41.0
Financing losses/(gains)			
– charged to administrative expenses			0.3
– charged to financing	**6.3**	5.2	6.1
Share of post-tax loss from associate			1.0
Other finance income – retirement benefits	**(2.4)**	(20.6)	(41.7)
Loss/(profit) on disposal of discontinued operation	**0.1**	(8.9)	(26.8)
	160.0	169.8	326.0
Amortisation of intangible assets	**23.9**	12.5	31.0
Profit on disposal of property, plant and equipment	**(13.6)**		(0.3)
Profit on disposal of business	**(0.7)**	(27.0)	(27.2)
Depreciation of property, plant and equipment	**30.3**	24.0	53.2
Impairment of property, plant and equipment			0.3
Share-based payment expense	**8.5**	6.6	12.9
Retirement benefits	**(7.8)**	(5.9)	(37.0)
Increase in inventories	**(7.7)**	(38.9)	(21.4)
Decrease/(increase) in trade and other receivables	**34.7**	30.8	(10.0)
Decrease in trade and other payables	**(57.8)**	(60.2)	(56.9)
(Decrease)/increase in provisions	**(1.7)**	5.3	49.9
Cash generated from operations	**168.1**	117.0	320.5
Interest	**(9.5)**	(10.2)	(48.6)
Tax paid	**(26.9)**	(42.5)	(73.8)
Net cash inflow from operating activities	**131.7**	64.3	198.1

17 Related party transactions

There were no significant changes in the nature and size of related party transactions for the period to those disclosed in the Annual Report for the year ended 31 July 2008.

18 Events after the balance sheet date

On 26 February 2009 the Group completed the raising of additional long-term debt capital from the issue of US$175m of Senior Notes in the US private placement market with a fixed 9 year maturity and a fixed coupon of 7.37%.

During the week beginning 23 February 2009 the Group announced to affected employees its decision to close the US defined benefit pension plans. This decision will take effect from 30 April. From that date no further benefits will accrue under these plans.

The Group has agreed, subject to regulatory approval, to acquire Shenzhen Dowin Lightning Technologies Co., Ltd., a Chinese based manufacturer of power and signal protection devices for Smiths Interconnect. The company had sales of RMB 110m in 2008.

In March 2009 the Group decided to cease manufacturing and selling the Cozmo diabetes pump. In the year ended 31 July 2008 this activity contributed £36m to revenue. This decision will be reflected in the Smiths Medical results for the year ended 31 July 2009.