

2 Operating and financial review

Performance in the first six months of 2004 was in line with management expectations and showed significant improvement in earnings and cash flow. Profit before tax increased to £16.7 million (2003 – £33.5 million loss), while net debt reduced by £22.5 million to £109.0 million (2003 – increase of £81.8 million to £186.2 million). Operating cash flow was strongly positive at £40.6 million (2003 – £21.5 million outflow). This reflected management focus on working capital, which was reduced by £8.7 million (2003 – £48.5 million increase), principally as a result of lower inventories.

Results

Our core Thread business performed broadly in line with expectations. On a like-for-like basis sales increased by 3.9%, due to the further development of our Asian business and a good performance from our South American business. However,

operating profit (before reorganisation, impairment and exceptional costs) fell by 1.1%, due mainly to the impact of declining industrial thread sales in Western Europe as customer migration to lower cost areas accelerated.

Exchange rate movements had an adverse effect on sales and operating profit (before reorganisation, impairment and exceptional costs) reported in sterling, of £35.1 million and £4.1 million respectively, with the translated results of Thread's predominantly overseas business impacted by the US dollar average exchange rate weakening to US\$1.82 (2003 – US\$1.61). Reported sales were £430.6 million (2003 – £455.0 million) generating an operating profit (before reorganisation, impairment and exceptional costs) of £25.9 million (2003 – £30.7 million).

Like-for-like sales and operating profit

January-June	2003 restated £m	Exchange retranslation £m	Acquisition/ disposal of businesses £m	2003 adjusted £m	2004 reported £m
Turnover					
Thread	455.0	(35.1)	(5.3)	414.6	430.6
Other/Discontinued	52.7	(0.9)	(12.8)	39.0	35.4
Total	507.7	(36.0)	(18.1)	453.6	466.0
Operating profit/(loss) pre reorganisation, impairment and exceptional costs (see Note 1)					
Thread	30.7	(4.1)	(0.4)	26.2	25.9
Other/Discontinued	(3.1)	0.1	1.7	(1.3)	(1.0)
Total	27.6	(4.0)	1.3	24.9	24.9
Operating profit/(loss)					
Thread	15.2	(3.4)	(0.4)	11.4	10.4
Other/Discontinued	(5.4)	0.1	1.7	(3.6)	(1.0)
Total	9.8	(3.3)	1.3	7.8	9.4

Strategy

Our strategy of reshaping the business in response to customer migration made good progress. Industrial thread capacity in Western Europe and North America was significantly reduced and reorganisation costs of £14.9 million (2003 – £8.4 million) were incurred in the period. At the same time expansion of capacity in lower cost countries, particularly China, enabled us to maintain growth in overall sales. Capital expenditure in the first half amounted to £22.1 million (2003 – £27.0 million). Key projects included the construction of two new plants in China for industrial thread and zip fasteners.

The refocusing of the Group on Thread is virtually complete with Bedwear now the only continuing non-Thread business. Sales and operating losses (before reorganisation, impairment and exceptional costs) from non-Thread businesses fell to £35.4 million (2003 – £52.7 million) and £1.0 million (2003 – £3.1 million) respectively.

Non-operating exceptional items arising in the period were property disposal gains of £9.5 million (2003 – £1.1 million) and gains on the sale or termination of operations of £1.9 million (2003 – £37.8 million loss), with the 2004 gain principally arising from the India Textiles business which was closed in 2003.

Outlook

Although we do not expect any significant improvement in overall trading conditions, second half results will benefit from a lower cost base in Western Europe and North America. For the full year we expect the Thread business to make progress on a like-for-like basis.