

Review of Operations



We are pleased to report another strong set of results for the first half of 2008. Trading conditions remained positive and we grew sales in all geographic regions. Currency movements favourably impacted both sales and profits. Our two specialist businesses in the industrial steam and the peristaltic pumping markets both produced good results and offer good opportunity for future growth.

Group sales in the half year were £238.7 million, up 19% from £200.1 million in 2007. The increase at constant exchange rates was 12%, including a small contribution from acquisitions made earlier in 2008.

We increased operating profits by 29% (15% at constant currency) from £31.6 million to £40.8 million in 2008. The operating profit margin in the first half improved from 15.8% to 17.1%, around half of which was due to exchange. We benefited from the organic sales growth, efficiency improvements and favourable currency movements, which more than offset the impact of higher material and energy costs.

Net finance income of £0.8 million was lower than the £0.9 million in the same period of 2007 due to the reduced net finance income in respect of pension schemes. The profit from Associates was £1.2 million in the period (2007: £0.6 million). Profit before tax was £42.7 million as against £33.1 million in 2007; the increase of 29% includes a gain of £3.9m from favourable currency movements, most notably the stronger euro.

The tax charge was 33% (2007: 34%) and the profit for the period increased by 32% to £29.1 million. Earnings per share for the period increased by 31% to 38.0p compared with 29.1p in the first half of 2007.

Trading

We are world leaders in our industrial steam and peristaltic pumping niche businesses. Both Spirax and Watson-Marlow Bredel have robust business models that are serving us well in today's market environment. We work closely with our customers in supplying a wide range of products, services and engineered systems to generate energy savings, process efficiency and quality improvements, and compliance assistance to meet increasingly stringent health and safety regulations. Today's high cost of energy, in particular, has provided a favourable backdrop in which we work with our customers to reduce their energy consumption - seen in good sales growth in the first half of 2008 for traditional steam specialty products and systems.

In the UK market, we achieved good organic sales growth of 11% to £25.1 million despite the poor climate for the manufacturing sector which we serve. The growth resulted primarily from our ongoing steam business initiatives in services and heat exchange systems related to energy saving projects for our customers. Operating profit was up 9% at £8.2 million compared with £7.6 million in the first half of 2007 (up 21% at constant currency).

Business momentum continued in Continental Europe although the economic environment is weakening. Sales increased 23% to £93.3 million and at constant exchange rates the increase was 8%, including a small contribution from the Flexicon and Colima acquisitions. The Spirax operations increased sales of controls, services and products/systems for clean steam applications. We have continued to see very strong sales and profit growth from Russia. The Watson-Marlow Bredel business grew sales and profits in most markets and the integration of the Flexicon acquisition is progressing well. Operating profit in Continental Europe increased by 48% (9% at constant currency) to £17.9 million.

North American sales increased 12% to £43.0 million (11% at constant currency), with continued strength in both the Spirax steam business and Watson-Marlow Bredel. The Spirax steam business increased due to success with heat exchange packages and traditional steam specialty products. The Watson-Marlow Bredel business achieved strong growth in sales in the general industrial and water/waste water markets and profits were well ahead. The much-publicised difficulties of the USA economy have thus far not impacted our business. The operating profit in North America was 22% higher than in the same period in 2007 (up 34% at constant currency).

On-demand hot water solves production headaches for Bendicks



UK chocolate manufacturer Bendicks (Mayfair) Ltd. now has an unlimited supply of hot water for washing down its equipment, thanks to the installation of a Spirax Sarco EasiHeat™ Engineered System.

Regulations dictate that water at 63°C or hotter must be used for washing down equipment to prevent microbial growth. Bendicks' old calorifier system caused problems because water was heated in a vessel and as it was used it was replaced by fresh cold water, causing the overall temperature to drop below the required level at peak times. The new Spirax EasiHeat system provides instant, constant hot water.

Spirax EasiHeat systems rely on a compact plate heat exchanger that uses plant steam to produce hot water on demand. This ensures a constant supply at all times, eliminates hot water storage and increases energy efficiency. Each compact Spirax EasiHeat system is supplied as a skid-mounted package, complete with all pipework and ancillaries, making it very simple to install and commission. The system has also given Bendicks flexibility for the future because expansion can be achieved by adding further plates to the heat exchanger.

Peristaltic pump provides nest egg for food processing company



A Japanese food processing company has managed to dramatically improve the quality of its product by the use of a Watson-Marlow Bredel 840 Series peristaltic pump.

The pump is used to process approximately 60000 egg yolks and whites through a chilling process before despatch to food manufacturers making extra-thick omelettes to accompany sushi. To guarantee that the quality matches that of the fine sushi, producers demand as many unbroken egg yolks as possible. The new pump processes the egg yolks with a 70% unbroken rate, allowing for a better quality end product than achieved with the previous sine pump which could achieve only a 20% unbroken rate.

The Watson-Marlow Bredel 840 Series pump was particularly suitable for this application because of its ability to meet gentle, yet high flow hygienic applications. Peristaltic pump technology is hygienic because nothing but the hose or tube touches the fluid being pumped.

The good performance continued in Asia, with overall sales growth of 15% to £45.2 million (13% at constant currency). Our large company in China performed particularly well with strong sales and profit growth. Sales by our Korean operation increased over the prior year but profits were lower due to the impact of the weaker local currency and some lower margin projects. Sales and profits in India (an Associate) were up substantially over last year as we benefited from major capital investment activities in the industrial sector and we also benefited from the increase in our shareholding to nearly 50% which was completed in April 2007. The Watson Marlow-Bredel business is still relatively small in Asia and we continue to invest to expand our sales operations in the region. Total operating profit in Asia was 17% ahead at £7.8 million (12% at constant currency).

Sales in the Rest of the World (South America, Africa and Australasia) increased 32% (up 22% at constant currency). The Spirax steam business in South America was exceptionally strong, with large sales and profit gains coming from improved domestic markets, particularly in Brazil. Australia and New Zealand increased sales and profits. Our Watson Marlow-Bredel business also did well. Operating profits in the region increased by 43% to £3.5 million (25% at constant currency).

Balance Sheet and Cash Flow

Total capital employed increased by only 6% in the first half (3% at constant currency) to £223 million, comprising a 3% increase in tangible net fixed assets and an 8% increase in working capital reflecting the good sales growth. Capital expenditure rose to £8.2 million including the start of the £9 million project to build our new factory and offices in China. This, together with a £6 million investment in expanding the Watson-Marlow tube and pump production plant and also the construction of our new offices in Korea, will lead to high capital expenditure in the second half year and into 2009.

There was a cash outflow of £12.2 million for acquisitions, largely in respect of Flexicon A/S in Denmark which as previously reported was completed in February, and including £0.5 million in respect of Colima which was completed in March. Despite this investment, and after payment of the 2007 final dividend, the net cash position of £12.2 million at 30th June 2008 was only £3.6m lower than at the start of the period, reflecting the continued strong underlying cash flow.

The net post-retirement benefits liability increased by £26 million to £47 million in the first half due mainly to a fall in the schemes' asset values.

Petrobrás



Spirax Sarco has been instrumental in helping a major oil company achieve many production and energy saving benefits, by improving control of the varying temperatures required across its plant.

Petrobrás is the largest company in Brazil, and will soon consolidate as the largest oil company in the world. The Repar refinery in Araucária represents 12% of Petrobras's national production, processing 189 000 barrels/day. But for many years the pre-heaters in its boilers suffered from waterhammer and energy loss due to high steam consumption. They had unsuccessfully tried many steam trap types and manufacturers to remedy the problems, eventually they invited Spirax Sarco to develop a definitive solution.

The solution was to use Spirax Sarco APT14 assembled packages. In 2008, after three years of successful operation, the system was established as the definitive solution. The APT14 is not only more energy and resource efficient, it has also eliminated waterhammer and removed sulphuric acid condensation.

Principal Risks and Uncertainties

Details of the principal risks and uncertainties are set out in note 12 and are followed by a Directors' Responsibility Statement. Commencing in 2009, this half year report will be produced only in electronic form, in line with the majority of similar companies.

Dividend

The Board has declared an interim dividend of 10.0p (2007: 8.3p) per ordinary share, an increase of 20%, reflecting the good increase in first half profits. The dividend will be paid on 7th November 2008 to shareholders on the register at the close of business on 10th October 2008. No scrip alternative to the cash dividend is being offered in respect of the 2008 interim dividend.

Prospects

The strong trading performance during the period has, so far, been maintained into the early weeks of the second half year, although the global macro-environment is deteriorating. We have seen sustained business investment by customers and are benefiting from expanding our selling opportunities and increasing market share. Due to the high cost of energy, our customers are increasingly valuing our energy-saving solutions. Subject to continuation of the favourable exchange rates, there is expected to be a further exchange benefit to trading in the second half year and, assuming our markets remain stable, we expect to achieve continued good progress for the year.

Note: Unless otherwise stated, the figures quoted in the text above exclude the amortisation of acquired intangible assets.