Chairman's statement

First half results

Trading conditions have remained very tough in each of our major markets throughout the half year. In particular our sales to customers in the telecommunications and related manufacturing sectors have continued to drop sharply, offsetting gains made elsewhere. Consequently, Group sales have declined by 4.8% (against the first half of last year, adjusted for trading days and exchange rates) to £365.3m from £381.3m. Profit before tax and amortisation of goodwill fell 6.7% to £46.3m from £49.6m.

The largest fall in sales was in our UK business, which continued to suffer from the loss of long-standing end users as manufacturing companies restructured and downsized. However, our North American business, Allied, recovered to year on year growth as the half year progressed. Our businesses in continental Europe achieved sales growth over the prior year even in weakening markets. Japan substantially increased its growth rate following successful investment in e-Commerce.

We have continued our strategic investment programmes, although as past investments are now generating benefits the impact on current profits is reduced. In this half year the net cost of strategic investments has reduced to £4.7m against £7.4m in the first half of last year. The large e-Commerce investments in Europe made last year have been successful and are now generating incremental sales and profits. Losses in Japan are reducing and losses in China are now small.

However, operating profit includes about £2.8m of one-off costs and provisions relating to a withdrawal from specialised activities in the United Kingdom directed to the telecommunications and related sectors.

Capital expenditure of £15.4m was £9.5m lower than the first half of last year as the peak of our spending on information systems and additional warehouse capacity in Europe has now passed.

Gross margins continued to improve as we had anticipated and were 52.6% in the half year, up 2.5 percentage points on the same period last year. We have also managed our costs tightly, but not by lowering customer service. Customer service is always critical, but is even more important when the market is difficult and our service has remained at very high levels.

The impact of the £16.0m sales decline on gross profit was partly offset by our actions on gross margin and costs so that operating profit (before amortisation of goodwill) declined £4.8m to £46.8m from £51.6m. Operating profit benefited from exchange rate movements by £0.3m. Lower average net debt and lower interest rates reduced the interest charge to £0.5m from £2.0m.

The tax rate of 29.0% (based on profit before tax and goodwill amortisation) is the anticipated rate for this financial year and compares to 29.5% in the first half of last year.

Before amortisation of goodwill, earnings per share declined 6.2% to 7.6p from 8.1p. After amortisation of goodwill the decline was 7.5% to 6.2p from 6.7p.

Working capital has again been kept under firm control and cash flow has been strong. Stocks were £19.9m lower than at the end of the first half of last year with the same stock turn, whilst service levels have been maintained. Since the year end, the cash outflow on stocks has been £4.2m in anticipation of the warehouse moves and systems implementation, but the overall working capital cash flow in this period was an inflow of £2.7m. The conversion of operating profit (before amortisation of goodwill) into operating cash flow remained high at 126%. After lower capital expenditure, free cash flow (from continuing operations) increased by £10.3m from the first half of last year to £28.6m. Net debt declined £24.1m to £67.2m from £91.3m at the end of the first half of last year, though was up from £53.0m at the year end due to the timing of dividend and tax payments.

Though we have not adopted the FRS 17 standard on Retirement Benefits, we did note that on 31 March 2002 our UK defined benefit pension scheme would have had an after tax surplus of £13.6m under FRS 17 rules. Following the decline in equity values and increase in bond yields this surplus would have become a deficit of £16.0m at 30 September 2002. There is no profit impact.

Ian Mason's report provides a more detailed review of the Group's trading.

Interim dividend

The Board has decided to increase the interim dividend by 7.1% to 5.25p from 4.90p. Although the reported earnings cover for our dividends has been depressed by the trading conditions and the implementation of our investment programmes, the Group's liquidity position and cash generation remain strong. The Board's dividend decisions are based on all these factors together with its assessment of the Group's growth opportunities.

Current trading

Sales per day across our major markets improved in September and October and are now at similar levels to those at the beginning of the financial year. Japan has shown a distinct increase in sales per day over this period. Year on year monthly sales declines in September and October have been lower than in previous months, but the comparison is influenced by the disruption after the 11 September tragedy last year.

Management continues to be focused on achieving sales improvements driven by our own actions, enhancing gross margins and controlling costs. We are targeting sectors outside our traditional manufacturing heartland in all our major markets and the results are encouraging. These sectors provide considerable long term growth opportunities. Incremental benefits from the e-Commerce investments are now being achieved and are being driven harder. Our warehouse moves and the start of major systems implementations are positive developments to improve future efficiencies which will incur one-off costs of around £2m over the coming months.

Recent leading indicators such as the Purchasing Managers Indices suggest continued weak markets. We do not anticipate improvement in trading conditions in the short term, but nor do we anticipate further deterioration. Our businesses remain well positioned to respond rapidly when the recovery happens and I remain very confident about the medium and long term growth prospects of the Group.

Bob Lawson

Bob Lawson, Chairman, 6 November 2002