

Financial review



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Accounting Standards The Group's accounting policies reflect the applicable standards issued by the Accounting Standards Board.

Two standards became mandatory during 1999. FRS12 (– Provisions, Contingent Liabilities and Contingent Assets) deals primarily with the definition and recognition of provisions and FRS13 (– Derivatives and Financial Instruments: Disclosures) increases disclosure requirements in respect of derivatives and other financial assets and liabilities. Both standards have been formally adopted in this Annual Report. The principal impact of FRS12 on these accounts is an exceptional provision of £4.6 million for vacant leasehold premises. Detailed disclosures in respect of FRS13 are contained in note 19 of the Report and Accounts. The Group will be adopting FRS15 (– Tangible Fixed Assets) with effect from 1 January 2000. This standard is not expected to have a significant effect on the Group accounts.

Review of operating results The Group's results have been significantly affected by the disposal of the Precision Engineering Division, the garments business in India and the acquisition of Hicking Pentecost PLC. The turnover for the year from continuing businesses was £1,568.0 million (1998: £1,726.8 million), a decrease of 9% on prior year, and the operating profit before exceptional items was £84.3 million (£86.9 million), a decrease of 3%. The reported Group turnover was £1,679.5 million (£2,082.9 million), and operating profit before exceptional items £92.7 million (£115.8 million).

Reorganisation of the Group was accelerated

leading to a charge of £67.0 million (£26.5 million) and there was an exceptional charge of £10.1 million principally arising from additional provisions on vacant leasehold premises of £4.6 million required by a new accounting standard, and a £5.6 million net loss arising from irregularities in a US subsidiary. The disposal of Precision Engineering gave rise to a profit of £114.7 million, but this was offset by the £3.2 million cost of disposing of Group investments and a loss of £30.9 million on the termination or disposal of peripheral operations.

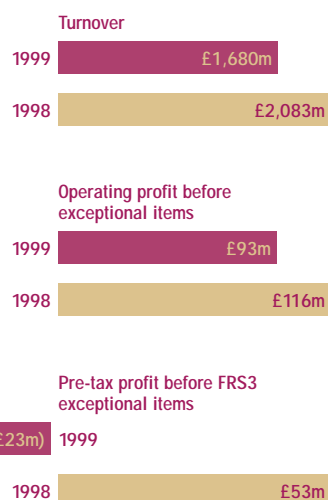
The result of these actions was that profit before tax is £63.6 million (£35.5 million), and the profit attributable to ordinary shareholders was £28.6 million (loss £26.6 million). Earnings per share were 4.1p (loss 3.8p) and the headline loss per share, after stripping out the exceptional gains on disposals, was 4.3p (1.4p).

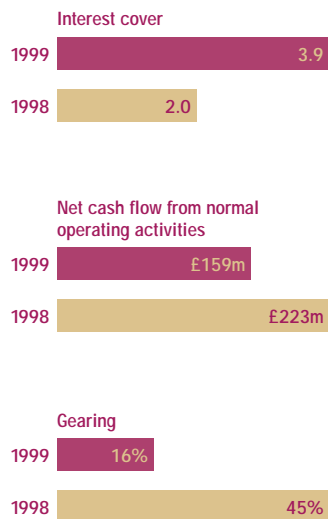
The Group proposes to maintain its dividend at 3p for this year. Coats Viyella's year end quoted share price was 41.5p (27p) which capitalises the Group at £292 million (£190 million).

On a like-for-like basis, excluding currency movements, and the effect of acquisitions and disposals, turnover of ongoing businesses was down 9% and operating profit before exceptional items decreased by 8%.

At 17% of sales, Marks & Spencer remained the Group's largest customer in 1999 with sales of £292 million (£317 million) which were predominantly in the UK.

The Group's **net interest costs** of £21.7 million were reduced from 1998





(£34.5 million) as a result of the proceeds of the sale of the Precision Engineering Division being used less the cost of acquiring Hicking Pentecost PLC.

The **tax rate** of 49% (158%) is significantly distorted by the tax effects of exceptional items. The underlying Group tax rate continues to be affected by unrelieved tax losses and reorganisation costs in certain territories, particularly the UK, which can only be relieved against future profits. Excluding exceptional items the tax rate would have been 45% (40%).

The principal **exchange rates** to sterling used in preparing the financial statements were:

		1999	1998
Average	US\$	1.62	1.66
	Deutschmark	2.98	2.92
Year End	US\$	1.61	1.66
	Deutschmark	3.14	2.77

The translation of 1998 overseas turnover and profits at 1999 average rates increases sales by £9 million and operating profit before exceptional items by £1 million.

No employer cash contributions were made to the **UK pension plan**. Owing to the continuing actuarial surplus of assets in the plan, a net credit of £4.5 million (£8.4 million) is included in the results for the period.

Net **cash inflow** from normal operating activities was £158.5 million (£222.9 million). Within this, continuing operations accounted for £158.3 million (£182.9 million). There was a further reduction in net working capital of £31.6 million (£49.1 million), but the cash cost of reorganisation increased to £40.1 million (£35.8 million), reflecting the faster rate

of restructuring. At the year end £43 million (£24.2 million) of the restructuring provision remained to be spent.

Average **net working capital** during the year was 26.2% of sales (25.2%).

Capital expenditure in 1999 was:

£m	1999	1998
UK	20.0	23.3
Overseas	35.6	49.5
Total	55.6	72.8

Despite difficult trading conditions the Group spent £55.6 million on upgrading its plant and equipment. This is broadly in line with depreciation.

Reorganisation costs In 1999, reorganisation costs of £67 million were incurred or provided, compared with £26.5 million in 1998. Benefits from previous schemes are being achieved but new schemes have been accelerated in order to keep pace with the shifts in the marketplace.

Of the costs and provisions in 1999, some £44 million is attributable to Coats of which £3 million was incurred in the Barbour Threads businesses acquired with Hicking Pentecost PLC, and the remainder in Viyella. A full segmental analysis of reorganisation costs is included in note 3 on page 27 of the report and accounts.

Acquisitions and disposals Hicking Pentecost PLC, the principal business of which is Barbour Threads, a manufacturer of speciality industrial threads, was acquired at the beginning of September 1999 at a cost of £80.2 million, paid by cash and loan notes. In addition, some £30.4 million of net debt was assumed with the acquisition.

As previously reported, the Group sold its Precision Engineering Division to Petcin in April 1999 for a net consideration of £294.4 million, giving rise to a net gain on disposal of £114.7 million after accounting for £60.3 million of goodwill previously written off on acquisition.

Losses on other sales and terminations of operations principally relate to the withdrawal from handknittings manufacture (£13.3 million) and the withdrawal from the Berghaus wholesale business with the former Russian states (£13.5 million). Other small disposals generated losses of £4.1 million. The total of other losses on sale or termination was £30.9 million including £14.3 million of previously written off goodwill.

Review of financial needs and resources

Year end net debt at £125.1 million was £195.7 million lower than at last period end and gearing as result decreased to 16% (45%).

Borrowings were primarily affected by the disposal of the Precision Engineering Division with a net cash inflow of approximately £290 million and a net cash outflow from the acquisition of Hicking Pentecost PLC of approximately £110 million (including the debt acquired). The Group continued to focus on working capital with the resultant improvement in stock levels and the maintenance of strong operating cash flow.

The Group's borrowing facilities are provided by a combination of permanent debt finance and a prudent combination of committed and uncommitted bank facilities to cover working capital requirements. As a result of significant cash generation during the year the Group felt able to reduce

its permanent debt finance. Details of this and other borrowings are provided in Note 19 on pages 37 to 41 of the Report and Accounts. The Group has facilities of £514 million (£726 million) of which £279 million were committed. The Group was not in breach of any of its borrowing covenants.

The Group policy on interest rates is to minimise exposures by ensuring an appropriate balance of fixed and floating rates. This exposure is managed through the use of interest rates swaps and forward rate agreements, the nominal principle of which does not exceed the underlying debt and cash positions covered.

The Group's translation exposure in the Profit and Loss account is not hedged, however, the Group's net assets are subject to hedges where it is felt that a currency revaluation could have a material impact on Shareholders' Funds. At 31 December 1999, after taking into account currency denominated liabilities approximately 20% of shareholders' funds are exposed to fluctuations in the Sterling/US dollar exchange rate, and approximately 11% to the Sterling/Euro exchange rate. Further details are provided in note 19 of the Report and Accounts.

Y2K and the euro Details of the Group's plans for addressing the Year 2000 issue were included in the 1998 Annual Report. All plans were implemented in time and no significant Y2K problems have been reported to date. Costs incurred in relation to Y2K compliance amounted to £0.7 million in revenue and £1.5 million in capital expenditure on new systems. No significant costs have been or are expected to be incurred in respect of the euro.