**Thread trading**

*Underlying operating profit before reorganisation, impairment, goodwill amortisation and exceptional costs: $104.8 million (2003 full year pro-forma – $110.3 million) (see below).*

On a like-for-like basis, including a full twelve months for 2003 and excluding the impact of exchange translation, acquisitions and disposals, underlying sales grew by 3%. This reflected strong growth in South America, Asia, and of crafts in North America.

Operating profit on the same basis, and before reorganisation, impairment, goodwill amortisation and exceptional costs, decreased by 5%. This reflected the Group's focus on cash generation and the impact of accelerated migration on production levels in Western Europe, which masked generally good performances in other parts of the Group.

In the following comments on Thread regional performance, all comparisons with 2003 are based on the table below:

**Thread like-for-like sales and operating profit***

| | 2003 comparatives (see note 2a) $m | 2003 1 January -7 April $m | Exchange retranslation $m | Acquisitions/ disposals $m | 2003 underlying $m | 2004 reported (see note 2a) $m | Increase/ (decrease) % |
|---|---|---|---|---|---|---|---|
| **External sales** | | | | | | | |
| UK and Europe | 425.8 | 147.0 | 51.2 | | 624.0 | 606.5 | (3) |
| North America | 304.6 | 96.9 | 1.7 | 2.4 | 405.6 | 412.6 | 2 |
| South America | 113.2 | 27.8 | | 1.3 | 142.3 | 169.1 | 19 |
| Asia | 295.1 | 85.5 | 3.8 | (20.9) | 363.5 | 399.3 | 10 |
| **Total** | **1,138.7** | **357.2** | **56.7** | **(17.2)** | **1,535.4** | **1,587.5** | **3** |
| **Operating profit*** | | | | | | | |
| UK and Europe | 18.8 | 5.8 | 0.6 | | 25.2 | 4.3 | (83) |
| North America | 6.4 | (2.9) | 0.5 | (0.1) | 3.9 | 8.2 | 110 |
| South America | 11.5 | 2.4 | | 0.1 | 14.0 | 17.1 | 22 |
| Asia | 52.2 | 12.0 | 0.1 | (1.6) | 62.7 | 64.5 | 3 |
| Corporate** | 5.3 | (1.0) | 0.2 | | 4.5 | 10.7 | 138 |
| **Total** | **94.2** | **16.3** | **1.4** | **(1.6)** | **110.3** | **104.8** | **(5)** |

*pre reorganisation, impairment, goodwill amortisation and exceptional costs.
**pre-goodwill amortisation of $18.2 million in 2004 and $0.2 million in 2003.

**UK and Europe**

Sales -3%; OP -83%

The market for industrial thread in Western Europe continued to decline as a result of customer migration to Eastern Europe and Asia. Zip sales were also affected by a fashion swing towards other fasteners. Continued growth in our industrial thread sales in Eastern Europe did not fully offset these negative trends. Modest growth was achieved in crafts, with a strong performance in handknittings offset by weak demand for embroidery and sewing thread. Despite past and current downsizing projects, the pace of the decline in Western European industrial thread sales had a significant impact on operating margins. This was exacerbated by the drive to reduce inventory levels which temporarily reduced production levels and, therefore, overhead recoveries. Benefits from the new bulk production unit in Romania were offset by losses in Italy, France and the UK.

**North America**

Sales +2%; OP +110%

Strong growth in crafts sales was driven by a buoyant handknittings market and recovery from the de-stocking by major customers which had depressed 2003 reported sales. Industrial sales continued to decline as a result of migration of apparel production to Asia. Improvement in operating profit came from recovery in crafts margins but industrial thread continued in loss. Benefits from restructuring and the new plant in Mexico have taken longer to come through than originally envisaged, but by the end of the year transitional operating issues had been largely resolved.

**South America**

Sales +19%; OP +22%

Improved economic conditions led to the best performance from the region in recent years. Growth was generally strong across the region and all product categories, with a particularly strong performance by industrial thread and zips in Brazil.

**Asia**

Sales +10%; OP +3%

Industrial thread sales continued to grow strongly. Sales growth in the region more than offset the declines experienced in North America/Western Europe, reflecting the benefit of our relationships with global retailers and brand owners. Although much of the growth was in premium corespun thread, operating margins were slightly lower. This was mainly as a result of a drive to reduce global grey thread stocks which led to lower capacity utilisation in the first half of the year. Nevertheless, at 16.2% (2003 – 17.2%), operating margins remain highly respectable.

**Corporate**

The $10.7 million (2003 – $4.5 million) underlying profit reflects increased royalties and technical fees.

### Thread reorganisation, impairment and exceptional costs

We continued to make progress in the year in downsizing Western Thread capacity, including in the UK, France and the US, whilst expanding in low cost locations. Thread reorganisation costs of $45.6 million (2003 – $19.5 million) were incurred. The reorganisation programme, which will continue in 2005, is principally designed to reduce the cost base of our industrial businesses in Western Europe and North America to address the migration of customers to lower cost regions.

Thread exceptional operating costs of $3.8 million (2003 – $nil) were accounted for in the year, largely in respect of the refinancing exercise completed in March 2004.

### Non-Thread

The refocusing of the Group on Thread has been completed, with the sale of our Bedwear business on 14 February 2005. Sales in 2004 from non-thread businesses of $124.4 million (2003 – $97.1 million) predominantly relate to Bedwear.

The results of Bedwear have been included within discontinued operations and the 2003 categorisation between continuing and discontinued operations has been restated accordingly.

Including related property sold separately, proceeds (net of expenses) from the disposal of Bedwear totalled approximately $19.0 million, resulting in an overall loss on disposal of approximately $15.0 million, which is recognised in 2005 under UK accounting standards. In addition, assets retained are expected to realise approximately $4.0 million in cash.

### Interest and tax

Net interest costs rose to $41.8 million (2003 – $23.1 million), largely due to the fact that 2003 included a $18.0 million net exchange gain on foreign currency borrowings. The stated interest expense includes a non cash element of $7.0 million (2003 – $5.1 million), largely arising from the unwinding of the discount on future pension liabilities.

A loss before tax of $4.1 million (2003 – $46.7 million profit) was recorded, reflecting the higher reorganisation and net interest costs. The tax charge of $14.3 million (2003 – $18.1 million) reflects expenses not deductible for tax purposes and losses which cannot be recognised. This charge is primarily made up of tax on profits of overseas subsidiaries net of a deferred tax credit of $12.3 million (2003 – charge of $3.6 million).

### Pension arrangements

The Group has a defined benefit plan in the UK and there are similar arrangements in North America. The Group accounts for pensions on a SSAP 24 – Accounting for Pension Costs basis. An actuarial review of the UK and USA schemes under SSAP 24 was conducted as at 7 April 2003 and indicates that these schemes are in surplus. Employer contributions continue to be suspended based on actuarial advice. The pension prepayments included in debtors in respect of these schemes on a SSAP 24 basis total $73.4 million (2003 – $68.6 million).

There are various pension and leaving indemnity arrangements in other countries, primarily in Europe, where the Group operates, which in general are not funded. These are predominantly included in provisions for liabilities and charges.

### Goodwill

$169.1 million of goodwill has arisen in the year in respect of the finalisation of the fair value adjustments in respect of the acquisition of Coats Holdings Ltd in the year ended 31 December 2003. This includes provisions made in respect of the European Commission investigation, referred to in the Chairman's statement. The Directors consider that the disclosure at this stage of further details in respect of these provisions could seriously prejudice the outcome of the investigation. Therefore no analysis has been included in these accounts of these fair value adjustments.

The goodwill amortisation charge arising in the year of $18.2 million (2003 – $0.2 million) reflects this additional goodwill.

### Balance sheet and cash flow

Net cash inflow from operating activities was $200.2 million (2003 – $134.8 million), including the benefit of a $93.5 million (2003 – $39.3 million) reduction in working capital. Stock reduced significantly over 2003 levels, resulting in a $54.7 million (2003 – $14.9 million) cash inflow.

$33.4 million (2003 – $18.4 million) tax was paid, broadly comparable with the Group's current tax charge of $26.5 million (2003 – $14.5 million).

The Group continues to make significant investments in its Thread business and capital expenditure was $93.6 million (2003 – $46.8 million). After adjusting for opening and closing year-end creditors, actual associated cash outflow was $92.7 million (2003 – $76.1 million). The principal project was the expansion of thread and zip capacity in China, culminating in the opening of a major new plant (80,000 sq.m) in Shenzhen just before the year-end.

The disposal of businesses and surplus assets generated $65.2 million (2003 – $59.7 million). In addition, current asset investments were realised for cash of $40.9 million (2003 – $0.2 million).

As part of the refinancing exercise completed in March 2004, new share capital of $137.8 million (2003 – $0.1 million) was subscribed.

The net result of the above was a $271.3 million reduction in the Group's net debt to $401.5 million at 31 December 2004, compared to $672.8 million at the start of the year. Shareholders' funds increased from a deficit of $17.6 million to $107.7 million, reflecting the $24.0 million (2003 – $19.5 million profit) retained loss for the year, offset by the new share capital injection referred to above and a $11.5 million exchange gain (2003 – $37.2 million loss) as shown in the statement of total recognised gains and losses.

### Functional currency

Following the refocusing of the Group on Thread, a review has taken place of the functional currency of the Group. Given the markets in which the Group operates and the global dimension of the business, the US dollar is the functional currency. In order to reflect more appropriately the underlying results of the business, the Group's results in these financial statements are prepared and presented in US dollars.

The 2003 comparative figures have been translated from the sterling reported figures to US dollars by applying the 2003 US dollar average exchange rate of 1.64 to profit and loss account and cash flow items, and by applying the 2003 US dollar year end exchange rate of 1.79 to balance sheet items.

The principal exchange rates (to the US dollar) used in preparing the financial statements are as follows:

| | | 2004 | 2003 |
|---|---|---|---|
| Average | Sterling | **0.55** | 0.61 |
| | Euro | **0.80** | 0.88 |
| Year end | Sterling | **0.52** | 0.56 |
| | Euro | **0.73** | 0.79 |

As at 31 December 2004, a proportion of borrowings are drawn in sterling and euros and represent a hedge against the impact of changes in exchange rates on the translation of sterling and euro denominated assets. The Group's translation exposure in the profit and loss account is not hedged.