smiths
bringing technology to life

Making the world safer, healthier and more productive

Smiths Group plc
Interim Report & Accounts 2008

Smiths Group plc

Smiths Group is a global technology company. A world leader in the practical application of advanced technologies, we deliver products and services for the threat & contraband detection, medical devices, energy and communications markets worldwide. Our products and services make the world safer, healthier and more productive.

This Interim Report contains certain forward-looking statements with respect to the operations, performance and financial condition of the Group. By their nature, these statements involve uncertainty since future events and circumstances can cause results and developments to differ materially from those anticipated. The forward-looking statements reflect knowledge and information available at the date of preparation of the Interim Report and the Company undertakes no obligation to update these forward-looking statements. Nothing in this Interim Report should be construed as a profit forecast.

Financial performance

Interim results 2008

	Headline*			Statutory	
	2008 £m	2007 £m	Growth	**2008 £m**	2007 £m
Continuing activities					
Sales	**1,088**	1,021	7%	**1,088**	1,021
Operating profit	**158**	148	7%	**170**	149
Operating margin	**14.5%**	14.5%	–	**15.6%**	14.6%
Pre-tax profit	**159**	134	19%	**165**	136
Basic EPS (p)	**30.8p**	17.4p		**34.3p**	18.6p
Interim dividend (pps)	**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 (incl. impairment of assets and income and expenditure relating to John Crane litigation), amortisation of acquired intangible assets, profit/loss on disposal of businesses and financing gains/losses from currency hedging.

Business highlights

Smiths Detection: Headline operating profit up 13% to £31m

- Strong sales of checkpoint explosive detection systems to UK and US customers
- Roll-out of the joint chemical agent detector (JCAD) to the US military
- Customs and border cargo screening continues to grow

Smiths Medical: Headline operating profit flat at £61m

- 24-month performance improvement programme underway
- New product launches to be boosted with increased investment in R&D

Smiths Specialty Engineering: Headline operating profit up 10% to £66m

- John Crane reports strong demand from petrochemical customers
- Margins to be enhanced through cost control and top line growth
- Smiths Interconnect has benefited from the roll-out of 4G communications in the US

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Interim report to shareholders

Smiths Specialty Engineering and Detection divisions delivered strong sales and profit growth in the first half, offsetting a flat performance from Medical. In Medical, we have initiated a detailed performance improvement programme and its delivery is a key priority.

Since joining three months ago, I have begun a thorough review of operations and I find a business that has many strong positions in growing markets. There are significant opportunities to improve performance progressively over a two-year period. Smiths will focus on margin improvement, top line growth – especially in developing markets – and financial returns. There is also scope to grow the business through bolt-on acquisitions, such as Indufil and Fiberod. Going forward, I believe there are clear opportunities to grow Smiths and improve returns for shareholders.

Philip Bowman
Chief Executive

Statutory reporting

Statutory reporting takes account of all items excluded from headline performance. On a statutory basis, pre-tax profit from continuing operations was £165m (2007: £136m) and earnings per share were 34.3p (2007: 18.6p). The items excluded from headline performance comprise amortisation of acquired intangible assets of £7m (2007: £7m), profit on disposal of businesses of £27m (2007: £15m), acquisition integration costs of £2m (2007: £5m), financing losses of £3m (2007: £1m gain) and adjustments to the discounted provision for John Crane litigation of £8m (2007: nil). These adjustments to the provision arise from changes in US interest rates and the unwind of the discount and do not represent any change in the underlying assessment of the base provision before discount. The discontinued operations represent items in respect of the Aerospace division, sold in May 2007.

Chief Executive's review

Smiths Group has a strong set of technology-based businesses, well-positioned in growth markets and with the capacity to demonstrate resilience in an economic downturn. There are clear opportunities to improve performance progressively over a two year period. Our focus will be on enhancing margins in all the divisions through a combination of improved data, cost control and top line growth – especially in developing markets such as India and China. There are also opportunities to drive future growth through a targeted increase in R&D investment, and to focus it more tightly on high growth areas that can deliver attractive returns. We also recognise the need to invest capital in additional manufacturing capacity and that our working capital requirement is likely to grow as we exploit these growth opportunities. For example, John Crane has significant scope to build further manufacturing capacity and aftermarket service centres to meet the strong demand from the petrochemical industry. Detection is succeeding in winning new contracts but the increasing size, the different counterparties and the changing nature of those contracts has raised its working capital requirements, which is reflected in its first half performance. In order to improve data flow and speed up decision making, we are also investing in information systems, such as Enterprise Resource Planning (ERP) in a number of areas.

Looking across the Group, there are opportunities to leverage the Group's scale – particularly as the divisions have been run independently with little incentive to share best practice or back office services. The structure of the organisation will be reviewed to deliver efficiencies. The Board will also continue to consider the structure of the Group, with the objective of maximising shareholder value. In the current environment, the Board believes that there are valuable opportunities to build the business with bolt-on acquisitions – particularly in John Crane, Interconnect and Detection. Such acquisitions may bring complementary technologies, support geographic expansion into new markets or leverage existing infrastructure. We announced on 19 March 2008 agreements to acquire Indufil BV (Indufil) and Fiber Composite Company Inc. (Fiberod) which will both expand John Crane's offering. Indufil is a Dutch-based specialist in filters for the petrochemical and process industries. Fiberod is a Texas-based equipment manufacturer that will extend John Crane's upstream oilfield services offering. Completion of both acquisitions is subject to regulatory approvals.

The profile of Smiths Group offers significant opportunities for growth in resilient markets. Given the current conditions in financial markets and the scope for investment in organic growth and acquisitions, the Board has reviewed its dividend policy and intends to grow dividends consistent with increasing cover to around 2.5 times in the medium term. In pursuit of this policy, the Board has declared an unchanged interim dividend of 10.5p per share and intends to recommend a total dividend for the year of at least 34p per share. The interim dividend will be paid on 25 April to shareholders registered at the close of business on 28 March. The ex-dividend date is 26 March.

Smiths Group delivered a good first half performance with sales from continuing activities up 7% to £1,088m. On an underlying basis*, sales increased by 8% with the main contributors being Specialty Engineering and Detection; Medical was flat. Headline operating profit grew by 7%, or £10m, to £158m on both an underlying and a reported basis. Overall headline operating margin for the Group was maintained at 14.5%. Of the £10m reported increase in headline operating profit, £6m came from Specialty Engineering while Detection contributed £4m. The key drivers for the growth in headline operating profit were:

- Strong demand from the petrochemical industry for John Crane's products and services;
- Good progress at Interconnect with new contracts to support USA 4G wireless broadband and the next generation of Satellite Communications On The Move (SOTM) for the military; and
- Benefit of new contracts in Detection, particularly for checkpoint detection systems; the Joint Chemical Agent Detector (JCAD) with the US Department of Defense; and high energy x-ray screening systems.

*Underlying performance excludes the year-on-year impact of currency translation, acquisitions and disposals.

The net interest charge reduced from £30m to £20m reflecting the lower net debt position following the Aerospace sale and lower interest rates. There was a pensions financing gain of £21m (2007: £16m) relating to continuing activities, which reflected the funding position of the company's retirement benefit schemes at July 2007.

Headline pre-tax profit increased by 19% to £159m (2007: £134m). The company's tax rate on headline profit for the period was 25% (2007: 26%). Headline earnings per share were 30.8p (2007: 17.4p). The comparison in earnings per share is distorted by the share consolidation carried out in June last year; on a pro-forma basis, earnings per share grew by 20%.

Headline operating cash-flow from continuing operations totalled £99m, representing 63% of headline operating profit, and reflects investment in capital projects and increased working capital to support business growth. The working capital investment was particularly driven by the timing and nature of contracts in Detection and John Crane. Net debt has increased since July 2007 by £85m to £675m.

Outlook

Smiths Detection is expected to deliver continued growth, although the rate of increase is not likely to be as strong as in the first half. John Crane and Interconnect will continue to benefit from their strong market positions. Flex-Tek will be held back by the ongoing uncertainty in the US residential construction market. A detailed performance improvement programme for Medical is underway and its delivery is a key priority. The first six months provide a solid foundation for meeting expectations for the full year.

Operational review

Smiths Detection

			Growth	
	2008 £m	2007 £m	Reported	Underlying
Sales	**222**	182	22%	21%
Headline operating profit	**31**	27	13%	10%
Headline operating margin	**14.0%**	15.0%		
Statutory operating profit	**31**	27		

Smiths Detection has grown strongly over recent years and is a global leader in its field. It has a broad geographic reach and benefits from significant investment in technology and intellectual property. Sales grew by 22% and headline operating profit increased by 13%. This growth was driven by contract wins, particularly for airport checkpoint explosive detection systems; for JCAD, the advanced chemical point detector; and for cargo screening systems. Margins were held back in the period by the start-up costs associated with the scaling-up of our manufacturing to meet the strong customer demand for new products and by the timing and mix of the new contracts compared with last year.

In transportation, Detection won substantial contracts in the UK and US for the roll-out of new airport checkpoint explosive detection systems. The introduction of these systems helps airports speed up passenger security checks.

Demand has remained strong for advanced, high-energy cargo screening solutions in the ports and borders segment to inspect inbound and outbound shipping containers and trucks. Deliveries to the Russian authorities from the St Petersburg facility were completed in December, while a major order from US Customs and Border Protection is now being fulfilled.

In the military segment, the recently developed JCAD programme has begun to roll-out with further orders received from the US Department of Defense. The 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.

Throughout the period, preparations have been underway for the launch during the second half of a new ERP implementation. This single system will replace 14 legacy business software systems. A project team of some 50 in-house and external staff has planned the staged implementation of this system which is expected to conclude by June 2009. Investment to date has been £11m, with a total budget investment of £22m. We anticipate the project will generate efficiencies in costs and working capital of equivalent to between 1% and 2% of sales over the next three years and that these savings will be re-invested to grow the business.

Smiths leadership in the sector is maintained by ongoing product innovation developed by in-house R&D, government-funded research and through partnerships and licences. Company-funded R&D over the period increased by 11% to some £13m or 6% of sales. Smiths Detection actively seeks customer and government support for R&D, which totalled £4m in the period (2007: £3m).

Looking ahead, the sector is set for continued growth and Detection should benefit from its leadership position and the roll-out of new technologies. The order book is at record levels which supports a positive outlook in line with expectations for the full year.

Smiths Medical

	2008 £m	2007 £m	Growth Reported	Growth Underlying
Sales	**346**	347	0%	1%
Headline operating profit	**61**	60	0%	4%
Headline operating margin	**17.5%**	17.4%		
Statutory operating profit	**53**	50		

Smiths Medical focuses on three distinct therapy areas – vital care, medication delivery and safety – within the much broader medical devices market. It aims to leverage these products through a widespread and growing international sales network.

Medical reported sales and margin at broadly similar levels to last year. Growth was hampered by a weak performance in Critical Care, which faced two specific supplier problems, and adverse currency translation. In addition, Medical has continued to experience supply chain problems caused by several long-term initiatives. The simultaneous relocation of manufacturing to lower cost regions, the integration of the Medex acquisition, and the implementation of a new ERP system have all posed operational challenges. These factors combined to adversely affect relationships with major customers. A 24-month performance improvement programme has begun and a new global operations team recruited to address these issues. The implementation of a global ERP system has now restarted and this will help support the creation of an effective supply chain. The volume of unfulfilled orders with customers has been reduced in the first half but there is long way to go in rebuilding relationships with customers. Delivering this improvement programme is a key priority.

In early March, in consultation with the US Food and Drugs Administration (FDA), Medical began notifying a small proportion of people using certain ambulatory pumps, of the need for a voluntary recall of their equipment. Medical's internal processes had identified a fault in a component supplied by a third party and some 2,000 pumps will be replaced. The issue has been traced to a quality breach by a longstanding supplier who has taken appropriate actions to ensure future consistency.

A number of significant two- or three-year contracts were secured across the product portfolio during the period. These include a three-year Group Purchasing Organisation (GPO) contract with Premier Purchasing Partners, to supply PORT-A-CATH® implantable access systems to Premier's 1,700 hospitals and almost 50,000 other healthcare sites across the US. Since the period end, a new three-year agreement has also been signed with MedAssets for five categories of anaesthesia products and a contract has been secured with Amerinet, for closed suction products. In addition we have agreed a ground-breaking initiative with Cardinal Health that will see co-branding of Smiths EDGE safety needles. This agreement adds a significant new potential market for this highly successful line. Over the course of the past three months, these and other GPO contracts totalling $18m have been secured.

We have seen double digit growth, albeit from a low base, in emerging markets served via our distributors, particularly in Latin America, Russia and Saudi Arabia. Last year's investment in new infrastructure for Greater China contributed to a 31% growth in sales in that territory.

There is an ongoing focus on margin improvement through cost control and efficiencies. For example, the manufacturing rationalisation programme increased the proportion of all employees working in low-cost countries from 28% last year to 34% for this period. 61% of direct manufacturing employees are now working in Mexico, compared with 53% in the same period last year.

Total R&D investment has increased by 4%, and as a proportion of sales has increased from 3.4% to 3.6%. Looking forward, we expect this commitment to increase further. We are now focusing our investment more tightly on product areas and segments which will deliver higher growth. For example, our R&D investment in medication delivery infusion pumps is typically much higher at around 7% of sales. We plan to increase the number of new product launches by about 50% in the current year, with the aim of raising the percentage of sales from products that are less than three years old.

To support this aim, we have recently introduced an improved new product development process. Over the course of the past six months, the US Food and Drugs Administration (FDA) has issued clearance for the Saf-T Closed Blood Collection System® Devices, the dual-lumen implantable access systems (P.A.S. PORT® T2 POWER P.A.C. and PORT-A-CATH® II POWER P.A.C), the Theraheat heated humidification system and the GRIPPER® Micro Safety Needle. We have also launched this month CADD Solis™, a next generation ambulatory pump system, which features error detection software and data connectivity to hospital IT systems. A full range of EDGE safety needles has also been recently launched, together with the latest closed blood sampling product, Hemodraw, which is already winning market share in the US.

Looking ahead, the key priority for Medical is to reduce unfulfilled orders and address the issues caused by the supply chain disruption last year, while refreshing the existing customer offering through the introduction of new products. It will also focus on operating efficiencies and margin improvement while improving service to regain customers.

Specialty Engineering

	2008 £m	2007 £m	Growth Reported	Growth Underlying
John Crane				
Sales	**283**	252	12%	8%
Headline operating profit	**37**	31	18%	8%
Headline operating margin	**13.0%**	12.4%		
Statutory operating profit	**30**	43		

	2008 £m	2007 £m	Growth Reported	Growth Underlying
Specialty – Other*				
Interconnect and Flex-Tek*				
Sales	**237**	240	(2)%	7%
Headline operating profit	**30**	29	1%	7%
Headline operating margin	**12.5%**	12.2%		
Statutory operating profit	**56**	29		

*The reported figures include three months of trading for Marine Systems and six months in the comparative period.

Specialty Engineering is Smiths largest division, accounting for 48% of sales. Following the disposal of Marine Systems in November, it now operates in three areas: John Crane, Interconnect and Flex-Tek. John Crane is a market leader in sealing systems and related technologies with a strong presence in the petrochemical sector. It has opportunities to increase margins, create further efficiencies and grow through bolt-on acquisitions. Interconnect, which manufactures electronic sub-systems, performed well in its major markets of military and wireless communications. It has demonstrated the potential to improve margins, expand its low cost manufacturing and extend its geographic reach. Flex-Tek designs and manufactures heating and fluid movement components for the domestic appliance, aerospace and medical devices markets. It has been adversely affected by the US housing recession but has the opportunity to expand its non-construction business, reduce costs and rationalise its production sites.

John Crane

John Crane grew sales by 12%, headline operating profit by 18% and margins increased by 60 basis points to 13.0%. On an underlying basis, both sales and headline operating profit rose by 8%. This growth has been driven by high levels of investment by the petrochemical industry, reflecting the strong demand for oil and gas.

John Crane's largest sector is the petrochemical industry where growth is focused in two areas. First to broaden its technological footprint by adding new product lines and services that complement John Crane's market-leading positions in mechanical seals and related sectors. Second to expand into upstream energy services which leverage its strong global service and support infrastructure.

Investments reflect this two-track strategy. For example, larger and higher pressure gas seals are now being developed for customers as a result of our investment in high-pressure test equipment at a new world-leading testing facility in Slough (UK). In addition, the acquisition of Sartorius Bearing Technology in November 2007 expands John Crane's offering into the area of rotating bearings for turbo machinery. We announced on 19 March 2008 the agreement, subject to approvals, to acquire Indufil which will add specialist filtration systems to John Crane. Indufil designs and manufactures systems for rotating equipment in the oil and gas, chemical and power sectors. It serves similar customers to John Crane and has a strong aftermarket for its products which fits well with John Crane's business model. Indufil had estimated sales of £26m in the financial year ending 31 December 2007. Acquisition of CDI Energy Services in March 2007 expanded John Crane's upstream energy services capability. The CDI service and product offering extends the reliability of artificial lift systems which pump oil from depths of more than 10,000 feet. Over the course of the last six months, John Crane has already begun to benefit from CDI's service offering being leveraged across John Crane's geographic footprint. The agreement to acquire Fiberod, announced on 19 March 2008, will complement the CDI business. Fiberod is a world-leading manufacturer of fibre-glass sucker rods. These are used as a light-weight alternative to traditional metal rods for the artificial lift of oil and gas from the reservoir and will add to the upstream service we are now internationalising. In the financial year to 31 December 2007, it reported sales of £12m.

The growth in the petrochemical sector has increased original equipment orders to record levels. To help meet these requirements John Crane has invested over £4m worldwide to increase manufacturing capacity by over 20%.

The provision of maintenance and repair services to customers through the aftermarket represents two-thirds of John Crane's sales. The sale of original equipment for new production facilities creates subsequent aftermarket service opportunities that are delivered via John Crane's network of service centres, and the business has continued to build its global service base. Local service centres are now present in 52 countries worldwide. This capability significantly reduces downtime for customers by avoiding seals being shipped over long distances for repair. Current developments are focused on key growth markets. For example, in Saudi Arabia we are building a new service, sales and manufacturing facility in Dammam. This new facility has an upgraded gas seals test capability and adds significant service capacity in an area where extensive investment is planned by the petrochemical industry over the next 10 years.

Another growth opportunity is China where construction began in August 2007 on a new facility in Tianjin. This will support further growth as well as enable the relocation and consolidation of two existing businesses to a single site. This new facility will accommodate sophisticated manufacturing, including assembly testing and enhanced product development, as well as providing a sales and service centre for the domestic Chinese market.

Looking ahead, sustained growth in demand for oil and gas is likely to continue to drive investment by petrochemical companies and original equipment manufacturers into new technology and facilities. John Crane is building on its strong position to support this demand in the future.

Specialty – Other

Specialty – Other comprises Interconnect and Flex-Tek. Interconnect recorded double-digit growth in sales and profit, while at Flex-Tek a good performance in sales of components and services for commercial and military aircraft helped offset the impact of the substantial decline in the US residential construction market. A third business element, Marine, was disposed of after three months of trading in this financial year. The reported results for Specialty – Other include the three months of trading in the current period and the whole six months in the prior period. The underlying performance adjusts for the impact of this disposal and currency translation. Sales for Specialty– Other fell by 2% and headline operating profit rose by 1%. Operating margin increased by 30 basis points to 12.5%.

Interconnect

Smiths Interconnect delivered strong sales and profit growth with increased margin. Performance in the period was enhanced by sales of lightning and surge protection solutions supplied to major US 4G wireless broadband providers for mobile internet access. A development contract was secured for Interconnect's next generation Satellite Communications On The Move (SOTM) antenna systems, which deliver effective mobile communications for the armed forces in areas of conflict.

Interconnect has seen good progress from a number of important military programmes that will continue for some years. These include three-frequency band data link (MDAS) to support multiple unmanned aircraft systems; the Multi-Function Radio Frequency System (MFRFS) that can detect and track a full spectrum of threats to current and future ground vehicles; and the Warfighter Information Network-Tactical (WIN-T) the US army system for reliable, secure and seamless high bandwidth communications.

Interconnect is seeking opportunities, where appropriate, to bring its manufacturing together in lower-cost environments and progress on this continued in the half year. Manufacturing in Mexico and Tunisia has risen significantly while manufacturing in China and Costa Rica continues to play an important role.

There are good opportunities for Interconnect to grow – particularly in Asia Pacific – and it operates in an industry with scope for bolt-on acquisitions. Looking ahead, Interconnect's markets remain robust and good opportunities are expected over the next six months.

Flex-Tek

Flex-Tek's sales remained flat while profit declined. Sales of fluid distribution components and services for commercial and military aircraft helped to offset the impact of the decline in the US residential construction market. Illustrating this, Flex-Tek announced on 19 March 2008 an $18m contract for the provision of flexible and rigid fuel and hydraulic hoses on the Boeing 787 Dreamliner.

During the period, Flex-Tek completed the reorganisation of its tubular systems business with a relocation and consolidation of manufacturing in Tennessee. This project will cut costs and improve customer service.

Flex-Tek is facing continued uncertainty in the US residential construction market. The challenge is to reduce costs and position this business to deliver future value when its main markets improve.

Financial review

Cash-flow and net debt

Operating cash-flow from continuing operations (before the cash impact of exceptional items and special pension payments and after capital expenditure) totalled £99m, representing 63% of headline operating profit, and reflects investment in capital projects and increased working capital to support business growth. The working capital investment was particularly driven by the timing and nature of contracts in Smiths Detection and John Crane.

On a statutory basis, net cash inflow from continuing operations was £64m. Cash expenditure on exceptional items was £14m. The company made special pension contributions of £7m. Free cash-flow from continuing operations (after interest and tax but before acquisitions and dividends) was £26m.

Net debt at the period end was £675m, up from £590m at the start of the fiscal year. The net debt at both period ends is stated after taking account of accrued interest and the fair value of swapped debt, in line with the requirements of IFRS. During the period, the company invested £19m on acquisitions and received £37m from disposals.

Acquisitions and disposals

Smiths made a number of acquisitions and disposals in the period to improve the business mix of its continuing activities. In November, Sartorius Bearing Technology, a leading provider of high performance rotating equipment for the oil and gas industry, was acquired for €20m. In November, Smiths sold its Marine Systems business for £44m, after a working capital adjustment. In December, Smiths acquired the majority ownership of the John Crane business in Japan for a consideration of £4m, increasing its ownership share from 49% to 70%. After the period end, the Heating Element Division of Fast Heat was acquired for $18m: it manufactures a wide range of specialty heating elements for HVAC, industrial and medical applications. We announced on 19 March 2008 that agreements have been signed to acquire Indufil BV and Fiber Composite Company Inc., both of which are subject to approvals.

Research and development

Company-funded R&D in this period was £34m (2007: £34m). This represents an average across the three divisions of 3% of sales, with Medical and Detection above that level and Specialty Engineering below it. Of the total, £26m was charged against profit and the balance capitalised. The company is currently carrying £46m of capitalised development costs, which are amortised over timescales of typically 3–5 years.

Productivity

The company made further efficiency gains in this period, with higher input costs, including raw materials and payroll costs, more than offset by restructuring, pricing and the benefits of establishing production by a growing number of Smiths businesses in low-cost countries, including Mexico, India and China. Average employment in the continuing activities was 22,000 (2007: 22,000) during the half year. The US remains the company's largest market, accounting for 46% of sales by origin and 58% of headline operating profit.

In all three divisions, the Group has ongoing projects focused on business systems efficiency. ERP projects are underway in Detection, Medical and John Crane. The successful completion of these new ERP systems over the coming years will help to enhance margins and improve service quality.

Retirement benefits

The balance sheet continues to reflect a net surplus in retirement benefit plans despite the economic turbulence in the global financial sectors. The funded schemes show a surplus of £242m, compared to £297m at July 2007.

Risks and uncertainties

The principal risks and uncertainties affecting the business activities of the Group remain those identified on pages 17 and 18 of the Report and Accounts for the year ended 31 July 2007, a copy of which is available at the Company's website at www.smiths.com. In the view of the Board, these properly reflect the uncertainties in respect of the remaining six months of the year.

B share repurchase

The Company expects to advise holders of B shares shortly of arrangements for their shares to be repurchased at 365p per share.

Statement of directors' responsibilities

The Interim Report and Accounts is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the Interim Report and Accounts in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority. The Disclosure and Transparency Rules ('DTR') require that the accounting policies and presentation applied to the half-yearly figures must be consistent with those applied in the latest published annual accounts, except where the accounting policies and presentation are to be changed in the subsequent annual accounts, in which case the new accounting policies and presentation should be followed, and the changes and the reasons for the changes should be disclosed in the Interim Report and Accounts, unless the United Kingdom Financial Services Authority agrees otherwise.

The directors confirm that this condensed set of financial statements has been prepared in accordance with International Accounting Standard 34, 'Interim Financial Reporting' as adopted by the European Union, and that the interim management report herein includes a fair review of the information required by DTR 4.2.7 and DTR 4.2.8.

The directors of Smiths Group plc are listed in the Smiths Group plc Annual Report and Accounts for the period ended 31 July 2007, with the exception of the following changes that took place in the six months ended 2 February 2008:

- Mr K O Butler-Wheelhouse retired on 10 December 2007
- Mr P Bowman was appointed on 10 December 2007

By Order of the Board

John Langston
Finance Director

19 March 2008

Independent review report to Smiths Group plc

Introduction
We have been engaged by the company to review the condensed set of financial statements in the Interim Report and Accounts for the six months ended 2 February 2008, which comprises the consolidated income statement, consolidated balance sheet, consolidated statement of recognised income and expense, consolidated cash flow statement and related notes. We have read the other information contained in the Interim Report and Accounts and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

Directors' responsibilities
The Interim Report and Accounts is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the Interim Report and Accounts in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

As disclosed in note 1, the annual financial statements of the group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this Interim Report and Accounts has been prepared in accordance with International Accounting Standard 34, 'Interim Financial Reporting', as adopted by the European Union.

Our responsibility
Our responsibility is to express to the company a conclusion on the condensed set of financial statements in the Interim Report and Accounts based on our review. This report, including the conclusion, has been prepared for and only for the company for the purpose of the Disclosure and Transparency Rules of the Financial Services Authority and for no other purpose. We do not, in producing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of review
We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion
Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the Interim Report and Accounts for the six months ended 2 February 2008 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

PricewaterhouseCoopers LLP
Chartered Accountants
London

19 March 2008

Notes
(a) The maintenance and integrity of the Smiths Group plc website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the interim report since it was initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of financial information may differ from legislation in other jurisdictions.

Consolidated income statement (unaudited)

	Notes	Period ended 2 February 2008 £m	Period ended 3 February 2007 £m	Period ended 31 July 2007 £m
Continuing operations				
Revenue	2	**1,087.8**	1,021.2	2,160.9
Cost of sales		**(595.9)**	(544.0)	(1,159.1)
Gross profit		**491.9**	477.2	1,001.8
Sales and distribution costs		**(151.9)**	(155.7)	(311.5)
Administrative expenses				
– normal activities		**(191.5)**	(185.2)	(394.2)
– provision for John Crane, Inc. litigation	4	**(5.7)**	(44.3)	(100.7)
Other operating income			42.9	66.9
Profit/(loss) on disposal of businesses		**27.0**	14.5	(5.2)
Operating profit	2	**169.8**	149.4	257.1
Interest receivable		**5.7**	3.3	21.4
Interest payable		**(25.5)**	(32.8)	(57.8)
Other financing gains/(losses)	3	**(5.2)**	1.1	2.1
Other finance income – retirement benefits		**20.6**	16.0	33.7
Finance costs		**(4.4)**	(12.4)	(0.6)
Share of post-tax loss of associates			(0.7)	(0.5)
Profit before taxation		**165.4**	136.3	256.0
Comprising				
– headline profit before taxation	3	**158.9**	134.0	344.4
– exceptional items	4			
• profit/(loss) on disposal of businesses		**27.0**	14.5	(5.2)
• commutation of insurance policies			42.9	42.9
• provision for John Crane, Inc. litigation	4	**(8.2)**	(44.3)	(100.7)
• other		**(2.4)**	(5.0)	(35.2)
– amortisation of acquired intangible assets		**(7.2)**	(7.0)	(14.8)
– other financing gains/(losses)	3	**(2.7)**	1.2	0.6
– profit on sale of financial asset				24.0
		165.4	136.3	256.0
Taxation		**(32.5)**	(30.4)	(53.1)
Profit after taxation – continuing operations		**132.9**	105.9	202.9
Profit after taxation – discontinued operations	6	**8.5**	43.1	1,525.2
Profit for the period		**141.4**	149.0	1,728.1
Profit for the period attributable to equity shareholders of the Parent Company		**141.4**	149.0	1,728.1
Earnings per share	8			
Basic		**36.5p**	26.2p	314.7p
Basic – continuing operations		**34.3p**	18.6p	36.9p
Diluted		**36.0p**	26.1p	310.3p
Diluted – continuing operations		**33.8p**	18.5p	36.4p
Dividends per share (declared)				
– interim		**10.5p**	10.5p	10.5p
– final				23.5p
		10.5p	10.5p	34.0p

Consolidated statement of recognised income and expense (unaudited)

	Period ended 2 February 2008 £m	Period ended 3 February 2007 £m	Period ended 31 July 2007 £m
Exchange gain/(loss)	**78.7**	(51.1)	(72.2)
Cumulative exchange losses recycled on disposals			49.2
Fair value gain on acquisition of former associate	**0.2**		
Taxation recognised on exchange losses			
– current			2.4
Taxation recognised on share-based payment			
– current			10.3
– deferred	**(3.6)**	2.7	(9.4)
Actuarial (losses)/gains on retirement benefits	**(88.2)**	17.5	70.3
Taxation recognised on actuarial (losses)/gains – deferred	**26.9**	(5.8)	(30.1)
Fair value (losses)/gains:			
– on cash-flow hedges	**(2.2)**	7.2	(11.9)
– on net investment hedges	**(40.1)**	13.4	8.2
Net (cost)/income recognised directly in equity	**(28.3)**	(16.1)	16.8
Profit for the period	**141.4**	149.0	1,728.1
Total recognised income and expense for the period attributable to equity shareholders of Smiths Group plc	**113.1**	132.9	1,744.9

Consolidated balance sheet (unaudited)

	Notes	**2 February 2008 £m**	3 February 2007 £m	31 July 2007 £m
Non-current assets				
Intangible assets	12	**1,100.5**	1,018.9	1,021.3
Property, plant and equipment	13	**283.8**	289.2	260.9
Investments accounted for using the equity method		**10.3**	12.8	12.0
Financial assets – other investments		**0.2**	0.7	0.7
Retirement benefit assets	9	**306.6**	179.2	333.7
Deferred tax assets		**135.6**	94.8	94.0
Trade and other receivables		**17.3**	10.1	14.7
Financial derivatives		**3.7**	0.1	0.4
		1,858.0	1,605.8	1,737.7
Current assets				
Inventories		**382.2**	319.8	319.7
Trade and other receivables		**496.5**	465.4	489.8
Cash and cash equivalents	14	**142.6**	274.1	186.2
Financial derivatives		**6.8**	16.4	13.5
		1,028.1	1,075.7	1,009.2
Assets of businesses held for sale			1,316.6	31.3
Total assets		**2,886.1**	3,998.1	2,778.2
Non-current liabilities				
Financial liabilities:				
– borrowings	14	**(639.9)**	(897.6)	(567.1)
– financial derivatives		**(0.2)**	(3.3)	(2.5)
Provisions for liabilities and charges	15	**(166.7)**	(57.2)	(143.4)
Retirement benefit obligations	9	**(184.9)**	(173.1)	(150.1)
Deferred tax liabilities		**(130.3)**	(48.7)	(118.0)
Trade and other payables		**(23.0)**	(34.1)	(22.5)
		(1,145.0)	(1,214.0)	(1,003.6)
Current liabilities				
Financial liabilities:				
– borrowings	14	**(177.6)**	(328.3)	(212.1)
– financial derivatives		**(29.7)**	(12.3)	(2.8)
Provisions for liabilities and charges	15	**(88.0)**	(60.1)	(90.1)
Trade and other payables		**(375.8)**	(385.5)	(412.6)
Current tax payable		**(139.1)**	(130.9)	(137.5)
		(810.2)	(917.1)	(855.1)
Liabilities of businesses held for sale			(449.3)	(16.2)
Total liabilities		**(1,955.2)**	(2,580.4)	(1,874.9)
Net assets		**930.9**	1,417.7	903.3
Shareholders' equity				
Share capital		**145.5**	143.3	144.6
Share premium account		**302.9**	265.6	289.0
Capital redemption reserve		**5.7**		5.7
Revaluation reserve		**1.7**	1.7	1.7
Merger reserve		**234.8**	234.8	234.8
Retained earnings		**261.7**	725.2	208.9
Hedge reserve		**(23.5)**	47.1	18.6
Total shareholders' equity	17	**928.8**	1,417.7	903.3
Minority interest equity		**2.1**		
Total equity		**930.9**	1,417.7	903.3

Consolidated cash-flow statement (unaudited)

	Notes	**Period ended 2 February 2008 £m**	Period ended 3 February 2007 £m	Period ended 31 July 2007 £m
Net cash inflow from operating activities	18	**64.3**	190.5	246.0
Cash-flows from investing activities				
Expenditure on capitalised development		**(8.4)**	(52.8)	(87.4)
Expenditure on other intangible assets		**(7.4)**	(16.6)	(29.6)
Purchases of property, plant and equipment		**(25.9)**	(51.1)	(118.3)
Disposal of property, plant and equipment		**2.0**	1.4	25.6
Proceeds from sale of/(additions to) financial assets		**1.0**	(0.3)	15.0
Acquisition of businesses		**(18.8)**	(14.7)	(34.9)
Disposal of Aerospace		**(5.1)**		2,495.0
Disposals of businesses		**42.2**	11.2	9.1
Net cash-flow used in investing activities		**(20.4)**	(122.9)	2,274.5
Cash-flows from financing activities				
Proceeds from issue of ordinary share capital		**17.3**	22.3	77.7
Purchase of own shares		**(20.7)**		(7.0)
Dividends paid to equity shareholders		**(90.8)**	(122.3)	(182.4)
Cash paid to shareholders under B share scheme				(2,090.9)
Increase in new borrowings		**99.3**		19.0
Reduction and repayment of borrowings		**(47.6)**	56.8	(284.7)
Net cash-flow used in financing activities		**(42.5)**	(43.2)	(2,468.3)
Net increase in cash and cash equivalents		**1.4**	24.4	52.2
Cash and cash equivalents at beginning of period		**3.1**	(51.1)	(51.1)
Exchange differences		**(0.4)**	2.6	2.0
Cash and cash equivalents at end of period		**4.1**	(24.1)	3.1
Cash and cash equivalents at end of period comprise:				
– cash at bank and in hand		**124.4**	268.4	148.5
– deposits		**18.2**	8.0	40.8
– bank overdrafts		**(138.5)**	(300.5)	(186.2)
		4.1	(24.1)	3.1
Included in cash and cash equivalents per the balance sheet		**142.6**	274.1	186.2
Included in overdrafts per the balance sheet		**(138.5)**	(299.7)	(186.2)
Included in the assets of the disposal group			1.5	3.1
		4.1	(24.1)	3.1

Notes to the Interim Report & Accounts (unaudited)

1 Basis of preparation

The condensed interim financial information covers the six month period ended 2 February 2008 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. It is unaudited but has been reviewed by the auditors and their report is attached to this document.

The interim financial information does not constitute statutory accounts as defined in Section 240 of the Companies Act 1985. It should be read in conjunction with the statutory accounts for the period ended 31 July 2007, 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 2008. These accounting policies are consistent with those applied in the preparation of the financial statements for the period ended 31 July 2007, except for the adoption of IFRS 7: 'Financial Instruments: Disclosures'.

The adoption of this standard has no impact on the consolidated financial results or position of the Group for the six months ended 2 February 2008.

Recent accounting developments

The following standards, amendments and interpretations have been issued by the International Accounting Standards Board or by the IFRIC, but have not yet been adopted. Subject to endorsement by the European Union, these will be adopted in future periods. IFRS 8 has been endorsed, and the other standards, amendments and interpretations are being considered for endorsement.

- IFRS 8 'Operating segments'
- IAS 23 'Borrowing costs' (revised)
- IFRIC 12 'Service concession arrangements'
- IFRIC 13 'Customer loyalty programmes'
- IFRIC 14 'The limit of a defined benefit asset, minimum funding requirements and their interaction'
- IAS 27 'Consolidated and separate financial statements' (revised)
- IFRS 3 'Business combinations' (revised)

The adoption of IFRS 3 (revised) will significantly change the recognition of goodwill, acquisition costs and contingent consideration relating to acquisitions. However, it applies only to acquisitions made after it has been adopted, which will minimise any restatements required. IAS 27 (revised) requires different accounting treatment for minority interests but it is not expected to affect the Group's financial results or position materially. Smiths will determine an appropriate implementation date after these standards have been adopted by the European Union.

For the other standards and interpretations, there has been no change to the expected impact on future annual reports and accounts from those disclosed in the Annual Report and Accounts for the period ended 31 July 2007.

Date of approval

The interim financial statements were approved by the directors on 19 March 2008.

2 Analyses of revenue and operating profit by business segment

For management purposes, the Group is organised into three business segments – Detection, Medical and Specialty Engineering. These business segments are the basis on which the Group reports its primary segment information.

For reporting purposes, Specialty Engineering is analysed into two segments: John Crane and Specialty – Other.

					Period ended 2 February 2008
			Specialty Engineering		
	Detection £m	**Medical £m**	**John Crane £m**	**Specialty – Other £m**	**Total £m**
Revenue	**222.0**	**346.3**	**282.8**	**236.7**	**1,087.8**
Headline operating profit	**31.0**	**60.6**	**36.8**	**29.7**	**158.1**
Exceptional operating items (note 4)	**(0.1)**	**(2.4)**	**(6.1)**	**27.5**	**18.9**
Amortisation of acquired intangible assets	**(0.2)**	**(5.5)**	**(0.6)**	**(0.9)**	**(7.2)**
Operating profit	**30.7**	**52.7**	**30.1**	**56.3**	**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)/profits of associated companies	**(0.4)**		**0.4**		
Profit before taxation					**165.4**
Taxation					**(32.5)**
Profit for the period – continuing operations					**132.9**

					Period ended 3 February 2007
			Specialty Engineering		
	Detection £m	Medical £m	John Crane £m	Specialty – Other £m	Total £m
Revenue	182.0	347.0	251.9	240.3	1,021.2
Headline operating profit	27.3	60.4	31.2	29.3	148.2
Exceptional operating items (note 4)	0.2	(5.1)	12.3	0.7	8.1
Amortisation of acquired intangible assets	(0.2)	(5.4)	(0.2)	(1.2)	(7.0)
Financing losses	(0.3)	0.4	0.1	(0.1)	0.1
Operating profit	27.0	50.3	43.4	28.7	149.4
Net finance costs					(12.4)
Share of post-tax (losses)/profits of associated companies	(1.0)		0.3		(0.7)
Profit before taxation					136.3
Taxation					(30.4)
Profit for the period – continuing operations					105.9

					Period ended 31 July 2007
			Specialty Engineering		
	Detection £m	Medical £m	John Crane £m	Specialty – Other £m	Total £m
Revenue	437.5	690.6	532.4	500.4	2,160.9
Headline operating profit	78.6	127.3	75.3	66.4	347.6
Exceptional operating items (note 4)	(13.0)	(9.6)	(73.2)	(2.4)	(98.2)
Amortisation of acquired intangible assets	(0.4)	(11.5)	(0.6)	(2.3)	(14.8)
Financing losses	(0.1)	(0.2)	(0.2)	(1.0)	(1.5)
	65.1	106.0	1.3	60.7	233.1
Profit on sale of financial assets					24.0
Operating profit					257.1
Net finance costs					(0.6)
Share of post-tax (losses)/profits of associated companies	(1.1)		0.6		(0.5)
Profit before taxation					256.0
Taxation					(53.1)
Profit for the period – continuing operations					202.9

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.

	Period ended 2 February 2008 £m	Period ended 3 February 2007 £m	Period ended 31 July 2007 £m
Other financing gains and losses			
Financing gains and losses on financial instruments	**(2.7)**	1.1	2.1
Exceptional finance costs – adjustment to discounted provision (note 4)	**(2.5)**		
Other financing gains/(losses)	**(5.2)**	1.1	2.1
Financing gains and losses in operating profit			
Financing gains and losses on financial instruments		0.1	(1.5)
	(5.2)	1.2	0.6

Financing gains and losses on financial instruments represent the results of derivatives and other financial instruments which do not fall to be hedge accounted under IAS 39. These items are included either within operating profit or profit before taxation depending on the nature of the transaction. The application of IFRS accounting principles makes this item potentially volatile, and it is therefore excluded to give a clearer picture of the underlying performance.

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 2 February 2008 £m	Period ended 3 February 2007 £m	Period ended 31 July 2007 £m
Operating items			
Integration of acquisitions	**(2.4)**	(5.0)	(9.0)
Impairment of goodwill and other assets			(10.3)
Profit/(loss) on disposal of businesses (note 11)	**27.0**	14.5	(5.2)
Aborted transaction costs			(12.7)
Litigation			
– Commutation of insurance policies (note 15)		42.9	42.9
– Provision for John Crane, Inc. litigation (note 15)	**(5.7)**	(44.3)	(100.7)
– Provision for other litigation (note 15)			(8.6)
– Class action settlement			5.4
	18.9	8.1	(98.2)
Financing items			
Exceptional finance costs – adjustment to discounted provision (note 15)	**(2.5)**		
	16.4	8.1	(98.2)

Restructuring costs in connection with the integration of Medex amounting to £2.4m (period ended 3 February 2007 £5.0m; period ended 31 July 2007 £9.0m) were incurred in the period. The charge of £5.7m in respect of John Crane, Inc. asbestos litigation arises from changes in US interest rates (see note 15) and does not represent a change in the assessment of the gross cash flows expected to be incurred before discount.

5 Taxation

The interim tax charge of 19.6% (six months ended 3 February 2007: 22.3%) is calculated by applying the estimated effective headline tax rate of 25% for the year ending 31 July 2008 (six months ended 3 February 2007: 26%) 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 2 February 2008		Period ended 3 February 2007		Period ended 31 July 2007	
	Continuing operations £m	**Tax rate**	Continuing operations £m	Tax rate	Continuing operations £m	Tax rate
Profit before taxation	**165.4**		136.3		256.0	
Taxation	**(32.5)**	**19.6%**	(30.4)	22.3%	(53.1)	20.7%
Adjustments						
Non-headline items excluded from profit before taxation (note 8)	**(6.5)**		(2.3)		88.4	
Taxation on non-headline items	**(7.2)**		(4.4)		(33.3)	
Headline						
Headline profit before taxation	**158.9**		134.0		344.4	
Taxation on headline profit	**(39.7)**	**25.0%**	(34.8)	26.0%	(86.4)	25.1%

6 Discontinued operations

Discontinued operations disclosed in the income statement consist of the Aerospace operations, which were sold to General Electric Company on 5 May 2007. The Aerospace operations comprised the Aerospace business segment previously reported and the microwave company previously reported in Specialty – Other.

During the period the proceeds of sale of the Aerospace business were adjusted following ongoing negotiations with the purchaser after completion, as laid out in the sale agreement. As a result, further proceeds were received and adjustments made to net assets. The resultant profit of £5.6m has been recorded within discontinued operations as a profit on disposal.

In addition, ongoing negotiations in respect of the transfer of Aerospace active pensioners have led to a reduction in the disposal provision (see note 15) of £1.3m; £2.0m of the pensions financing credit relates to the expected transfer and all these amounts are treated within discontinued operations as profit on disposal of Aerospace. A tax charge of £0.4m has been recorded.

Net cash outflows from investing activities of £5.1m are included within the consolidated cash flow statement.

The assets and liabilities of businesses held for sale on the 3 February 2007 balance sheet relate to the Aerospace operation.

7 Dividends

The following dividends were declared and paid in the period:

	Period ended 2 February 2008 £m	Period ended 3 February 2007 £m	Period ended 31 July 2007 £m
Ordinary final dividend of 23.50p for 2007 (2006: 21.50p) paid 23 November 2007	**90.8**	122.3	122.3
Ordinary interim dividend 10.50p for 2007 paid 27 April 2007			60.1
	90.8	122.3	182.4

An interim dividend of 10.5p per share (2007: 10.5p) was declared by the Board on 19 March 2008 and will be paid to shareholders on 25 April 2008. 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 28 March 2008.

8 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 2 February 2008 £m	Period ended 3 February 2007 £m	Period ended 31 July 2007 £m
Profit/(loss) for the period			
– continuing	**132.9**	105.9	202.9
– total	**141.4**	149.0	1,728.1
Average number of shares in issue during the period	**387,070,514**	569,049,918	549,153,733

Diluted earnings per share are calculated by dividing the profit attributable to equity shareholders by 393,138,707 (period ended 3 February 2007: 571,928,823; period ended 31 July 2007: 556,934,401) 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 2 February 2008		Period ended 3 February 2007		Period ended 31 July 2007	
		Continuing operations £m	**EPS (p)**	Continuing operations £m	EPS (p)	Continuing operations £m	EPS (p)
Attributable to equity shareholders of the Parent Company		**132.9**	**34.3**	105.9	18.6	202.9	36.9
Exclude							
– exceptional operating items (note 4)		**(18.9)**		(8.1)		98.2	
– profit on sale of financial asset						(24.0)	
– amortisation of acquired intangible assets		**7.2**		7.0		14.8	
– financing gains	– charged to administrative expenses			(0.1)		1.5	
	– exceptional finance cost – adjustment to discounted provision (note 4)	**2.5**					
	– charged to financing	**2.7**		(1.1)		(2.1)	
		(6.5)		(2.3)		88.4	
– less tax		**(7.2)**		(4.4)		(33.3)	
		(13.7)	**(3.5)**	(6.7)	(1.2)	55.1	10.1
Headline		**119.2**	**30.8**	99.2	17.4	258.0	47.0
Headline EPS – diluted (p)			**30.3**		17.3		46.3

9 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:

	2 February 2008		31 July 2007	
	UK	**US**	UK	US
Rate of increase in salaries	**4.3%**	**3.8%**	4.1%	3.8%
Rate of increase in pensions in payment	**3.3%**	**n/a**	3.1%	n/a
Rate of increase in deferred pensions	**3.3%**	**n/a**	3.1%	n/a
Discount rate	**6.2%**	**6.3%**	5.8%	6.4%
Inflation rate	**3.3%**	**2.8%**	3.1%	2.8%

An operating charge of £10.7m and an interest credit of £22.6m have been recognised in the six months to 2 February 2008 in respect of defined benefit pension and post-retirement healthcare plans. The operating charge includes a curtailment gain of £1.1m relating to the disposal of Marine Systems and is reported as a profit on business disposal. The interest credit includes £2.0m relating to the disposal of the Aerospace operations and is reported within discontinued operations.

Special contributions of £4.1m in relation to the sale of Aerospace have been made in the period.

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

9 Post-retirement benefits continued

The amounts recognised in the balance sheet were as follows:

	2 February 2008 £m	3 February 2007 £m	31 July 2007 £m
Market value of funded plan assets	**3,245.7**	3,221.4	3,318.9
Present value of funded scheme liabilities	**(3,000.9)**	(3,033.9)	(3,019.2)
Unfunded pension plans	**(55.8)**	(43.7)	(51.5)
Post-retirement healthcare	**(64.9)**	(60.8)	(62.2)
Unrecognised asset due to surplus restriction	**(2.4)**	(76.9)	(2.4)
Net retirement benefit asset	**121.7**	6.1	183.6
Retirement benefit assets	**306.6**	179.2	333.7
Retirement benefit liabilities	**(184.9)**	(173.1)	(150.1)
Net retirement benefit asset	**121.7**	6.1	183.6

The unrecognised asset due to surplus restriction shown at 3 February 2007 was based on an estimate of the impact of the Aerospace disposal on the Smiths pension plans. At 31 July 2007 the unrecognised asset was reduced to £2.4m following a detailed actuarial review.

10 Acquisitions

Acquisitions during the period include the acquisition of the entire issued share capital of Sartorius Bearing Technology on 15 October 2007 and acquisition of a controlling interest over an associate on 21 December 2007. Both companies have been included in the Specialty – John Crane business segment.

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	**0.5**	**4.8**	**5.3**
– Property, plant and equipment	**2.9**		**2.9**
Current assets			
– Cash and cash equivalents	**3.1**		**3.1**
– Other current assets	**13.3**	**0.4**	**13.7**
Current liabilities			
– Overdrafts	**(1.1)**		**(1.1)**
– Other current liabilities	**(8.1)**	**(1.4)**	**(9.5)**
Minority interest and assets accounted for using the equity method		**(5.0)**	**(5.0)**
Net assets acquired	**10.6**	**(1.2)**	**9.4**
Asset revaluation surplus			**(0.2)**
Goodwill			**11.4**
Consideration			**20.6**
– cash paid during the period – current year acquisitions			**19.4**
– direct costs relating to current year acquisitions			**0.7**
– deferred consideration paid in respect of prior year acquisitions			**0.5**
Total consideration satisfied by cash			**20.6**

The fair value adjustments in respect of intangible assets are due to the recognition of £4.8m in respect of customer relationships. The adjustments to current assets and liabilities relate to valuation adjustments and are provisional, based on management's best estimates.

The goodwill is attributable to synergies and intangibles which do not qualify for separate recognition. Included within goodwill above is £0.5m in respect of an additional payment relating to a prior year acquisition.

The minority interest and assets accounted for using the equity method adjustment represents assets not acquired by Smiths Group plc when a controlling interest in the associate was acquired. The asset revaluation surplus represents fair value gains and losses on the associate's net assets.

From the date of acquisition to 2 February 2008 the acquisitions contributed £4.0m to revenue, £0.5m to headline profit before taxation and £0.9m to profit before taxation. If Smiths had acquired the assets at 1 August 2007, the acquisitions would have contributed £16.4m to revenue and £1.8m to profit for the period.

11 Disposals

On 8 November 2007 the Marine Systems business was sold to KH Finance Limited, a company owned by ECI Partners LLP. Marine Systems was part of Specialty – Other. In addition to the consideration recognised there is an unrecognised deferred payment of £4 million contingent on the terms of any future disposal of KH Finance Limited by the purchasers. The assets and liabilities of businesses held for sale on the 31 July 2007 balance sheet relate to the Marine Systems business.

Additional costs relating to prior year disposals amounted to £0.7m.

	Total £m
Marine Systems	
Consideration	**43.9**
Transaction costs	**(2.8)**
Disposal provisions	**(2.0)**
Net consideration received	**39.1**
Net assets disposed of:	
– Intangible assets	**2.2**
– Property, plant and equipment	**2.2**
– Inventory	**8.6**
– Trade and other receivables	**14.0**
– Cash and cash equivalents	**0.9**
– Trade and other payables	**(16.5)**
	11.4
Profit on disposal of Marine Systems	**27.7**
Other disposal adjustments	**(0.7)**
	27.0

12 Intangible assets

	Goodwill £m	Development costs £m	Acquired intangibles £m	Other £m	Total £m
Cost					
At 31 July 2007	921.3	51.2	131.3	76.3	1,180.1
Exchange adjustments	56.2	2.7	6.1	3.3	68.3
Business combinations	10.9		5.3		16.2
Adjustments to prior year acquisitions	0.5		1.3	(1.3)	0.5
Additions at cost		8.4		7.4	15.8
Disposals				(0.4)	(0.4)
At 2 February 2008	**988.9**	**62.3**	**144.0**	**85.3**	**1,280.5**
Amortisation					
At 31 July 2007	77.0	12.5	29.1	40.2	158.8
Exchange adjustments	4.0	0.9	1.7	2.5	9.1
Adjustments to prior year acquisitions			0.5	(0.5)	
Disposals				(0.4)	(0.4)
Charge for the period		2.7	7.2	2.6	12.5
At 2 February 2008	**81.0**	**16.1**	**38.5**	**44.4**	**180.0**
Net book value at 2 February 2008	**907.9**	**46.2**	**105.5**	**40.9**	**1,100.5**
Net book value at 3 February 2007	852.2	32.8	102.4	31.5	1,018.9
Net book value at 31 July 2007	844.3	38.7	102.2	36.1	1,021.3

13 Property, plant and equipment

	Land and buildings £m	Plant and machinery £m	Fixtures, fittings, tools and equipment £m	Total £m
Net book value at 31 July 2007	92.4	123.7	44.8	260.9
Exchange adjustments	4.7	5.6	2.8	13.1
Business combinations	0.9	1.2	0.8	2.9
Additions	2.3	15.2	8.4	25.9
Transfer from disposal group	0.5			0.5
Disposals and business disposals	(0.4)	(1.0)	(0.5)	(1.9)
Adjustment to disposal of Aerospace operations	6.4			6.4
Depreciation charge for the period	(2.6)	(13.8)	(7.6)	(24.0)
Net book value at 2 February 2008	**104.2**	**130.9**	**48.7**	**283.8**
Net book value at 3 February 2007	114.0	126.3	48.9	289.2

14 Cash and borrowings

	2 February 2008 £m	3 February 2007 £m	31 July 2007 £m
Cash and cash equivalents			
Net cash and deposits including assets of disposal group	**142.6**	276.4	189.3
Short-term borrowings			
Bank overdrafts including impact of cash pooling gross up (note 1 below)	**(138.5)**	(300.5)	(186.2)
Bank loans	**(1.5)**	(5.9)	(0.2)
Other loans	**(2.8)**	(3.1)	(3.1)
B shares	**(18.5)**		(18.1)
Interest accrual	**(16.3)**	(19.6)	(4.5)
Disposal group loans		(4.6)	
	(177.6)	(333.7)	(212.1)
Long-term borrowings			
One to two years	**(0.5)**	(0.3)	(0.5)
Two to five years	**(479.6)**	(614.2)	(287.8)
After five years	**(159.8)**	(283.1)	(278.8)
	(639.9)	(897.6)	(567.1)
Borrowings	**(817.5)**	(1,231.3)	(779.2)
Net debt	**(674.9)**	(954.9)	(589.9)

Total cash and overdrafts, including that disclosed as part of the disposal group, as at 2 February 2008 are as follows:

	2 February 2008 £m	3 February 2007 £m	31 July 2007 £m
Cash and cash equivalents			
Continuing operations	**142.6**	274.1	186.2
Disposal group		2.3	3.1
	142.6	276.4	189.3
Bank overdrafts			
Continuing operations	**(138.5)**	(299.7)	(186.2)
Disposal group		(0.8)	
	(138.5)	(300.5)	(186.2)

Note 1
IAS 32 requires that cash and overdraft balances within cash pooling systems be reported gross on the balance sheet. The gross up included above amounted at 2 February 2008 to £98.8m (3 February 2007: £243.5m; 31 July 2007: £123.2m).

15 Provisions for liabilities and charges

	At 31 July 2007 £m	Exchange adjustments £m	Provisions charged £m	Provisions released £m	Discounting £m	Utilisation £m	**At 2 February 2008 £m**
Warranty provision and product liability	34.5	2.7	14.9	(1.2)		(5.8)	**45.1**
Reorganisation	10.8		1.3	(0.3)		(4.1)	**7.7**
Property	6.7		0.5	(0.5)		(0.5)	**6.2**
Disposal	60.3		10.3	(2.7)			**67.9**
Litigation	121.2	3.5	0.5		8.2	(5.6)	**127.8**
	233.5	6.2	27.5	(4.7)	8.2	(16.0)	**254.7**

Analysed as:

	2 February 2008 £m	3 February 2007 £m	31 July 2007 £m
Current liabilities	**88.0**	60.1	90.1
Non-current liabilities	**166.7**	57.2	143.4
	254.7	117.3	233.5

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

Significant parts of the Group's operations have been undergoing a phased restructuring programme. Full provision is made for reorganisation approved and committed by the end of each financial year.

Reorganisation provisions include £4.9m costs relating to restructuring supply arrangements following the automotive seals disposal. This provision is expected to be utilised over the next five years.

Disposal

The terms of disposal of businesses include certain obligations for which provision has been made, including £23.0m in respect of the costs of transferring Aerospace active pensioners. These costs are expected to be agreed in the current financial year.

Litigation

John Crane, Inc.

As stated in note 16 John Crane, Inc. ('JCI') is one of many co-defendants in litigation relating to products previously manufactured which contained asbestos, the manufacture of which ceased in 1985. Until recently, the awards, the related interest and all material defence costs were met directly by insurers. In the previous period, JCI secured the commutation of certain insurance policies in respect of product liability. While substantial insurance remains in place, JCI has begun to meet defence costs directly, seeking appropriate contribution from insurers thereafter. 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. Last year, JCI established a provision to meet defence costs. No provision is held against awards (note 16).

The provision is based upon an assessment of the probable costs of defending known and expected future claims to the extent that such costs can be reliably estimated. The assumptions made in assessing the appropriate level of provision include the number of years over which claims will continue to be received – currently estimated at a 20 year period: the future trend of legal costs – assuming four years based on historical experience (allowing for 3% cost inflation) before allowing for decreasing costs in line with a published table 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 a discount rate of 4.4% (2007: 5.3%), being the risk-free rate on US debt instruments. 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:

	2 February 2008 £m	31 July 2007 £m
Gross provision	**142.2**	142.2
Discount	**(39.0)**	(45.8)
Discounted pre-tax provision	**103.2**	96.4
Deferred tax	**(39.2)**	(36.6)
Discounted post-tax provision	**64.0**	59.8

The movement in discounting on this provision comprises £5.7m relating to the change in the discount rate, which is recognised in exceptional operating items (note 4), and £2.5m relating to the unwinding of the discounting, which is recognised in exceptional finance costs (note 3).

15 Provisions for liabilities and charges continued

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, none of the other provisions are discounted.

16 Contingent liabilities

John Crane, Inc. ('JCI'), a subsidiary of the Company, is one of many co-defendants 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. 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 156,000 claims over the last 29 years. JCI is currently a defendant in cases involving approximately 138,000 claims. Despite this large number, JCI has had final judgments against it, after appeals, in only 67 cases, amounting to awards of some US$60.5m over the 29 year period.

Whilst this represents a very low proportion of claims that has historically resulted in final judgment against JCI, the incidence of such judgments in the future cannot be meaningfully estimated and the scale of future awards is accordingly unquantifiable and therefore no provision is made for any future awards. As explained in note 15, a provision for the legal costs of defending asbestos claims has been established.

In common with many other enterprises of similar size, the Company and its subsidiaries are from time to time engaged in litigation in respect of a variety of commercial issues.

17 Changes in shareholders' equity

	Period ended 2 February 2008 £m	Period ended 3 February 2007 £m	Period ended 31 July 2007 £m
At beginning of period	**903.3**	1,362.9	1,362.9
Exercises of share options	**17.3**	43.0	77.7
Purchase of own shares	**(20.7)**	(7.0)	(7.0)
Return of capital to shareholders and redemption of B shares			(2,108.9)
Fair value gains and losses on cash-flow and net investment hedging:			
– transfers to profit for the period	**(0.7)**	(4.7)	(16.7)
– (losses)/gains taken to equity	**(41.6)**	25.3	13.0
Profit for the period	**141.4**	149.0	1,728.1
Dividends paid to equity shareholders	**(90.8)**	(122.3)	(182.4)
Dilution of interest in associated company			(1.2)
Share-based payment	**6.6**	8.2	17.3
Deferred tax (charge)/ benefit related thereto	**(3.6)**	2.7	(9.4)
Current tax credit related thereto			10.3
Actuarial gains and losses on retirement benefit schemes	**(88.2)**	17.5	70.3
Deferred tax charge/(credit) related thereto	**26.9**	(5.8)	(30.1)
Cumulative exchange losses recognised on disposals			49.2
Fair value gain on acquisition of former associate	**0.2**		
Exchange rate changes (including tax on recognised gains)	**78.7**	(51.1)	(69.8)
At end of period	**928.8**	1,417.7	903.3

18 Cash-flows from operating activities

	Period ended 2 February 2008 £m	Period ended 3 February 2007 £m	Period ended 31 July 2007 £m
Profit before taxation – continuing operations	**165.4**	136.3	256.0
Profit before taxation – discontinued operations	**8.9**	59.4	1,613.4
	174.3	195.7	1,869.4
Net interest payable	**19.8**	30.3	37.6
Financing losses/(gains)			
– charged to administrative expenses		(0.1)	1.5
– charged to financing	**5.2**	18.2	(2.8)
Share of post-tax loss from associate		0.7	0.5
Other finance income – retirement benefits	**(20.6)**	(17.7)	(36.8)
Profit on sale of financial asset			(24.0)
Profit on disposal of discontinued operation	**(8.9)**		(1,469.6)
	169.8	227.1	375.8
Amortisation of intangible assets	**12.5**	15.6	29.7
Impairment of intangible assets			2.2
Provision against non-current investment		0.3	
Profit on disposal of property, plant and equipment		(0.7)	(0.4)
Profit/(loss) on disposal of business	**(27.0)**	(8.5)	5.2
Depreciation of property, plant and equipment	**24.0**	31.9	52.2
Impairment of property, plant and equipment			8.2
Share-based payment expense	**6.6**	9.5	13.9
Retirement benefits	**(5.9)**	3.5	(66.2)
(Increase) in inventories	**(38.9)**	(71.4)	(84.2)
Decrease/(increase) in trade and other receivables	**30.8**	20.1	(84.8)
(Decrease)/increase in trade and other payables	**(60.2)**	24.2	29.7
Increase in provisions	**5.3**		84.5
Cash generated from operations	**117.0**	251.6	365.8
Interest	**(10.2)**	(15.5)	(27.0)
Tax paid	**(42.5)**	(45.6)	(92.8)
Net cash inflow from operating activities	**64.3**	190.5	246.0

19 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 & Accounts for the period ended 31 July 2007.

20 Events after the balance sheet date

On 4 February 2008, the Company acquired the Heating Element division of Fast Heat, Inc. for cash consideration of $18m, subject to closing adjustments.

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