The Morgan Crucible Company plc
Annual Report 2009

# The advanced materials group


# Morgan Crucible is a world leader in advanced materials.

## Our highly skilled, dynamic people provide high-technology solutions for specialised applications in selected global markets.

## A look at some of our markets...

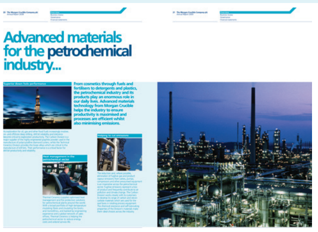
### Aerospace P06


### Defence and protection P10


### Power generation P12


### Medical P16


### Petrochemical P20




### Metals P24


**Overview**



**Business review**



**Governance**



**Financial statements**

# Operational and financial highlights

- Revenue for the year grew to £942.6 million, up 12.9% on the previous year.
- Group EBITA* was £89.0 million, delivering a margin of 9.4%.
- Net cash flow from operations increased substantially to £134.5 million, 21% up on the previous year.
- Final dividend maintained at last year's level of 4.5 pence, giving a full-year dividend of 7.0 pence.

**Revenue**
Continuing businesses £m


**Group EBITA***
Continuing businesses £m


**Group EBITA margin***
Continuing businesses %


**Underlying earnings per share****
Pence


* Defined as operating profit before restructuring costs, other one-off items and amortisation of intangible assets.
** Defined as basic earnings per share adjusted to exclude amortisation of intangible assets.

# Morgan Crucible at a glance

Morgan Crucible is a global advanced materials company listed on the London Stock Exchange. The Group's products and services help make the world safer, healthier and more efficient. Morgan Crucible employs some 9,400 people around the world and has operating sites in 34 countries serving customers in over 100 countries. Its three Divisions have leading positions in their target niches in the aerospace, defence and protection, power generation, medical, petrochemical and iron and steel markets.

## Our Divisions

### Carbon Division

The Carbon Division is a global provider of advanced materials technology with extensive expertise in the processing and application of carbon, graphite, silicon carbide, oxide ceramics and related materials. This includes advanced composite technology developed within the ballistic protection business. Working at the forefront of materials technology, the Division is a world leader in the development of value-added customer solutions through engineering innovation and an understanding of industry-specific needs, opportunities and challenges. The Division has sites in 25 countries, and employs some 3,400 people worldwide.

**Core products/applications:**
- Electrical brushes
- Seals and bearings
- Protective ballistic armour
- Ultra high-temperature insulation

### Technical Ceramics Division

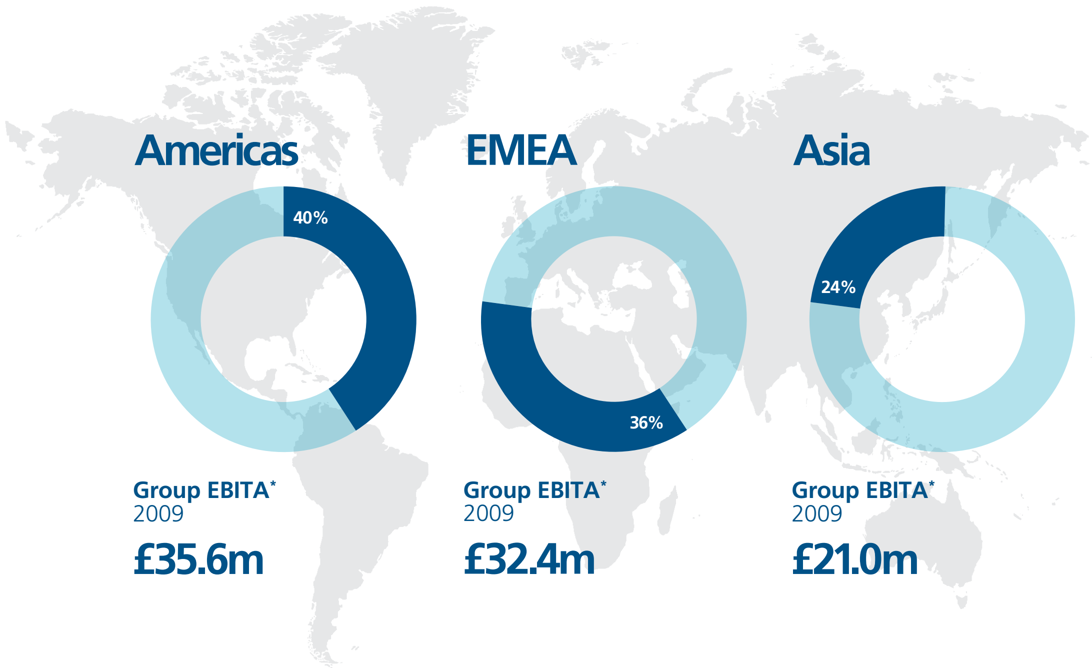
The Technical Ceramics Division utilises advanced ceramic, glass, precious metals, piezoelectric and dielectric materials combined with innovative design and applications engineering to provide an extensive range of ceramic components, assemblies and related products for niche technological applications in selected markets. In many applications, the technology provided by Technical Ceramics defines the performance of the customer's end product. The Division is a world leader in its target markets with sites in 6 countries around the world, employing some 2,600 people.

**Core products/applications:**
- Ceramic cores for complex turbine blades
- Components for electron tubes
- Feedthroughs for medical implants
- Piezoelectric ceramic actuators

### Insulating Ceramics Division

The Insulating Ceramics Division designs, manufactures and installs a wide variety of engineered solutions from its range of world-renowned advanced insulation and thermal management products. These solutions help customers to protect equipment and personnel and to reduce energy consumption in their processes and, in many applications, reduce emissions to the environment. The Division is a world leader in the production of insulating fibre, insulating fire bricks, monolithics and crucibles, with sites in over 30 countries around the world and employing more than 3,400 people.

**Core products/applications:**
- Engineered thermal management solutions
- High-temperature insulating fibres
- High-temperature insulating fire bricks
- Monolithics
- Crucibles and furnaces




**Target markets:**
- Defence and protection
- Electrical current transfer systems
- Fluid handling
- Power generation
- Semiconductor processing

**Carbon revenue** £

# 391.4m

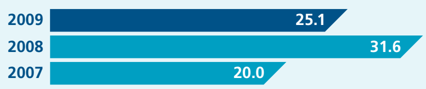
**Divisional EBITA****
Continuing businesses £m


**Target markets:**
- Aerospace
- Medical
- Industrial equipment
- Power generation
- Electronics

**Technical Ceramics revenue** £

# 206.0m

**Divisional EBITA****
Continuing businesses £m

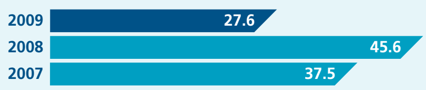



**Target markets:**
- Metals/Iron and steel
- Petrochemical
- Fire protection
- Ceramics
- Power generation

**Insulating Ceramics revenue** £

# 345.2m

**Divisional EBITA****
Continuing businesses £m




* Operating profit before restructuring costs, other one-off items and amortisation of intangible assets.
** Defined as segment operating profit before restructuring costs, other one-off items and amortisation of intangible assets.

# Chief Executive Officer's strategic overview

**Mark Robertshaw**
Chief Executive Officer

Our strategy of reducing our exposure to economically cyclical markets has delivered resilient results in 2009 against the challenging background of the major global downturn.

**2003**
Morgan Crucible announces a three-year profit improvement programme as a result of a strategic review, which identifies substantial opportunities to transform the Group and generate improved performance.

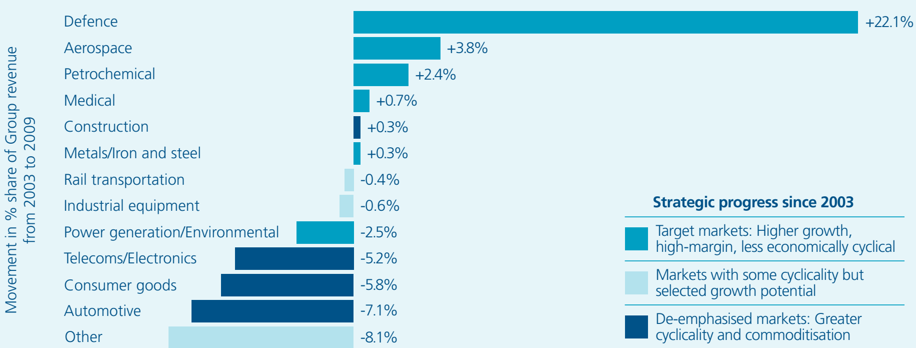
**2004**
Disposal of the Auto and Consumer business completed in June, as part of the Group's strategy of disposing of non-core businesses and to simplify and focus the Group's structure.

**2005**
Magnetics Division disposal completed in September, continuing the transformation of Morgan Crucible into a more simplified and focused Group.

**2006**
Businesses continue to refocus their organic growth plans towards higher margin, less economically cyclical markets.

**2007**
Morgan Crucible acquires a 49% equity stake in NP Aerospace, a composite technical moulding business in key higher margin, non-economically cyclical defence and medical markets.

## End-market mix change since 2003



# The next stage

**2008**
Acquisition of the Technical Ceramics businesses of the Carpenter Technology Corporation to increase the Group's presence in higher margin, higher growth sectors of the aerospace and power generation markets.

**2009**
Morgan Crucible increases its equity stake in NP Aerospace to 60% in January, becoming a majority shareholder and allowing the results of NP Aerospace to be fully consolidated for the first time.

**2010 and beyond**
Continued focus on providing differentiated advanced materials to high-value, non-economically cyclical markets.

## Our vision

→ Our vision is to be one of the world's very best advanced materials companies

## Our aim

→ Our aim is to create long-term sustainable shareholder value

## Strategic priorities

→ Focus on higher growth, higher margin, non-economically cyclical markets

→ Be high value-added to our customers

→ Have a culture of operational excellence and cost efficiency

→ Be number one or number two in our chosen market segments

→ Find, keep and develop the right people

# At the leading edge of aerospace...

## With the rapid development of increasingly complex aerospace technology, our customers are demanding more from the materials they use. In Morgan Crucible they have a partner who can help them respond to the pace of change.

### Innovative materials for the aerospace industry

Advanced materials technology from Morgan Crucible is used throughout many modern aircraft, including in guidance and satellite positioning systems, ignition systems, fire protection and suppression, instrument displays and engine monitoring. For example, the Technical Ceramics Division's seals, thermocouples and feedthroughs are ideal for aerospace applications due to their ability to withstand the high temperatures, vibration and mechanical shock experienced in aircraft engines and other high-stress locations.

### Enhancing aerospace production processes

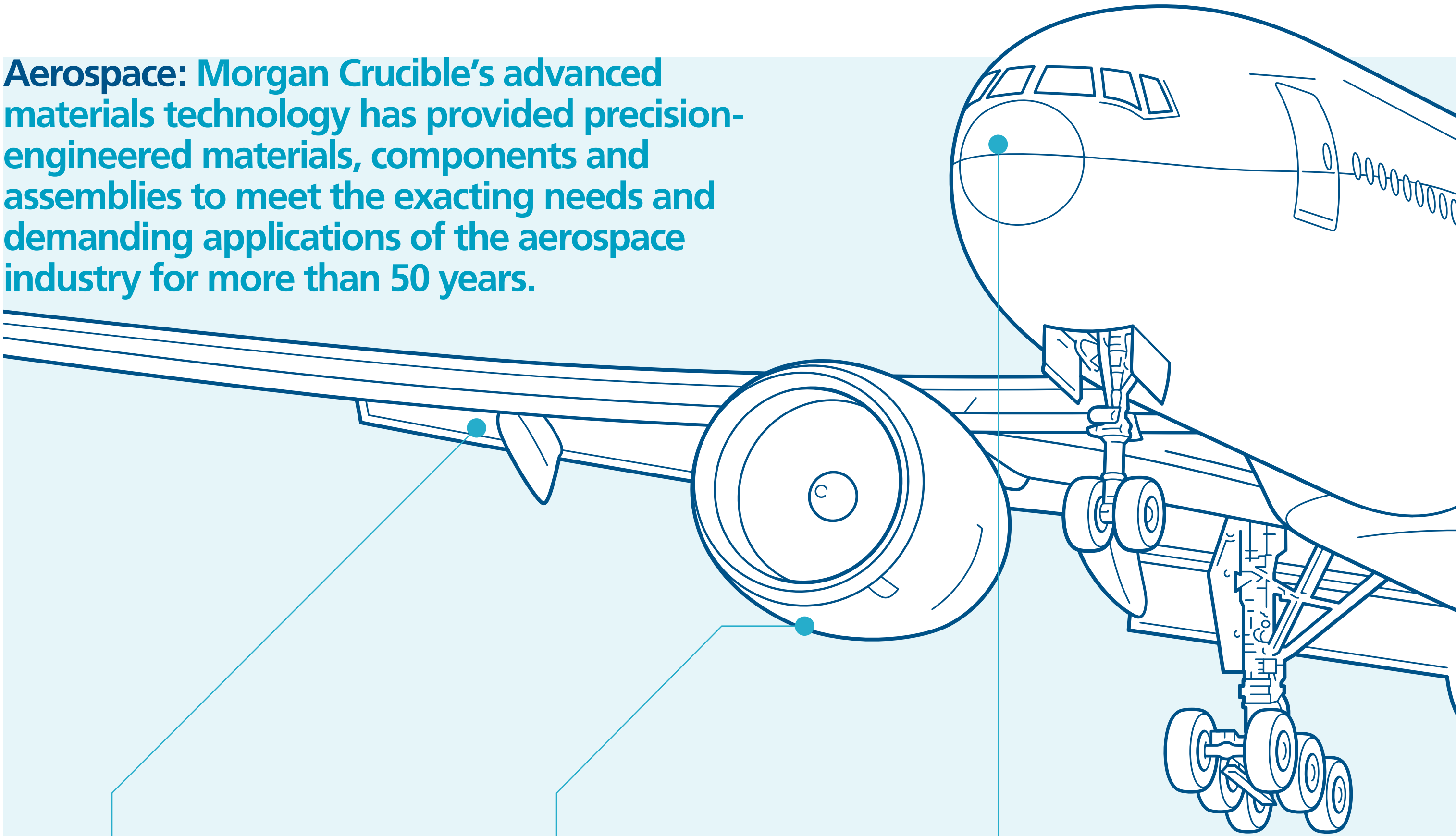
Morgan Crucible is helping to make aerospace production processes more efficient and safer. For example Thermal Ceramics is working with a leading UK investment casting company to develop single use bio-soluble mould wrap insulation for casting the turbine blades for many civilian and military aircraft. This is based on our Superwool 607HT™ and is critical to ensure that the nickel-based super-alloy blades develop the right crystal structures as they are gradually cooled from 1,600°C to room temperature.

### Long life and high-altitude performance

Through the Carbon Division's advanced engineering, an innovative carbon material has been developed to transfer electrical current between stationary wires and moving parts in low-humidity environments at high altitude and in space. Used to transfer the high current loads required by starter generators on fixed and rotary wing aircraft, the material offers longer life with no compromise on performance, thereby helping to reduce maintenance requirements and associated operating costs.

# ...providing performance-enhancing components.

**Aerospace:** Morgan Crucible's advanced materials technology has provided precision-engineered materials, components and assemblies to meet the exacting needs and demanding applications of the aerospace industry for more than 50 years.

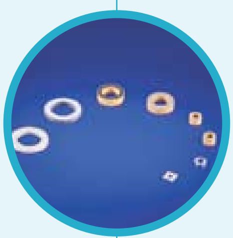


### Measuring aircraft fuel consumption

Technical Ceramics' piezoceramic materials are used in ultrasonic fuel level sensors to provide highly accurate readings regardless of the orientation of the aircraft. Each Boeing 777 has over 50 fuel level sensors.

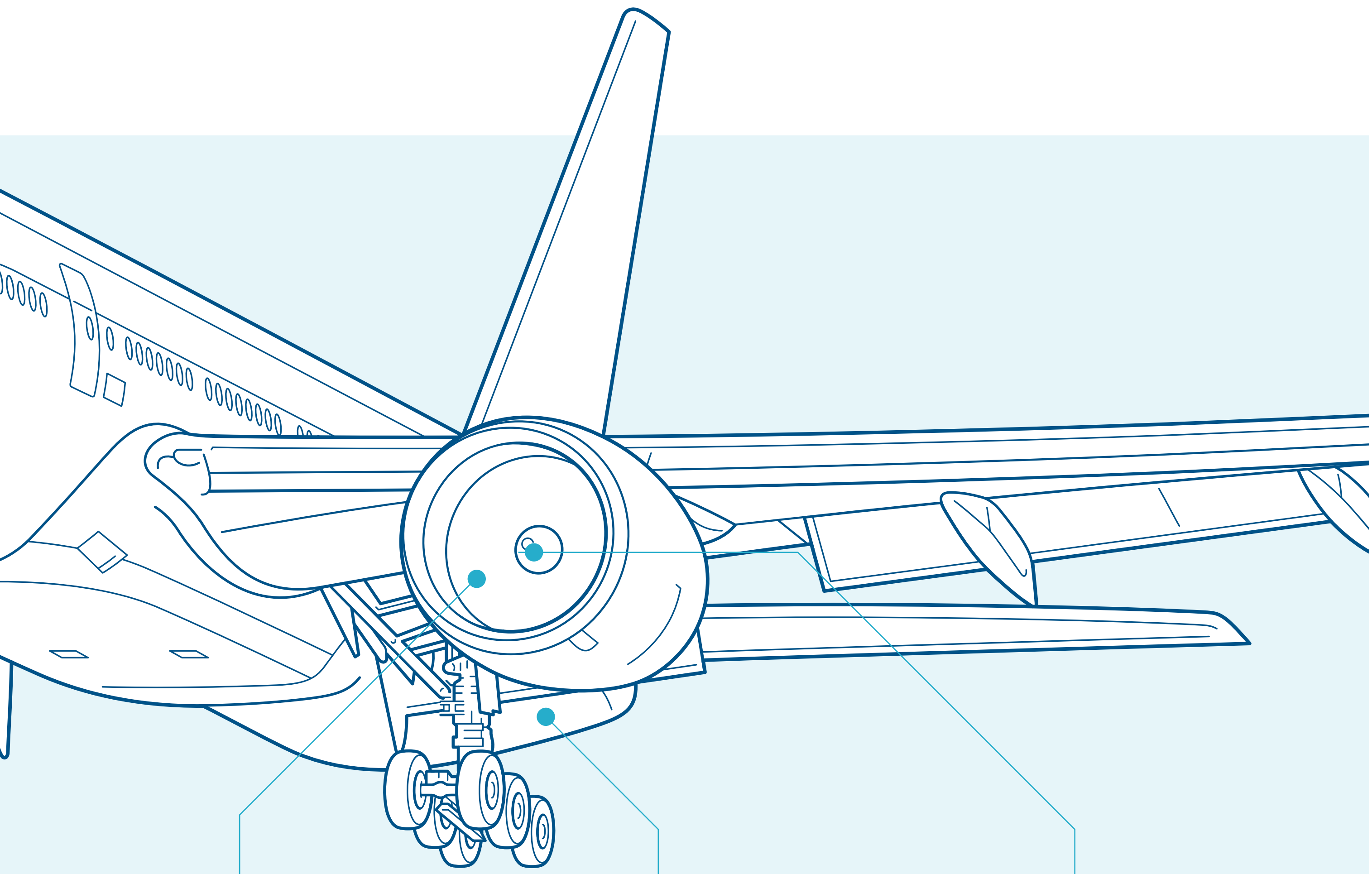
### Reverse thruster insulation

Thermal Ceramics provides flexible Min-K™ insulation which protects the reverse thrusters from hot exhaust gases. The thrusters help the aeroplane decelerate once it has touched down, helping cut landing distances and reducing wear on the brakes and other components.



### Aircraft instrumentation

Technical Ceramics' piezoelectric and dielectric ceramic materials are used in the accelerometers and gyroscopes which measure the acceleration, vibration and pitch of the aircraft.



### Quieter and more efficient engines

Technical Ceramics uses its proprietary materials and injection moulding processes to make the ceramic cores which enable turbine blades to be cast with an intricate network of cooling channels. These cooling channels allow aircraft engines to run at higher temperatures, which makes them quieter and more efficient.

### High-temperature insulation for flight data recorders

Thermal Ceramics provides the moulded Min-K™ high-temperature thermal protection which helps safeguard the data recorder's memory boards in the event of a post-accident fire.

### Improving engine efficiency

The Carbon Division's materials are invaluable in the seals which protect the main shaft bearings and the lubrication system from the hot combustion gases in the high-speed, high-temperature environment of modern aircraft engines.

# High-technology defence and protection solutions.

**Our materials technology, ballistic expertise and integration capabilities help protect customers in defence, police and civilian applications from new and increasing threats. With particular focus on personnel protection, Morgan Crucible is a leader in the advanced materials used in body armour, helmets and protective vehicles.**

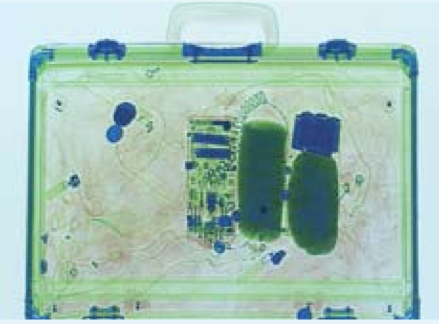
## NP Aerospace/Force Protection joint venture

Integrated Survivability Technologies is a joint venture formed to offer speed of response and flexibility in the increasingly important market for vehicle protection systems. The Wolfhound – a highly protected tactical support vehicle which will transport general stores, food and water in high-threat areas – is the first vehicle to benefit from this approach, providing the customer with a truly integrated product offering and the ability to tailor vehicle solutions to customer needs.

## Marine fire protection

Fire safety and damage limitation are key considerations in the design of coastal protection and naval ships worldwide. Lightweight but heavy-duty fire protection products are increasingly used, sometimes with the need to withstand much higher fire temperatures than are specified for commercial vessels. Thermal Ceramics' FireMaster™ systems fulfil the requirement for efficient fire insulation solutions in this, one of the most demanding marine operating sectors.

## Security scanners



The superior dielectric properties and high mechanical stability of Technical Ceramics' metallised alumina ceramics enable security scanners to operate with higher accelerating voltages. As a result our customers can build smaller x-ray tubes, with a much better resolution, for luggage, cargo and parcel inspection around the globe.

# Performance in power generation and renewable energy...

## New and advancing technology is making electricity production and transmission more efficient and, in the case of renewables, increasingly cost efficient.

### Customised technology for wind power

Wind turbines are often located in hostile environments around the world and in many cases this makes maintenance a difficult and costly task. The Carbon Division is leveraging its advanced materials capabilities to tailor its portfolio of wind power technologies according to climate. Using customised materials helps to increase maintenance intervals, making wind power an environmentally friendly, more economic alternative to standard electricity generation processes.

### Thermal solutions in power generation

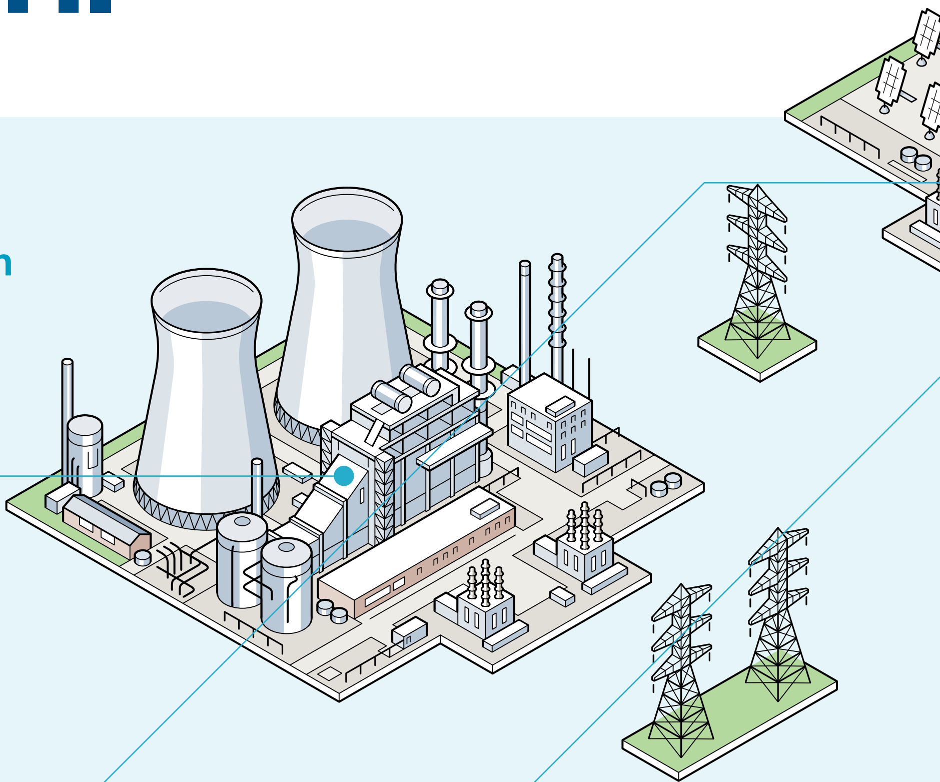
Rising fuel costs and the escalating demand for electricity is increasing the focus on technology to enhance efficiency. Thermal Ceramics has developed advanced insulation solutions to help reduce heat losses in power generation using its Superwool™ low-bio-persistence, high-temperature insulating fibre and its insulating fire bricks and monolithics. The Division plays a key role in helping leading electricity generators around the world to reduce the amount of energy consumed per unit of electricity generated.

### Enabling reliable power generation

Whether electricity is generated from gas, coal, oil, wind, water or nuclear energy, carbon materials are used to transfer current between moving and stationary points. The indispensable nature of our materials technology means that most power stations worldwide depend on products from the Carbon Division to transfer electrical current safely and effectively from their generators to the distribution grid.

# ...leading to more sustainable power generation.

**Power generation:** Morgan Crucible's advanced materials technologies are extensively used across the power generation sector. Our products are key to enhancing the sustainability of traditional generation and to enabling electricity to be produced from new and renewable sources.



### Boosting efficiency in power generation

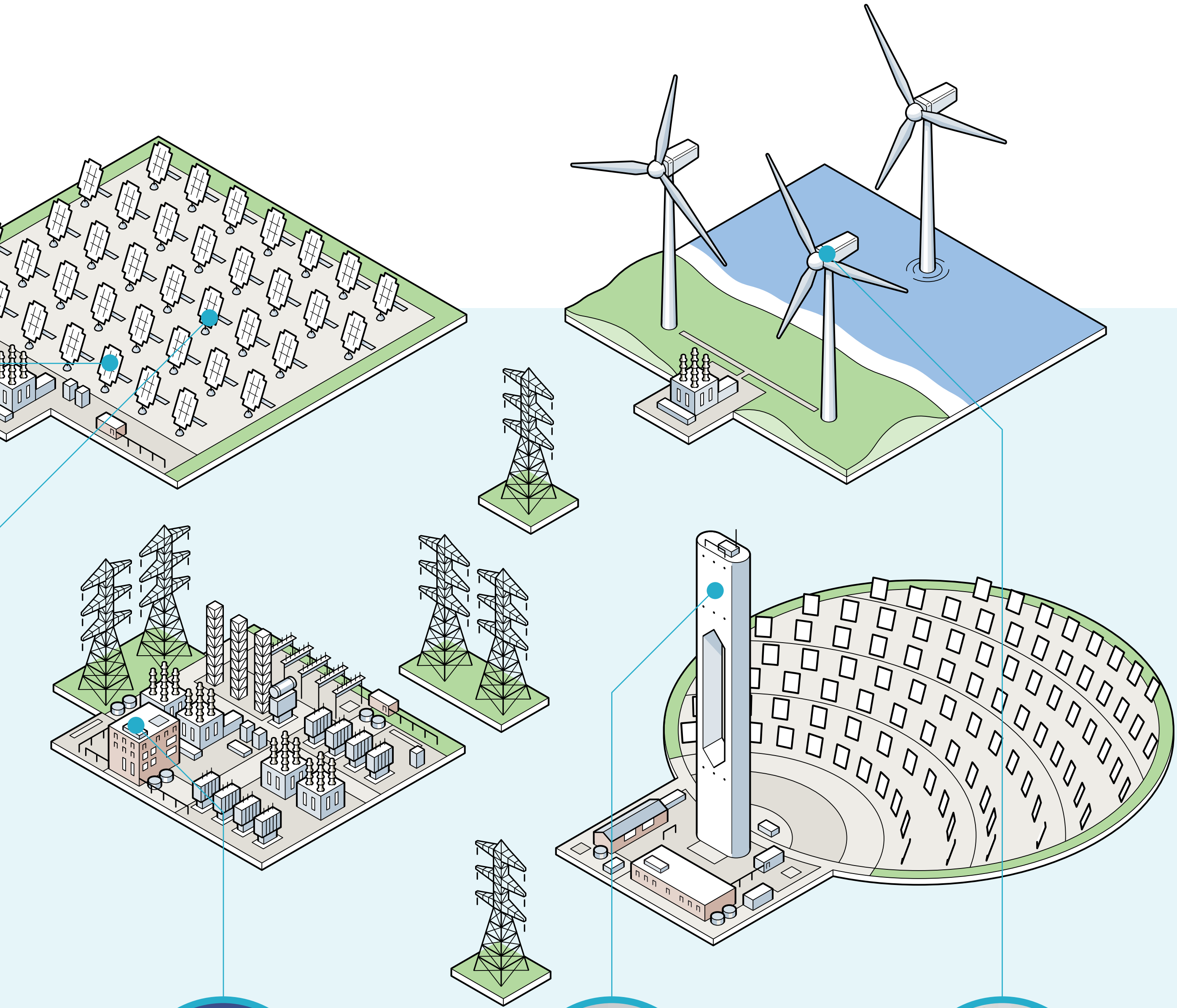
Thermal Ceramics' Superwool™ insulating fibre offers high-temperature resistance and low bio-persistence. It is seen as the preferred solution for duct and boiler insulation in heat recovery steam generator systems which can help boost power station efficiency by 35%.

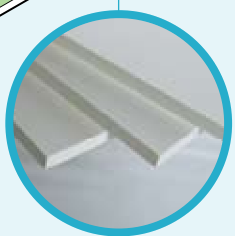
### Photovoltaic cells – towards grid parity

The Technical Ceramics Division is leveraging the outstanding mechanical properties and special surface quality of its fused silica roller technology to help manufacturers of thin-film photovoltaic cells to enhance efficiency and cut costs, bringing grid parity for renewable power ever closer.

### Enhancing photovoltaic cell performance

The Carbon Division is a world leader in advanced carbon/graphite-based solutions for the solar industry. These are highly engineered from hybrid materials to provide polysilicon and crystalline silicon manufacturers with the benefits of energy efficient production and enhanced photovoltaic cell performance.





## Reliability in power transmission

The Technical Ceramics Division's ceramic capacitors are used in the systems which remotely indicate when an electrical transmission line fails. These 'live-line' capacitors are used all over the world in onerous service conditions to ensure electrical integrity and long service life.

## Power tower – solar thermal electricity

Concentrated solar power focuses vast amounts of solar energy to harvest heat energy from the sun to generate electricity. Thermal Ceramics supplies multiple high-performance insulation products to protect the tower and preserve the stored heat energy.

## Harvesting the wind – reliable wind power generation

The Carbon Division supplies slip ring transmitters and rotating current transfer systems, three-phase generator slip rings and environment-specific brush-holders for high current transmission in the harsh environments experienced by wind farms around the world.

# Technical expertise for medical applications...

# With the growing pace of scientific discovery, developments in health and wellbeing are increasingly technology-led. Morgan Crucible is leveraging its advanced materials and manufacturing technologies to help deliver innovations in healthcare.

## Medical fire protection

The complexity of modern hospitals necessitates specialist fire protection solutions. These help contain a fire to the room of origin and protect people, equipment and the building. Thermal Ceramics fire protection products were used in the construction of the new 835,000ft² Columbia St Mary's Hospital, Milwaukee, WI, USA.

## Manufacturing and materials technology combined

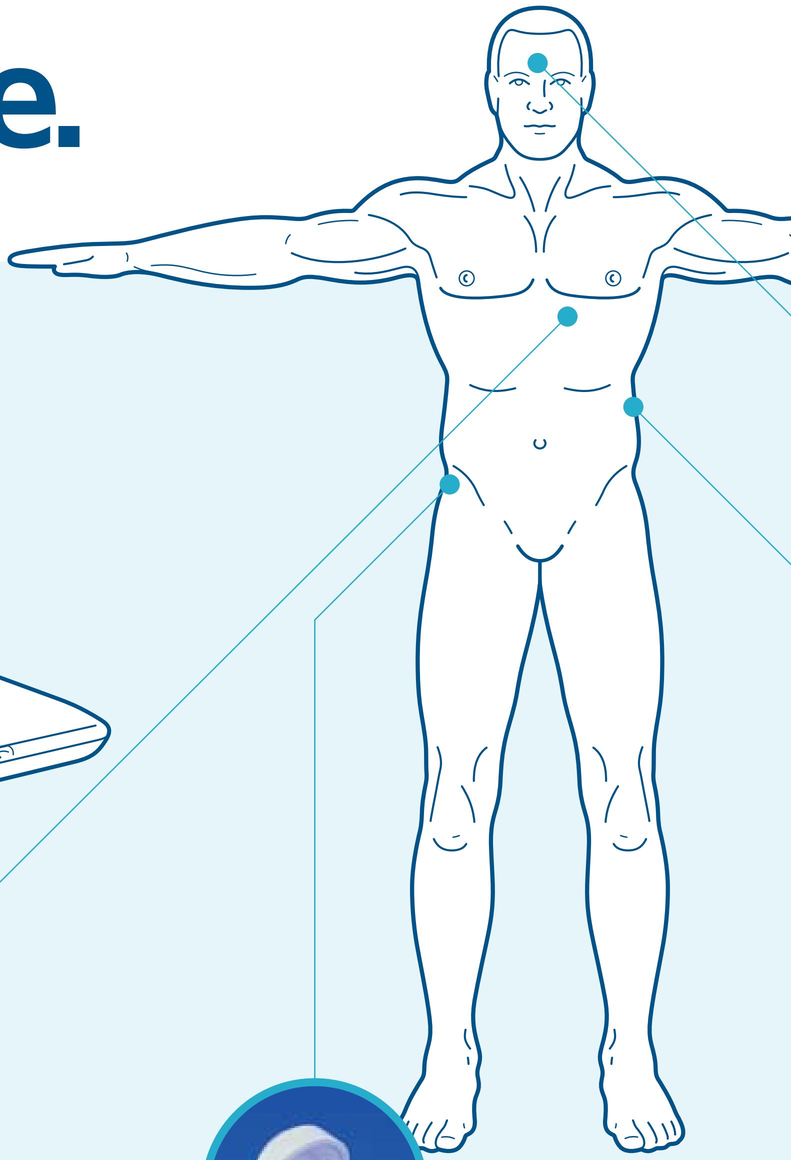
The Technical Ceramics Division combines world-leading ceramic injection moulding capabilities, ISO 13485-certified manufacturing facilities and advanced materials technology to offer medical innovators and practitioners the biocompatibility, repeatability and reliability required for human body implants and medical applications. For example, the Division has achieved ISO 13356:2008 'Implants for surgery using non-metallic materials' compliance for its Y-ZTP Zirconia material used in the manufacture of dental abutments and copings.

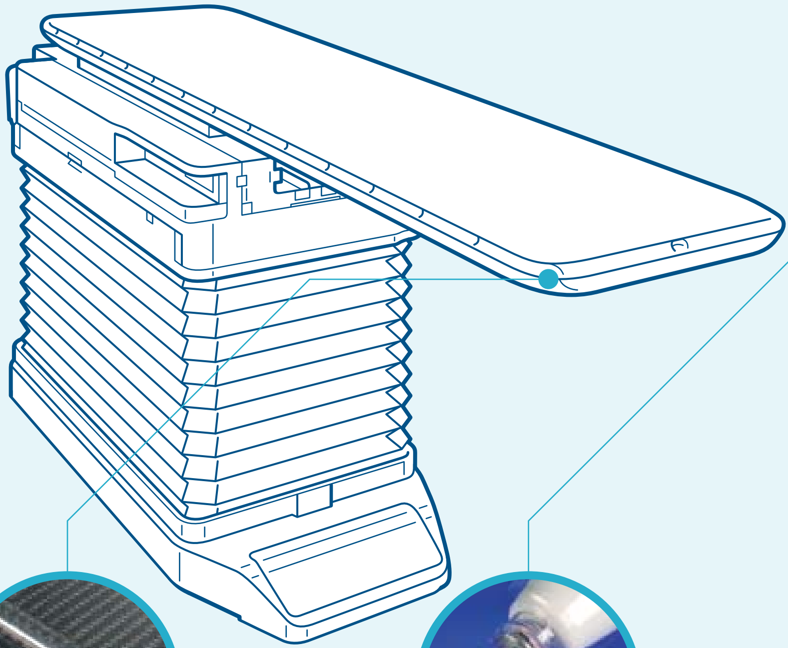
## More precise and predictable ultrasound transducers

Technical Ceramics' piezoelectric materials produce a voltage proportional to applied mechanical pressure and, conversely, if a voltage is applied they change shape. Technical Ceramics uses these advanced materials to dramatically improve the performance of ultrasound transducers in medical applications, including sensors for catheters, blood pressure, vascular flow and medical imaging.

# ...helping to improve quality of life.

**Medical:** Advanced materials and manufacturing techniques developed by Morgan Crucible serve critical functions in medical diagnosis and therapeutic processes.





### Precise imaging – replacing metals with advanced composites

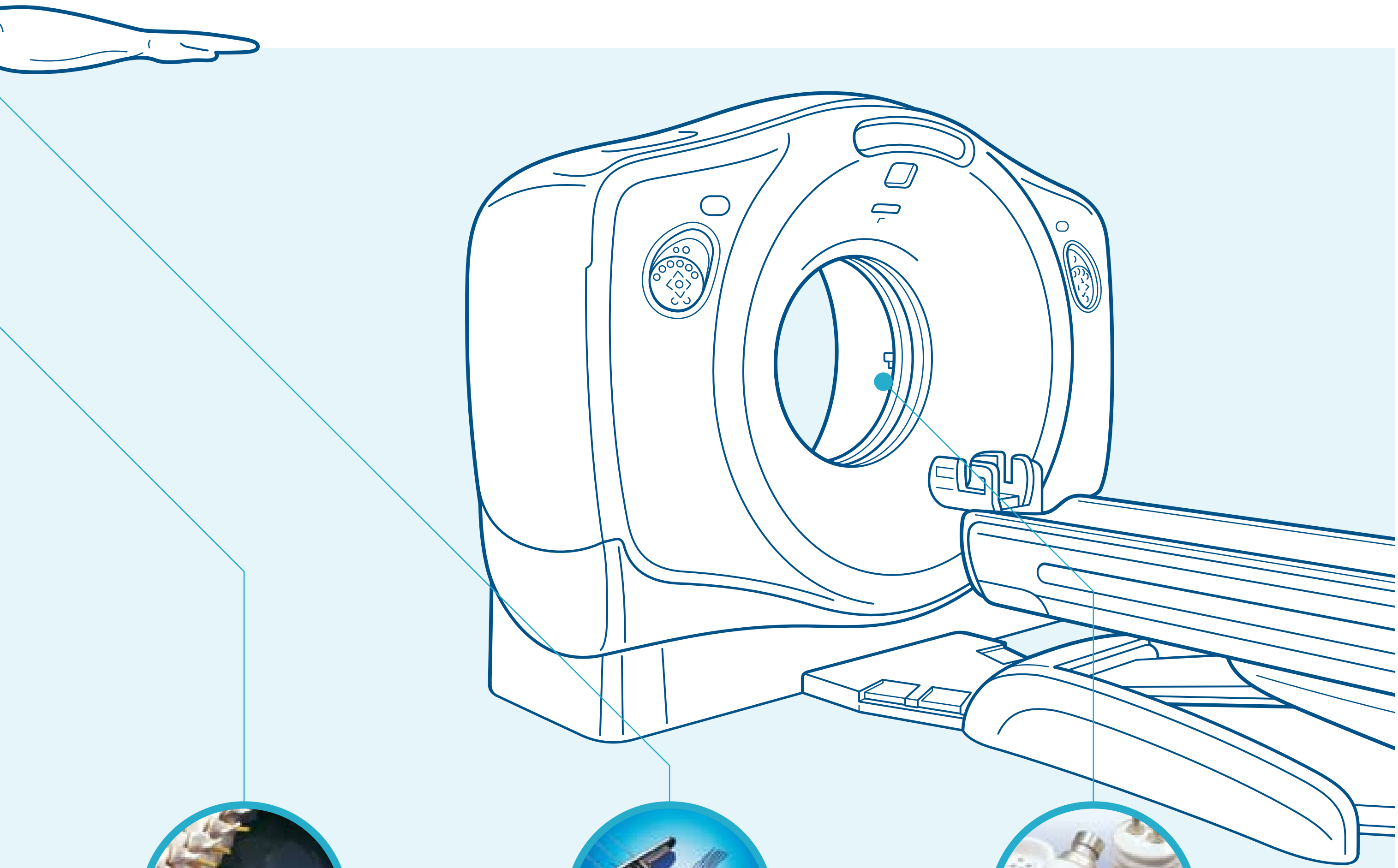
By replacing metal x-ray treatment couch components with advanced composites, NP Aerospace helps ensure patients are positioned correctly for treatment whilst also facilitating higher image quality and lower x-ray doses.

### Blood handling

Multiple products from the Technical Ceramics Division are used in critical blood handling applications. These include seals for automated blood collection devices, Diamonex™ coated valves and bearing surfaces, custom-developed ultrasonic sensors to detect air bubbles in the blood flow and pressure sensors to detect occlusions.

### Hip joints – helping restore quality of life

The Technical Ceramics Division has developed Vitox™ AMC, an alumina matrix composite material for surgically implanted devices, including hip joints. It can be used to manufacture femoral heads with diameters close to that of a natural joint and for thinner wall section acetabular cups. This offers recipients a wider range of motion and a reduced risk of dislocation.



## Orthopaedic implants

The Technical Ceramics Division is leveraging its experience in hip joints to offer other surgical implants using Vitox™ and Zyranox™ Zirconia bioceramic materials. Our spinal devices offer faster bone fusion, no allograft or autologous bone graft, anterior and posterior operative procedures and optimum biomechanical stability.

## Treatment through neurostimulation

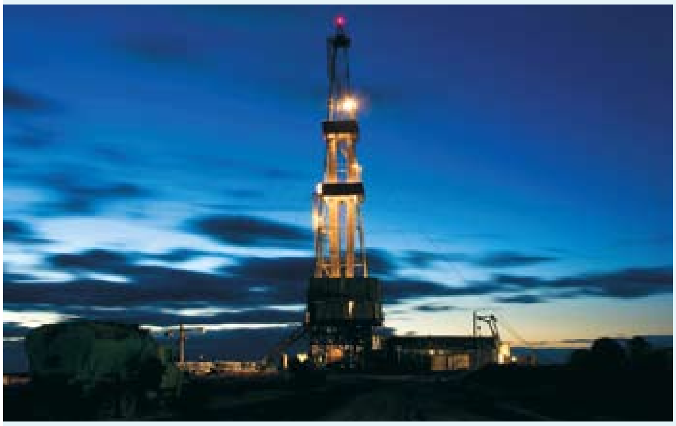
Advanced ceramics are making innovative treatment methods possible. Ceramic-to-metal brazed feedthroughs from Technical Ceramics provide the electrical connection needed to communicate with neurostimulators that pulse various nerves for pain management and to treat epilepsy, depression, migraine and other conditions.

## Ceramics at the heart of a scanner

Ceramic assemblies and components from the Technical Ceramics Division are critical in demanding diagnostic applications including computed tomography scanning equipment and x-ray machines for mammography. It is the design, material purity and quality of the ceramic components that defines the quality of the diagnostic images.

# Advanced materials for the petrochemical industry...

## Superior down-hole performance



As exploration for oil, gas and other fossil fuels increasingly involves on- and offshore deep drilling, drill bit reliability and tolerance become critical to exploration productivity. The Carbon Division is a major supplier of the highly engineered graphite powder used in the manufacture of polycrystalline diamond cutters, whilst the Technical Ceramics Division provides the braze alloys which are critical to the manufacture of drill bits. Their performance is a critical factor for drill bit productivity and reliability.

**From cosmetics through fuels and fertilisers to detergents and plastics, the petrochemical industry and its products play an enormous role in our daily lives. Advanced materials technology from Morgan Crucible helps the industry to ensure productivity is maximised and processes are efficient whilst also minimising emissions.**

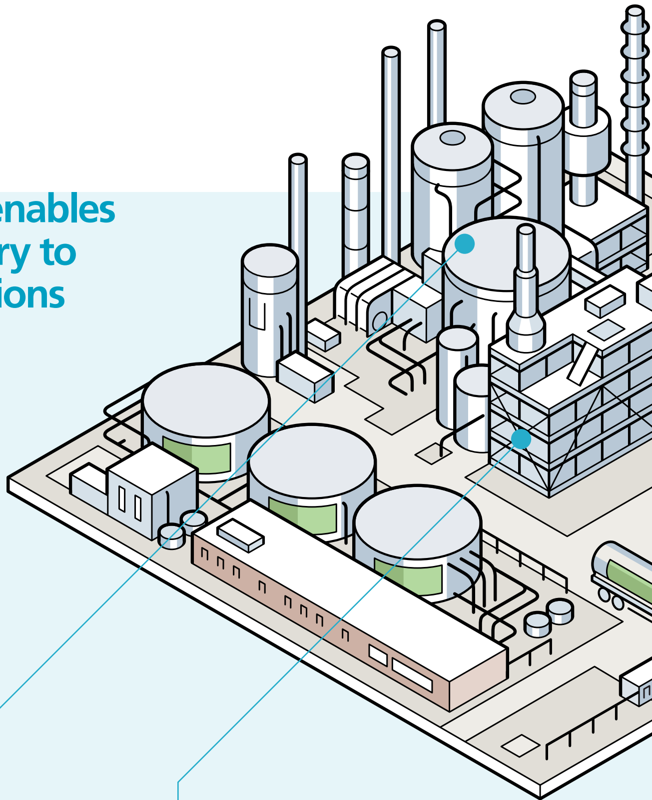
## Heat management in the petrochemical sector

Thermal Ceramics supplies optimised heat management and fire protection solutions for petrochemical plants around the world. With a broad portfolio of high-temperature insulating fibres and insulating fire bricks and monolithics, and backed by engineering experience and a global network of sales offices, Thermal Ceramics is helping the petrochemical sector to reduce energy costs and extend service life.

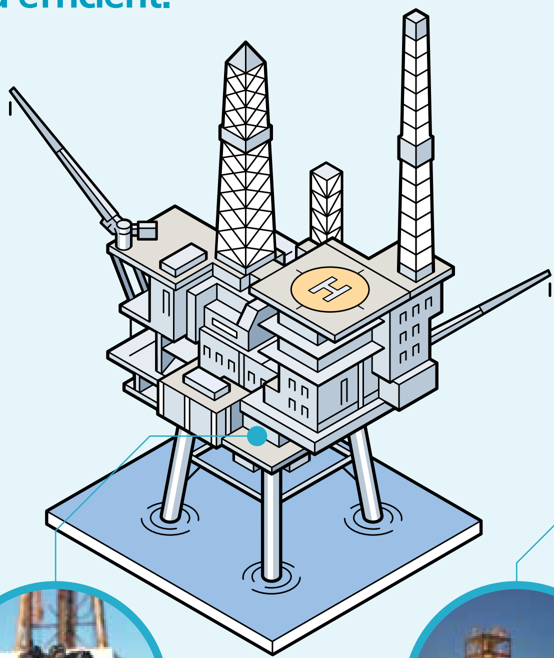
## Helping to cut emissions

The reduction and, where possible, elimination of fugitive gas and product vapour emissions from valves, pumps, compressors and other pressurised equipment is an imperative across the petrochemical sector. Fugitive emissions represent a loss of product and frequently contribute to air pollution and climate change. The Carbon Division works closely with its customers to develop its range of carbon and silicon carbide materials which are used for the seal faces in rotating process equipment. The chemical resistance and self-lubricating properties of the Division's materials make them ideal choices across the industry.

# ...enabling greater performance and efficiency.



**Petrochemicals:** Morgan Crucible's global spread enables customers in the worldwide petrochemical industry to access our leading materials technology and solutions to help them reduce energy consumption in their processes and to make them more reliable and efficient.



## Drill bit performance

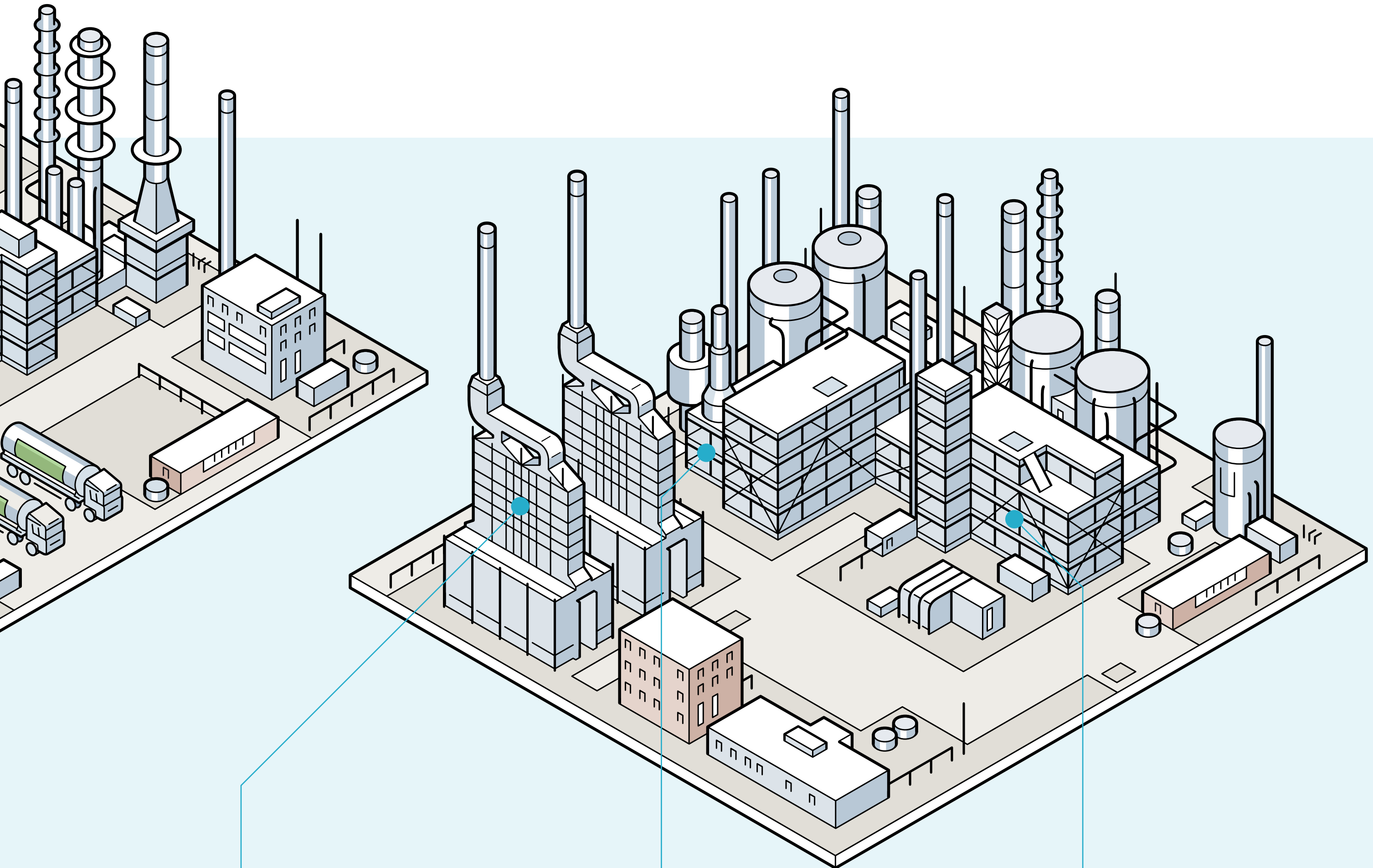
In partnership with its customers, the Technical Ceramics Division has developed a proprietary process for the production of the high-strength, high-purity brazing alloys used in highly specialised drill bits, offering superior down-hole performance, increased tool life and enhanced productivity.

## Rugged fluid handling

Carbon-graphites and silicon carbides are used extensively in pump sealing applications. The sealing challenge increases as refiners process contaminated and abrasive-laden oil. Silicon carbide and other seal materials developed by the Carbon Division are at the heart of high-temperature, high-pressure sealing systems in refineries worldwide.

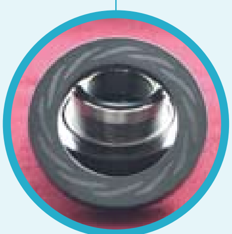
## Fire protection in the petrochemical sector

A fire in a refinery can quickly spiral out of control with disastrous consequences. The destruction of instrumentation and control cabling can prevent the refinery from being shut down, making the fire worse. Thermal Ceramics' FireMaster™ system protects cables, helping maintain control in an emergency situation.



## Enhanced efficiency ethylene cracking

The steam cracking process is the most energy-consuming process in the chemical industry. Thermal Ceramics is working with ethylene cracking technology providers to improve the energy efficiency of their designs, offering solutions from our range of insulating fire bricks and high-temperature insulating fibre.



## Self-lubricating sealing materials

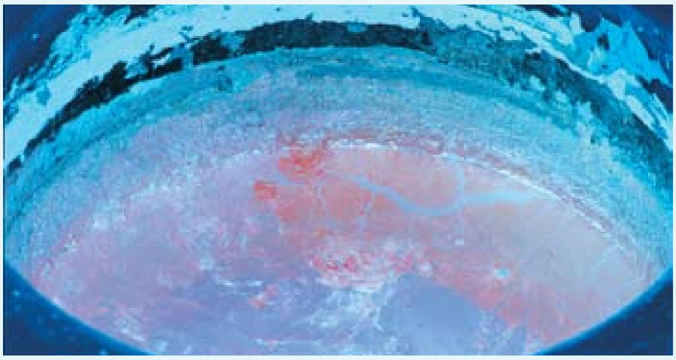
Fluid handling pumps and compressors are key to the operation of a chemical plant. Leading pump and seal manufacturers around the world depend on the self-lubricating properties of the Carbon Division's axial face seal materials to help increase maintenance intervals and to increase productivity.

## Temperature measurement

Thermocouple tubes from the Technical Ceramics Divison are made from specialist ceramics, custom designed and up to 3.9 metres long. They enable the accurate and fast measurement of temperatures of up to 2,000°C in the aggressive and rapidly changing environment of chemical processing.

# Market-leading solutions for the global metals industry...

## Speciality carbon and graphite in the metallurgical industries



The unique properties of carbon and graphite are fundamental to the efficiency and performance of the metals industry. As well as comprehensive engineering support, the Carbon Division provides a wide range of technically advanced products to aluminium processors, including graphite flux tubes and degassing rotors for purification, Permacast™ rings for semi-continuous casting and multiple components used in slab casting. These are enhanced as required with the Division's proprietary impermeable coating systems or anti-oxidation treatments.

## Energy-conserving refractory solutions

Thermal Ceramics provides thermal management solutions to help the metals industry control product quality and conserve energy. Focused on high-temperature applications, world-leading product performance is combined with engineered refractory solutions for the complete metal-making process. Monolithic Higun™ is used in blast furnaces, Pyro-Bloc™ in reheating and heat treatment furnaces, Tri-Mor™ Plascast for lining walls and arches and Tri-Mor Hicast™ Extra insulating fire bricks and Morflo™ for hearth and reheating furnaces.

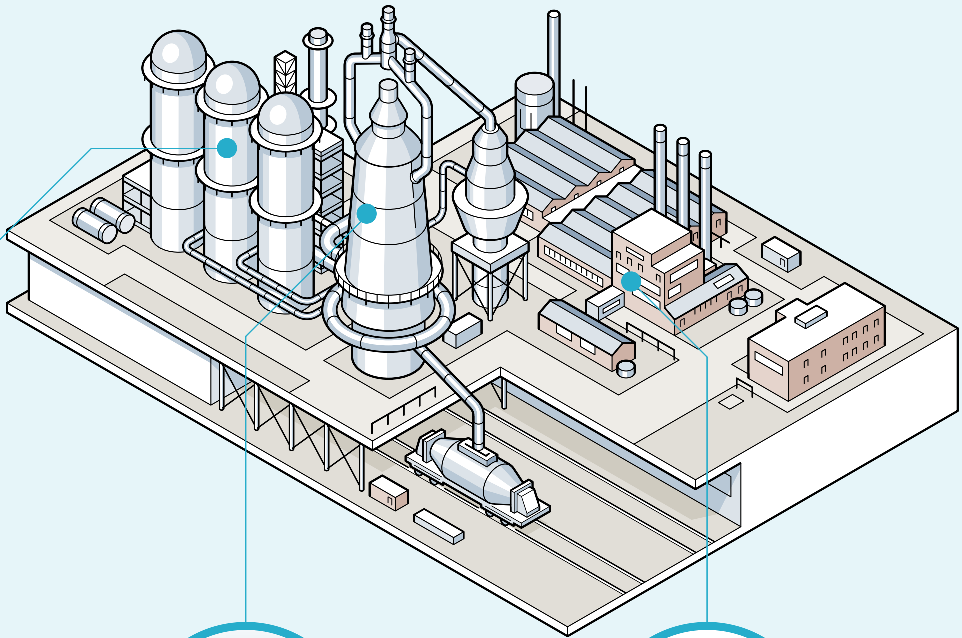
**Around the world the metals industry is investing to reduce its environmental footprint, particularly in relation to energy use and associated $CO_2$ emissions. Morgan Crucible offers a comprehensive range of advanced engineered solutions to help.**

## Efficient furnaces for quality casting


Ajax X-Ray Inc is a specialist non-ferrous casting manufacturer with 40 years of experience. Keen to enhance competitiveness and to reduce emissions, the company embarked on a programme to replace its existing metal-melting furnaces. Following a competitive evaluation, Ajax X-Ray installed five Morgan Molten Metals Systems Recuperative Bale-Out furnaces at its foundry in Sayre, PA, USA. The recuperative furnaces recycle waste heat and use much less energy to deliver the same rate of metal melt. Nancy Brittain, Ajax X-Ray business manager, commented: "The new furnaces lose so little heat that we may have to start heating the foundry building in winter!"

# ...enhancing efficiency and operational yields in iron and steel.

**Metals:** Morgan Crucible is uniquely positioned technically and geographically to offer a full range of advanced thermal management solutions to the world's iron and steel industries.



## Hot blast stove (Cowpers)

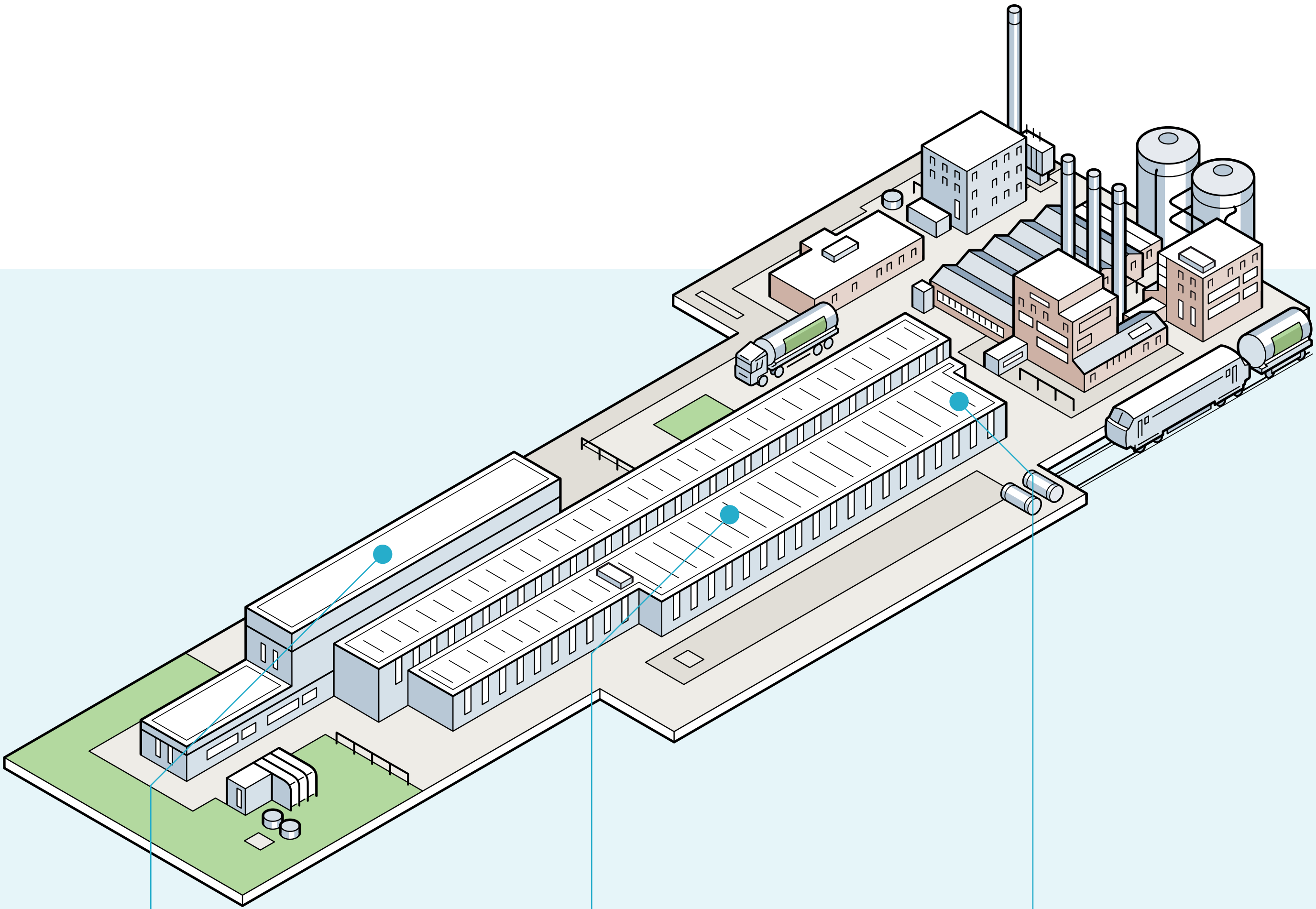
Cowper stoves are critical to blast furnace efficiency. They preheat the blast air to 900-1,300°C and recover heat from the hot gases from the furnace. Thermal Ceramics provides the insulating fire bricks which are essential to the thermal management and reliability of this part of the process.

## Blast furnace

Modern blast furnaces can produce up to 80,000 tonnes of iron per week, requiring large quantities of energy and raw materials. Thermal Ceramics supplies its Monolithic Higun™ to help ensure blast furnace yields, throughput and thermal efficiency are maximised.

## Continuous casting

Continuous casting eliminates multiple steps in the steel-making process by casting the steel into semi-finished shapes. Thermal management and control are key and Thermal Ceramics' range of fibre-based high-temperature insulation boards, vacuum-formed shapes and paper provide solutions.



## Annealing bell furnace

Heating steel sheets, coil, wire and other products to above their recrystallisation temperature in a controlled atmosphere, the annealing furnace ensures the finished steel has a uniform crystal structure and good dynamic properties. Thermal Ceramics' insulating fire bricks and Superwool™ insulating fibre offer the heat management and durability required.

## Galvanising line

Coating steel by hot-dipping it in a bath of molten zinc at 460°C provides it with the corrosion protection needed in multiple consumer, construction and automotive applications. To help ensure the galvanising line is thermally efficient, Thermal Ceramics provides multiple products including insulating fire bricks, insulating fibre and vacuum formed shapes.

## Walking beam furnace

Used for heating slabs of steel up to 250mm thick, the walking beam furnace is a heat-intensive challenge. Leveraging its range of Pyro-Bloc™ modules, Hicast™ Extra, insulating fire bricks and Morflo™, Thermal Ceramics is a leader in heat management for walking beam and other continuous reheating furnaces.

# Taking our responsibilities seriously.

# Corporate responsibility is integral to Morgan Crucible's business. We take the needs and expectations of our key stakeholders into account as we work to implement our five strategic priorities. Our framework of policies, procedures and reporting helps to ensure our approach is consistent worldwide.

## Focus on sustainability

Many of Morgan Crucible's products and services help to improve the sustainability of our customers' operations. For example, Thermal Ceramics' advanced high-temperature insulation solutions dramatically reduce energy consumption and associated emissions in the metals, petrochemical, power generation and other sectors of the economy. Whilst the energy saved by the use of our products may exceed the amount consumed in their production by a wide margin, we cannot be complacent. Internally we continue to work to conserve energy and reduce our carbon footprint in absolute and relative terms. As a result our $CO_2$ emissions intensity was down by 18% over the past two years and we are targeting further reductions in the coming years.

## Science, Engineering & Technology Student of the Year

To help foster the best engineering talent, Morgan Crucible sponsors the annual Science, Engineering & Technology Student of the Year Awards. Morgan Crucible is proud to sponsor this event as we believe it allows high-calibre students to showcase their remarkable research work and demonstrates the capability of graduates in the UK. The 2009 winner of the Best Materials Student award, Michael Robinson from Sheffield University, received his award from Mark Robertshaw, Chief Executive Officer of Morgan Crucible.

## New training centre

A new training centre has been opened at the Carbon Division's site in South Africa, providing greater flexibility to support a range of training initiatives from adult basic education through to production technology qualifications.

# Chairman's statement

**Tim Stevenson**
Chairman

Morgan Crucible has shown real resilience in its performance during the most severe downturn in global industrial production that we have seen in most of our lifetimes.

## Overview

In my Chairman's statement last year I commented that I believed that the Group's strategy of reducing its exposure to economically cyclical, more commoditised markets would stand us in good stead to weather the very difficult economic circumstances that we expected to lie ahead in 2009. The past year has confirmed this view and Morgan Crucible has shown real resilience in its performance during the most severe downturn in global industrial production that we have seen in most of our lifetimes.

The changes to the Group's portfolio in recent years, with the disposal of under-performing and cyclical businesses combined with the acquisition of higher margin, more differentiated businesses, have delivered significant improvements in Morgan Crucible's through-cycle margins.

Specifically, at the beginning of 2009 we acquired a further 11% stake in NP Aerospace, taking the Group's equity holding to 60% and enabling us to consolidate NP Aerospace in Morgan Crucible's financial results. The remaining 40% stake will be acquired in annual tranches of 10% from 2010 to 2013. NP Aerospace's strong business in ballistic armour protection delivered an excellent performance at a time when general industrial markets were significantly depressed. As we look to the future, the goal for your Board is to leverage Morgan Crucible's extensive global footprint to develop opportunities for NP Aerospace beyond its traditional position as a predominantly UK-focused business.

Both NP Aerospace and the technical ceramics businesses acquired in 2008 from the Carpenter Technology Corporation have delivered operating profit margins well

**Dividend per share**
Pence


into double digits in a particularly difficult macroeconomic environment. This, combined with a robust performance from the existing businesses, has helped the Group deliver overall operating profit margins before restructuring and one-off costs of 9.4%.

I am pleased with the results delivered by Morgan Crucible in such a challenging market environment. Group revenues for the year were £942.6 million compared to £835.0 million in 2008. Operating profit before restructuring and one-off items was £89.0 million compared to £108.8 million in 2008, and underlying diluted earnings per share was 12.6 pence (2008: 22.8 pence). From a balance sheet perspective, a strong and consistent focus on cash generation during the year resulted in net debt being reduced from a £290.4 million opening year position to £252.7 million by the year end.

## Dividend

The Group's resilient profit performance and solid cash generation mean that the Board is confident to recommend maintaining a final dividend of 4.5 pence per Ordinary share. This brings the total dividend for the year to 7.0 pence.

## Board

Given the extreme volatility of the market environment, your Board remained very close to the operational performance of the business during 2009. A significant amount of our time was focused on ensuring that the right mitigating actions were taken quickly and decisively in the face of the global industrial downturn to ensure that the cost base remained as closely aligned to revenue demand as possible. This close operational cost base focus was a key factor in delivering the robust profits and margins that were achieved in 2009.

## Outlook

As we look forward, we remain cautious on the outlook for the world economy which we believe still faces a number of challenges and uncertainties as various national stimulus packages are withdrawn. However, encouragingly, in the latter parts of 2009 we did begin to see signs of modest demand recovery in our business, particularly in the Chinese and Indian markets.

Regardless of whether the economic outlook remains depressed or does indeed begin to show recovery in 2010, I am confident that Morgan Crucible is a more resilient, higher quality business that is well equipped to thrive and prosper in the future.

It has been, undeniably, a difficult market environment in 2009. That the Group has prospered during this period and that it is so well positioned for the future is due, of course, to the hard work and commitment of all our employees around the world. The Board is grateful as always for all that they have achieved.

**Tim Stevenson**
Chairman

# Chief Executive Officer's review

**Mark Robertshaw**
Chief Executive Officer

I am extremely proud of what Morgan Crucible has achieved in 2009 against a backdrop of the most difficult market environment for industrial companies for many decades.

## Group results

The Group's well-established strategy of reducing our exposure to economically cyclical, more commoditised markets has served us well. Operating profit margin before restructuring and one-off items in 2009 was a highly creditable 9.4%. The performance of the NP Aerospace business in particular merits highlighting, having achieved stellar results in 2009 with revenues of £186.2 million (compared to £72.0 million in 2008) and operating profit of £28.8 million (compared to £10.7 million in 2008). This is primarily attributable to significant business with the UK Ministry of Defence in providing high-specification vehicle and personal ballistic protection solutions.

Given the challenging market environment, we have kept a tight and rigorous focus on cash generation and on the health of our balance sheet throughout the year. Our five-year banking facilities, which were coming to the end of their term in 2009, were successfully renewed in the first quarter during a period of significant uncertainty for the world's banking system. The fact that we were able to bring two new banks into our syndicate of lenders at a time of such turbulence in financial markets was a very pleasing endorsement of the strength and resilience of your Group. Furthermore, I am pleased to report that we ended 2009 having successfully maintained our position on the key net debt to EBITDA financial covenant at 2.1 times, which is exactly where we were at the end of last year. This is having purchased a further 11% stake in NP Aerospace to move us to a majority equity holding of 60%. We are also in a position of being able to recommend a full-year dividend in line with the prior year.

## Divisional highlights

All of the Group's Divisions have shown pleasing resilience during this period of pronounced global recession, with each delivering sound profit levels in 2009. I have already commented on the excellent performance of NP Aerospace in its maiden set of figures as a majority-owned Morgan Crucible business.

The Technical Ceramics Division also deserves special mention for delivering £25.1 million of Divisional EBITA before restructuring and one-off costs, representing an operating profit margin of 12.2%. Revenues were £206.0 million (compared to £212.2 million in 2008), driven by the Division's increasing exposure to more secular growth markets, with our medical business performing especially well. The integration of the businesses we acquired from the Carpenter Technology Corporation in 2008 was delivered successfully to plan.

The Insulating Ceramics Division has also demonstrated a much improved resilience of operating profit margins compared to previous downturns, achieving 8.0% in 2009. The Division's strong and increasing business presence in emerging-market economies including China, India and Latin America helped offset the weakness of western-world economies. Good progress was also made in the Division's operating efficiencies driven by the Thermal Ceramics 'World Class Manufacturing' programme.

The Carbon Division, excluding NP Aerospace, arguably had the most difficult environment of our Divisions in 2009 with market downturns in core industrial markets combined with demand slowdowns in newer end-markets such as solar and US body armour. Nevertheless, the business made a respectable profit contribution in 2009, with an encouraging pick-up in orders seen in the latter part of the year.

One area where all of our businesses did an excellent job during the course of the year was in aligning their cost bases with prevailing demand levels. Their decisive actions during a period of pronounced economic downturn were a key factor in your Group weathering this difficult environment so robustly. I would like to extend a personal thank-you to all our employees for their commitment and individual contributions towards making this happen.

## Looking forward

Even though we have seen some degree of recovery in many end-markets in the latter part of 2009, our expectation is that the demand environment is likely to remain challenging and will certainly be unpredictable. The deep global recession of 2009 was a thorough test of our strategy and business model, which have stood up to this stern examination in a pleasing manner.

Looking to the future, I am therefore confident that Morgan Crucible is emerging from the downturn as a stronger, more resilient business which is well placed to capitalise on opportunities as 2010 develops.

# Group business review

## Group activities

Morgan Crucible is a world leader in advanced materials, focused on specialist ceramics, carbon and composites. We employ around 9,400 people in over 34 countries and serve customers in over 100 countries around the world. Working at the forefront of advanced materials technology, we develop solutions that help to make the world more efficient, better protected and healthier.

The Group has three global Divisions: Carbon, Technical Ceramics, and Insulating Ceramics.

**Carbon Division** is a global supplier of highly engineered solutions built on carbon, silicon carbide, oxide-based ceramics and advanced polymeric composite materials technology. Applications include current transfer systems for industrial and rail transportation, seals and bearings for fluid handling, high-temperature insulation for solar silicon wafer production and advanced lightweight ceramic/composite armour systems for personal and vehicle protection.

**Technical Ceramics Division** is a leading supplier of bespoke applications-engineered industrial products. These are manufactured from advanced materials including ceramic, glass, precious metals and piezoelectric and dielectric materials. Key markets are electronics, aerospace, industrial equipment, medical and power generation.

**Insulating Ceramics Division** is a global supplier of thermal management and metal melting solutions for high-temperature applications which benefit technically, financially and environmentally from increased thermal and energy efficiency and management. The Division consists of two global reportable operating segments: Thermal Ceramics, with the core products of high-temperature insulating fibre, bricks and monolithics, and Molten Metal Systems (MMS), with the core products of crucibles, foundry consumables and furnaces.

## Group strategy

Morgan Crucible's vision is to be one of the world's very best advanced materials companies.

Our aim is to create long-term sustainable shareholder value.

The Group's five strategic priorities are:

- To focus on higher growth, higher margin, non-economically cyclical markets.
- To be high value-added to our customers.
- To be number one or number two in our chosen market segments.
- To have a culture of operational excellence and cost efficiency.
- To find, keep and develop the right people.

We use our strategic priorities to test new investment opportunities, to screen our businesses for fit with the existing Group and to identify areas requiring strategic attention and action.

## Revenue and profits

Group revenues increased by 12.9% to £942.6 million (2008: £835.0 million). Group EBITA before restructuring charges and one-off items was £89.0 million (2008: £108.8 million), representing a margin of 9.4% (2008: 13.0%). The main factors for these movements are as follows:

- **Carbon:** Revenues were up by 63% compared to 2008 at £391.4 million (2008: £239.9 million). This increase reflects the inclusion of NP Aerospace in the Division's consolidated results for the first time following the increase in Morgan Crucible's shareholding from 49% to 60% in January 2009. Revenues for the underlying Carbon business, excluding NP Aerospace, were down approximately 25% on a like-for-like constant currency basis, reflecting the impact the economic downturn had on almost all of the markets we serve, combined with a significant reduction in North America body armour revenues. Divisional EBITA including NP Aerospace was £40.5 million, a margin of 10.3%, compared to £36.3 million, and a margin of 15.1%, for 2008.
- **Technical Ceramics:** Revenues for 2009 were £206.0 million (2008: £212.2 million), a decrease of 3%. This included £45.9 million (2008: £41.4 million, for nine months of ownership) of revenue contributed by the businesses acquired from the Carpenter Technology Corporation at the end of March 2008. Revenues for the underlying Technical Ceramics business, including the businesses acquired from the Carpenter Technology Corporation as if they had been owned for 12 months in 2008, were down by 19.4% on a like-for-like constant currency basis. Despite the unprecedented economic conditions, Technical Ceramics was, in the main, able to protect Divisional EBITA profit margins, which were 12.2% for the year (2008: 14.9%).
- **Insulating Ceramics:** Revenues for the Insulating Ceramics Division decreased by 9.8% to £345.2 million in 2009. Divisional EBITA and margins dropped to £27.6 million and 8% from £45.6 million and 11.9% in 2008, reflecting challenging end-market demand, particularly in the second half of the year.

## Cash generation

The net cash inflow from operating activities was £134.5 million (2008: £111.2 million), an increase of 21% over the previous year. Free cash flow before one-off items and dividends was £85.9 million, a substantial increase in cash generation on the previous year (2008: £34.7 million). This was driven by strong working capital management which resulted in a net inflow of £25.8 million compared to last year's outflow of £21.8 million. As a result our net debt at the year end was £252.7 million; an improvement of £37.7 million compared to the 2008 year-end position.

# Key performance indicators

To support the Group's strategy and to monitor performance, the Board of Directors and the Executive Committee use a number of financial and non-financial key performance indicators (KPIs). These KPIs are selected as being important to the success of the Group in delivering its strategic objectives. Progress is assessed by comparison with the Group's strategy, its budget for the year and against historic performance. At a business level, a range of further benchmarks and other KPIs are also used as part of the Divisional planning and performance review processes. In order to measure the underlying performance of the business, management further analyse the headline KPIs to exclude the impact of acquisitions and foreign exchange.

As Morgan Crucible's businesses grow and evolve we will review and update the list of KPIs selected to ensure they remain important to the success of the Group.

Financial and non-financial performance is reviewed in more detail in the Divisional, financial and corporate responsibility sections of this Business review.

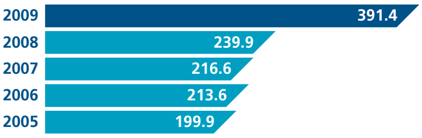
| KPI | Performance 2009 | 2008 | Relevant strategic objective |
|---|---|---|---|
| **Financial KPIs** | | | |
| Revenue growth | **12.9%** | 20.5% | → Creating consistent long-term value for shareholders<br>→ Focus on higher growth markets |
| Underlying profit* (decline)/growth | **(21.6)%** | 24.5% | → Creating consistent long-term value for shareholders<br>→ Focus on higher growth markets<br>→ To be high value-added to our customers<br>→ To have a culture of operational excellence and cost efficiency |
| Underlying profit* margin | **8.2%** | 11.8% | → Creating consistent long-term value for shareholders<br>→ Focus on higher growth markets<br>→ To have a culture of operational excellence and cost efficiency |
| Free cash flow before one-off costs and dividends | **£85.9m** | £34.7m | → Creating consistent long-term value for shareholders |
| Underlying earnings per share** | **13.2p** | 23.4p | → Creating consistent long-term value for shareholders |
| Dividend per share | **7.0p** | 7.0p | → Creating consistent long-term value for shareholders |
| **Non-financial KPIs♦** | | | |
| Year-on-year pricing change | **2.0%** | 3.5% | → To be high value-added to our customers |
| Total employment costs as % of sales | **28.6%** | 31.2% | → To have a culture of operational excellence and cost efficiency |
| Employee turnover† | **16.7%** | 14.2% | → To find, keep and develop the right people |
| Training hours per employee† | **12.4** | 14.9 | → To find, keep and develop the right people |
| Lost time accident frequency (per 100,000 hours worked) | **0.56** | 0.69 | → To have a culture of operational excellence and cost efficiency<br>→ To find, keep and develop the right people |
| Tonnes $CO_2$ per £m revenue | **400** | 464 | → To have a culture of operational excellence and cost efficiency |
| Tonnes waste per £m revenue | **65** | 73 | → To have a culture of operational excellence and cost efficiency |

* Defined as operating profit before amortisation of intangible assets.
** Defined as basic earnings per share adjusted to exclude amortisation. See note 9 on pages 109 and 110 for definition of basic earnings per share.
♦ Non-financial KPIs are at constant currency.
† 2009 HR data covers 100% of employees (2008: 96%).

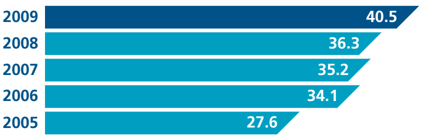
# Review of operations

## Carbon

### Divisional revenue
£m




### Divisional EBITA*
£m




### Key performance indicators

| | 2009 | 2008 |
|---|---|---|
| Divisional revenue growth | **63%** | 11% |
| Divisional EBITA* growth | **12%** | 3% |
| Divisional EBITA* margin | **10.3%** | 15.1% |

**Business description**
The Carbon Division is a leading global supplier of highly engineered solutions built on advanced materials technology. The Division's capabilities originated in the unique properties of carbon and graphite materials and have evolved to include silicon carbide which is used in fluid handling and multiple other critical applications including composite protective armour. The acquisition of NP Aerospace in 2009 extended the Division's materials and ballistic technologies to include lightweight ceramics/composites. The Division leverages its extensive array of advanced materials capabilities through its global infrastructure to serve a wide portfolio of end-markets. Today the Carbon Division has strong positions in carbon brushes for industrial and rail traction applications, seals and bearings for fluid handling, high-temperature insulation for silicon wafer production and advanced lightweight protective ceramic/composite armour systems.

The Carbon Division employ some 3,400 people**, serving customers in around 100 countries worldwide. The Division's global presence includes 40 operating facilities in 25 countries, with major materials processing plants in the USA, UK and China feeding an integrated network of finishing plants strategically located to serve customers across the globe and providing the Division with a network of low-cost manufacturing sites in Mexico, China, Hungary and India.

The Division's strategy aligns with the Group's strategic priorities and has driven the Division's success in the ballistic protection market, as well as the recent entry to the silicon solar cell market. Specifically, the Carbon Division's strategy is to:

- Add value to advanced materials and technology to deliver engineered solutions to chosen markets.
- Engender a culture of operational excellence with a focus on continually improving the value we deliver to our customers.
- Establish and fully embed a mindset for growth through focused business development, specifically in high-growth and high-margin markets.
- Invest in our future through our technology centres of excellence and through acquisitions, alliances and partnerships.

# Stellar performance from NP Aerospace.

* Defined as segment operating profit before restructuring costs, other one-off items and amortisation of intangible assets.
** As at 3 January 2010.

- Fully engage our entire workforce and instil a culture of continuous reinvention.
- Continuously seek and develop the right people.

The Carbon Division's channels to market are primarily direct with sales and applications engineers serving both the original equipment market and the aftermarket. The Division is structured regionally and is able to leverage its global footprint and infrastructure to ensure that the best possible resource is deployed to provide advanced materials and technologies in the form of engineered solutions to the following key global markets:

### Defence and protection

The Carbon Division is a major supplier of advanced ceramic technology to the US body armour market and is the major supplier of protective body armour systems to the UK's defence forces. The addition of NP Aerospace to the Division at the beginning of the year broadened our materials portfolio and competency in ballistics, positioning Morgan Crucible as a leader in lightweight armour systems. Morgan is now a critical resource to the UK's Ministry of Defence for major integration contracts for the fielding of next-generation tactical wheeled vehicles and our highly advanced systems have seen service in both Iraq and Afghanistan. The Division continues to invest heavily in the development of ballistic solutions to counter ever-increasing threats. The protection market was robust during the year and, although expectations are for lower defence spend in 2010, going forward the market will offer solid opportunities due to the continued escalation of ballistic threats and increasing demand for lighter, more mobile solutions for both vehicles and personnel.

### Electrical current transfer

The Carbon Division has a strong position in the global market for electrical current transfer systems which are critical enablers for many industries. The Division utilises its core technology portfolio and global support network to supply carbon brushes, collectors and rotary current transfer products to railways, the mass transit industry, open pit and deep shaft mining, and a variety of other key industrial markets. During the year, demand in European markets and the Americas was down significantly due to the global economic crisis. However, Asian markets were more resilient, particularly China. The medium- and long-term prospects are positive, with demand in western markets expected to improve during 2010.

### Fluid handling

Seals and bearings are critical to the pumps and compressors used in many fluid handling applications in the petrochemical, food processing, residential and oil and gas industries. The Carbon Division has a wide and expanding range of carbon and silicon carbide materials and is the globally recognised leading provider of seal faces, bearings, rotors, vanes and other technical solutions required for a large variety of fluid handling applications. Market demand declined significantly in 2009, but is expected to recover slightly ahead of global GDP growth in the medium term.

### Power generation and renewables

Over the past two years the global energy sector has become an increasingly important target market for the Carbon Division. The Division's technology and product portfolio includes components which are critical to traditional power generation companies, the nuclear industry and the renewables sector, including solar and wind power. In solar power, the Carbon Division is a world leader in advanced high-temperature solutions providing major producers of polysilicon and silicon ingots with the means to enhance solar cell performance. In wind power generation, the Division supplies carbon brushes and rotary transfer systems which perform in the harshest environments around the globe. Investment in wind power slowed during 2009, but installed capacity represents a large and more stable aftermarket for carbon brushes. Looking forward, demand for both solar and wind power capacity is expected to grow significantly and the Division is well placed to capitalise on this growth.

### Semiconductor processing

The Carbon Division's products are at the heart of many electronic innovations, and are used in semiconductor manufacturing processes such as ion implantation, epitaxy and compound crystal growth. With the drive to faster, smaller and lower cost devices, semiconductor processing equipment companies are dependent on advanced materials being able to work at higher temperatures and having higher purity levels to achieve the required performance. The Carbon Division also

# Review of operations continued

## Carbon continued

supplies products used in the manufacture of components such as optical fibres, laser diodes, and transistors for mobile and satellite communications. The sector started to decline in mid 2008 and by early 2009 demand was down very significantly. The market began to improve in the summer of 2009 and is expected to grow in 2010. Although this sector is a relatively small portion of the Division's turnover, our engineered solutions are highly valued and prospects for future growth through innovation are promising.

### Research and development

The Division is a leader in carbon-based materials, oxide and non-oxide ceramics and lightweight composites, having expanded its materials technology portfolio through in-house research and development and through the strategic acquisitions of NP Aerospace in 2009 and Aceram in 2006. The Division's research activities cover both material and process capabilities and are located within our major material processing facilities in the USA, the UK and China. Carbon's application development engineers in 25 countries worldwide work with our customers to apply the Division's advanced materials and process technologies to develop leading-edge solutions according to customer need and to position the Division as a leader in high-growth and emerging markets.

### Divisional performance

Total revenues for the Carbon Division were up by 63% on a reported basis at £391.4 million (2008: £239.9 million). This increase reflects the inclusion of NP Aerospace in the Division's consolidated results for the first time following the increase in Morgan Crucible's shareholding from 49% to 60% in January 2009. The like-for-like revenue increase (ie including NP Aerospace revenues for all of 2008 when they were accounted for as an associate) on a constant currency basis was 13%. This was driven by an exceptionally strong performance from the NP Aerospace business with revenues of £186.2 million, up 159% on the previous year (2008: £72.0 million).

Revenues for the underlying Carbon Division business, excluding NP Aerospace, were down approximately 25% on a like-for-like constant currency basis, reflecting the impact of the economic downturn combined with a significant reduction in North America body armour revenues. Second half revenues were broadly flat on the first half, reflecting a seasonally quiet third quarter, especially in Europe, and some improvement in quarter four.

The traditional electrical brush and the seals and bearings businesses were affected by a significant contraction in mature western markets, although growth was achieved in China with the introduction of new products.

The rotary business was impacted by a continued slowdown in the industrial and construction markets however, significant progress was made in the global wind energy sector and in China.

The high-temperature insulation business delivered some growth in 2009, despite deeply contracted markets. Demand for these products is driven by the processing of advanced materials for markets such as solar energy and semiconductors. The Division continued to improve its operational capability and product offering and is well positioned to take advantage of the expected market improvements.

Full-year EBITA on a reported basis was £40.5 million, a margin of 10.3%, compared to £36.3 million and a margin of 15.1% for 2008. EBITA margins were 15.5% in NP Aerospace and 5.7% in the underlying Carbon business and, whilst the margin in the underlying Carbon business was below that achieved in 2008, second half margins improved over the first half of 2009.

The NP Aerospace business had a very strong year, with revenues in each half in excess of £90 million. Demand for Mastiffs, Ridgbacks and Wolfhounds from the UK Ministry of Defence (UK MoD) remained strong throughout 2009 and progress was made in the development of new product offerings. NP Aerospace has successfully established itself as a critical supplier to the UK MoD and is, through the deployment of its technology into combat theatre, gaining global recognition for its highly advanced lightweight armour systems.

**Business developments**
The key developments in 2009 were the excellent performance of the NP Aerospace business and the response to the global economic crisis.

At the beginning of 2009 the Group increased its equity stake in NP Aerospace from 49% to 60% as part of the strategy to further develop the Group's presence in the market for personal and vehicle protection. During the year NP Aerospace more than doubled its sales and profits and has strengthened its position as a critical supplier to the UK MoD for the armouring and integration of tactical wheeled vehicles and for personal protection in terms of body armour and helmets. Good progress was also made in developing future strategies for accessing the Division's wider global footprint across a number of key geographic regions.

In the underlying Carbon business, a series of significant cost reduction actions were initiated in the second half of 2008 in anticipation of weakening demand. Total headcount has been reduced by nearly 700 (18%) since the summer of 2008. Reductions in the working week were also implemented at a large number of sites and the relocation of manufacturing to lower cost regions such as Mexico, China and Hungary was accelerated wherever possible. As a result of these actions, full-year total employment costs were reduced by more than £12 million compared with 2008. However, the Division maintained its commitment to devote resources to new growth opportunities, advancing its position in the renewable energy sector, in the global armour market and in China.

Looking forward, the actions taken to meet the challenges of the global economic downturn provide a more efficient and flexible structure to respond effectively as market demand recovers, and the increased focus on global growth markets has improved the prospects for growth entering 2010.

**Outlook**
End-market demand in the Carbon Division's underlying business stabilised during the third quarter of 2009 and has shown some signs of recovery entering 2010. Improvements to the cost base and to global operational capability, along with the focus of effort and resource on higher growth markets, means that the Division is well positioned to take advantage of improvements in the global economy.

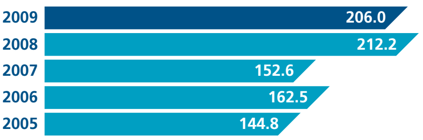
NP Aerospace is expected to continue to perform well above pre-acquisition levels; however, revenues in 2010 are expected to be below the record levels of 2009. Opportunities beyond the UK market are being pursued and could allow a further 'reinvention' of the business.

Through the course of 2010 the Division's operational footprint will continue to be refined, while appropriate resource is committed to markets that offer the greatest long-term profitable growth. After a year of consolidation and considerable reinvention, the Division is much better positioned for future challenges and opportunities.

# Review of operations
continued

## Technical Ceramics

### Divisional revenue
£m




### Divisional EBITA*
£m


### Key performance indicators

| | 2009 | 2008 |
|---|---|---|
| Divisional revenue (decline)/growth | **(3)%** | 39% |
| Divisional EBITA* (decline)/growth | **(21)%** | 58% |
| Divisional EBITA* margin | **12.2%** | 14.9% |

### Business description

The Technical Ceramics Division is a leading supplier of bespoke, application-engineered industrial products. These are manufactured from advanced materials including ceramic, glass, precious metals and piezoelectric and dielectric ceramics. Key markets include electronics, aerospace, industrial equipment, medical and power generation. Applications include ceramic cores used in the manufacture of turbine blades; components and sub-assemblies for electron tubes used in communications, security and medical devices; and medical implants.

The Technical Ceramics Division operates worldwide with 23 manufacturing sites across the USA, UK, Germany, Mexico, Australia and China. The three largest sites are in California, USA, Massachusetts, USA and Germany. The Division employs some 2,600 people** and offers full technical support and advice to customers throughout their product development cycle, working closely with them to provide engineered solutions that add value and help differentiate their end products.

The Division is structured regionally with global support from marketing, technology, business development, strategy and finance.

The Division's strategy is aligned with that of the Group with the objective of being a world leader in engineered solutions based on advanced ceramic materials.
The Division's strategy is to:

- Focus on niche applications in growth markets.
- Deliver innovation in materials technology.
- Use applications engineering and distinctive competencies to provide customers with differentiated solutions.
- Be the supplier of choice in our chosen markets, exhibiting excellent customer service.
- Demonstrate dissatisfaction with the status quo and through continuous improvement and best practice initiatives achieve higher levels of business performance.
- Through recruitment, development and training ensure we have the strongest teams in all areas of the business.
- Constantly review our manufacturing footprint and its ability to deliver our growth and profit objectives.

# Resilient performance in challenging conditions.

* Defined as segment operating profit before restructuring costs, other one-off items and amortisation of intangible assets.
** As at 3 January 2010.

The Technical Ceramics Division offers an extensive range of products for hundreds of high-technology application niches, including:

- Ceramic cores used in the casting of turbine blades for aero engine and industrial gas turbines.
- Braze alloys for aero engine build and repair and ceramic components and sub-assemblies for aero engine monitoring and control equipment.
- Components and sub-assemblies for a broad range of medical applications, primarily implantable devices, prosthetics and surgical and diagnostic equipment.
- Ceramics and assemblies for electron tubes used in a range of medical, security, industrial and research applications, such as airport security scanners, TV and radio broadcasting and x-ray equipment.
- Engineered ceramics used in fluid handling equipment.
- Piezoelectric ceramic actuators used in electronic data storage.
- Components and assemblies used in a variety of lasers for product marking and medical and industrial applications.

Technical Ceramics leverages its advanced ceramic materials capabilities to serve its major markets – aerospace, automotive, electronics, household goods, industrial equipment, medical, power generation, process control and monitoring and security and defence. Ninety percent of sales are designed and manufactured to customer-specific requirements. Our main channel to market is direct with sales and applications engineers working closely with our customers to establish their needs and support them through the design and production process. The Division has strong niche positions within its target markets. The performance and prospects of the five main markets are described below.

## Aerospace

As engines run hotter in order to increase efficiency and reduce $CO_2$ emissions, demands on the materials used in their construction become greater, as does the need to monitor and control operating conditions. Technical Ceramics produces braze alloys for engine build and repair and ceramic components and sub-assemblies for engine monitoring and control equipment. Our Certech business manufactures cores used in the casting of turbine blades. We also supply piezoelectric components and sensors, including fuel level sensors and gyroscopes, and our Diamonex™ engineered coatings are used on critical components of aircraft fuel systems. As passenger numbers fell during 2009, our sales to the aerospace market declined significantly. Forecasts for 2010 are expected to show growth year on year, but the market will remain difficult in the medium term.

## Medical

An ageing population and step-change improvements in procedural practice maintain growth rates consistently above GDP in this market. Our medical engineering expertise includes ceramic orthopaedic joint replacements and highly specialised ceramic-to-metal assemblies for implantable devices such as pacemakers, cochlear implants and defibrillators. In addition we supply key components for instrumentation and diagnostic equipment such as ultrasonic imaging, CAT and MRI scanners. Our superior piezoelectric ceramic components are enabling increased resolution of ultrasonic imaging and are used extensively in medical ultrasound. Piezoelectric components are also the key technology in applications such as blood flow measurement and foetal heart monitors, providing increased reliability and accurate detection. Additionally, they can be found in ultrasonic air-in-line sensors in medical devices and infusion pumps. The high-performance piezoelectric material is used in high-power transmission of high-frequency waves to assist with surgical cutting. We supply efficient materials for small medical tools such as ultrasonic dental descalers and ultrasonic scalpels, which are used in applications such as cataract removal. Multilayer chip capacitors are used extensively in MRI systems to tune the magnetic field accurately and our ceramic capacitors can also be found in lasers for eye surgery.

The medical market again showed itself to be resilient in times of recession. Sales growth was strong during the year and the market is expected to continue to grow strongly in the medium term.

# Review of operations
continued

## Technical Ceramics
continued

### Industrial equipment
The mechanical, electrical, chemical and thermal characteristics of our materials make them ideally suited for use in harsh processing environments such as those found in valves, pumps and a variety of manufacturing processes. Our ceramic rollers are used in kilns used for the manufacture of metals, glass, ceramic-ware and fuel cell production. Our kiln furniture and high-temperature components are used in a wide range of specialist thermal processing applications from industrial annealing to medical device manufacture and scientific equipment.

Our range of high-efficiency piezoelectric materials are used in many high-power ultrasonic systems such as those for cleaning and welding. We also design and manufacture complete sensors and transducers for these industrial applications. The global downturn in manufacturing and equipment sales impacted our revenues in this market and we saw a decline compared to 2008. A steady recovery is expected in the coming year and medium-term prospects are generally positive.

### Power generation and distribution
Energy generation, management and distribution is arguably one of the fastest evolving industries of modern times. Our precision-engineering capabilities are increasingly being called on to develop components and sub-assemblies for new products across the power sector. Increasing global demand for power and dramatic increases in energy costs have led to an increased emphasis on environmental issues and the need for renewable energy.

We supply a range of products that are used in the manufacture of thin-film photovoltaic cells for the solar industry and our Certech business manufactures cores used in the manufacture of turbine blades used for industrial gas turbines. A slowdown in equipment sales and cutbacks in funding of new projects caused sales to the power sector to decline significantly during the year. However, the outlook for the coming year is more encouraging.

### Electronics
Technical Ceramics' components and sub-assemblies are used extensively in the electron tubes used in communications, healthcare, security and research applications. Our components are used in hand-held, land-based and satellite communications equipment and networks for the telecommunications sector; as well as PCs, servers, data storage and a range of peripheral equipment for IT hardware producers. Demand for mobile devices that offer increasing functionality, together with increased requirements for data storage, drives the consumer products segment of this market to develop and introduce a constant flow of new products. In addition, the laser market continues to find new applications that drive growth in healthcare, product marking and process control. During 2009 demand for consumer-related products weakened but this was offset by sales of electron tube products, driven by security and related applications. Sales of products for data storage devices were also strong, driven by new product launches. Overall the electronics market declined slightly, but prospects for 2010 are more positive with growth expected in the medium term.

### Research and development
Technical Ceramics' research and development capabilities are led by the Divisional Technical Director with a network of materials scientists and process engineers across our operations. They work with our customers to engineer solutions that address their needs. The Division also undertakes research in collaboration with leading universities in Europe and North America.

Our internal research and development focus has been on product development for the medical and solar markets. In the medical sector, we have developed and released a new implantable grade of ceramic (Vitox™ AMC) which will have applications for orthopaedic implants. In solar energy, we have developed products that are used in the growth and subsequent processing of silicon substrates for solar panels as well as a variety of uniquely stable ceramic products that are used by panel producers using thin-film manufacturing techniques.

In 2009, Technical Ceramics registered a number of new patents. These include a controlled textured ceramic surface called Sharkskin™ which will have a variety of end application uses in the semiconductor, medical and other markets. Another is for a new silicon carbide diamond pad conditioner named Phoenix™ which is used for chemical-mechanical polishing in semiconductor manufacturing.

### Divisional performance

Revenues for 2009 were £206.0 million (2008: £212.2 million), a decrease of 3.0%. This included £45.9 million (2008: £41.4 million, for nine months of ownership) of revenue contributed by the businesses acquired from the Carpenter Technology Corporation in 2008. The proforma underlying revenue decrease at constant currency was 19.4% compared to the full year 2008 (the proforma calculation assumes that Carpenter was included for a whole year in 2008 to enable a like-for-like comparison).

Despite the unprecedented and difficult economic conditions, the Division was, in the main, able to protect margins, which were 12.2% for the year (2008: 14.9%). EBITA for the year was £25.1 million (2008: £31.6 million). The Division made progress during the year and finished 2009 well, with an EBITA margin of 13.4% in the second half. (first half 2009: 11.1%).

In response to the weaker global market conditions, we took early and decisive action to protect our margins. These cost control measures included headcount reductions of 670 employees compared to June 2008, with the majority taking place in the first half of 2009. These measures continued to deliver benefits in the second half of the year, driving the improved margins seen over the first half.

### Business developments

During the year, Technical Ceramics maintained its focus on positive mix shift, moving towards higher margin, higher value-added end-markets such as medical and aerospace, whilst concurrently reducing exposure to more commoditised and economically cyclical product areas. Our continuous operational improvement programme, cost reduction initiatives and our emphasis on positive price pass-through are all contributing to supporting operating margins in very difficult market conditions.

In 2009 major investments were controlled due to the uncertain market outlook. Work on consolidating our footprint continued throughout the year. In July we announced and initiated the move of business from our Auburn site into the Hayward location in California, USA and expect to realise the benefits of this in 2010. In October we announced the sale of the small Metal Injection Moulding (MIM) business for £1.1 million. The MIM business was based at our New Bedford, MA, USA site and the sale will make room to expand the medical business there. The Shanghai, China site, which produced mostly commodity products for domestic applications, was successfully closed on time and to plan during the first half of the year.

### Outlook

Although overall market demand declined in 2009 there are some areas that showed positive signs of improvement as we enter 2010.

The US market appears to have stabilised, although we continue to watch carefully for any signs of a further downturn. Some weakness in the aerospace and industrial gas turbine sector is being offset by improvements in demand from sectors within the electronics market. An example of this is our initiation of a production ramp-up to meet demand for the next generation of hard disk drive products.

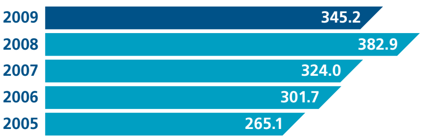
Our European business had a difficult year, being consistently challenged by weak market conditions in general industrial markets and construction. This principally affects our business in Germany, which supplies products for manufacturing applications involving thermal processing.

Since the half year we have seen a reduction in industrial gas turbine demand, which is continuing into 2010. In both Europe and North America a highlight of 2009 has been the continuing strength of our medical customers. Developing our presence in this sector remains an important focus for the Division during 2010. We continue to look carefully at potential bolt-on acquisition opportunities that would enhance our offering in our core markets, which together with our strong new business pipeline leaves the Division well placed for the future.

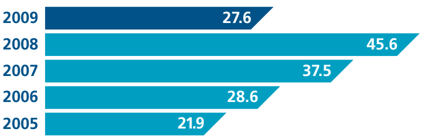
# Review of operations
continued

## Insulating Ceramics

### Divisional revenue
£m




### Divisional EBITA*
£m




### Key performance indicators

| | 2009 | 2008 |
|---|---|---|
| Divisional revenue (decline)/growth | **(10)%** | 18% |
| Divisional EBITA* (decline)/growth | **(39)%** | 22% |
| Divisional EBITA* margin | **8.0%** | 11.9% |

### Business description

The Insulating Ceramics Division is a global supplier of thermal management and metal melting solutions for high-temperature applications which benefit technically, financially and environmentally from increased thermal and energy efficiency and management. The Division consists of two global reportable operating segments: Thermal Ceramics and Molten Metal Systems (MMS).

### Thermal Ceramics

Thermal Ceramics is a world leader in heat management solutions, serving a broad spectrum of industrial and non-industrial markets with insulation requirements ranging from 500°C to 1,600°C, as well as passive fire protection for the building and construction sectors. Thermal Ceramics serves highly demanding markets worldwide, which are increasingly influenced by legislative and environmental requirements. Customers increasingly demand advanced insulation solutions and superior quality to reduce energy costs and improve environmental performance through reduced $CO_2$ emissions.

Thermal Ceramics' core products are manufactured from advanced insulating materials and include high-temperature insulating fibres, insulating fire bricks and monolithics. These are marketed under a number of leading brands including Superwool™, JM™, Pyro-Bloc™, FireMaster™ and Tri-Mor™.

Thermal Ceramics employs over 2,900 people** across a network of 34 manufacturing facilities and 50 sales offices worldwide. The business is structured geographically, with regional teams supported by global engineering, sales and marketing, technology and research and development functions. Major sites are located in Argentina, Brazil, China, France, India, Italy, Japan, Korea, Mexico, Russia, UK and the USA.

Thermal Ceramics' vision is to be the world's leading provider of advanced insulation solutions. This is implemented through:

- → Focusing on high-growth, high-margin and high value-added products and markets.
- → Establishing and maintaining leading positions in target markets.
- → Changing the scale and location of manufacturing operations to deliver the best value.
- → Constantly improving operational performance towards a goal of World Class Manufacturing.
- → Satisfying customers.
- → Ensuring that Thermal Ceramics is 'A Great Place to Work'.

**Strong contribution from our emerging markets business.**

* Defined as segment operating profit before restructuring costs, other one-off items and amortisation of intangible assets.
** As at 3 January 2010.

Thermal Ceramics' routes to market include both direct sales and distribution. The Division's application engineering and design capabilities are a key competitive advantage and its customer base is broadly diversified.

The business targets growth opportunities in the following key markets:

### Metals/Iron and steel

Thermal Ceramics has a strong position in the supply of monolithic linings for blast furnaces, fibre modules in reheating and heat treatment furnaces and insulating fire bricks for hearth and reheating furnaces where product quality is a key differentiator. Channels to market include distribution with direct sales to major accounts and where engineering input is required. Demand from the iron and steel sector declined in the year although demand for higher technology heat management solutions from Asia was strong. In the medium term, as the global economy recovers, the demand for steel will begin to rise again fuelled by industrialisation, population growth and construction. In addition, steel producers are seeking new heat management solutions to tackle environmental concerns and rising energy costs and to increase operational efficiency.

### Petrochemical processing

Thermal Ceramics targets both new and retro-fit projects in the global petrochemical sector, supplying heat management solutions for fired heaters, sulphur recovery units, fluid catalytic cracking units and boilers. As petrochemical and refining process technology develops, high-temperature heat management and energy efficiency become increasingly critical. Long-term growth in the sector is geared to population expansion with projects lasting many years in planning and implementation. Thermal Ceramics is well positioned in the market and with its leading capability offers bespoke packaged solutions of insulation bricks, fibre and fibre products. During the year the sector was relatively strong and is seen as likely to remain so in the short and medium term.

### Fire protection

Thermal Ceramics' FireMaster™ fire protection systems are comprehensively certified and extensively tested to meet national and international standards, offering customers proven fire protection performance in various sectors including commercial buildings, hotels, airports, industrial plants, offshore platforms, cruise ships, military vessels and tunnels and other underground construction. Thermal Ceramics works with fire protection specialists in the sector and channels to market include direct sales and distribution. Fire protection-related legislation is a key factor in driving demand in the sector, which is also linked to construction output. During the year, demand was down but increased penetration enabled Thermal Ceramics to outperform the underlying market. It is expected that the new lighter weight solutions of the FireMaster™ product range, combined with the increasing regulatory requirements for fire protection, will create opportunities for growth in 2010.

### Ceramics

Thermal Ceramics' fibre products offer multiple benefits to the ceramics industry, including saving energy by reducing kiln car mass. Each year over one million square metres of Thermal Ceramics insulating products is installed in kilns firing ceramic products from tiles to tableware and from sanitaryware to fine bone chinaware. Insulating fire bricks are sold under the JM™, K™ and TJM™ brands, for use in roller kilns, shuttle kilns, tunnel kilns and hobby kilns. Thermal Ceramics is well positioned in the market based on its high-quality products and engineering support. Demand in the ceramics industry is broadly linked to building and construction and has suffered from a severely reduced market in the last year. The outlook remains good longer term but with the market moving faster from Europe to Asia following the downturn.

### Power generation

Increasing demand for electricity across the world, and particularly in the emerging economies, is driving expansion in the power generation sector. Environmental and energy/cost efficiency issues make heat and thermal management a key issue for all operators. For example, Thermal Ceramics' low bio-persistent fibre Superwool™ is used for duct insulation in heat recovery steam generators (HRSGs), offering high-temperature resistance with the important reassurance that the materials utilised are an environmentally friendly solution. The new-generation fibre Superwool Plus™ improves HRSG design further by reducing heat losses or reducing panel thickness. Power generation is a global industry with the specification, fabrication, financing and installation of projects potentially taking place on different continents. Such long-term projects are proving resilient to market downturns. Thermal Ceramics has a strong position in higher end applications in the power generation and renewables sector, serving the market through both direct sales with engineering support and via distributors.

# Review of operations
continued

## Insulating Ceramics
continued

### Research and development
The Thermal Ceramics business carries out the majority of its research and development at its Bromborough, UK site, in a purpose-built world-class facility. With 25 dedicated scientists, the team has led the market in the development of low bio-persistent fibres, low-energy furnace operation and product development. The work of this team has been at the heart of all of Thermal Ceramics' major product launches of the last five years and in the past year investment has been increased as the business positions itself for future growth.

### Molten Metal Systems (MMS)
MMS has a leading position in the supply of crucibles to the non-ferrous metals industry and manufactures equipment and foundry products used in the melting, holding and processing of metals and alloys.

MMS employs some 500 people** at its 10 locations worldwide, including five manufacturing facilities with localised technical support and five distribution centres. MMS is managed as an integrated global business with three product lines: crucibles, foundry consumables and furnaces. In 2009 Germany and India accounted for 90% of production output.

MMS's strategy is to deliver targeted solutions for metal casters, focused on improving their metal quality, increasing efficiency and reducing energy consumption and related $CO_2$ emissions.

This strategy is implemented by:

- Focusing on high-value/high-challenge opportunities.
- Striving for operational excellence worldwide.
- Developing a growth culture throughout the business.

MMS serves its customers through a combination of direct sales and distribution with targeted technical support. MMS's key growth opportunities are driven by multiple end-use markets. These include:

- Non-ferrous castings for the automotive, marine and rail markets.
- The recycling and refining of precious metals from mining projects.
- The production of metal powder for the cosmetics, aerospace and defence markets.
- Copper and brass castings for the construction, chemical processing and oil and gas sectors.
- The production of pure aluminium for electronics applications.

MMS has a leading market position in crucibles, which make up 80% of its revenue; key markets are North America, India, Brazil and Germany. Sales to the Indian market were up by over 15% in the year. Future growth will continue to come from the 'BRIC' countries and smaller developing markets.

MMS's technology capability is focused in its global research and product development facilities which form part of the Indian operations.

### Divisional performance
The Insulating Ceramics Division comprises two reportable operating segments, Thermal Ceramics and Molten Metal Systems (MMS).

In 2009 the Insulating Ceramics Division's revenue decreased by 9.8% to £345.2 million (2008: £382.9 million). On a constant currency basis, the year-on-year decline was 19.7%. Divisional EBITA and margins dropped to £27.6 million and 8.0% respectively from £45.6 million and 11.9% in 2008.

### Thermal Ceramics
Thermal Ceramics' revenues decreased by 9.3% to £315.1 million in 2009 (2008: £347.4 million). On a constant currency basis, the year-on-year decline was 19.4%. End-market demand was more challenging in the second half of the year with a revenue decline of 6.6% at constant currency compared to the first half of 2009.

Due to early management action, Thermal Ceramics' profitability showed encouraging resilience to this sales decline compared with the performance in previous downturns, with EBITA margins holding up well at 8.5% (2008: 11.9%) and with EBITA for the year of £26.7 million (2008: £41.4 million).

Our businesses in the developed economies of Europe and North America were most affected by the global downturn. In contrast, markets in Asia and Latin America held up somewhat better and in the latter part of the year started to show some order book recovery.

** As at 3 January 2010.

Margin improvements were made with a number of operational excellence initiatives underway, including our 'World Class Manufacturing' programme.

### Molten Metal Systems

MMS revenues decreased by 22.5% in 2009 on a constant currency basis. The decline in customer demand was most severe in Europe and North America. The foundry products and crucibles product lines fared significantly better than the furnace equipment product line.

While the business traded at just above breakeven in the first half of 2009, it improved in the second half of 2009 as benefits of the cost reduction and manufacturing footprint moves began to take effect.

### Business developments

Whereas 2008 represented a growth period for Thermal Ceramics, 2009 has been one of cost control and consolidation in the face of the challenging global economic conditions. Commencing in late 2008, the business implemented a cost reduction programme that led to a 12% headcount reduction at the end of 2009. The cost reduction programme included the closure of two fibre plants: Erwin, USA and Skawina, Poland.

Thermal Ceramics' new product development remains concentrated in the field of low bio-persistent fibre with the continued roll-out of Superwool 607™, the improved insulation performance product of Superwool Plus™, as well as the higher temperature Superwool HT™. The Division is positioned as the global technology leader in the production of its bio-soluble product range.

The objective of Thermal Ceramics 'World Class Manufacturing' programme is to increase productivity overall by improving health, safety and environmental performance, quality, cost, logistics and customer satisfaction. The roll-out of the programme covered three plants in 2009 with a further three plants planned for 2010. At the same time, engineering and research time is being utilised to optimise manufacturing processes to improve gross margins through improved raw material and energy yield enhancements.

The relocation of MMS's manufacturing footprint to India and China was completed in 2009. Both facilities are fully functional. The focus in 2010 is to leverage our low-cost advantage and move the business into a period of profitable growth.

### Outlook

Towards the end of 2009 Thermal Ceramics' order intake rate started to improve in all regions except Europe. This has continued into the early part of 2010 with the expectation that the year will show a trend of continued improvement, although Europe is likely to remain slow until 2011.

The long-term outlook for Thermal Ceramics remains encouraging, driven by the growth in global population and the continuing industrialisation of emerging economies. In 2009 some 39% of revenues were generated in the Asian and Latin American regions and this percentage is set to increase. These factors, combined with the need to reduce energy expenditure and the increasingly stringent environmental legislation that favours low bio-persistent fibres such as Superwool™, will continue to drive demand for Thermal Ceramics' heat management solutions.

The outlook for MMS is positive with the order book having improved markedly due to modest recovery in Europe and strong growth in India and China. Having successfully completed the relocation of its manufacturing facilities, approximately 70% of MMS's 2010 output will come from India, Brazil and China. MMS is well placed to take advantage of the continuing industrialisation of emerging economies and to retain its market-leading position.

# Corporate responsibility

## Introduction

At Morgan Crucible, corporate responsibility is integral to our business, supporting each of our five strategic priorities. In this section we report on our policies, procedures and performance in respect of business ethics, community relations and suppliers and customers. Subsequent pages cover Environment, health and safety (EHS) and Our people. In addition, our 2009 EHS Report, planned for publication on our website in April 2010, will provide a more comprehensive review of our 2009 environmental and health and safety performance.

The Board is accountable for corporate responsibility policies and procedures. The Chief Executive Officer, Mark Robertshaw, is the executive in charge of all corporate responsibility matters including internal and external stakeholders.

During the year, all of Morgan Crucible's corporate responsibility-related and other policies went through a review and updating process, with external benchmarking where appropriate. The revised policies were agreed by the Executive Committee and approved by the Board.

The Company relaunched its Group-wide intranet in January 2010. This provides employees with online access to the Group's policies and related procedures and guidance notes.

## Corporate responsibility policies and procedures

### Core values

Morgan Crucible's approach to corporate responsibility is encapsulated in our Core Values Statement which was first published in 2004 and is regularly reviewed. As we work to implement our strategic priorities our Core Values Statement provides the framework for our policies, programmes and relevant procedures. The statement is available on our website and applies to all Morgan Crucible businesses and employees worldwide.

### Business ethics

The Audit Committee is responsible for overseeing the Group's Ethics Policy, and reports to the Board on its effectiveness.

Our Core Values Statement and Ethics Policy oblige all employees to operate in accordance with applicable laws and regulations and specifically prohibit the giving or receiving of bribes. These policies apply, so far as is appropriate, to our business partners, including contractors, agents, joint ventures and suppliers. The Company also requires that no employee shall suffer discrimination as a result of refusing to pay or receive a bribe.

During the year the Morgan Crucible Ethics Policy was reviewed and updated. Senior management training has been taking place. The Group-wide launch of the policy and related training programme took place with the launch of the intranet, as referred to above.

Our Anti-Trust Compliance Programme helps ensure that we comply with anti-trust and competition laws around the world. The programme has been in place since 2002 and was updated in 2008 to include new training materials and an updated programme structure.

### Community

Our practice is to engage with local communities in relation to matters of mutual interest and concern. At a local level, where Morgan Crucible often has long-established roots and is frequently a major employer, this helps to foster mutual understanding and credibility. In addition, Morgan Crucible engages with local and national governments and agencies, both directly and through professional bodies. Donations to political parties or causes are prohibited.

### Customers and suppliers

Morgan Crucible's customer service strategy is: to respond quickly to changing customer demand; to identify emerging needs; and to improve product availability, quality and value. We stay close to our current and potential customers, building long-term relationships.

Over 90% of the Group's manufacturing capacity is accredited to ISO 9001 and our quality management systems help ensure that our products meet or exceed customer requirements. Management of the supply chain is a key part of ISO 9001 and ISO 14001 accreditation and includes supplier questionnaires as appropriate.

We aim to work with our customers, suppliers and other partners in mutually beneficial ways and, so far as is practicable, require that our customers and suppliers, joint venture partners and contractors throughout the supply chain act in accordance with our policies and values. Our support for the Universal Declaration of Human Rights, referred to in the Our people section on page 54, commits us in respect of all those who work for the Company and those who have dealings with it, including suppliers.

## Corporate responsibility policy implementation

The implementation of our corporate responsibility-related policies and procedures is aligned with the overall governance structure of the Group. The implementation of our environmental, health and safety and people-related policies is covered in more detail on pages 51 to 55.

We describe below some of the processes for implementing and monitoring our key corporate responsibility policies and procedures and those in respect of verification of our environmental, social and governance (ESG) disclosures.

### Business ethics

The Board of Morgan Crucible is committed to ensuring that the Company's policies relating to business integrity are upheld. Our Core Values Statement and Ethics Policy are translated into appropriate languages for our sites worldwide. The statement and policy are promoted to employees globally, in particular through coverage in the global employee magazine, which is available in eight languages. Appropriate training is provided, including induction training for new employees and via e-learning.

The Morgan Crucible Whistleblowing line enables employees and other stakeholders who are aware of, or suspect, misconduct, illegal activities, fraud, abuse of Company assets or violations of Morgan Crucible's Ethics Policy to report these confidentially without fear of retribution should they feel they cannot use a local channel.

Morgan Crucible's global Anti-Trust Compliance Programme is ongoing, with regular training for appropriate employees across the Group. Anti-Trust Compliance Officers within each business report to the Company Secretary as Global Compliance Director on the continuing effectiveness of the programme. The Anti-Trust Compliance Programme includes independent audits, the results of which are considered by the Company Secretary who reports to the Executive Committee and the Board on the effectiveness of the programme and on any issues arising.

### Community

The implementation of our community-related policies and procedures is aligned with the management of our overall business and is focused at site level on engagement and initiatives which are relevant to the local community and to our business. Divisional and Group support is made available where appropriate. All charitable and other donations are fully accounted for.

### Customers and suppliers

The Chief Executives of each of our Divisions have specific responsibility for customers and suppliers and the related policies and procedures within their respective Divisions.

### Verification of ESG disclosures

Our Company Secretary, the Director of Risk Assurance and the Director of EHS work with independent external consultants to review and where appropriate verify our environmental, social and governance disclosures. This process covers the environmental and health and safety-related non-financial key performance indicators included in this Report.

All Morgan Crucible businesses are regularly reviewed under the Group's Compliance Audit Programme and those sites and businesses certified to ISO 9001, ISO 14001, OHSAS 18001 and other standards have regular external audits. The Group also uses external professional advisers in relation to specific health and safety and environmental matters as required.

The Board considers that these procedures provide a reasonable level of assurance that the Group's ESG disclosures are free from material misstatement, whether caused by fraud or other irregularity or error.

# Corporate responsibility continued

## Corporate responsibility policy effectiveness

### Business ethics

During the year ethics-related issues raised through the Whistleblowing line, the dedicated ethics email facility or via other channels were followed up by the Director of Risk Assurance in consultation with the Company Secretary. Further investigations may be conducted through the Audit Committee as required. Where appropriate, disciplinary action is taken and/or additional guidance and training provided. In respect of the Anti-Trust Compliance Programme, the independent audits referred to above confirm the continued effectiveness of the programme.

### Customers and suppliers

Morgan Crucible continues to benefit from long-term relationships with many customers and suppliers, reflecting the effectiveness of our customer service and supplier-related strategies. Some examples of our customer relationships are included on pages 6 to 27 of this Annual Report.

### Community

During the year, and including donations of £235,592 made by NP Aerospace, the Group's charitable donations increased to £302,232 (2008: £114,736). This is in addition to the time given and donations made by Morgan Crucible employees around the world.

During 2009, Morgan Crucible supported a number of initiatives at Group, Divisional and site level. The main emphasis of this support is to help disadvantaged young people and sponsor local community projects which can also engage and involve employees. Example initiatives include:

- The Group continued its three-year, £60,000 programme to support the Army Cadet Force Association (ACFA) Outreach Project.
- Morgan Crucible continues to support the joint Barnardo's/Outward Bound initiative which provides opportunities for young people to develop life skills at a centre in Ullswater, UK.
- Our Divisions sponsor a number of local sports facilities and the teams that use them. For instance, NP Aerospace is a major sponsor of the Godiva Harriers, the oldest athletics club in Coventry, UK. Formed in 1879, the Godiva Harriers cater for all types of athletic events and age groups. In addition, Technical Ceramics, Stourport, UK provides support to the local football team, and in the USA, the Carbon Division supports a number of athletic teams in St Mary's, PA, USA.
- NP Aerospace also supports Help for Heroes, the UK based charity which helps wounded Servicemen and women, as well as a number of related charitable causes.
- The Company also supports the British Transplant Games, an annual four-day event which encourages transplant patients to regain fitness whilst also increasing public awareness of the value of organ donation.
- The Carbon Division's site near Johannesburg, South Africa, organised a 'wellness day'. Some 100 employees participated, increasing their awareness of the importance of a healthy lifestyle, preventative screening and staying HIV negative. The wellness day is planned to be an annual event in future.

Our staff also support a variety of local and national initiatives and projects, helping to raise funds and giving their time. Examples of employee activities include:

- Employees at the Carbon site in Greenville, SC, USA and at the Technical Ceramics site in New Bedford, MA, USA continue to be strong community supporters. Working closely with United Way, employees pledge payroll deductions to local charities, make donations to local United Way programmes and participate in the United Way Day of Caring, when they help with landscaping, painting and other community tasks.
- The Technical Ceramics site in Waldkraiburg, Germany held an on-site auction which raised £1,500 for a local children's day-care centre.
- The Morgan Crucible head-office team participated in the 26.2 mile Maidenhead relay marathon to raise money for The Link Foundation, a charity which helps care for children in difficult circumstances.

# Environment, health and safety

Our Environment, Health and Safety (EHS) Policy and implementation programmes support our five strategic priorities and our Core Values Statement. The regular collection and reporting of EHS key performance indicators (KPIs) and the setting of EHS-related targets assist us in the development and monitoring of programmes to reduce the impact of our operations on the environment.

The Company is committed to conducting all its activities in a manner which achieves the highest practicable standards of health and safety for our employees and others affected by our operations.

This Report includes a summary of our EHS Policy and its effectiveness as demonstrated through our EHS KPIs and programmes. Further detail will be included in our 2009 EHS Report to be published on our website in April 2010. The EHS Report will also include case studies to help demonstrate our approach to enhancing the sustainability of our business.

## EHS Policy

The Group's EHS Policy applies Group-wide. It is made available to all employees and is published on our website and in our annual EHS Report.

During 2009, we reviewed and externally benchmarked our Group EHS Policy. The revised policy has been agreed by the Executive Committee and approved by the Board. In addition to statements of EHS policy, the new EHS Policy clearly sets out the responsibilities for EHS matters throughout the Group.

Our EHS Policy requires high standards of EHS management at all sites. This is achieved through risk assessment and the management and mitigation of identified risks to help provide continuous improvement in environmental, health and safety performance in support of our strategic priorities.

## EHS Policy implementation

Our EHS Policy forms the basis of our environment, health and safety management systems and processes. The management of our environmental and health and safety performance is aligned with the operation of our day-to-day business. The Chief Financial Officer has specific responsibility for EHS Policy and performance, supported by the Director of Environment, Health and Safety. Operational responsibility is delegated to the Chief Executive of each Division and the manager of each operation. In practice, all employees are responsible for ensuring that our EHS Policy is implemented and for identifying additional areas and opportunities for further development.

Morgan Crucible's environmental and health and safety management processes include the EHS Compliance Audit Programme carried out by external auditors in Europe and Asia and in-house resources in the Americas. This programme provides assurance of the EHS management at each site and helps ensure compliance with local regulations and good management practice. All of the Group's manufacturing facilities are audited on a three-year rolling cycle. Thirty-three sites were audited during 2009, including all seven of the Group's Chinese facilities. This enabled the effectiveness of the first stage of the Group's Chinese EHS training and improvement programme to be independently assessed. Our target for 2010 is to audit a further 26 sites.

Training is an integral part of our EHS Policy implementation. During 2008 we implemented an in-depth EHS training programme at all of the Group's facilities in China. The programme was carried out with the assistance of external consultants and included comprehensive training of senior management and the development and implementation of EHS management systems at all sites. The EHS Compliance Audits carried out at all of these facilities in 2009 showed a substantial improvement in EHS performance. A small number of areas requiring further improvement were identified and these are being addressed in the next stage of the programme, which is currently underway.

The success of the Chinese programme demonstrated the benefits of focused EHS training and a similar programme is being developed for the Group's six manufacturing facilities in India. This programme will be implemented in 2010.

Environmental management systems are in place at 89 sites worldwide, representing over 90% of output, including 34 major sites or 38% of output certified to ISO 14001 (2008: 27 sites and 43% of output). Seven sites achieved certification in 2009, however, the proportion of our output covered by ISO 14001 certification declined due to the consolidation of NP Aerospace. We plan for the main NP Aerospace sites to be certified over the period of 2010-11. These new certifications are in addition to the ongoing programme of recertifications. All of our major sites worldwide have health and safety management systems in place, with nine sites certified to or working towards OHSAS 18001.

# Corporate responsibility
continued

## Environment, health and safety
continued

**$CO_2$ intensity***
Tonnes/£m revenue**

| | |
|---|---|
| 2009 | 400 |
| 2008 | 464 |
| 2007 | 487 |
| 2006 | 516 |

**Energy intensity†**
mWh/£m revenue**

| | |
|---|---|
| 2009 | 1,283 |
| 2008 | 1,471 |
| 2007 | 1,541 |
| 2006 | 1,692 |

**Waste intensity♦**
Tonnes/£m revenue**

| | |
|---|---|
| 2009 | 65 |
| 2008 | 73 |
| 2007 | 85 |
| 2006 | 94 |

**Water intensity#**
$m^3$/£m revenue**

| | |
|---|---|
| 2009 | 2,563 |
| 2008 | 2,816 |
| 2007 | 3,321 |
| 2006 | 4,450 |

### EHS Policy effectiveness
In addition to the EHS Compliance Audit Programme, the Group monitors the effectiveness of its EHS Policy through a series of EHS KPIs. These are reported Group-wide on a monthly basis and the Executive Committee and the Board receive reports every six months.

During 2009 we extended our EHS reporting to cover NP Aerospace. The data in this Report includes the environmental and health and safety impacts of this business following the Group's acquisition of a majority stake in January 2009.

Where necessary, historic data has been restated to reflect changes to the business with environmental intensity KPIs reported at constant currency. The summary charts on pages 52 and 53 represent the Group's EHS performance in real terms, covering 100% of production sites during the year.

The verification of our environmental, social and governance disclosures is discussed on page 49.

### Environmental performance
Wherever possible we work to minimise the impact of our business on the environment and to maximise the positive environmental benefit of our products.

Our environmental target for the two years 2009-10 is to reduce the intensity of our $CO_2$ emissions due to all sources of energy use by 5% in real terms. $CO_2$ intensity was down by 14% in 2009. In absolute terms total $CO_2$ emissions due to energy use were some 393,000 tonnes against 464,000 tonnes in 2008, 444,000 tonnes in 2007 and 419,000 tonnes in 2006. Our waste intensity was down by 11% in the year, ahead of our 5% reduction target for the two years 2009-10. The proportion of total waste which was recycled was 28% in 2009, down one percentage point on the prior year and thus we are not on track to achieve our target to increase the level of recycling to 35% of total waste over the period 2009-10. Water intensity was down 9% in 2009 and we are ahead of the targeted 5% reduction over the two years 2009-10.

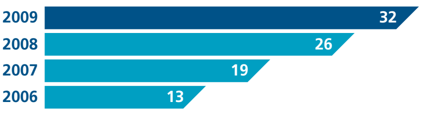
We will again be targeting reductions in our energy, emissions, waste and water intensity in 2010 to ensure we achieve our targets for the two-year period 2009-10. Further details will be included in our EHS Report to be published on our website in April 2010.

* $CO_2$ equivalent from all energy sources, including country-specific electricity.
** Constant currency basis, includes inter-company sales.
† Energy from all sources.
♦ Hazardous and non-hazardous waste. Includes recycled material.
# Water from all sources. Includes process and irrigation use.

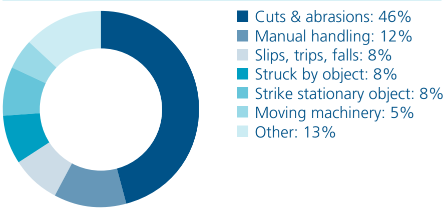
**Lost time accident frequency***
LTAs/100,000 hours


**Health and safety-related lost time**
% of total working time


**Lost time per LTA***
Days per LTA




**Accident causes**
%




## Health and safety performance

Our long-term health and safety objective is to have no accidents. In 2010 we will continue to extend our accident prevention and training programmes throughout the Group with the objective of reducing the time lost per lost time accident and placing particular focus on those sites with below average performance.

Our health and safety KPIs include accident frequencies and causes and related lost working time. These are used to monitor the effectiveness of our health and safety policies and related systems on a monthly basis.

The Group's accident reporting and analysis systems continue to be refined to enable us to produce KPIs that more accurately reflect the health and safety situation throughout the Group.

Our EHS Policy implementation programmes, including the training programme mentioned on page 51, helped to drive down the frequency of lost time accidents across the Group to 0.56 per 100,000 hours worked. The number of lost time accidents was down by over 25%. Manual handling cuts and abrasions are the most common cause of accidents and we will be working to address this, specifically targeting businesses with below-average performance.

The number of days lost due to accidents was down 13% in the year but, as a result of the reductions in working time at many facilities worldwide, relative lost time performance was flat at 0.14% of working time although many businesses improved performance in this area. However, with the reduced number of lost time accidents, the average time lost per lost time accident increased to 32 days, although this figure includes a small number of more long-term cases.

* Lost time accident (LTA): accident which results in one or more days' lost time.

# Corporate responsibility continued

## Our people

During a period of global economic recession, the capabilities, flexibility and tenacity of our people have enabled Morgan Crucible to achieve a resilient performance in 2009. In almost every area of the business our people have been affected in some way and while the business has been constrained to directly reward them their commitment and effort have not waned. We will continue to leverage that commitment and the significant talents of our people around the world to create a network that reaches our customers and supports their individual needs globally.

### People policies

We support the Universal Declaration of Human Rights and our Human Rights Policy commits us to protect the rights of everyone who works for the Company and all those who have dealings with it. The principles of the policy cover child labour, forced labour, health and safety, freedom of association, discrimination, discipline, working hours and compensation and the policy is published on our website. The Director of Human Resources reports to the Chief Executive Officer and is responsible for the development of human rights policy and related matters, with the Chief Executive of each Division having responsibility for policy implementation within their respective Divisions. The Morgan Crucible Whistleblowing line enables employees who are aware of or suspect issues under our Human Rights Policy to report these confidentially.

Our global Human Resources Policy provides an infrastructure of human resource activities that enables the business to attract, retain and engage people with the skills and capabilities to deliver its business plans and outperform the competition.

Key to building and maintaining the trust and respect of our people is open, timely and factual communication. Our systems provide two-way communication forums through online working areas encouraging greater collaboration. The Divisions communicate regularly through employee forums, team briefs and Divisional magazines. We are committed to providing our people with the opportunity to give feedback through regular global employee surveys. Listening to our people and harnessing their knowledge and experience of Morgan Crucible is essential to continuously improve and grow the business over the long term.

Demands on the business are constantly growing and changing, requiring the placement of current and new talent into jobs that fit those business requirements, at the time they are needed. We review short- and long-term business needs on a regular basis and carry out succession planning and talent reviews to identify any skill gaps. When recruiting for a vacant position we will draw from internal talent and where necessary seek external candidates. Selection is based on many factors including a candidate's relevant education, work experience, competencies and performance record. We provide equal opportunities in recruitment and employment ensuring we do not discriminate against any person based on sex, race, caste, origin, religion, disability, gender, sexual orientation, age or any other status protected by law. Should existing employees become disabled, our policy is to provide continuing employment and training wherever practicable.

For the business to achieve superior performance there is an expectation that our people need to operate at superior levels. We aim to support them through a formalised performance management system cascaded through the businesses that focuses on setting clear results-based objectives directly linked to the strategic goals and annual objectives of the business. Providing people with the skills to perform at a superior level is also critical, and we see continuous learning and their professional development as a major investment in our future.

We recognise and celebrate the accomplishments achieved by our people individually or as teams. In acknowledging and celebrating achievement, loyalty, innovation and creativity, we strive to motivate and inspire employees towards the pursuit of performance excellence, creating a sense of pride in their work and in Morgan Crucible. Our compensation systems reward people who apply their knowledge, skills and talents to support the achievement of business goals. We pay for performance in all our compensation practices. The total reward package includes a mix of base pay, variable pay and benefits. We establish compensation levels that are both competitive and affordable to Morgan Crucible. We have the flexibility to respond to changing market conditions and competition for high-demand skills, while maintaining equity in salary ranges and pay levels.

### Implementation of our people-related policies

The implementation of our Human Rights Policy is supported by an online learning programme that is translated into Brazilian Portuguese, Latin American Spanish and Mandarin Chinese. The assessment of compliance with this policy is part of our annual certification process.

During the year we launched the Morgan Crucible intranet, renamed by our people as 'MorgaNet'. MorgaNet provides fast and efficient access to information from diverse sources across the globe. We also introduced our global '360' e-magazine in an online version in addition to having hard copies available in 13 languages. The Divisions continue to issue regular Divisional newsletters in both soft and hard formats. In Europe we have an established consultative arrangement that provides an arena for the exchange of relevant and appropriate information across the European region. We also held our 13th annual European Employee Forum in April 2009 where site representatives attended from France, Germany, Hungary, Italy, the Netherlands and the UK.

**Total lost time***
% of working time


**Employee turnover***
% per year


**Training***
Hours per employee


We have introduced a Learning Management System that enables managers and employees to track and record their learning and development and link specific development to the achievement of business goals and objectives. In our online Development Centre, we added a number of new e-learning programmes throughout the year: Microsoft IT, e-appraisal and compliance training, while continuing with a Business English language module. A number of new employee development initiatives have been introduced in our businesses. Insulating Ceramics has developed and introduced e-learning programmes to support the implementation of its 'World Class Manufacturing' programme, while Carbon China has set up a Virtual Learning Resource Centre with Time Guanghua School to support a breadth of technical and business management training. A new training centre has been opened at Morgan Carbon South Africa providing greater flexibility to support a range of training initiatives from adult basic education through to production technology qualifications.

In pursuit of growing capability in the labour market, Morgan Crucible continues to sponsor annually the Science, Engineering & Technology Student of the Year Awards. We are proud to sponsor this event as we believe it allows high-calibre students to showcase their remarkable research work and demonstrate the depth of ability of graduates in the UK. In 2009 the winner of the Best Materials Student award was Michael Robinson from Sheffield University.

### People policy effectiveness

At the end of the year, Morgan Crucible employed some 9,400 people, a reduction of 11.9% on the previous year. Our geographic coverage has 35% of employees in Europe, Middle East and Africa, 37% in the Americas, and 28% in Asia Pacific. Of these employees 97% are 'permanent' and 73% are male. Lost time as a proportion of total working time was 2.7% with lost time due to accidents in the workplace of 0.14%. The training hours per employee were 12.4.

This reflects a reduction in expenditure on direct training during this period. However, we are looking forward to this increasing in 2010 with the ability to collate data from our new Learning Management System. Our employee turnover increased to 16.7% in 2009. This regrettably reflects an increase in the number of people made redundant during the year and the challenges of retaining talent in China where the labour market is exceptionally fluid.

During this period 19 employees around the world celebrated 40 years of loyal service with Morgan Crucible, with 117 employees celebrating anniversaries of 20, 25 and 30 years service. This year we regretfully said goodbye to Bill Byrd who retired at the age of 83. The transportation specialist based in our Insulating Ceramics plant in Augusta, GA, USA, decided to retire after 62 years' of loyal service with Morgan Crucible. To reflect our long-serving employee base we have improved our method of calculating employee tenure for 2009 and our average length of service is 11.3 years.

Morgan Crucible carried out an employee survey in October 2008 and an overview of the results was reported in the 2008 Annual Report. Throughout 2009 we have focused on completing actions related to improving communications and growing the skills of our employees through effective performance management and focused development programmes.

* 2009 data covers 100% of employees (2008: 96%; 2007: 66%) (for comparison purposes these KPIs exclude the Indian facility which was subject to a 'lock-out' during part of 2008 and 2007).

# Financial review

**Kevin Dangerfield**
Chief Financial Officer

Our strategy of focusing on higher growth, higher margin, less economically cyclical markets has generated a good performance with greatly improved resilience of earnings.

### Introduction

These results are produced under International Financial Reporting Standards as adopted by the EU (adopted IFRSs). All the figures referred to below are extracted from the financial statements on pages 88 to 148 and comply with adopted IFRSs.

Reference is made to 'Underlying operating profit'* and 'Underlying earnings per share (EPS)'. EPS is defined in note 9 on pages 109 and 110. These measures of earnings are shown because the Directors consider that they give a better indication of underlying performance.

### Group revenue and operating profit

Group revenue was £942.6 million (2008: £835.0 million), an increase of 12.9% compared to 2008. On a proforma constant currency basis Group revenue declined by 8.7% from the previous year. The proforma calculation assumes that NP Aerospace had been consolidated in 2008 to enable a like-for-like comparison.

Group EBITA before restructuring costs and one-off items was £89.0 million (2008: £108.8 million) representing a margin of 9.4% (2008: 13.0%).

Group underlying operating profit was £77.0 million (2008: £98.2 million). Underlying operating profit margins were 8.2%, compared to 11.8% for 2008.

Group operating profit was £60.7 million (2008: £95.0 million). Operating profit margins were 6.4%, compared to 11.4% for 2008.

* Underlying operating profit is defined as operating profit before amortisation.

| | Carbon | | Technical Ceramics | | Insulating Ceramics | | Consolidated | |
|---|---|---|---|---|---|---|---|---|
| | **2009 £m** | 2008 £m | **2009 £m** | 2008 £m | **2009 £m** | 2008 £m | **2009 £m** | 2008 £m |
| Revenue | **391.4** | 239.9 | **206.0** | 212.2 | **345.2** | 382.9 | **942.6** | 835.0 |
| Divisional EBITA* | **40.5** | 36.3 | **25.1** | 31.6 | **27.6** | 45.6 | **93.2** | 113.5 |
| Unallocated central costs | | | | | | | **(4.2)** | (4.7) |
| Group EBITA | | | | | | | **89.0** | 108.8 |
| Restructuring costs and other one-off items | | | | | | | **(12.0)** | (10.6) |
| Underlying operating profit | | | | | | | **77.0** | 98.2 |
| Amortisation of intangible assets | | | | | | | **(16.3)** | (3.2) |
| Operating profit | | | | | | | **60.7** | 95.0 |

* Divisional EBITA is defined as segment operating profit before one-off items and amortisation of intangible assets.

The Group has undertaken extensive cost reduction programmes across its business in 2009, the majority of which were completed in the first half of the year. Our focus, particularly in the first half of the year, was to rapidly resize and adjust our cost base to reflect weakening market demand. Net restructuring costs and gain on disposal of property were £12.9 million in 2009 (2008: £9.7 million) and costs recovered associated with the settlement of prior period anti-trust litigation were £0.9 million (2008: cost incurred £0.9 million).

**Foreign currency impact**

The principal exchange rates used in the translation of the results of overseas subsidiaries were as follows:

| | Average rate | | Year-end rate | |
|---|---|---|---|---|
| | **2009** | 2008 | **2009** | 2008 |
| US$ | **1.5687** | 1.8552 | **1.6149** | 1.4450 |
| Euro | **1.1249** | 1.2582 | **1.1255** | 1.0408 |

The potential impact of changes in foreign exchange rates is given in note 19 on pages 125 and 126.

**Amortisation of intangible assets**

The Group amortisation charge was £16.3 million (2008: £3.2 million). The increase in amortisation is mainly attributable to a fair value assessment of the assets of NP Aerospace at the date of the 11% acquisition. The amortisation calculation is driven by the NP Aerospace order book which has been 'fair valued' as part of the intangible assets and amortised over the 12-month period over which the orders were delivered. Hence in 2009 the Group had a one-off increase in its amortisation charge for the year. In 2010 the Group amortisation charge will be reduced to circa £7.5 million per annum, which includes the amortisation on the other ongoing intangible assets the Group has booked on the acquisition of NP Aerospace, the Carpenter businesses and other historical acquisitions.

**Finance costs**

The net finance charge was £29.3 million (2008: £12.7 million). Net bank interest and similar charges were £22.8 million (2008: £14.3 million), an increase of £8.5 million, due mainly to the increase in average net debt in 2009 following the NP Aerospace and Carpenter business acquisitions. A significant part of the finance charge under IFRSs is the net interest charge on pension scheme liabilities which was £4.3 million (2008: £0.1 million gain). Also included in the finance charge is an interest expense on unwinding of discount on deferred consideration of £2.2 million (2008: £nil) which relates to the NP Aerospace acquisition.

The impact of potential changes in interest rates on profit or loss is stated in note 19 on pages 124 and 125.

**Taxation**

Group taxation for the year was £8.7 million (2008: £20.1 million). The effective tax rate was 27.7% (2008: 24%).

**Earnings per share**

Underlying earnings per share was 13.2 pence (2008: 23.4 pence), Basic earnings per share, was 7.1 pence (2008: 22.2 pence). Details of these calculations can be found in note 9 on pages 109 and 110.

**Dividend**

The Board is recommending a final dividend of 4.5 pence per share, bringing the total dividend for the year to 7.0 pence per share, in line with the previous year's dividend. The dividend will be paid on 9 July 2010 to Ordinary shareholders on the register of members at the close of business on 21 May 2010. Subject to shareholder approval at this year's Annual General Meeting a scrip alternative to the cash dividend will be offered and will replace the existing DRIP scheme.

A five-year summary of the Group's financial results is set out on page 148 of this Report.

# Financial review
continued

## Cash flow

The net cash inflow from operating activities was £134.5 million (2008: £111.2 million), an increase of 21% over the previous year. Free cash flow before one-off costs and dividends was £85.9 million, a substantial increase in cash generation on the previous year (2008: £34.7 million), driven by strong working capital management. Working capital generation was a net inflow of £25.8 million compared to last year's outflow of £21.8 million. At the year end, the Group had net borrowings of £252.7 million, an improvement of £37.7 million compared to the 2008 year-end position of £290.4 million.

| | 2009 £m | 2008 £m |
|---|---|---|
| **Net cash inflow from operating activities** | 134.5 | 111.2 |
| Net capital expenditure | (13.7) | (31.5) |
| Net interest paid | (23.2) | (16.9) |
| Tax paid on ordinary activities | (11.7) | (28.1) |
| **Free cash flow before one-off costs and dividends** | **85.9** | **34.7** |
| One-off costs: | | |
| – Restructuring costs and other one-off items | (12.1) | (11.5) |
| – Tax settlement | (20.3) | – |
| Dividends paid | (12.1) | (18.8) |
| Cash flows from other investing and financing activities | (32.0) | (98.3) |
| Exchange rate movement | 28.3 | (76.8) |
| Opening net debt* | (290.4) | (119.7) |
| **Closing net debt** | **(252.7)** | **(290.4)** |

* Net debt is defined as interest-bearing loans and borrowings and bank overdrafts less cash and cash equivalents.

Commitments for property, plant and equipment and computer software for which no provision has been made are set out in note 24 on page 137.

## Capital structure

At the year end total equity was £214.6 million (2008: £208.0 million) with closing net debt of £252.7 million (2008: £290.4 million).

Non-current assets were £619.6 million (2008: £583.8 million) and total assets were £1,041.2 million (2008: £1,078.7 million). The most significant elements of these movements were the translation effect of the US dollar and the purchase of a further 11% stake in NP Aerospace in January 2009, taking Morgan Crucible's stake to a controlling 60% holding. As a result this business has been consolidated into the Group results for the first time in 2009. Please refer to note 3 on pages 104 to 106 for further details of the accounting in respect of this transaction.

Details of undiscounted contracted maturities of financial liabilities and capital management are set out in note 19 on page 123.

There have been no significant post-balance sheet events.

Capital structure is further discussed in note 19 on page 126 under the heading Capital management.

## Pensions

The Group operates a number of pension schemes throughout the world, the majority of which are of a funded defined benefit type. The largest of these are located in the UK and the US with others in Continental Europe. Net employee benefit liabilities totalling £105.9 million are included in the financial statements at the end of the year, an increase of £4.1 million compared with the previous year. The main movements have been in the US and UK pension schemes. The US scheme deficit improved by £15.2 million to £46.2 million (2008: £61.4 million) while the UK scheme deficit deteriorated to £34.5 million (2008: £13.1 million), mainly due to an increase in the inflation rate and a lower discount rate. Refer to note 20 on pages 129 to 132 for further details.

## Treasury policies

The following policies were implemented and in place across the Group throughout the year. The manager of each business unit is required to confirm this as part of the year-end process.

### Financial risk management and treasury policy

Group Treasury works within a framework of policies and procedures approved by the Audit Committee. It acts as a service to Morgan Crucible's business, not as a profit centre, and manages and controls risk in the treasury environment through the establishment of such procedures. Group treasury seeks to align treasury goals, objective and philosophy to those of the Group. It is responsible for all of the Group's funding, liquidity, cash management, interest rate risk, foreign exchange risk and other treasury business. As part of the policies and procedures, there is strict control over the use of financial instruments to hedge foreign currencies and interest rates. Speculative trading in derivatives and other financial instruments is not permitted.

### Foreign exchange risks

Due to the international reach of the Group, currency transaction exposures exist. The Group has a policy in place to hedge all material firm commitments and highly probable forecast foreign currency exposures, and achieves this through the use of the forward foreign exchange markets. The Group continues its practice of not hedging income statement translation exposure.

There are exchange control restrictions which affect the ability of a small number of the Group's subsidiaries to transfer funds to the Group. The Group does not believe such restrictions have had or will have any material adverse impact on the Group as a whole or the ability of the Group to meet its cash flow requirements.

Currency translation risks are controlled centrally. To defend against the impact of a permanent reduction in the value of its overseas net assets through currency depreciation, the Group seeks to match the currency of financial liabilities with the currency in which the net assets are denominated. This is achieved by raising funds in different currencies and through the use of hedging instruments such as swaps, and is implemented only to the extent that the Group's gearing covenant under the terms of its loan documents, as well as its facility headroom, are likely to remain comfortably within limits. In this way, the structure of the Group's borrowings becomes more aligned to the trading cash flows that service them.

### Interest rate risk
The Group seeks to reduce the volatility in its interest charge caused by rate fluctuations. The Group adopts a policy of ensuring that between 30% and 80% of its exposure to changes in interest rates on borrowings is on a fixed rate basis. This is achieved through a combination of fixed rate debt and interest rate swaps.

### Borrowing facilities and liquidity
All of the Group's borrowing facilities are arranged by Group Treasury and the funds raised are then lent to operating subsidiaries on an arm's-length basis. In a few cases operating subsidiaries have external borrowings but these are supervised and controlled centrally. Group Treasury seeks to obtain certainty of access to funding in the amounts, diversity of maturities and diversity of counterparty as required to support the Group's medium-term financing requirements and to minimise the impact of poor credit market conditions.

In May 2009 the Group announced the signing of a new three-year multi-currency facility for £280 million from a syndicate of eight banks. This has replaced the US$420 million facility which was due to mature in March 2010. Further information on the Group's debt and maturity profile is provided in note 18 on page 119.

### Credit risk
Credit risk arises when a counterparty fails to perform its obligations. The Group is exposed to credit risk on financial instruments such as liquid assets, derivative assets and trade receivables. Credit risk is managed by investing liquid assets and acquiring derivatives in a diversified way from high-credit-quality financial institutions. Counterparties are reviewed through the use of rating agencies, systemic risk considerations, and through regular review of the financial press. The Group has a credit policy in place in relation to trade receivables and exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. The nature of the Group's operations are such that the Group has a significant number of low-value trade receivables. The risk is therefore considered minimal. Credit risk is further discussed in note 19 on pages 121 and 122.

### Capital investment
The Group has well-established formal procedures for the approval of investment in new businesses and of capital expenditure to ensure appropriate senior management review and sign-off.

### Tax planning risk
The Group's reported after-tax income is calculated based on the relevant tax legislation in each of the jurisdictions that it operates in. Changes in tax legislation (including tax rates) could materially affect the Group's after-tax income. The Group undertakes tax planning initiatives where appropriate. The outcome of such planning cannot be assured and could materially influence the effective tax rate.

### Accounting policies
We adopted International Financial Reporting Standards as adopted by the EU ('adopted IFRSs') in 2005. All accounting policies shown on pages 93 to 101 are compliant with adopted IFRSs.

### Going concern
The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business review on pages 32 to 63. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described earlier in this Financial review. In addition, note 19 includes the Group's policies and processes for managing financial risk; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

The Group announced in May 2009 the signing of a new £280 million three-year multi-currency revolving facility agreement with a syndicate of eight banks. This replaced a US$420 million facility with the same financial covenants which was due to mature in March 2010. The Group meets its day-to-day working capital requirements through local banking arrangements that are supported through the flexibility provided by the new facility. The Group's forecasts and projections, taking account of reasonably possible changes in trading performance and exchange rates, show the Group operating comfortably within the Group's debt financial covenants for the next 12 months.

The current economic climate continues to have an impact on the Group, its customers and suppliers. The Board fully recognises the challenges that lie ahead but, after making enquiries, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and Accounts.

# Risk management

## Introduction

Our risk management processes are designed to be forward-looking in the identification, management and mitigation of business risks that could impact the Group's short- and long-term performance and value. The processes will not eliminate risks but rather mitigate them to an acceptable level within the context of the business environment in which we operate. The process covers both risks and opportunities.

Management of business risk is an integral part of delivering performance and is the responsibility of all managers. Our risk management decision-making and reporting procedures are integrated in our formal business reporting up to the Board.

The Group appointed a new Director of Risk Assurance at the end of 2008. During the year the Group reviewed and benchmarked its risk management methodologies and processes against external good practice. Following this review, the Board approved a plan to evolve the existing processes to a more coherent approach by using a formalised and standardised risk management methodology throughout the Group.

Implementation commenced in 2009 and will continue through 2010 with regular reports covering risk management processes and key risks to the Audit Committee and the Executive Committee through the Risk Management Committee. The Risk Management Committee is chaired by the Chief Financial Officer and includes representation from each Division. The effectiveness of risk management and internal control processes is monitored by the Audit Committee, which also ensures that the Board has sufficient information in this regard.

During the year the Group and its subsidiaries complied with its policies and procedures for managing material risks.

The risks described below include the main areas of risk that could impact Morgan Crucible. These cover most areas of known and emerging business risk. They include internal risks where we have a greater degree of control and influence as well as external risks where our ability to completely control them may be more limited. They are nevertheless assessed and managed down to an acceptable level. The relative importance of some of these risks has changed during 2008-09 as a result of the world recession. As a consequence the controls to manage risk have been adjusted to ensure that the risks continue to be managed within acceptable limits.

## Strategic planning risks

These risks relate to the appropriateness of strategy, business model or product portfolio, acquisitions and disposals. The risks to planning and delivery of the strategy are also included.

## External risks

### Political, economical and social

We are exposed to these risks in a number of countries in which we operate as part of realising business opportunities. We operate within the local conditions while monitoring the political, economic and social changes in these countries and adjusting our business plan, operations and controls accordingly.

### Financial

Operating in a number of countries, we are exposed to events in the financial environment including commodity and energy prices, currency exchange, the current credit crisis and other financial market incidents, market volatility, interest rates, liquidity, pension funding, tax planning etc. These risks are managed through proactive assessment, contingency planning and the use of appropriate mitigation.

Examples of mitigation include:

- → Optimising exchange rate exposure through the supply chain by raw material sourcing, manufacturing and selling locally to minimise exchange rate impact.
- → Minimising the impact on the Group of a major currency devaluation.
- → Fixing long-term pricing for the purchase of energy and other materials.
- → Entering into certain hedging arrangements to help manage the impact of currency fluctuations (the Group's relevant treasury policies are summarised in the Financial review on pages 58 and 59).
- → Managing pension funds using independent, competent Trustee Boards and external advisers.

Further details of the Group's pension plans and employee benefits are included in note 20 on pages 129 to 136.

### Market dynamics and competition

Our products tend to be technologically advanced and use complex and high-added-value manufacturing techniques. We operate in a business environment where we need to be proactive with respect to market dynamics including customer preference, new technology and new competition.

We monitor our current areas of business, working with our customers to ensure that we continue to satisfy their evolving needs. We adjust our strategies and business plans to reflect changing conditions, thereby helping to ensure that risks are managed within acceptable limits.

## Compliance and ethics risks

### Legal, regulatory and litigation

We are subject to varying laws and regulations around the world. Changes in these could affect the long- and short-term value of the Group. As a listed company we are also exposed to the risks of ensuring compliance with listing requirements. We cannot always predict whether future developments in laws and regulations concerning our businesses will have an adverse or a positive effect.

For example, a failure to comply with export control regulations could have a negative impact, whilst new environmental performance legislation which affects our customers could increase the demand for our energy-conserving products and services which can help our customers to address the requirements of such legislation.

To manage these risks, we monitor potential changes in regulation as well as having appropriate training and compliance processes in place.

From time to time, and in the normal course of business, we are subject to certain litigation, in particular in the USA. Provisions for the expected costs and liabilities are set out in note 21 to the accounts. If the liabilities arising were significantly to exceed the amounts provided for, there could be a material financial effect on the value of the Group.

### Health, safety and environmental

Our operations involve the normal environmental, health and safety risks associated with manufacturing operations in the countries in which we operate. Although we believe that our operations are in compliance with current regulations, we cannot eliminate the risk of all accidents or non-compliance.

Further detail of the programmes in place to manage these risks are included on pages 51 to 53.

### Business conduct risks

Risks such as a potential breach in the area of ethical behaviour could impact the Group's reputation or image.

Our reputation with our stakeholders is fundamental to the continued success of the Group and we mitigate reputational risks through various means, including:

- Our corporate responsibility programme, and our Core Values Statement.
- Our Ethics Policy, Whistleblowing line and related procedures.
- Our systems of internal control and risk management.

The Group's Ethics Policy and Anti-Trust Compliance Programme are further described in the Corporate responsibility section. These programmes address the risk of unethical business behaviour and are supported by mandatory training and the Group's Whistleblowing line and related procedures.

## Operational risks

### Financial, physical property, intellectual property and information

The Group's financial, physical and intellectual property assets are exposed to risks such as theft, loss, natural catastrophe, accidental disclosure etc. Such incidents can also impact the continuity of the business.

These risks are managed through internal controls, proactive design and protection of facilities and business continuity measures to minimise the impact of an incident. Audits by experts in their fields (including financial auditors) review and assess the effectiveness of such measures.

In some cases, risks are partially transferred through insurance programmes.

### Human resources risks

The Group maintains human resource policies and processes to manage the risks relating to our people, eg reward and recognition, health and safety, talent management including succession planning, skills assessment and development, performance management and employee consultation.

### Product development, performance and safety risks

Our products are used in many industrial sectors including medical, aerospace and defence. These sectors require high quality and conformance to specification as well as consideration of the health and safety of the end users.

Robust research and development processes, both in-house and where undertaken in co-operation with our customers, minimise product development risks. Our design, testing and quality assurance processes, including ISO 9001 accreditations, help to control manufacturing risks.

# Key resources and contractual relationships

Morgan Crucible has built up significant resources and benefits from contractual and other relationships with multiple stakeholders, including customers and suppliers, employees and joint venture partners. These have been built up over many years to support the Group's competitive positioning in the key markets which the Group serves.

As is described below, no one contractual or other relationship is considered essential to the business of the Group as a whole. Further information on the Group's stakeholder relationships is included elsewhere in this Business review, including in the Corporate responsibility section on pages 48 to 55. As referred to in the Directors' report on page 68, a number of commercial and contractual agreements include change of control provisions which come into effect in the event of a change in ownership of the Company following a takeover.

In accordance with its vision, aim and strategic priorities, the Group continues to invest in the areas discussed below to maintain its leading market positions.

### Commercial relationships, market position and reputation

Morgan Crucible is generally ranked number one or two in its chosen market segments. The Group is a world leader in advanced ceramic and composite materials. The Company was founded in 1856 and has a worldwide reputation.

The Group's businesses provide products and services to other companies and we have developed close working relationships with many of our customers and suppliers and work in collaboration with them to develop new products.

None of the Group's customers or suppliers are individually essential to the business of the Group as a whole. Notwithstanding this, the Group devotes significant resources to ensure these relationships continue to operate satisfactorily.

### Employees

Morgan Crucible's most important resource is its people and we employ a highly skilled and qualified workforce. One of our strategic priorities is 'finding, keeping and developing the right people'. Many employees stay with the Company for their whole careers as is highlighted on page 55. We place great emphasis on recruitment and training and our policies and performance in these areas are set out on pages 54 and 55.

Succession plans are in place covering key management and technical roles and as such no individual employee is considered essential to the business of the Group as a whole.

The Directors' contracts are referred to on page 82 and are available for inspection prior to the Annual General Meeting and at the Company's registered office.

### Research and development, patents and intellectual property

The Group's vision is to be one of the world's very best advanced materials companies, supported by the strategic priority of 'offering high added value to our customers'. The Group's Divisions use their extensive knowledge base, particularly in the areas of advanced ceramic and composite materials, to develop new products and services to meet customer needs and to differentiate themselves in the markets they serve.

The Group benefits from technological know-how and other forms of intellectual property, some of which is covered by patents. Collectively this intellectual property supports the development and manufacture of new products and services to meet customer needs, but no one single patent is considered essential to the business of the Group as a whole.

Each of the Group's Divisions has a Technical Director, with research and development capabilities variously located at Divisional centres of excellence and diffused through the business in the form of applications engineering. Further details are included in the review of operations for each Division on pages 36 to 47.

### Manufacturing capabilities

Over many years Morgan Crucible has invested heavily in manufacturing capacity and technology to develop its capability to serve its chosen markets worldwide. In recent years the Group has developed and extended its manufacturing presence and capabilities in China, India and Latin America to meet customer needs in both local and global markets. This investment supports our strategic priority of 'having a culture of operational excellence and cost efficiency'.

### Joint venture partners

In a number of territories around the world, the Group has established joint ventures with local partners. Many of these joint ventures have been in operation for many years; however, no individual joint venture agreement is considered to be essential to the business of the Group as a whole.

### Banking and other financial relationships

Details of significant banking and other relationships are referred to on page 68 in the Directors' report. However, no one banking relationship is considered to be essential to the performance and value of the Company.

# Cautionary statement

This Business review has been prepared for and only for the members of the Company as a body and no other persons. Its purpose is to assist shareholders to assess how the Directors have performed their duties, the Company's strategies and the potential for those strategies to succeed and for no other purpose. The Company, its Directors, employees, agents or advisers do not accept or assume responsibility for any other purpose or to any other person to whom this document is shown or into whose hands it may come and any such responsibility or liability is expressly disclaimed. This Business review and certain other sections of the Annual Report contain forward-looking statements that are subject to risk factors associated with, amongst other things, the economic and business circumstances occurring from time to time in the countries, sectors and markets in which the Group operates. These and other factors could adversely affect the outcome and financial effects of the plans and events described. Forward-looking statements by their nature involve a number of risks, uncertainties and assumptions because they relate to events and/or depend on circumstances that may or may not occur in the future and could cause actual results and outcomes to differ materially from those expressed in or implied by the forward-looking statements. It is believed that the expectations reflected in these statements are reasonable but they may be affected by a wide range of such variables. No assurances can be given that the forward-looking statements in this Report will be realised. The forward-looking statements reflect the knowledge and information available at the date of preparation and will not be updated during the year but will be considered in the Annual Report for next year. Nothing in this document should be construed as a profit forecast. This Business review has not been audited or otherwise independently verified.

# Board of Directors

**Tim Stevenson OBE†§**
Chairman

**Mark Robertshaw§**
Chief Executive Officer

**Kevin Dangerfield**
Chief Financial Officer

**Martin Flower*†§**
Senior Independent Director

**Andrew Given*†§**
Non-executive Director

**Simon Heale*†§**
Non-executive Director

# Executive Committee

**Don Klas**
CEO Carbon

**Andrew Hosty**
CEO Technical Ceramics

**Tim Hayter**
CEO Thermal Ceramics

**Paul Boulton**
Company Secretary

**Amanda Wooding**
Director of Human Resources

* Member of the Audit Committee.
† Member of the Remuneration Committee.
§ Member of the Nomination Committee.

# Board of Directors

**Tim Stevenson OBE†§**
**Non-executive Chairman**
Tim was appointed as Chairman of Morgan Crucible in December 2006. He is also Chairman of Travis Perkins plc, a position that he has held since November 2001. He was a non-executive Director of Tribal Group plc from 2004 to 2008 and was latterly the Senior Independent Director. From 1975 to 2000, Tim held a variety of senior management positions at Burmah Castrol plc, including Chief Executive from 1998 to 2000. He is a qualified barrister and is Lord Lieutenant of Oxfordshire.

**Martin Flower*†§**
**Senior Independent Director**
Martin was appointed as a non-executive Director in December 2004 and Senior Independent Director in April 2008. He is also Chairman of Croda International Plc and is a non-executive Director of Low & Bonar PLC. He was previously Chairman of Autogrill Holdings UK plc and a non-executive Director of Autogrill Group Inc. Martin held a variety of senior management positions with Coats plc from 1968 to 2004 and was Group Chief Executive of that Group and Chairman of the Board from 2001 to 2004.

**Mark Robertshaw§**
**Chief Executive Officer**
Mark was appointed as Chief Executive Officer in August 2006. Prior to this he was Chief Operating Officer from February 2006 and Chief Financial Officer from October 2004. Before joining Morgan Crucible he was Chief Financial Officer of Gartmore Investment Management Plc from 2000 to 2004. Mark is a non-executive Director of Rathbones Brothers plc. He previously worked for the NatWest Group and also spent nine years as a management consultant with Marakon Associates.

**Andrew Given*†§**
**Non-executive Director**
Andrew was appointed as a non-executive Director in December 2007 and is the Chairman of the Audit Committee. He is the senior non-executive Director and Chair of the Audit Committee at VT Group plc and was previously the Senior Independent Director and Chair of the Audit Committee of Spectris plc. He was also formerly a non-executive Director and Chair of the Audit Committee of Spirent Communications plc. He was previously Deputy Chief Executive of Logica CMG plc and held senior management positions in Plessey and Nortel Networks.

**Kevin Dangerfield**
**Chief Financial Officer**
Kevin was appointed as Chief Financial Officer in August 2006, having joined Morgan Crucible in July 2000 as Deputy Group Financial Controller before being promoted to Group Financial Controller. Before joining Morgan Crucible Kevin worked for London International Group plc and Virgin Retail Europe Limited. He qualified as a chartered accountant with PricewaterhouseCoopers.

**Simon Heale*†§**
**Non-executive Director**
Simon was appointed as a non-executive Director in February 2005 and is the Chairman of the Remuneration Committee. He is also Chairman of Panmure Gordon and Co plc and is a non-executive Director of Kazakhmys plc, PZ Cussons plc and Marex Group Limited. He was Chief Executive of China Now from 2007 to 2008 and was Chief Executive of the London Metal Exchange from 2001 to 2006. Simon qualified as an accountant with Price Waterhouse and has had extensive experience in the Far East, having held senior positions with the Swire Group in Japan and Hong Kong and with Jardine Fleming in Hong Kong.

# Executive Committee

**Mark Robertshaw**
Chief Executive Officer

**Kevin Dangerfield**
Chief Financial Officer

**Don Klas**
CEO Carbon

**Andrew Hosty**
CEO Technical Ceramics

**Tim Hayter**
CEO Thermal Ceramics

**Paul Boulton**
Company Secretary

**Amanda Wooding**
Director of Human Resources

* Member of the Audit Committee.
† Member of the Remuneration Committee.
§ Member of the Nomination Committee.

# Directors' report

The Directors present their report together with the financial statements and independent auditors' report for the year ended 3 January 2010. This Directors' report was approved by the Board on 18 February 2010.

## Principal activities and business review

The Morgan Crucible Company plc ('the Company') and its subsidiary undertakings comprise three reporting Divisions (as outlined on page 34) that design, manufacture and market primarily carbon and ceramic components for applications for a wide range of markets. A review of developments affecting the Group during the year and of its prospects for the future appears on pages 32 to 62, to be read in conjunction with the cautionary statement on page 63.

The Companies Act 2006 requires the Directors' report to include a Business review. Certain information that fulfils the requirements of the Business review can be found in this Directors' report and on page 34 (Group business review), pages 36 to 47 (Review of operations), 56 to 59 (Financial review), 60 and 61 (Risk management), and 48 to 55 (Corporate responsibility), to be read in conjunction with the cautionary statement on page 63.

## Financial results

The total profit for the year ended 3 January 2010 was £22.7 million (2008: £62.7 million). Profit before taxation for the same period was £31.4 million (2008: £82.8 million). Revenue was £942.6 million (2008: £835.0 million) and operating profit was £60.7 million (2008: £95.0 million). Basic earnings per share was 7.1 pence (2008: 22.2 pence). Capital and reserves at the end of the year were £214.6 million (2008: £208.0 million). The total profit of £22.7 million will be transferred to equity. The Group's accounting policies can be found on pages 93 to 101.

## Dividends

The Directors recommend the payment of a final dividend at the rate of 4.5 pence per share on the Ordinary share capital of the Company, payable on 9 July 2010 to shareholders on the register at the close of business on 21 May 2010. Together with the interim dividend of 2.5 pence per share paid on 12 January 2010, this final dividend, if approved by shareholders, brings the total distribution for the year to 7.0 pence per share (2008: 7.0 pence).

## Acquisitions and disposals

On 5 January 2009 the Company increased its equity stake in NP Aerospace from 49% to 60% by acquiring an additional 11% of the equity for £12.2 million, with a deferred consideration based on 2009 performance payable in 2010.

On 6 April 2009 the Company acquired, via its subsidiary NP Aerospace Limited, a 50% stake in Integrated Survivability Technologies Limited for £1.5 million.

On 25 September 2010 Morgan Advanced Ceramics Inc disposed of its Metal Injection Moulding business for £1.1 million cash.

On 9 October 2009 the Company acquired a further 9.0% of the issued share capital of Carbo San Luis SA for £1.1 million, bringing its interest in Carbo San Luis to 84.6%.

## Post-balance sheet events

There have been no material events since the year end. The Company proposes to pay a final ordinary dividend of 4.5 pence per share in respect of the 2009 financial year.

## Share capital

As at 3 January 2010, pursuant to an authority granted at the Company's Annual General Meeting on 17 April 2009, the Company was authorised pursuant to the Companies Act 1985 to purchase up to 9.99% of its issued share capital. This authority expires on the date of the Annual General Meeting to be held on 23 April 2010.

This authority was not used by the Company during the year under review.

The Company's share capital is set out in note 17 on pages 117 to 119. The Company's Ordinary shares represent 99.36% of the total issued share capital, with the 5.5% Cumulative First Preference shares representing 0.18% and the 5.0% Cumulative Second Preference shares representing 0.46%. The rights and obligations attaching to the Company's Ordinary shares, and restrictions on the transfer of shares in the Company, are set out in the Company's Articles of Association, copies of which can be obtained from Companies House in the UK or the Company Secretary. The holders of Ordinary shares are entitled to receive dividends, when declared; to receive the Company's reports and accounts; to attend and speak at general meetings of the Company; to appoint proxies; and to exercise voting rights. Details of the structure of the Company's Preference share capital and the rights attached to the Company's Preference shares are set out on page 119. No person holds securities in the Company carrying special rights with regard to control of the Company. The Company is not aware of any agreements between holders of securities that may result in restrictions on the transfer of securities or on voting rights. Unless expressly specified to the contrary in the Articles of Association of the Company, the Company's Articles of Association may be amended by a special resolution of the Company's shareholders.

## Policy on the payment of creditors

The Company's policy in relation to its suppliers is, where possible, to settle terms of payment when agreeing the terms of the transaction and to abide by those terms, provided that it is satisfied that the supplier provided the goods and services in accordance with the agreed terms and conditions. The Company and its subsidiaries do not follow any one code or standard on payment practice due to the diverse nature of the global markets in which the Group operates.

The number of days' purchases outstanding for payment by the Company at the end of the year was 18 days (2008: 33 days) and for the Group was 54 days (2008: 68 days).

## Research and development

Innovative use of existing and emerging technologies will continue to be crucial to the successful development of new products and solutions to customer demands. The Company has research and development facilities at its key manufacturing sites. The spend on research and development, which excludes the amounts spent working with customers and others by way of product enhancement and application engineering, was £14.6 million during the year (2008: £11.4 million), including £0.7 million of capitalised development costs (2008: £1.6 million).

## Financial instruments

Details of the Group's use of financial instruments, together with information on policies and exposure to credit, interest rate and currency risks, can be found in note 19 on pages 120 to 128.

## Human resources

Details of the Company's and the Group's personnel policies (including its policy on equal opportunities for disabled employees) and employee involvement are set out on pages 54 and 55.

There are no agreements between the Company and its Directors or employees providing for compensation for loss of office or employment (whether through resignation, purported redundancy or otherwise) that occurs because of a takeover bid.

## Employee share and share option schemes

The Company continues to encourage employee ownership of its shares through the provision of a number of employee share and share option schemes. 147 employees hold awards under the Morgan Crucible Long Term Incentive Plan, 36 employees hold awards under the Morgan Crucible Bonus Deferral Share Matching Plan, 58 employees have options under the Company's Executive Share Option Schemes and 621 employees participate in the Company's UK Sharesave Plan. There are 84 participants in the Company's German Employee Share Purchase Plan. There are currently no participants in the Company's US Employee Share Purchase Plan. Details of outstanding options are given in note 20 on pages 132 to 136.

NP Aerospace operates an employee share option scheme pursuant to which NP Aerospace employees who were in employment as at 31 July 2007 have been granted options over shares in Clearpower Limited, the NP Aerospace holding company. 146 employees hold awards under the NP Aerospace share option scheme. The NP Aerospace employee benefit trust holds 33,335 shares in Clearpower Limited in respect of the scheme.

All of the Company's share schemes contain provisions relating to a change of control. Outstanding options and awards would normally vest and become exercisable on a change of control, subject to the satisfaction of any performance conditions at that time.

The Morgan General Employee Benefit Trust ('the Trust') held 1,984,022 shares on 3 January 2010 in connection with awards granted under the Company's employee share schemes. In the period 3 January 2010 to 18 February 2010 no shares were transferred out of the Trust. The trustees of the Trust ('Trustees') have agreed to waive their entitlement to the payment of dividends on the shares held by the Trust. The Directors are not aware that any other shareholders waived or agreed to waive any dividends or future dividends during the period under review.

The Trustees have absolute and unfettered discretion in relation to voting any shares held in the Trust at any general meeting. Their policy is not to vote the shares. If any offer is made to shareholders to acquire their shares, the Trustees will have absolute and unfettered discretion on whether to accept or reject the offer in respect of any shares held by them.

## Directors

All those who served as Directors throughout the year under review are listed on page 64.

Details of Directors' interests in the share capital of the Company are listed on page 83. In the period from 3 January 2010 to 18 February 2010 the executive Directors acquired further Ordinary shares in the Company pursuant to the Company's Dividend Reinvestment Plan. The Directors' shareholdings are shown on page 83.

The details of those Directors who will be offering themselves for re-election at the forthcoming Annual General Meeting on 23 April 2010 are set out in the Circular to Shareholders which will be posted in March 2010.

# Directors' report
continued

Details of the background and experience of all the Directors can be found on page 64 and details of the Board Committees on which they serve can be found on pages 74 and 75.

The Company's Articles of Association ('the Articles') give the Directors power to appoint and replace Directors. Under the terms of reference of the Nomination Committee, any appointment must be recommended by the Nomination Committee for approval by the Board of Directors. The Articles also require Directors to retire and submit themselves for election at the first Annual General Meeting following appointment and all Directors are required to submit themselves for re-election at the third Annual General Meeting following their appointment or re-election.

Subject to the Company's Memorandum and Articles of Association, UK legislation and any directions given by special resolution, the business of the Company is managed by the Board, which may exercise all the powers of the Company.

The Directors may also seek authority from shareholders at each Annual General Meeting to allot shares, to disapply pre-emption rights and to make market purchases of the Company's Ordinary shares. These powers may be exercised under authority of resolutions of the Company passed at its Annual General Meeting.

As at the date of this Report, indemnities are in force under which the Company has agreed to indemnify all of the Directors, to the extent permitted by law and the Company's Articles of Association, in respect of all losses arising out of, or in connection with, the execution of their powers, duties and responsibilities, as Directors of the Company or any of its subsidiaries.

### Donations
During the year, Morgan Crucible companies made charitable donations of £302,232 (2008: £114,736).

Further details of charitable donations and activities of the Group are given on page 50. No political donations have been made.

### Significant agreements
As referred to in the Key resources and contractual relationships section on page 62, the Group has a number of borrowing facilities provided by various financial institutions. These facility agreements generally include change of control provisions which, in the event of a change in ownership of the Company, could result in renegotiation or withdrawal of these facilities.

The most significant such agreements are the UK £280 million Multicurrency Revolving Facility Agreement which was signed on 1 May 2009 and the privately placed Note Purchase and Guarantee Agreements signed on 6 March 2003 and 15 December 2007, for which the outstanding loan amounts are US$45 million and US$350 million respectively.

There are a number of other agreements that take effect, alter or terminate upon a change of control of the Company following a takeover bid, such as commercial contracts and joint-venture agreements. No such individual contract is considered to be significant in terms of its potential impact on the business of the Group as a whole.

### Substantial shareholdings
As at 18 February 2010, the Directors have been advised of the following holdings representing 3% or more of the issued Ordinary share capital of the Company*:

| Company | Number of Ordinary shares | %** |
|---|---|---|
| Standard Life Investments Ltd | 40,506,809 | 14.991 |
| JPMorgan Chase & Co | 13,591,569 | 5.030 |
| Schroders plc | 12,494,272 | 4.623 |
| Lloyds TSB Group plc | 10,907,770 | 4.037 |
| BT Pension Scheme Trustees Limited | 10,780,464 | 3.990 |
| Aegon UK | 10,751,020 | 3.979 |
| Legal & General Group plc | 10,738,156 | 3.974 |
| BAE Systems Pension Funds Management Ltd | 10,142,618 | 3.754 |
| Aviva plc | 9,039,613 | 3.345 |

* As at 23 February 2010, there was no change in the details shown in the above table with the exception of a notification received by the Company from JPMorgan Chase & Co that its disclosable holding had decreased to 11,935,619 Ordinary shares, representing 4.42% of the Company's issued Ordinary issued share capital at that date.
** Percentages are shown as a percentage of the Company's issued share capital as at 18 February 2010.

## Disclosures of information to auditors

The Directors who held office at the date of approval of this Directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware, and that each Director has taken all steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

## Auditors

KPMG Audit plc has expressed its willingness to continue in office. Resolutions for its reappointment as auditors and authority for the Directors to determine the auditors' remuneration will be proposed at the forthcoming Annual General Meeting.

## Annual General Meeting

The Annual General Meeting of the Company will be held on 23 April 2010 at St Anne's Manor, London Road, Wokingham RG40 1ST. A Circular will be sent with this report to shareholders in March 2010 incorporating the Notice of Annual General Meeting and detailing any special business to be transacted at that time.

## Directors' responsibility statement in respect of the Disclosure and Transparency Rules

We confirm to the best of our knowledge:

- The Group financial statements in this Report, which have been prepared in accordance with International Financial Reporting Standards as adopted by the EU ('adopted IFRSs'), including interpretations issued by the International Accounting Standards Board (IASB) and those sections of the Companies Act 2006 applicable to companies reporting under IFRSs as adopted in the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group taken as a whole.
- The parent Company financial statements in this Report, which have been prepared in accordance with UK Accounting Standards (UK Generally Accepted Accounting Practice) and applicable law, give a true and fair view of the assets, liabilities, financial position and loss of the Company.
- The Business review contained in this Report includes a fair review of the development and performance of the business and the position of the Company and the Group taken as a whole, together with a description of the principal risks and uncertainties they face.

For and on behalf of the Board

**Paul Boulton**
Secretary
18 February 2010

The Morgan Crucible Company plc
Quadrant, 55-57 High Street, Windsor, Berkshire SL4 1LP
Registered in England, No. 286773

# Corporate governance

## Statement of compliance with the Combined Code

Throughout the year ended 3 January 2010 the Company has been in compliance with Section 1 of the June 2008 edition of the Combined Code on Corporate Governance ('the Code').

This statement describes how the Company has applied the main and supporting principles of the Code. It should be read in conjunction with the Business review and Remuneration report on pages 32 to 63 and pages 77 to 85 respectively.

## Directors

### The Board

The Board is collectively responsible to the Company's shareholders for the success of the Company. The Board is satisfied it has met the Code's requirements for its effective operation. It has set the Company's strategic aims, which were reviewed by the Board at its strategy meeting during the year, and has ensured that there is a framework of prudent and effective controls which enable risk to be assessed and managed. The Board sets the Company's values and standards, which are contained in the Core Values Statement and Ethics Policy, both of which are referred to on pages 48 and 49 in the Business review.

The Board met formally 11 times during the year to review current performance against agreed objectives and to make and review major business decisions. There is a schedule of matters specifically reserved for the Board including significant contractual commitments (including the acquisition or disposal of companies/businesses, treasury and intellectual property transactions), the review of the effectiveness of risk management processes, major capital expenditure and corporate responsibility. One meeting each year is specifically focused on strategy and the longer term development of the Company. Various matters are delegated to duly authorised sub-committees of the Board, as is further described below.

There were no changes to the membership of the Board during the year and there were no changes of role.

As at 3 January 2010 the Board comprises Tim Stevenson, Chairman; Mark Robertshaw, Chief Executive Officer; Kevin Dangerfield, Chief Financial Officer, and three independent non-executive Directors. Martin Flower is the Senior Independent Director. Biographies of the Directors, including details of their other main commitments, are set out on page 64.

All Directors submit themselves for election by the shareholders at the first Annual General Meeting following their appointment and for re-election at least once every three years. Should a non-executive Director serve for more than six years, his re-election would be subject to particularly rigorous review. Should any Director serve for longer than nine years he would then be subject to annual re-election.

The attendance of each Director at Board and Audit, Remuneration and Nomination Committee meetings is set out in the table below.

| Director | Board Eligible to attend | Board Attended | Audit Eligible to attend | Audit Attended | Remuneration Eligible to attend | Remuneration Attended | Nomination Eligible to attend | Nomination Attended |
|---|---|---|---|---|---|---|---|---|
| Tim Stevenson* | 11 | 11 | – | – | 7 | 7 | 1 | 1 |
| Mark Robertshaw | 11 | 11 | – | – | – | – | 1 | 1 |
| Kevin Dangerfield | 11 | 11 | – | – | – | – | – | – |
| Martin Flower* | 11 | 11 | 5 | 5 | 7 | 7 | 1 | 1 |
| Andrew Given* | 11 | 11 | 5 | 5 | 7 | 6 | 1 | 1 |
| Simon Heale* | 11 | 11 | 5 | 4 | 7 | 7 | 1 | 1 |

Excludes meetings attended by invitation for all or part of a meeting.
* Indicates a Director deemed by the Board to be independent, or in the case of the Chairman, independent on appointment.

The Chairman and the non-executive Directors met without the executive Directors present on multiple occasions during the year. In addition, the Senior Independent Director and the other non-executive Directors met without the Chairman present.

Should a Director have concerns about the running of the Company or a proposed action which are not resolved, their concerns would be recorded in the Board minutes.

An appropriate Directors' and Officers' liability insurance policy is in place.

### Chairman and Chief Executive Officer

The roles of Chairman and Chief Executive Officer are separate, clearly established, set out in writing and agreed by the Board. The Chairman is responsible for running the Board and the Chief Executive Officer is responsible for running the Company's business. The management of the Group's operating Divisions report to the Chief Executive Officer.

## Board balance and independence

Throughout the year the Company complied with the requirement of the Code that at least half the Board, excluding the Chairman, should comprise non-executive Directors determined by the Board to be independent. At the year end, in addition to the Chairman, whom the Company deemed to be independent on appointment, the Board comprised two executive Directors and three further non-executive Directors deemed by the Board to be independent. In addition to the factors set out in the Code, the Board's assessment of a non-executive Director's independence and effectiveness covers their total number of commitments and any relationships with major suppliers or with charities receiving material support from the Company.

The structure and shape of the Board were reviewed during the year. The Board has frequent interaction with senior management and the Divisional Chief Executives normally attend Board meetings. Thus, it was considered that the current level of executive representation on the Board remains appropriate.

## Appointments to the Board

As is further detailed in the report of the Nomination Committee, set out on page 75, there is a formal, rigorous and transparent procedure for appointments to the Board.

The Board is satisfied that there are succession plans in place for appointments to the Board and for senior management.

There were no new appointments to the Board during the year and none of the Directors changed role.

## Information and professional development

The Board receives, in a timely manner, information in a form and of a quality appropriate to enable it to discharge its duties, with Board papers generally sent out five working days before each meeting.

All Directors received a full, formal and tailored induction on joining the Board. Each Director's experience and background is taken into account in developing a tailored programme.

Non-executive Directors are encouraged to visit operating sites and to meet with management. In addition to visits by individual Directors and the Chairman, each year at least one Board meeting is held at an operating facility. During 2009 formal Board meetings took place at the Technical Ceramics site in Rugby, UK and at the Carbon Division's site at Swansea, UK. In addition, the Board visited the NP Aerospace site in Coventry, UK.

Training and development needs are assessed as part of the Board performance review process and the Directors regularly update and refresh their skills and knowledge, taking into account environmental, social and governance matters. The Company Secretary keeps the suitability of external courses under review.

The Directors have access to the advice and services of the Company Secretary who, with the Chairman, is responsible for ensuring that Board procedures are followed and that applicable rules and regulations are observed. A procedure is in place to enable the Directors to seek independent professional advice at the Company's expense in connection with their duties as Directors.

## Performance evaluation

The Board undertook a formal evaluation of its performance, its committees and of the individual Directors during the year. The review consisted of a structured interview between the Chairman and each Director, the Divisional Chief Executives and the Company Secretary. These one-to-one discussions were complemented by a questionnaire and each Director had the opportunity to raise broader issues relating to the Company's strategy and governance. The results of the review were communicated to the Board with one-to-one feedback where appropriate.

The evaluation concluded that the Board performs effectively, that the Board calendar and agendas are appropriate with open discussions and effective follow-through by the executive team. The Chairman and the non-executive Directors also confirmed that they have sufficient time to fulfil their commitments to the Company. As noted above, training needs are assessed.

The recommendations to be implemented following the 2009 Board performance evaluation include: increasing the amount of interaction outside the formal Board environment, reviews of the Board procedures in relation to capital expenditure proposals and the Board evaluation process for 2010, increasing the focus on succession planning throughout the business and further presentations of the Group's technology to the Board.

The non-executive Directors, led by the Senior Independent Director, met without the Chairman present to evaluate the Chairman's performance during the year, taking into account the views of the executive Directors.

The recommendations made following the 2008 Board performance review were implemented during the year, including with regard to increased reporting between meetings, enhancing the exposure of the Board to senior management, with the Divisional Chief Executives normally attending Board meetings and with Board meetings held at two manufacturing locations and a Board visit to a third manufacturing site during 2009.

# Corporate governance
continued

### Remuneration
Remuneration policy and practice is discussed in the Remuneration report on pages 77 to 85.

### Accountability and audit
#### Financial reporting
In its reporting to shareholders, the Board aims to present the balanced and understandable assessment of the Company's position and prospects required by the Code and in accordance with the Accounting Standards Board's Reporting Standard 1, *The Operating and Financial Review*. This is included in the Business review on pages 32 to 63. The Board also presents updated information in its Interim and other public reports.

A summary of the statement of Directors' responsibilities in respect of the Annual Report and the financial statements is set out on page 76 and the 'going concern' statement is set out in the Business review on page 59.

#### Internal control
The Board has overall responsibility for establishing and maintaining a sound system of internal control to safeguard shareholders' investment and the Company's assets. Through the Audit Committee, the Board reviews the effectiveness of the internal control system annually and did so during the year. This review covered all material controls, including financial, operational and compliance controls, and risk management systems. The Audit Committee receives regular risk management reports covering the full range of risks faced by Morgan Crucible as a Group and ensures there are adequate systems in place and evaluates their effectiveness.

The Directors believe that the Group's system of internal financial controls provides reasonable, but not absolute, assurance that: the assets of the Group are safeguarded; transactions are authorised and recorded in a correct and timely manner; and that such controls would prevent and detect, within a timely period, material errors or irregularities. The system is designed to manage, rather than eliminate, risk and to address key business and financial risks, including social, environmental and ethical risks. The internal control framework complements the Group's management structure. The main features of the Group's systems for internal control and for assessing the potential risks to which the Group is exposed are summarised as follows:

- → Control environment The Group's management processes include delegated authorities and the segregation of duties with documented policies and manuals. These cover financial procedures, environmental, health and safety practice and other areas. In addition, there is a schedule of matters reserved for the Board. The Group's Core Values Statement, Ethics Policy and other supporting policies and procedures set out the Group's commitment to the highest standards of corporate and individual behaviour and provide guidance for employees. The Group's Whistleblowing line is available to employees and others in this regard. The Chief Executive of each Division makes an annual statement of compliance to the Board confirming that for each of the businesses for which he is responsible, the financial statements are fairly presented in all material respects, appropriate systems of internal controls have been developed and maintained and the businesses comply with Group policies and procedures.
- → Financial reporting A detailed budgeting system for each Division exists with an annual consolidated budget reviewed and approved by the Board. Businesses present their revenue and capital expenditure budgets for approval. Monthly results for the Group are presented to the Executive Committee and the Board, including comparisons against budget and the prior year. The Group's annual and half-yearly results are reported externally, in addition to interim management statements. The annual results are audited.
- → Performance monitoring There are regular meetings of the Board and of the Executive Committee. A comparison of forecast and actual results is considered, including cash flows and comparisons against budget and the prior year. Divisional management teams also meet regularly to review performance. Presentations of actual and forecast performance are made to the Executive Committee and the Board by the Group's Divisional Chief Executives. In addition, regular site visits are made by members of the Executive Committee.
- → Risk management The identification of major business risks is an ongoing process carried out in conjunction with operating management. Steps are taken to mitigate or manage any material risks identified. The Board, either directly or through the Audit Committee, receives reports on financial, taxation, insurance, pension, legal and social, environmental and ethical risks from management. The Divisional Chief Executives cover risk issues at their management meetings and the Director of Risk Assurance helps to ensure that internal control and risk management is embedded into the Group's operations through the Risk Management Committee, which is chaired by the Chief Financial Officer and is attended by the Chief Financial Officer of each Division.
- → Risk factors Morgan Crucible's businesses are affected by a number of factors, many of which are influenced by macroeconomic trends and are therefore outside the Company's immediate control, although, as described above and in the Business review, the identification and management of such risks is carried out systematically. These are further discussed in the Risk management section on page 60.
- → Internal audit The Group's internal audit function reviews internal control and risk management processes. The Audit Committee approves the plans for internal audit reviews and receives reports accordingly. Actions resulting from internal audit reviews are agreed with management. A new internal auditor was appointed during the year and has direct access to the Chairman of the Audit Committee.

### Audit Committee and auditors

The Board has formal and transparent arrangements for considering how the Directors apply the Company's financial reporting and internal control principles, and for maintaining an appropriate relationship with the Company's auditors. This requirement is met by the work of the Audit Committee, as described below, and by the audit work carried out by the Company's external auditors, KPMG Audit plc. The Audit Committee has received confirmation from KPMG Audit plc that its general procedures support the auditors' independence and objectivity in relation to non-audit services. After considering such procedures the opinion of the Audit Committee was that the auditors' objectivity and independence was safeguarded despite the provision of non-audit services by KPMG Audit plc.

### Conflicts of interest

The Board has procedures in place to address the requirements of Section 175 of the Companies Act 2006 concerning the duty of the Directors to avoid conflicts of interest. These procedures are in accordance with the GC100 guidance.

Accordingly the Directors are required to continue to (1) disclose proposed outside interests before they are taken in order to enable a prior assessment of any actual or potential conflict; and (2) disclose without delay any situation which arises which gives rise to an actual or potential conflict.

During the year the Board undertook a review of Directors' outside interests to identify actual or potential conflicts of interest, including the interests of connected persons where such interests could give rise to an indirect conflict. This confirmed that there were no actual conflicts of interest and the only potential conflicts of interest identified were outside directorships. The Board considered each Director's situation and authorised any potential conflicts for a period of 15 months from December 2009. Such authorisation is revocable at any time at the Board's discretion.

Should an actual or potential conflict be identified, the Board shall consider whether to authorise the situation and, if so, the terms of any authorisation. In the event of an actual conflict arising, the Director concerned is to notify the Chairman (the Chairman would notify the Senior Independent Director) and the Director would be excluded from the relevant information, debate and decision.

The Board is responsible for undertaking a regular review of any authorisations given and will itself, or through one of its committees, ensure that the procedures for reporting and, if appropriate, authorising conflicts and potential conflicts of interest are operated correctly. In addition, the Nomination Committee will review the outside interests of a proposed Director to identify actual or potential conflicts of interest and will make recommendations to the Board as to whether the situation should be authorised.

## Relations with shareholders

### Dialogue with shareholders

The importance of dialogue with major shareholders is recognised and meetings are held in order to help achieve a mutual understanding of objectives. In this respect, the Chief Executive Officer and Chief Financial Officer make themselves available to major shareholders as appropriate throughout the year, in particular at the time of the Preliminary and Interim announcements. The Chairman also discusses governance and other matters directly with shareholders. The Chairman and the non-executive Directors are invited to investor briefings and attend meetings with major shareholders when requested. The Senior Independent Director is available to attend separate meetings with major shareholders on request.

Following the announcement of the Group's Preliminary and Interim results and after other significant statements and presentations, investor opinion is canvassed and any feedback is made available to the Board. In addition, the Board is provided with brokers' reports and feedback from shareholder meetings on a regular basis.

To help facilitate dialogue with shareholders, the Investors section of the Company's website includes details of Stock Exchange announcements, press releases, presentations, webcasts and other relevant information.

### Constructive use of the AGM

The Annual General Meeting is normally attended by all members of the Board and by a representative of the auditors. At the AGM held in April 2009, the Chief Executive Officer made a short business presentation. Shareholders are also invited to ask questions during the meeting and have the opportunity to meet the Directors and other members of senior management before and after the formal meeting. The results of the proxy voting on all resolutions are provided for all attendees and are released to the London Stock Exchange and published on the Company's website as soon as practicable after the meeting.

# Corporate governance
continued

## Board committees

The full terms of reference of the following Board committees are available upon request and are also available on the Company's website.

### Audit

The Audit Committee assists the Board in effectively discharging its responsibilities for financial reporting and corporate control. Martin Flower, Andrew Given and Simon Heale were members of the Committee throughout the year. All members of the Committee are independent Directors and Andrew Given, the Chairman of the Committee, has the requisite financial experience.

The Audit Committee met five times during the year and has the power to, and does, request the attendance at meetings of any Director, auditor or member of management as may be considered appropriate by the Chairman of the Committee. At the end of each meeting the non-executive Directors who are members of the Committee also meet the auditors without the executive Directors or other members of management present.

The Committee identifies and confirms that it receives the information it needs to enable it to fulfil its responsibilities. This is complemented by an annual presentation made by the Divisional Chief Executives and Chief Financial Officers on the internal control environment within their respective Divisions.

The Audit Committee's terms of reference include:

- Monitoring and making appropriate recommendations to the Board with regard to the financial reporting process, the integrity of the financial statements of the Company, any formal announcements relating to the Company's financial performance and reviewing significant financial reporting judgments contained in them.
- Reviewing and monitoring the effectiveness of the Company's internal control, internal audit and risk management systems.
- Making recommendations to the Board, for it to put to the shareholders for their approval in general meeting, in relation to the appointment, reappointment and removal of the external auditors and to approve the remuneration and terms of engagement of the external auditors.
- Reviewing and monitoring the external auditors' independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements.
- Developing and implementing policy on the engagement of the external auditors to supply non-audit services, taking into account relevant ethical guidance regarding the provision of non-audit services by the external auditors.
- Reporting to the Board, identifying any matters in respect of which it considers that action or improvement is needed and making recommendations as to the steps to be taken.

The Committee has the authority to investigate any matters according to its terms of reference and may obtain external advice at the cost of the Company. The Director of Risk Assurance and the internal auditor both have access to the Chairman of the Committee and meet, when appropriate, with the Committee without other executives present.

The work of the Committee in discharging those responsibilities in respect of 2009 included:

- Reviewing the Group's 2008 financial statements and 2009 Interim statements prior to Board approval.
- The review of the process by which the Group's main business risks are assessed and managed, with the principal risks being considered by the Board as a whole.
- Reviewing the effectiveness of the Group's internal audit and risk management systems.
- Consideration of the work and plans for the internal audit function.
- Appraisal of the Company's Whistleblowing line and related procedures and policies.
- Confirmation of the external auditors' terms of engagement and fee structures.
- Monitoring the level of non-audit work of the auditors, which in 2009 included services amounting to £0.1 million, mainly in connection with tax advice.

To ensure the objectivity and independence of the external auditors, the policy implemented by the Committee for the provision of non-audit services by the external auditors is in summary as follows:

- Certain non-audit services may not be provided by the external auditors, including the review of their own work; they may not make management decisions; their work must not create a mutuality of interest; and they may not put themselves in the position of advocate.
- Any non-audit work proposed to be placed with the external auditors with a fee in excess of £200,000 should be referred to the Audit Committee.
- The prior approval of the Audit Committee is required for any non-audit work which, when added to the fees paid for other non-audit work, would total more than 80% of the audit fee.

During the year the proportion of the auditors' fees for non-audit work relative to the audit fee was 5% (2008: 11%).

The external auditors have processes in place to safeguard their independence and have written to the Committee confirming that, in their opinion, they are independent. The Company last changed its auditors in late 2001 and undertook a formal review of the external auditors which included a re-tender presentation during 2007. During 2008 the external auditors rotated the partner responsible for the Group's audit work. As a result the Committee recommended to the Board that the Group's audit work should not be put out to third-party tender during 2009.

### Remuneration

As is further described in the Remuneration report on pages 77 to 85, the Remuneration Committee has responsibility for setting remuneration for all executive Directors and the Chairman, including benefits such as share options and awards under the Company's incentive plans, pension rights and any compensation payments. The Committee also monitors the level and structure of remuneration for senior management.

Tim Stevenson, Martin Flower, Andrew Given and Simon Heale, who is the Committee Chairman, were members of the Committee throughout the year. The Committee is assisted in its duties by the Chief Executive Officer, the Company Secretary and the Director of Human Resources. No member of the Committee or attendee is present when their own remuneration is under consideration, nor do they participate in any relevant voting. The Committee also has the power to request, for all or part of any meeting, the attendance of any Director or member of management as may be considered appropriate by the Chairman of the Committee. The Committee met seven times during the year.

It is the Company's policy to disclose the fees of any executive Director who serves as a non-executive Director of another company. During the year Mark Robertshaw served as a non-executive Director of Rathbone Brothers plc. The fees received by Mark Robertshaw in this regard are shown on page 82.

The report of the Remuneration Committee, which includes details of the Committee's responsibilities and terms of reference and of the Directors' remuneration and Directors' interests in options and shares, is set out on pages 77 to 85.

### Nomination

The Nomination Committee leads the process for Board appointments and makes recommendations to the Board on the appointment of new Directors. A majority of members of the Nomination Committee are independent non-executive Directors. Tim Stevenson as Chairman of the Committee, Martin Flower, Andrew Given, Simon Heale, and Mark Robertshaw were members of the Committee throughout the year.

The Committee has the power to request the attendance of any other Director or member of management, for all or part of any meeting, as may be considered appropriate by the Chairman of the Committee. The Committee formally met once during 2009 and also held further informal discussions regarding the shape and size of the Board. No nominations to the Board or changes in role were made during the year.

The Nomination Committee reviews the balance of skills, knowledge and experience on the Board, succession planning and the leadership needs of the Group. In the light of this review, the Committee prepares a description of the role and capabilities required for a particular appointment.

Candidates for appointment as Director are considered by the Committee, taking advice from external consultants where appropriate.

The terms and conditions of appointment of non-executive Directors are available for inspection. Non-executive Directors, including the Chairman, are asked to undertake that they will have sufficient time to meet their commitments to the Company. Their other significant commitments are disclosed to the Board before appointment, with an indication of the time involved, and the Board is informed of any subsequent changes. The terms of appointment for non-executive Directors do not include a notice period.

### Disclosure and Transparency Rules

This statement complies with sub-sections 2.1; 2.2(1); 2.3(1); 2.5; 2.7 and 2.10 of Rule 7 of the UK Listing Authority Disclosure and Transparency Rules. The information required to be disclosed by sub-section 2.6 of Rule 7 is shown in the Directors' report on pages 66 to 69 and is incorporated in this statement by reference.

# Statement of Directors' responsibilities in respect of the Annual Report and the financial statements

The Directors are responsible for preparing the Annual Report and the Group and parent Company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and parent Company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the parent Company financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

Under Company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and parent Company and of their profit or loss for that period.

In preparing each of the Group and parent Company financial statements, the Directors are required to:

- Select suitable accounting policies and then apply them consistently.
- Make judgments and estimates that are reasonable and prudent.
- For the Group financial statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU.
- For the parent Company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the parent Company financial statements.
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the parent Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' report, Directors' Remuneration report and Corporate governance statement that comply with that law and those regulations.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board

**Paul Boulton**
Secretary
18 February 2010

# Remuneration report

The Directors' Remuneration report has been prepared by the Remuneration Committee ('the Committee') and has been approved by the Board. Shareholders will be given the opportunity to approve the report at the Annual General Meeting on 23 April 2010.

The report has been drawn up in accordance with the Combined Code on Corporate Governance, Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 and the UK Listing Authority Listing Rules.

The Remuneration report is divided into two parts. The first part contains commentary on remuneration policy, which is not required to be audited. The second part contains the remuneration tables that have been audited in accordance with the relevant statutory requirements.

## The Remuneration Committee

The Remuneration Committee is responsible for developing Group policy on executive remuneration and for determining, on behalf of the Board, specific remuneration packages for the executive Directors and the Chairman. The Committee's terms of reference are available on our website.

During the year the members of the Committee were: Simon Heale, who is the Chairman of the Committee, Martin Flower, Tim Stevenson and Andrew Given. Each of the non-executive Directors is regarded by the Board as independent. Tim Stevenson was independent at the time of his appointment as Chairman of the Board.

The Committee met on seven occasions during the year.

The Company Secretary acts as secretary to the Committee. The Chief Executive Officer and the Director of Human Resources attend meetings of the Committee by invitation. The Committee also had access to advice from the Chief Financial Officer. No executive Director or other attendee is present when his or her own remuneration is under consideration.

Deloitte LLP was appointed by the Committee as its retained advisers in February 2007 and has provided advice on market practice and remuneration policy as well as Total Shareholder Return (TSR) analysis.

During the financial year, Deloitte LLP has also provided unrelated tax advice to the Company.

During the year, Imbucon provided TSR analysis relating to the Company's share plans. Imbucon did not provide any other services to the Company.

## Remuneration policy

The Remuneration Committee aims to ensure that remuneration packages offered are competitive and designed to attract, retain and motivate executive Directors and senior executives of the right calibre in order to run the Company successfully and to create value for shareholders.

The policy of the Committee is to ensure that a significant proportion of the total remuneration opportunity is performance-related and based on the achievement of measurable targets which are relevant to and support the business strategy. This is in order to create a strong link between performance and reward which should be beneficial to shareholders, employees and the Company.

In assessing all aspects of pay and benefits, the Committee takes into account the packages offered by similar companies to ensure the remuneration packages for executive Directors are competitive against the market in which the Company competes for talent. For the purposes of such analysis, comparator companies are chosen having regard to: the size of the company (eg market capitalisation, turnover and number of people employed); the diversity and complexity of its businesses; and the geographical spread of its businesses. The Committee also considers the level of pay throughout the Company when determining executive Directors' remuneration.

The Committee believes that the current remuneration structures are appropriate and support the business strategy.

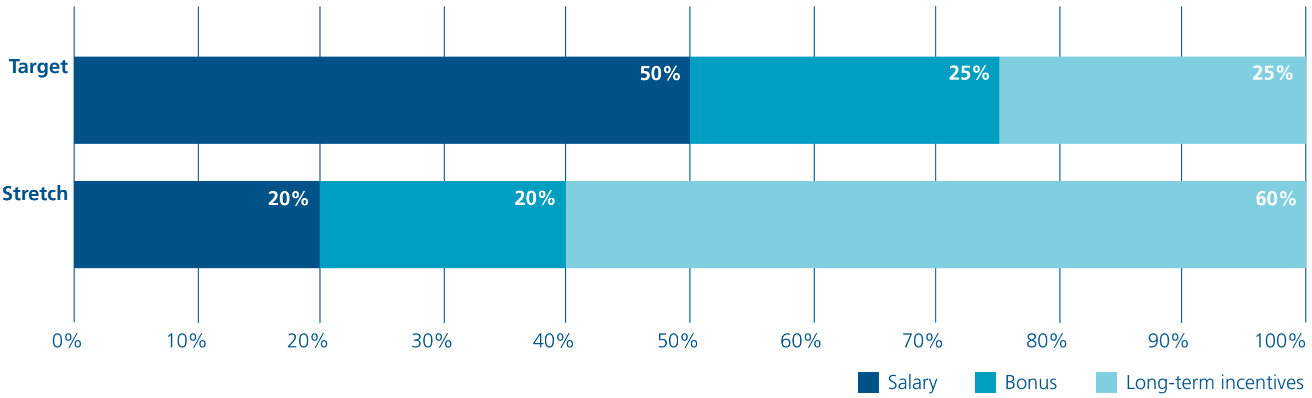
# Remuneration report
continued

## Main components of remuneration

The table below summarises the Company's policies in respect of each of the key elements of executive Directors' remuneration as they applied during the year.

| Element | Policy | Details |
|---|---|---|
| Base salary | → Provides the fixed element of the remuneration package<br>→ Set at competitive levels against the market | → Benchmarked against companies of a similar size and complexity in the FTSE 350<br>→ Annual review date of 1 January |
| Annual bonus | → Incentivises the achievement of specific goals over the short term that are also aligned to the long-term business strategy | → Maximum bonus award of 100% of salary<br>→ Targets based on underlying operating profit performance (60% of salary) and cash conversion (40% of salary) |
| Deferred Bonus Share Matching Plan | → Designed to encourage long-term Company growth and to retain key individuals over this time period<br>→ Provides an opportunity for individuals to invest in Company shares and receive matching shares based on Group performance | → Designed to work alongside the Long Term Incentive Plan<br>→ Up to 50% of the annual bonus may be voluntarily deferred into shares for three years (up to 75% in 2010)<br>→ A matching award of up to three shares for each deferred share may be earned based on the Company's performance against stretching earnings per share (EPS) targets |
| Long Term Incentive Plan | → Aligns the interests of executives and shareholders by delivering executive Directors and other senior executives shares as a reward for outstanding performance | → Award of shares based on performance over a three-year period<br>→ Awards to be made in 2010 will be based on TSR and EPS performance |
| Pension | → Provides post-retirement benefits for participants in a cost-efficient manner | → Defined benefit scheme subject to a notional earnings cap with an above-the-cap allowance for current executive Directors |
| Shareholding guidelines | → Encourages executives to build an interest in the Company's shares and supports alignment with shareholder interests | → Policy of 100% of basic salary for executive Directors<br>→ Supported by the Deferred Bonus Share Matching Plan which encourages investment in Company shares |

The relative proportion of fixed and variable remuneration for the executive Directors at 'target' and 'stretch' performance is illustrated below. This is based on our ongoing remuneration policy.




Calculated on a projected value basis assuming 10% pa share price growth at 'target' performance and 15% pa share price growth at 'stretch'.

### Base salary

The base salary for each executive Director is determined by the Remuneration Committee, taking into account the performance of the individual and having regard to practice in companies of comparable size and complexity in the FTSE 350. Salaries are normally reviewed on an annual basis.

No increase to base salaries was made in 2009. In line with the approach being taken across the organisation, executive Directors' salaries will be increased in 2010. In considering the level of increase, the Committee has been mindful of the general level of increase across the Company as well as the positioning of roles against the market. The table below shows the salaries in 2009 and with effect from 1 January 2010.

| | 2009 | Salary 2010 |
|---|---|---|
| Mark Robertshaw | £440,000 | £450,000 |
| Kevin Dangerfield | £255,000 | £265,000 |

Base salary is the only element of the remuneration package that is pensionable.

### Annual bonus

The targets for the annual bonus are set by the Remuneration Committee, taking into account the short- and long-term requirements of the Company. Challenging goals are set, which must be met before any bonus is paid. This approach is intended to align executive reward with shareholder return by rewarding the achievement of 'stretch' targets.

The bonus scheme provides the opportunity for executive Directors to earn a bonus of up to 100% of basic salary if stretching performance targets are achieved.

For 2009, the bonus was based wholly on financial performance. The targets for the awards were set to address the new demands placed on the business in the current economic climate and were based on underlying operating profit performance (up to 60% of salary) and cash conversion (up to 40% of salary).

For 2010, the bonus will be based on profit before tax. This incentivises the executive Directors to manage much more of the 'income statement' to improve the earnings per share of the Group.

In addition to the achievement of the targets set, in considering any awards to be made the Committee also takes into account the quality of the overall performance of the Company.

The bonuses awarded to executive Directors in respect of 2009 were as follows:

- Mark Robertshaw – 20% of salary (2008: 60%).
- Kevin Dangerfield – 20% of salary (2008: 30%).

This award was made on the basis that in 2009 the underlying operating profit target was not achieved, but the cash conversion measure was partially satisfied, resulting in a bonus payment of 20% of salary.

### Long-term incentive arrangements

The Committee believes that share ownership by the executive Directors and senior executives helps align their interests with those of the shareholders. Accordingly the Company operates a number of share schemes for the executive Directors and other senior employees, details of which are set out below.

#### Deferred Bonus Share Matching Plan

In 2008 shareholder approval was gained for the introduction of a new long-term incentive plan, the Deferred Bonus Share Matching Plan. This Plan now operates alongside the other long-term incentive arrangements. To date, participants have been offered the opportunity to defer up to 50% of their annual bonus on a pre- or post-tax basis into Company shares. Participants must hold the deferred shares for three years to be eligible for a matching award based on the pre-tax value of their deferred shares. Matching shares may be earned at the end of three years in the event that stretching EPS targets have been met.

For the 2009 performance year, participants will be given the opportunity to defer up to 75% of their bonus under the Plan. This is in order to provide participants with a meaningful opportunity to invest in Morgan Crucible shares. This change is within the limits in the Plan rules approved by shareholders in 2008. This approach will be reviewed for future award cycles.

# Remuneration report
## continued

As is set out in the table below, the targets for the 2010 matching awards will revert to referencing a growth above RPI as used in 2008.

| EPS performance | Matching shares |
|---|---|
| RPI+ 15% pa | 3x match |
| RPI+ 10% pa | 1.75x match |
| RPI+ 7.5% pa | 1x match |
| RPI+ 5% pa | 0.5x match |
| RPI+ 4% pa | 0.25x match |
| < RPI+ 4% pa | 0x match |

There is straight-line vesting in between each point above.

The performance targets for awards made in 2009 did not reference growth above RPI. Given the difficult economic climate at that time, the Committee considered the targets to be stretching.

### Long Term Incentive Plan (LTIP)

The LTIP was approved at the 2004 Annual General Meeting and offers executive Directors and other senior executives the opportunity to receive shares as a reward for outstanding performance. The scheme allows awards of up to 150% of basic salary, although in exceptional circumstances the Committee is able to make awards of up to 200% of basic salary. The vesting of the awards is subject to the achievement of performance targets measured over the three-year period from the start of the year in which the award is made.

During the year, an award over 489,705 shares was made to Mark Robertshaw and an award over 283,806 shares was made to Kevin Dangerfield.

Due to the real economic uncertainty at the time the 2009 awards were made, the Remuneration Committee decided to recalibrate the focus of awards between internal financial targets and relative share price targets. Consequently, awards made under the LTIP in 2009 were based wholly on the Company's TSR performance against the comparator group below. If the Company's TSR places it at the median of the comparator group, 30% of the award will vest, with 100% of the awards vesting for performance at the upper quartile or above. For performance between median and upper quartile, awards vest on a straight-line basis. The Committee must also be satisfied that the Company's underlying financial performance justifies the level of vesting.

For 2010 awards, the Remuneration Committee believes it is appropriate to return to the previous split between TSR and EPS targets on the basis that the Company is now able to set robust three-year EPS targets which have a meaningful line of sight for participants. The split between TSR and EPS targets provides the right balance between incentivising strong financial growth while taking into account the share price performance relative to peers. Therefore, for awards to be made under the LTIP in 2010, 50% will be based on TSR against the comparator group ones leaf and 50% will be based on EPS growth above RPI. Following a review during the year, the comparator group for the 2010 awards has been extended to include six new comparator companies. This is to ensure that the comparator group is of a robust size and reflects the different markets in which Morgan Crucible operates. The Committee must be satisfied that the Company's underlying financial performance justifies the level of vesting. The awards made under the LTIP in 2007 and 2008 were based on the same measures and targets as will apply for the 2010 awards.

The vesting schedule for the 2010 awards is as follows:

| | % of the award which vests TSR performance against the sector comparator group | % of the award which vests EPS growth | |
|---|---|---|---|
| Upper-quartile-ranked performance | 50% | RPI+ 10% pa | 50% |
| Median-ranked performance | 15% | RPI+ 4% pa | 15% |
| Below-median-ranked performance | 0% | < RPI+ 4% pa | 0% |

Straight-line vesting applies between each point (for both vesting schedules).

The TSR comparator group* for the 2007–2010 awards is set out below:

| | | |
|---|---|---|
| Bodycote | Meggit | Spectris |
| Charter International | Porvair** | Spirax-Sarco |
| Chemring Group | Qinetiq** | Tomkins |
| Cobham | Renishaw** | TT Electronics |
| Cookson Group | Ricardo** | Ultra Electronics Holdings |
| Halma | Rotork | Umeco** |
| IMI | Senior | Weir Group |
| Laird Group | Smiths Group** | |

* The original comparator group also included FKI and Foseco which have subsequently delisted.
** Additional comparator companies for 2010 awards.

The details of awards held by all Directors are shown on page 84.

Executive Share Option Scheme (ESOS)
The ESOS was approved at the 2004 Annual General Meeting and offers executive Directors and other senior executives the opportunity to receive options granted at the market price of the Company's shares at the time of the grant. The scheme allows awards of up to 150% of basic salary, although in exceptional circumstances the Committee is able to make awards of up to 200% of basic salary.

There are two remaining awards to the executive Directors. Mark Robertshaw has a vested option grant from 2004 that he has not exercised. Kevin Dangerfield has an unvested option from 2001 that is subject to annual re-test for up to 10 years from the date of the grant (see Directors' share options table on page 83). There is currently no intention to make awards under the ESOS in 2010.

Savings-related Share Option Scheme (SAYE)
As UK employees, the executive Directors may also participate in the Savings-related Share Option Scheme on the same basis as other eligible employees and subject to UK legislation. Scheme members save a fixed amount per month over three years and options have been granted with an exercise price at 80% of the market price at the date of grant. Those Directors who received options under this scheme are shown in the table on page 85. No performance conditions apply to these options as they are a tax-efficient mechanism for all employees to acquire shares in the Company at their own cost.

**Other benefits**
Executive Directors are eligible to receive certain benefits including a car allowance, health insurance and, where appropriate, relocation and other expenses.

**Shareholding guidelines**
In order to encourage alignment with shareholders, individual shareholding guidelines are operated for executive Directors and senior executives. Under such guidelines, executive Directors are encouraged to build and maintain over time a shareholding in the Company equivalent to at least 100% of basic salary. This policy is supported by the Deferred Bonus Share Matching Plan under which participants are encouraged to invest their bonus in Company shares.

**Chairman and non-executive Directors**
Tim Stevenson was appointed as Chairman on 1 December 2006. Since the date of his appointment his annual fee has been set at £125,000.

Non-executive Directors receive a basic annual fee of £40,000. Additional payments of £4,500 per annum are made to the Senior Independent Director, £7,500 to the Chairman of the Audit Committee and £5,000 to the Chairman of the Remuneration Committee. The Chairman and non-executive Directors are also entitled to reimbursement of expenses incurred in attending Board, strategy and other meetings. No changes were made to non-executive fees during the year.

Annual fees paid to the Chairman and non-executive Directors are reviewed on a biennial basis. A review was held in 2008 and, while no increases were recommended for the non-executive Directors, an increase for the Chairman was recommended. At the request of the Chairman, the 2009 increase was deferred for 12 months. Therefore, with effect from 1 January 2010 his annual fee will be increased to £140,000.

None of the non-executive Directors has a service contract with the Company although they do have letters of appointment which contain no obligations relating to any notice period. There are no obligations on the Company to make any payments in lieu of notice to any non-executive Director. The non-executive Directors do not participate in any of the incentive, share or share option plans. Each of the non-executive Directors is subject to re-election by shareholders every third year after their initial confirmation by shareholders as a Director.

Should any non-executive Director serve for nine or more years they would be subject to annual re-election.

# Remuneration report
continued

## Service contracts

Executive Directors are employed on contracts subject to 12 months' notice at any time. Contracts may be terminated on 12 months' notice given by the Company or on six months' notice given by the Director concerned. Contracts end on each Director's anticipated normal retirement date. The following table shows the date of the contract for each executive Director who served during the year.

| Executive Director | Date of appointment | Date of service agreement |
|---|---|---|
| Kevin Dangerfield | 3 August 2006 | 15 August 2008 |
| Mark Robertshaw | 4 August 2006 | 15 August 2008 |

The service agreements for Mark Robertshaw and Kevin Dangerfield do not contain specific termination provisions. In the event of early termination, the Company may be liable to pay an amount in damages having regard to salary, bonus and other benefits that would have been received had they served out their notice period. The value of any termination payment made will be at the judgment of the Committee having regard to all relevant factors including ensuring that the full benefit of mitigation is obtained. There is no automatic entitlement to bonus as part of the termination arrangements.

## Company pensions policy

The executive Directors participate in The Morgan Group Senior Staff Pension and Life Assurance Scheme which is a contributory, HMRC-registered, defined benefit, funded occupational pension scheme. With effect from 6 April 2006 the basis of the scheme changed from final salary to career average and the normal pension age increased by five years. The main features of the plan are:

- A normal pension age of 65.
- Pension at normal pension age of two-thirds career average pensionable salary, subject to completion of 20 years' employment (26 years and eight months for new members).
- Life assurance of four times basic salary.
- Dependants' pension on death.

Pensionable salary is the member's basic salary restricted to a scheme earnings cap of £123,600 for the 2009-10 tax year.

In addition, executive Directors received a pension allowance derived from employer contributions based notionally on the registered scheme pensionable salary in excess of the earnings cap. The value of the pension allowance for each executive Director is set out in the Directors' emoluments table on page 83.

## External directorships

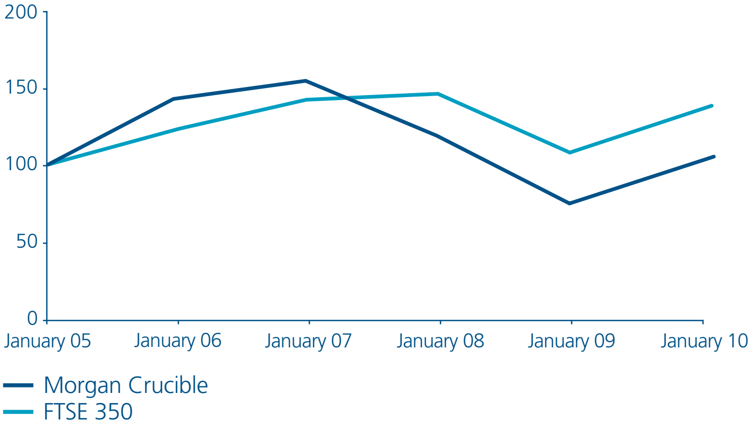
With the approval of the Board in each case, and subject to the overriding requirements of the Company, executive Directors may accept external appointments as non-executive Directors of other companies and retain any fees received.

The total amount of fees received by Mark Robertshaw in respect of a non-executive Directorship was £35,000.

## Performance graph

The following graph shows the cumulative total shareholder return (TSR) for the Company for the five-year period to 4 January 2010 against the FTSE 350. Both are rebased to 100 as at 5 January 2005. The FTSE 350 is considered to be appropriate for comparison as it is a broad market index and the Company forms part of that index.

**Total shareholder return for the five-year period January 2005 to January 2010**



The auditors are required to report on the following information:

### Directors' interests in shares

Directors' interests in the Ordinary share capital of the Company are as follows:

| | As at 5 January 2009 | As at 3 January 2010 | As at 18 February 2010* |
|---|---|---|---|
| **Executive Directors** | | | |
| Mark Robertshaw | 331,595 | 338,595 | 339,277 |
| Kevin Dangerfield | 138,717 | 138,717 | 138,914 |
| **Non-executive Directors** | | | |
| Tim Stevenson | 29,000 | 29,000 | 29,000 |
| Martin Flower | 15,000 | 15,000 | 15,000 |
| Simon Heale | 18,000 | 18,000 | 18,000 |
| Andrew Given | 10,000 | 10,000 | 10,000 |

* The date of report. As at 23 February 2010, there was no change to the details listed in the above table.

At the market price on 18 February 2010, Mark Robertshaw and Kevin Dangerfield respectively held shares worth 131% and 92% of their basic salaries.

### Directors' emoluments

| | Fees/salary £000 | | Annual bonus £000[1] | | Other benefits £000[2] | | Total emoluments £000 | | Pension allowance £000 | | Other payments[2] £000 | | Total remuneration £000 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 | 2009 | 2008 | 2009 | 2008 | 2009 | 2008 | 2009 | 2008 | 2009 | 2008 |
| **Executive Directors** | | | | | | | | | | | | | | |
| Mark Robertshaw | 440 | 440 | 88 | 264 | 13 | 13 | 541 | 717 | 114 | 108 | – | – | 655 | 825 |
| Kevin Dangerfield | 255 | 255 | 51 | 77 | 12 | 12 | 318 | 344 | 66 | 60 | – | – | 384 | 404 |
| **Non-executive Directors** | | | | | | | | | | | | | | |
| Tim Stevenson (Chairman) | 125 | 125 | – | – | – | – | 125 | 125 | – | – | – | – | 125 | 125 |
| Martin Flower | 45 | 43 | – | – | – | – | 45 | 43 | – | – | – | – | 45 | 43 |
| Andrew Given[3] | 53 | 45 | – | – | – | – | 53 | 45 | – | – | – | – | 53 | 45 |
| Simon Heale | 45 | 45 | – | – | – | – | 45 | 45 | – | – | – | – | 45 | 45 |

1. Annual bonus shows the total bonus payable in respect of the relevant year. Mark Robertshaw and Kevin Dangerfield voluntarily deferred 25% of their 2008 bonus awards into the Bonus Deferral Share Matching Plan as set out in the table on page 84.
2. Other benefits include private medical insurance and a car allowance.
3. Andrew Given received a back-payment in 2009 for non-payment in 2008 of the additional fees due to him following his appointment as Chairman of the Audit Committee on 18 April 2008.

### Directors' share options

| | At 5 January 2009 | Granted during the year | Exercised during the year | Lapsed during the year | At 3 January 2010 | Exercise price | Earliest date of exercise | Expiry date |
|---|---|---|---|---|---|---|---|---|
| Mark Robertshaw | 200,000 | – | – | – | 200,000 | 145.275p | 01.11.07 | 01.11.14 |
| | 1,000,000* | – | – | 1,000,000 | 0 | 256p | 20.12.09 | 20.12.16 |
| Kevin Dangerfield | 10,520 | – | – | – | 10,520 | 180.08p | 23.11.04 | 23.11.11 |
| | 150,000 | | | 150,000 | 0 | 256p | 20.12.09 | 20.12.16 |

* This relates to an award made to Mark Robertshaw on his appointment as Chief Executive Officer in February 2006. The award is structured as a market value option over 1,000,000 shares subject to the performance conditions that apply to awards under the Executive Share Option Scheme.

The performance measure for the Executive Share Option Scheme awards above was based on the Company's Total Shareholder Return performance against the FTSE 350. Thirty per cent of the awards vest for achieved median-ranked performance with full vesting for upper-quartile-ranked performance. For performance between median and upper quartile, awards vest on a straight-line pro-rata basis. The performance condition for the awards granted in 2006 was not met and these awards have therefore lapsed in full.

The share price at the year end was 157.7 pence and the high and low during the year were 192.3 pence and 70.3 pence respectively.

# Remuneration report
continued

### Awards to Directors under the Long Term Incentive Plan

| | As at 5 January 2009 | Allocations during the year | Shares released during the year | Shares lapsed during the year | As at 3 January 2010 | Market price at date of allocation | Market price at date of release | Performance periods |
|---|---|---|---|---|---|---|---|---|
| Mark Robertshaw | | | | | | | | |
| 2006 LTIP (May) | 250,000 | – | – | 250,000 | – | 242.95p | – | 05.01.06 – 04.01.09 |
| 2006 LTIP (December) | 50,000 | – | – | 50,000 | – | 256p | – | 05.01.06 – 04.01.09 |
| 2008 LTIP | 220,000 | – | – | – | 220,000 | 203p | – | 05.01.08 – 04.01.11 |
| 2009 LTIP | – | 489,705 | – | – | 489,705 | 89.85p | – | 05.01.09 – 04.01.12 |
| Kevin Dangerfield | | | | | | | | |
| 2006 LTIP (December) | 107,500 | – | – | 107,500 | – | 256p | – | 05.01.06 – 04.01.09 |
| 2007 LTIP | 80,000 | – | – | – | 80,000 | 282p | – | 05.01.07 – 04.01.10 |
| 2008 LTIP | 120,000 | – | – | – | 120,000 | 203p | – | 05.01.08 – 04.01.11 |
| 2009 LTIP | – | 283,806 | – | – | 283,806 | 89.85p | – | 05.01.09 – 04.01.12 |

The performance measure for the 2006 LTIP awards is based on the Company's Total Shareholder Return (TSR) against the FTSE 350. Thirty per cent of the awards vest for achieving median-ranked performance with full vesting for upper-quartile-ranked performance. For performance between median and upper quartile, awards vest on a straight-line pro-rata basis. The performance condition for these awards was not met and therefore the awards lapsed in full.

### Awards to Directors under the Bonus Deferral Share Matching Plan

| | As at 5 January 2009 | Allocations during the year | Shares released during the year | Shares lapsed during the year | As at 3 January 2010 | Market price at date of allocation | Market price at date of release | Performance periods |
|---|---|---|---|---|---|---|---|---|
| Mark Robertshaw | | | | | | | | |
| 2008 award | | | | | | | | |
| Investment shares[1] | 104,743 | – | – | – | 104,743 | 197.625p | – | – |
| Matching shares[2] | 314,229 | – | – | – | 314,229 | 197.625p | – | 05.01.08 – 04.01.11 |
| 2009 award | | | | | | | | |
| Investment shares[1] | – | 48,222 | – | – | 48,222 | 80.75p | – | – |
| Matching shares[2] | – | 245,201 | – | – | 245,201 | 80.75p | – | 05.01.09 – 04.01.12 |
| Kevin Dangerfield | | | | | | | | |
| 2008 award | | | | | | | | |
| Investment shares[1] | 58,266 | – | – | – | 58,266 | 197.625p | – | – |
| Matching shares[2] | 174,798 | – | – | – | 174,798 | 197.625p | – | 05.01.08 – 04.01.11 |
| 2009 award | | | | | | | | |
| Investment shares[1] | – | 13,973 | – | – | 13,973 | 80.75p | – | – |
| Matching shares[2] | – | 71,052 | – | – | 71,052 | 80.75p | – | 05.01.09 – 04.01.12 |

1. Investment shares represent those shares acquired with a portion of the bonus set out in the emoluments table on page 83 voluntarily deferred into the Bonus Deferral Share Matching Plan.
2. This is the maximum number of shares based on the pre-tax value of the deferred shares that could be earned at the end of the performance period if the performance condition set out on page 79 is met in full.
3. In 2008 the executive Directors deferred their bonus payment on a gross basis and in 2009 deferral was on a net basis. The flexibility to defer on either basis is within the Plan rules.

Note: Prior to 6 April 2010, the Committee is intending to amend the terms of the Investment shares in order to allow individuals to crystallise the tax due on their earned deferred bonus awards. The net value of these awards will continue to be held until the normal vesting date. No amendment will be made to the terms of the matching shares.

## Options under the Sharesave scheme

| | As at 5 January 2009 | Granted during the year | Exercised during the year | Lapsed during the year | As at 3 January 2010 | Exercise price | Exercise periods |
|---|---|---|---|---|---|---|---|
| Mark Robertshaw 2006 scheme | 4,725 | – | – | – | 4,725 | 200p | 01.03.10 – 31.08.10 |
| Kevin Dangerfield 2008 scheme | 5,680 | – | – | – | 5,680 | 169p | 01.12.11 – 31.05.12 |

## Pension benefits earned by the Directors

Executive Directors participate in The Morgan Group Senior Staff Pension and Life Assurance Scheme. This is a contributory, HMRC-registered, defined benefit, UK occupational pension scheme. As noted above, the scheme was amended on 6 April 2006.

| Executive Directors | Accrued benefits at 3 January 2010 £000 | Increase in accrued benefits excluding inflation (A) £000 | Increase in accrued benefits including inflation £000 | Transfer value of (A) less Director's contributions £000 | Transfer value of accrued benefits at 4 January 2009 £000 | Transfer value of accrued benefits at 3 January 2010 £000 | Increase/ (decrease) in transfer value less Director's contributions £000 |
|---|---|---|---|---|---|---|---|
| Mark Robertshaw | 17 | 4 | 4 | 20 | 64 | 176 | 94 |
| Kevin Dangerfield | 27 | 4 | 4 | 28 | 140 | 336 | 185 |

Notes re. pension benefits:
1. The accrued benefit entitlement for Mark Robertshaw and Kevin Dangerfield is the pension which would be paid annually on retirement based on service at the end of the year.
2. The transfer values for the pension benefits have been calculated on the basis set by the Trustee of the pension scheme. The Trustee of the pension scheme is an independent body that is separate from the Company and they must calculate transfer values in accordance with legislation having taken actuarial advice from an independent adviser. The assumptions used in the calculation of the transfer values depend on market conditions. Over the year corporate bond yields fell and inflation expectations, as implied by government bond yields, rose. Both movements increase the assessed transfer values. The method for setting the assumptions used was also updated by the Trustee during the year on the advice of the actuary, following the introduction of new legislation. This too increased transfer values. These two factors were much more significant than the increase in accrued benefits over the year.
3. Members of the pension scheme had the option to pay Additional Voluntary Contributions. Neither the contributions nor the resulting benefits are included in the above table.

Mark Robertshaw and Kevin Dangerfield also received a pension allowance, details of which are set out in the Directors' emoluments table on page 83.

The Directors' Remuneration report has been approved by the Board and is signed on its behalf by:

**Simon Heale**
Chairman
Remuneration Committee
18 February 2010

# Shareholder information

**Analysis of shareholdings as at 3 January 2010**

| | | Number of holdings | % of total holdings | Number of shares | % of share capital |
|---|---|---|---|---|---|
| Size of holding | | | | | |
| | 1 – 2,000 | 6,514 | 75.00 | 3,618,987 | 1.34 |
| | 2,001 – 5,000 | 1,191 | 13.71 | 3,810,921 | 1.41 |
| | 5,001 – 10,000 | 394 | 4.54 | 2,822,911 | 1.04 |
| | 10,001 – 50,000 | 295 | 3.40 | 6,158,791 | 2.28 |
| | 50,001 – 100,000 | 81 | 0.93 | 5,892,143 | 2.18 |
| | 100,001 and above | 210 | 2.42 | 247,902,503 | 91.75 |
| | | 8,685 | 100.00 | 270,206,256 | 100.00 |
| Holding classification | | | | | |
| | Individuals | 7,561 | 87.06 | 17,599,117 | 6.51 |
| | Nominee companies | 1,012 | 11.65 | 248,777,277 | 92.07 |
| | Trusts (pension funds etc) | 11 | 0.13 | 336,322 | 0.12 |
| | Others | 101 | 1.16 | 3,493,540 | 1.29 |
| | | 8,685 | 100.00 | 270,206,256 | 100.00 |

**Key dates**

Dividends — Subject to the relevant detailed terms and approvals of the Board of Directors where applicable

5.5% Cumulative First Preference shares of £1 each and
5.0% Cumulative Second Preference shares of £1 each — 1 April 2010 and 1 October 2010

Annual General Meeting — 23 April 2010

Financial results — The Interim results are announced in July with the Report and Accounts for the year normally posted in March

**Other information**

Capital gains tax — The market values of quoted shares and stocks at 31 March 1982 were:

| | |
|---|---|
| Ordinary shares of 25 pence each | 122.5 pence |
| 5.5% Cumulative First Preference shares of £1 each | 30.5 pence |
| 5.0% Cumulative Second Preference shares of £1 each | 28.5 pence |

For capital gains tax purposes, the cost of Ordinary shares is adjusted to take account of rights issues. Any capital gains arising on disposal will also be adjusted to take account of indexation allowances. Since the adjustments will depend on individual circumstances, shareholders are recommended to consult their professional advisers

Share price — The price can be obtained on the Company's website: www.morgancrucible.com

**Company details**

Registered office — Quadrant, 55-57 High Street, Windsor, Berkshire SL4 1LP
Registered in England No. 286773
Telephone: 01753 837000
Fax: 01753 850872
Website: www.morgancrucible.com

**Company registrars**

Capita Registrars, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU
Telephone (in UK): 0871 664 0300 (calls cost 10p per minute plus network extras, lines are open 8.30am-5.30pm Monday-Friday)
Telephone (from overseas): +44 20 8639 3399
Email: ssd@capitaregistrars.com
Website: www.capitaregistrars.com

# Independent auditors' report to the members of The Morgan Crucible Company plc

We have audited the financial statements of The Morgan Crucible Company plc for the year ended 3 January 2010 set out on pages 88 to 148. The financial reporting framework that has been applied in the preparation of the Group financial statements is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU. The financial reporting framework that has been applied in the preparation of the parent Company financial statements is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

**Respective responsibilities of Directors and auditors**

As explained more fully in the Directors' responsibilities statement set out on page 76, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

**Scope of the audit of the financial statements**

A description of the scope of an audit of financial statements is provided on the APB's website at www.frc.org.uk/apb/scope/UKP.

**Opinion on financial statements**

In our opinion:

- The financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 3 January and of the Group's profit for the year then ended.
- The Group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU.
- The parent Company financial statements have been properly prepared in accordance with UK Generally Accepted Accounting Practice.
- The financial statements have been prepared in accordance with the requirements of the Companies Act 2006; and, as regards the Group financial statements, Article 4 of the IAS Regulation.

**Opinion on other matters prescribed by the Companies Act 2006**

In our opinion:

- The part of the Directors' Remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.
- The information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.
- Information given in the Corporate governance statement set out on pages 70 to 75 with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures is consistent with the financial statements.

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- Adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- The parent Company financial statements and the part of the Directors' Remuneration report to be audited are not in agreement with the accounting records and returns; or
- Certain disclosures of Directors' remuneration specified by law are not made; or
- We have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- The Directors' statement, set out on page 101, in relation to going concern; and
- The part of the Corporate governance statement relating to the Company's compliance with the nine provisions of the June 2008 Combined Code specified for our review.

**Stephen Cooper (Senior Statutory Auditor)**
**for and on behalf of KPMG Audit plc, Statutory Auditor**
**Chartered Accountants**
8 Salisbury Square, London EC4Y 8BB
18 February 2010

# Consolidated income statement
## for the year ended 3 January 2010

| | Note | **2009 £m** | 2008 £m |
|---|---|---|---|
| **Revenue** | 2 | **942.6** | 835.0 |
| Operating costs before restructuring costs, other one-off items and amortisation of intangible assets | 4 | **(853.6)** | (726.2) |
| **Profit from operations before restructuring costs, other one-off items and amortisation of intangible assets** | | **89.0** | 108.8 |
| Restructuring costs and other one-off items: | | | |
| Restructuring costs and costs associated with settlement of prior period anti-trust litigation | 8 | **(14.0)** | (11.4) |
| Gain on disposal of property | | **2.0** | 0.8 |
| **Profit from operations before amortisation of intangible assets** | 2 | **77.0** | 98.2 |
| Amortisation of intangible assets | 4 | **(16.3)** | (3.2) |
| **Operating profit** | 2 | **60.7** | 95.0 |
| Finance income | | **24.4** | 34.3 |
| Finance expense | | **(53.7)** | (47.0) |
| **Net financing costs** | 6 | **(29.3)** | (12.7) |
| Loss on disposal of business | | **–** | (0.7) |
| Share of profit of associate (net of income tax) | 12 | **–** | 1.2 |
| **Profit before taxation** | | **31.4** | 82.8 |
| Income tax expense | 7 | **(8.7)** | (20.1) |
| **Profit after taxation and for the period** | | **22.7** | 62.7 |
| Profit for period attributable to: | | | |
| Equity holders of the parent | | **19.0** | 59.2 |
| Non-controlling interests | | **3.7** | 3.5 |
| | | **22.7** | 62.7 |
| **Earnings per share** | 9 | | |
| Basic | | **7.1p** | 22.2p |
| Diluted | | **6.8p** | 21.6p |
| **Dividends** | | | |
| Interim dividend – pence | | **2.50p** | 2.50p |
| – £m | | **6.8** | 6.8 |
| Proposed final dividend – pence | | **4.50p** | 4.50p |
| – £m | | **12.2** | 12.2 |

The proposed final dividend is based upon the number of shares outstanding at the balance sheet date.

# Consolidated statement of other comprehensive income
## for the year ended 3 January 2010

| | 2009 £m | 2008 £m |
|---|---|---|
| **Profit for the period** | **22.7** | 62.7 |
| Foreign exchange translation differences | **(17.5)** | 69.1 |
| Actuarial loss on defined benefit plans | **(18.7)** | (47.0) |
| Deferred tax associated with defined benefit schemes | **–** | 5.4 |
| Revaluation on step acquisition (see note 3) | **10.8** | – |
| Net gain/(loss) on hedge of net investment in foreign subsidiary | **9.1** | (42.8) |
| Cash flow hedges: | | |
| Effective portion of changes in fair value | **0.2** | (4.6) |
| Transferred to profit or loss | **4.6** | 1.2 |
| Change in fair value of equity securities available-for-sale | **1.0** | (3.8) |
| Tax effect on components of other comprehensive income | **5.5** | – |
| **Total comprehensive income for the period** | **17.7** | 40.2 |
| | | |
| **Total comprehensive income attributable to:** | | |
| Equity holders of the parent | **17.1** | 29.2 |
| Non-controlling interests | **0.6** | 11.0 |
| **Total comprehensive income for the period** | **17.7** | 40.2 |

# Consolidated balance sheet
## as at 3 January 2010

| | Note | **2009 £m** | 2008 £m |
|---|---|---|---|
| **Assets** | | | |
| Property, plant and equipment | 10 | **276.2** | 319.6 |
| Intangible assets | 11 | **296.9** | 177.0 |
| Investment in associates | 12 | **1.5** | 6.4 |
| Other investments | 12 | **5.7** | 5.2 |
| Other receivables | 15 | **2.1** | 39.0 |
| Deferred tax assets | 13 | **37.2** | 36.6 |
| **Total non-current assets** | | **619.6** | 583.8 |
| Inventories | 14 | **146.3** | 143.9 |
| Derivative financial assets | 19 | **0.5** | 0.2 |
| Trade and other receivables | 15 | **165.8** | 196.3 |
| Cash and cash equivalents | 16 | **107.6** | 154.5 |
| Assets classified as held for sale | 10 | **1.4** | – |
| **Total current assets** | | **421.6** | 494.9 |
| **Total assets** | | **1,041.2** | 1,078.7 |
| **Liabilities** | | | |
| Interest-bearing loans and borrowings | 18 | **346.6** | 410.9 |
| Employee benefits | 20 | **105.9** | 101.8 |
| Grants for capital expenditure | | **0.2** | 0.2 |
| Provisions | 21 | **5.5** | 7.2 |
| Non-trade payables | 22 | **31.7** | 4.0 |
| Derivative financial liabilities | 19 | **4.1** | 0.8 |
| Deferred tax liabilities | 13 | **47.5** | 40.8 |
| **Total non-current liabilities** | | **541.5** | 565.7 |
| Bank overdraft | 16 | **1.2** | 17.3 |
| Interest-bearing loans and borrowings | 18 | **12.5** | 16.7 |
| Trade and other payables | 22 | **250.3** | 220.9 |
| Current tax payable | | **4.5** | 22.4 |
| Provisions | 21 | **10.9** | 12.5 |
| Derivative financial liabilities | 19 | **5.7** | 15.2 |
| **Total current liabilities** | | **285.1** | 305.0 |
| **Total liabilities** | | **826.6** | 870.7 |
| **Total net assets** | | **214.6** | 208.0 |
| **Equity** | | | |
| Share capital | 17 | **67.9** | 67.9 |
| Share premium | | **85.3** | 85.3 |
| Reserves | | **61.4** | 45.3 |
| Retained earnings | | **(30.0)** | (20.7) |
| **Total equity attributable to equity holders of parent Company** | | **184.6** | 177.8 |
| **Non-controlling interests** | | **30.0** | 30.2 |
| **Total equity** | | **214.6** | 208.0 |

The financial statements were approved by the Board of Directors on 18 February 2010 and were signed on its behalf by:

**Mark Robertshaw,** Chief Executive Officer
**Kevin Dangerfield,** Chief Financial Officer

# Consolidated statement of changes in equity
## for the year ended 3 January 2010

| | Share capital £m | Share premium £m | Translation reserve £m | Hedging reserve £m | Fair value reserve £m | Special reserve £m | Capital redemption reserve £m | Other reserves £m | Retained earnings £m | Total parent equity £m | Non-controlling interests £m | Total equity £m |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Balance at 5 January 2008** | **69.5** | **85.3** | **(8.9)** | **(1.2)** | **1.1** | **6.0** | **34.1** | **1.4** | **(11.1)** | **176.2** | **20.1** | **196.3** |
| Profit for the period | – | – | – | – | – | – | – | – | 59.2 | 59.2 | 3.5 | 62.7 |
| Other comprehensive income | – | – | 18.8 | (3.4) | (3.8) | – | – | – | (41.6) | (30.0) | 7.5 | (22.5) |
| Other movements | – | – | – | – | – | – | – | (0.4) | – | (0.4) | 0.6 | 0.2 |
| **Transactions with owners:** | | | | | | | | | | | | |
| Dividends | – | – | – | – | – | – | – | – | (18.7) | (18.7) | (1.5) | (20.2) |
| Own shares acquired for share buy-back programme | (1.6) | – | – | – | – | – | 1.6 | – | (12.1) | (12.1) | – | (12.1) |
| Own shares acquired for share incentive schemes | – | – | – | – | – | – | – | – | 0.4 | 0.4 | – | 0.4 |
| Equity-settled share-based payment transactions | – | – | – | – | – | – | – | – | 3.2 | 3.2 | – | 3.2 |
| **Balance at 4 January 2009** | **67.9** | **85.3** | **9.9** | **(4.6)** | **(2.7)** | **6.0** | **35.7** | **1.0** | **(20.7)** | **177.8** | **30.2** | **208.0** |
| **Balance at 5 January 2009** | **67.9** | **85.3** | **9.9** | **(4.6)** | **(2.7)** | **6.0** | **35.7** | **1.0** | **(20.7)** | **177.8** | **30.2** | **208.0** |
| Profit for the year | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **19.0** | **19.0** | **3.7** | **22.7** |
| Other comprehensive income | **–** | **–** | **0.2** | **4.8** | **1.0** | **–** | **–** | **10.8** | **(18.7)** | **(1.9)** | **(3.1)** | **(5.0)** |
| Other movements | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **(0.7)** | **0.2** | **(0.5)** | **0.5** | **–** |
| **Transactions with owners:** | | | | | | | | | | | | |
| Dividends | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **(12.1)** | **(12.1)** | **(1.3)** | **(13.4)** |
| Equity-settled share-based payment transactions | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **2.3** | **2.3** | **–** | **2.3** |
| **Balance at 3 January 2010** | **67.9** | **85.3** | **10.1** | **0.2** | **(1.7)** | **6.0** | **35.7** | **11.1** | **(30.0)** | **184.6** | **30.0** | **214.6** |

The movement in other reserves in 2009 through other comprehensive income reflects the increase in the fair value of the Group's original 49% interest in Clearpower Limited from the date of its original acquisition to 5 January 2009 excluding goodwill and to the extent not previously recognised as the Group's share of the results of Clearpower Limited. See note 3 for further details.

Details of the reserves are provided in note 17.

# Consolidated statement of cash flows
## for the year ended 3 January 2010

| | Note | 2009 £m | 2008 £m |
|---|---|---|---|
| **Operating activities** | | | |
| Profit for the period | | **22.7** | 62.7 |
| Adjustments for: | | | |
| Depreciation | 4 | **31.7** | 27.6 |
| Amortisation | 4 | **16.3** | 3.2 |
| Net financing costs | | **29.3** | 12.7 |
| Loss on disposal of business | | **–** | 0.7 |
| Share of profit of associate | 12 | **–** | (1.2) |
| Profit on sale of property, plant and equipment | | **(2.1)** | (0.7) |
| Income tax expense | 7 | **8.7** | 20.1 |
| Equity-settled share-based payment expenses | | **2.0** | 2.2 |
| **Cash generated from operations before changes in working capital and provisions** | | **108.6** | 127.3 |
| Decrease/(increase) in trade and other receivables | | **26.5** | (8.7) |
| Decrease/(increase) in inventories | | **8.1** | (11.9) |
| Decrease in trade and other payables | | **(8.8)** | (1.2) |
| Non-cash operating costs relating to restructuring | 4 | **1.5** | 4.2 |
| Decrease in provisions and employee benefits | | **(13.5)** | (10.0) |
| **Cash generated from operations** | | **122.4** | 99.7 |
| Interest paid | | **(25.5)** | (21.1) |
| Income tax paid | | **(32.0)** | (28.1) |
| **Net cash from operating activities** | | **64.9** | 50.5 |
| **Investing activities** | | | |
| Purchase of property, plant and equipment | | **(18.1)** | (33.4) |
| Proceeds from sale of property, plant and equipment | | **4.4** | 1.9 |
| Sale of investments | | **0.2** | 1.9 |
| Interest received | | **2.3** | 4.2 |
| Acquisition of subsidiaries and associate, net of cash acquired | | **(31.9)** | (79.2) |
| Forward contracts used in net investment hedging | | **(0.3)** | (8.9) |
| **Net cash from investing activities** | | **(43.4)** | (113.5) |
| **Financing activities** | | | |
| Purchase of own shares | | **–** | (12.1) |
| Increase in borrowings | 16 | **169.2** | 127.2 |
| Repayment of borrowings | 16 | **(204.7)** | – |
| Payment of finance lease liabilities | 16 | **(0.6)** | (0.3) |
| Dividends paid | | **(12.1)** | (18.8) |
| **Net cash from financing activities** | | **(48.2)** | 96.0 |
| Net (decrease)/increase in cash and cash equivalents | | **(26.7)** | 33.0 |
| Cash and cash equivalents at start of period | | **139.4** | 90.1 |
| Effect of exchange rate fluctuations on cash held | | **(5.1)** | 16.3 |
| **Cash and cash equivalents at period end** | 16 | **107.6** | 139.4 |

A reconciliation of cash and cash equivalents to net borrowings is shown in note 16.

# Notes to the consolidated financial statements

## 1. Accounting policies, estimates and judgments

### Accounting policies

The Morgan Crucible Company plc (the 'Company') is a company incorporated in the UK.

The Group financial statements consolidate those of the Company and its subsidiaries (together referred to as the 'Group'), and include the Group's interest in associates. The parent Company financial statements present information about the Company as a separate entity and not about its Group. Historically the Group has drawn up its consolidated financial statements to 4 January. These consolidated financial statements have been drawn up to Sunday 3 January 2010. As from this year, the Group will maintain a 52 or 53 week fiscal year ending on the Sunday nearest to the Accounting Reference Date of the Company, 1 January.

The Group financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU (adopted IFRSs). The Company has elected to prepare its parent Company financial statements in accordance with UK Generally Accepted Accounting Practice; these are presented on pages 139 to 147.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these Group financial statements.

During the period, the Group has applied IAS 1 *Presentation of Financial Statements* (*revised 2007*) which has introduced a number of terminology changes and has resulted in a number of changes in presentation and disclosure. The revised standard has had no impact on the reported results or financial position of the Group. In addition, the Group has adopted IFRS 2 *Amendment Regarding Vesting Conditions and Cancellations*, IFRS 8 *Operating Segments*, IAS 23 *Borrowing Costs (revised 2007)*, IFRIC 14 *IAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*, IFRIC 13 *Customer Loyalty Programmes* and Amendments to IAS 32 *Financial Instruments: Presentation* and IAS 1 *Presentation of Financial Statements*, none of which have had a significant effect on the reported results or financial position of the Group.

### (a) Measurement convention

The financial statements are prepared on the historical cost basis except that the following assets and liabilities are stated at their fair value: derivative financial instruments and financial instruments available-for-sale.

### (b) Functional and presentation currency

The Group financial statements are presented in pounds sterling, which is the Company's functional currency.

### (c) Basis of consolidation

#### (i) Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

#### (ii) Associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20% and 50% of the voting power of another entity. Associates are accounted for using the equity method and are initially recognised at cost. The Group's investment includes goodwill identified on acquisition, net of any accumulated impairment losses. The consolidated financial statements include the Group's share of the income and expenses and equity movements of associates, after adjustments to align the accounting policies with those of the Group, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds its interest in an associate, the carrying amount of that interest is reduced to nil and the recognition of further losses is discontinued except to the extent that the Group has an obligation or has made payments on behalf of the associate.

#### (iii) Transactions eliminated on consolidation

Intra-group balances and any unrealised gains and losses or income and expenses arising from intra-group transactions are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with associates are eliminated against the investment to the extent of the Group's interest in the associate. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

### (d) Foreign currency

#### (i) Foreign currency transactions

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to pounds sterling at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to pounds sterling at foreign exchange rates ruling at the dates the fair value was determined.

# Notes to the consolidated financial statements
continued

**1. Accounting policies, estimates and judgments** continued

(ii) Financial statements of foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to pounds sterling at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated to pounds sterling at an average rate for the period where this approximates to the foreign exchange rates ruling at the dates of the transactions. Foreign exchange differences arising on retranslation since the adoption of IFRS are recognised directly in a separate component of equity.

(iii) Net investment in foreign operations

Exchange differences arising from the translation of the net investment in foreign operations and of related hedges are taken to the translation reserve. They are released into the income statement upon disposal.

### (e) Derivative financial instruments

The Group uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from operational, financing and investment activities. In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for at fair value through profit or loss.

Derivative financial instruments are recognised initially at fair value. The gain or loss on remeasurement to fair value is recognised immediately in profit or loss. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged (see accounting policy 'f').

The fair value of forward exchange contracts is their quoted market price at the balance sheet date, being the present value of the quoted forward price.

### (f) Hedging

(i) Cash flow hedges

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a highly probable forecasted transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in equity. The associated gain or loss is removed from equity and recognised in the income statement in the period in which the transaction to which it relates occurs.

When a hedging instrument expires or is sold, terminated or exercised, or the entity revokes designation of the hedge relationship but the hedged forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in the hedging reserve and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, the cumulative unrealised gain or loss recognised in the hedging reserve is recognised immediately in the income statement.

(ii) Hedge of monetary assets and liabilities

Where a derivative financial instrument is used to hedge economically the foreign exchange exposure of a recognised monetary asset or liability, no hedge accounting is applied and any gain or loss on the hedging instrument is recognised in the income statement.

(iii) Hedge of net investment in foreign operations

The portion of the gain or loss on an instrument used to hedge a net investment in a foreign operation that is determined to be an effective hedge is recognised directly in the translation reserve. The ineffective portion is recognised immediately in profit or loss.

### (g) Property, plant and equipment

(i) Owned assets

Items of property, plant and equipment are stated at cost, or at deemed cost, less accumulated depreciation (see below) and impairment losses (see accounting policy 'l'). The cost of self-constructed assets includes the cost of materials, direct labour, and an appropriate proportion of production overheads.

Certain items of property, plant and equipment that had been revalued to fair value on or prior to 5 January 2004, the date of transition to adopted IFRSs, are measured on the basis of deemed cost, being the revalued amount at the date of that revaluation. Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

Gains and losses on the disposal of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of the asset. Gains and losses on the disposal of property are recognised in 'Other one-off items' in the income statement. Gains and losses on the disposal of plant and equipment are recognised in 'Operating costs' in the income statement.

(ii) Leased assets

Leases under the terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Leased assets acquired by way of a finance lease are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation and impairment losses.

## 1. Accounting policies, estimates and judgments continued

(iii) Depreciation

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Land is not depreciated. The estimated useful lives are as follows:

| | |
|---|---|
| Buildings | 50 years |
| Plant and equipment - presses, kilns and furnaces | 10-20 years |
| Other plant and equipment | 10 years |
| Fixtures and fittings | 10 years |
| Motor vehicles and IT equipment | 3 years |

### (h) Intangible assets

(i) Goodwill

All business combinations are accounted for by applying the purchase method. In respect of business acquisitions that have occurred since 5 January 2004, goodwill represents the difference between the cost of the acquisition and the fair value of assets, liabilities and contingent liabilities acquired.

In respect of acquisitions prior to this date, goodwill is included on the basis of its deemed cost, which represents the amount recorded under UK GAAP. The classification and accounting treatment of business combinations that occurred prior to 5 January 2004 has not been reconsidered. Goodwill is stated at cost less any accumulated impairment losses.

Goodwill is allocated to cash-generating units and is tested annually for impairment (see accounting policy 'l').

(ii) Research and development

Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognised in the income statement as an expense as incurred.

Expenditure on development activities, whereby research findings are applied to a plan or design for the production of new or substantially improved products and processes, is capitalised if the product or process is technically and commercially feasible and the Group has sufficient resources to complete development, use and sale of products or processes. The expenditure capitalised includes the cost of materials, direct labour and an appropriate proportion of overheads. Capitalised development expenditure is stated at cost less accumulated amortisation (see below) and impairment losses (see accounting policy 'l'). Other development expenditure is recognised in the income statement as an expense as incurred.

(iii) Other intangible assets

Other intangible assets that are acquired by the Group are stated at cost less accumulated amortisation (see below) and impairment losses (see accounting policy 'l').

(iv) Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets unless such lives are indefinite. Goodwill and intangible assets with an indefinite useful life are systematically tested for impairment at each balance sheet date. Other intangible assets are amortised from the date they are available for use. The estimated useful lives are as follows:

| | |
|---|---|
| Capitalised development costs | 3 years |
| Computer software | 3-6 years |
| Customer relationships | 15-20 years |
| Technology | 15-20 years |
| Order book | Amortised over the period in which the associated orders are fulfilled |

### (i) Trade and other receivables

Trade and other receivables are stated at their fair value less impairment losses (see accounting policy 'l').

### (j) Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

The cost of inventories is based on the first-in first-out principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of overheads based on normal operating capacity.

# Notes to the consolidated financial statements
continued

**1. Accounting policies, estimates and judgments** continued

### (k) Cash and cash equivalents
Cash and cash equivalents comprises cash balances and call deposits.

### (l) Impairment
The carrying amounts of the Group's assets, other than inventories (see accounting policy 'j') and deferred tax assets (see accounting policy 's'), are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated (see (i) below).

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units (group of units) and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro-rata basis.

When a decline in the fair value of an available-for-sale financial asset has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised directly in equity is recognised in profit or loss even though the financial asset has not been derecognised. The amount of the cumulative loss that is recognised in profit or loss is the difference between the acquisition cost and current fair value, less any impairment loss on that financial asset previously recognised in profit or loss.

#### (i) Calculation of recoverable amount
The recoverable amount of the Group's investments in receivables carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate (ie the effective interest rate computed at initial recognition of these financial assets). Receivables with a short duration are not discounted. The recoverable amount of other assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

#### (ii) Reversals of impairment
An impairment loss in respect of a receivable carried at amortised cost is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

An impairment loss in respect of an investment in an equity instrument classified as available-for-sale is not reversed through profit or loss. If the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss shall be reversed, with the amount of the reversal recognised in profit or loss.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount and when there is an indication that the impairment loss may no longer exist.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

### (m) Share capital

#### (i) Ordinary share capital
Ordinary shares are classified as equity.

#### (ii) Preference share capital
Preference share capital is classified as equity if it is non-redeemable and any dividends are discretionary, or is redeemable but only at the Company's option. Dividends on Preference share capital classified as equity are recognised as distributions within equity.

#### (iii) Repurchase of share capital and own shares held by ESOP trust (treasury shares)
When share capital recognised as equity is repurchased, the amount of the consideration paid, which includes directly attributable costs, is net of any tax effects and is recognised as a deduction from equity. Repurchased shares and the purchase of own shares by the Group-sponsored ESOP trust are presented as a deduction from total equity. Repurchased shares are classified as treasury shares until their subsequent cancellation.

## 1. Accounting policies, estimates and judgments continued

### (n) Employee benefits

#### (i) Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred.

#### (ii) Defined benefit plans

The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any plan assets is deducted. The discount rate is the yield at the balance sheet date on AA credit-rated bonds that have maturity dates approximating the terms of the Group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Group, the recognised asset is limited to the total of any unrecognised past service costs and the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. An economic benefit is available to the Group if it is realisable during the life of the plan, or on settlement of the plan liabilities. Actuarial gains and losses, differences between the expected and actual returns, and the effect of changes in actuarial assumptions, are recognised in full in equity in the year in which they arise.

#### (iii) Long-term service benefits

The Group's net obligation in respect of long-term service benefits, other than pension plans, is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The obligation is calculated using the projected unit credit method, or similar approximation, and is discounted to its present value and the fair value of any related assets is deducted. The discount rate is the yield at the balance sheet date on AA credit-rated bonds that have maturity dates approximating the terms of the Group's obligations.

#### (iv) Share-based payment transactions

The Group operates various share option programmes that allow Group employees to acquire shares in the Company. Under the Long Term Incentive Plan (LTIP) and The Morgan Crucible Bonus Deferral Share Matching Plan awards of shares are made to various key executives and under the Directors' Share Option Plan 2006 (2006 ESOP), the Executive Share Option Scheme 2004 (2004 ESOS) and the Executive Share Option Scheme 1995 (1995 ESOS) share options are granted by the Company. The Company also maintains an all-employee sharesave scheme available to employees in the UK and Germany. The grant date fair value of options granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period that the employees become unconditionally entitled to the options. The amount recognised as an expense is adjusted to reflect the actual number of share options for which the related service and non-market vesting conditions are met.

The fair value of the options and awards under each scheme have been measured using the following models:

| | |
|---|---|
| Directors' Share Option Plan 2006 | Monte Carlo model |
| Long Term Incentive Plan 2004 | Monte Carlo model |
| The Morgan Crucible Bonus Deferral Share Matching Plan | Monte Carlo model |
| Executive Share Option Scheme 2004 | Monte Carlo model |
| Executive Share Option Scheme 1995 (grants made since 2004) | Binominal Lattice option pricing model |
| Employee Sharesave Scheme 1995 (grants made since 2004) | Black-Scholes Merton model |
| Employee Sharesave Scheme 2004 | Black-Scholes Merton model |
| Employee Sharesave Scheme 2004 (Germany) | Black-Scholes Merton model |

The choice of model takes into account the terms and conditions upon which the awards were made and the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest except where forfeiture is only due to share prices not achieving the threshold for vesting.

# Notes to the consolidated financial statements
continued

## 1. Accounting policies, estimates and judgments continued

### (o) Provisions
A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

#### (i) Restructuring
A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly. Future operating costs are not provided for.

#### (ii) Onerous contracts
A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract.

#### (iii) Environmental
In accordance with the Group's environmental policy a provision is recognised for known environmental issues which the Group will rectify over the next few years. In a number of jurisdictions companies have a constructive obligation to remedy any known environmental problems.

### (p) Trade and other payables
Trade and other payables are stated at their fair value.

### (q) Revenue

#### (i) Goods sold
Revenue from the sale of products is measured at the fair value of the consideration received or receivable, net of returns, trade discounts and volume rebates. Revenue is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer.

#### (ii) Government grants
Government grants are recognised in the balance sheet initially as deferred income, as grants for capital expenditure, when there is reasonable assurance that they will be received and that the Group will comply with the conditions attaching to them. Grants that compensate the Group for expenses incurred are recognised as revenue in the income statement on a systematic basis in the same periods in which the expenses are incurred. Grants that compensate the Group for the cost of an asset are recognised in the income statement as other operating income on a systematic basis over the useful life of the asset.

### (r) Expenses

#### (i) Operating lease payments
Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognised in the income statement as an integral part of the total lease expense.

#### (ii) Finance lease payments
Leases where the Group assumes substantially all of the risks and rewards of ownership are classified as finance leases as if the asset had been purchased outright. Assets acquired under finance leases are recognised as assets of the Group and the capital elements of the leasing commitments are shown as obligations in creditors. Depreciation is charged on a basis consistent with similar owned assets or over the lease term if shorter. Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

#### (iii) Net financing costs
Net financing costs comprise interest payable on borrowings calculated using the effective interest rate method, interest receivable on funds invested, gains and losses on hedging instruments that are recognised in the income statement (see accounting policy 'f'), expected return on IAS 19 pension assets and interest on IAS 19 obligations. Interest income is recognised in the income statement as it accrues, using the effective interest method.

**1. Accounting policies, estimates and judgments** continued

(s) Income tax

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of goodwill, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(t) Segment reporting

The Group has adopted IFRS 8 *Operating Segments* with effect from 4 January 2009. The Group has identified four reportable operating segments. These have been identified on the basis of internal management reporting information that is regularly reviewed by the Group's Chief Operating Decision Maker in order to allocate resources and assess performance.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly investments and related income, loans and borrowings and related expenses, corporate assets (primarily the Company's headquarters) and head office expenses, and income tax assets and liabilities.

(u) Classification of financial instruments issued by the Group

Financial instruments issued by the Group are treated as equity (ie forming part of shareholders' funds) only to the extent that they meet the following two conditions:

(i) they include no contractual obligations upon the Group to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Group; and

(ii) where the instrument will or may be settled in the Company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the Company's own equity instruments or is a derivative that will be settled by the Company exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the Company's own shares, the amounts presented in these financial statements for called up share capital and share premium account exclude amounts in relation to those shares.

Finance payments associated with financial liabilities are dealt with as part of finance expenses. Finance payments associated with financial instruments that are classified in equity are dividends and are recorded directly in equity.

(v) Investments in debt and equity securities

Investments in debt and equity securities held by the Group are classified as being available-for-sale and are stated at fair value, with any resultant gain or loss being recognised directly in equity (in the fair value reserve), except for impairment losses and, in the case of monetary items such as debt securities, foreign exchange gains and losses. When these investments are derecognised, the cumulative gain or loss previously recognised directly in equity is recognised in profit or loss. Where these investments are interest-bearing, interest calculated using the effective interest method is recognised in profit or loss.

(w) Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

(x) Capitalisation of borrowing costs

Borrowing costs (interest and other costs) are capitalised when they are incurred on raising specific funds to finance a major capital project which will be a significant productive asset, or to the extent that funds borrowed generally are used for the purposes of obtaining a qualifying asset.

# Notes to the consolidated financial statements
continued

**1. Accounting policies, estimates and judgments** continued

(y) Dividends

Dividends payable are recognised as a liability in the period in which they are declared and approved.

(z) Step acquisitions

Step acquisitions arise when the Group acquires control of an entity through successive share purchases. The identifiable assets, liabilities and contingent liabilities acquired are recorded at fair value on the date that control is acquired. The amount recognised as goodwill or negative goodwill is determined separately for each tranche acquired, calculated as the difference between the fair value of the consideration paid and the fair value of the identifiable assets, liabilities and contingent liabilities acquired, in accordance with IFRS 3 *Business Combinations*. Any changes in the fair value of the identifiable assets and liabilities acquired between the acquisition date and the date that control is obtained are recorded in other reserves in equity to the extent that they have not previously been recognised in the income statement.

(aa) New Standards and Interpretations not yet adopted

A number of new Standards and amendments to Standards and Interpretations are not yet effective for the year ended 3 January 2010, and have not been applied in preparing these consolidated financial statements:

The following adopted IFRSs were available for early application but have not been applied:

(i) IFRS 3 (Revised 2008) *Business Combinations*

(ii) IAS 27 (Revised 2008) *Consolidated and Separate Financial Statements*

The revised standards introduce changes to acquisition accounting, notably in respect of treatment of acquisition costs, step and partial acquisitions, minority interests and contingent consideration.

The Group does not expect the above standards to have any significant impact on the financial statements for the period commencing 4 January 2010.

Amendments to the following adopted IFRSs were available for early application but have not been applied:

(i) IAS 17 *Leases*

(ii) IAS 18 *Revenue*

(iii) IAS 27 (Amended 2008) *Consolidated and Separate Financial Statements*

(iv) IAS 36 *Impairment of Assets*

(v) IAS 38 *Intangible Assets*

(vi) IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*

(vii) IFRS 8 *Operating Segments*

(viii) IAS 39 *Financial Instruments*

(ix) IFRIC 16 *Hedges of a Net Investment in a Foreign Operation*

The Group does not expect the above amendments to have any significant impact on the financial statements for the period commencing 4 January 2010.

Accounting estimates and judgments

Judgments made by the Directors in the application of these accounting policies that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed below.

Management discussed with the Audit Committee the development, selection and disclosure of the Group’s critical accounting policies and estimates and the application of these policies and estimates. The following accounting estimates are subject to significant uncertainty:

Provisions

Note 21 contains information about provisions. Provisions for closure and restructuring costs, environmental issues and settlement of litigation are judgmental by their nature. Amounts provided are the Group’s best estimate of exposure based on currently available information.

## 1. Accounting policies, estimates and judgments continued

### Recognition of identifiable intangible assets and goodwill

Note 3 contains information about intangible assets recognised on acquisition. These primarily relate to existing contracts, order books and customer relationships, which are supported by long-term relationships with key customers. The Group has estimated that the customer relationships have an economic life of 15-20 years.

### Impairment of goodwill

Note 11 contains information about the assumptions relating to goodwill impairment tests.

### Credit risk

Note 19 contains information about the Group's exposure to credit risk. The Group establishes both specific and general allowances for impairment losses against receivables. The general loss allowance is estimated based on historical data of payment statistics for similar financial assets.

### Foreign currency exposure

Note 19 contains information about the foreign currency exposure of the Group and risks in relation to foreign exchange movements.

### Pension assumptions

The principal actuarial assumptions applied to pensions are shown in note 20. The actuarial evaluation of pension assets and liabilities is based on assumptions in respect of inflation, future salary increases, discount rates, returns on investments and mortality rates. Relatively small changes in the assumptions underlying the actuarial valuations of pension schemes can have a significant impact on the net pension liability included in the balance sheet.

### Taxation

The level of current tax and deferred tax recognised is dependent on the tax rates in effect at the balance sheet date, and on subjective judgments as to the outcome of decisions to be made by the tax authorities in the various tax jurisdictions around the world in which the Group operates. Deferred tax assets are recognised based on management's assessment of the extent to which they are recoverable.

### Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business review on pages 32 to 63. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Business review. In addition, note 19 includes the Group's policies and processes for managing financial risk; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

The Group announced in May 2009 the signing of a new £280 million three-year multicurrency revolving facility agreement with a syndicate of eight banks. This replaced a $420 million facility with the same financial covenants which was due to mature in March 2010. The Group meets its day-to-day working capital requirements through local banking arrangements that are supported through the flexibility provided by the new facility. The Group's forecasts and projections, taking account of reasonably possible changes in trading performance and exchange rates, show the Group operating comfortably within the Group's debt financial covenants for the next 12 months.

The current economic climate continues to have an impact on the Group, its customers and suppliers. The Board fully recognises the challenges that lie ahead but, after making enquiries, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and Accounts.

# Notes to the consolidated financial statements
continued

## 2. Segment reporting

This year the Group adopted IFRS 8 *Operating Segments* which replaces IAS 14 *Segment Reporting*. The accounting policy for identifying segments is now based on internal management reporting information that is regularly reviewed by the Group's Chief Operating Decision Maker. In contrast, IAS 14 *Segment Reporting* required the Group to identify two sets of segments (business and geographical) based on the risks and rewards of the operating segments.

As a result of the adoption of IFRS 8 *Operating Segments*, the Directors are of the opinion that the primary business segments, as previously reported under IAS 14 *Segment Reporting*, should remain unchanged.

Hence the Group continues to comprise the following four reportable segments:

- Carbon – the Carbon Division produces a wide variety of technological solutions from carbon, graphite and silicon carbide.
- Technical Ceramics – the Technical Ceramics Division makes an extensive range of industrial ceramics products for a wide variety of applications.
- Thermal Ceramics – the Thermal Ceramics Division designs and manufactures a wide variety of heat insulation products.
- Molten Metal Systems – the Molten Metal Systems Division occupies a leading position in the supply of crucibles and manufactures equipment used in the melting, holding and processing of metals and alloys.

| | | | | | Insulating Ceramics | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Carbon | | Technical Ceramics | | Thermal Ceramics | | Molten Metal Systems | | Consolidated | |
| | **2009 £m** | 2008 £m | **2009 £m** | 2008 £m | **2009 £m** | 2008 £m | **2009 £m** | 2008 £m | **2009 £m** | 2008 £m |
| **Revenue from external customers** | **391.4** | 239.9 | **206.0** | 212.2 | **315.1** | 347.4 | **30.1** | 35.5 | **942.6** | 835.0 |
| **Divisional EBITA[1]** | **40.5** | 36.3 | **25.1** | 31.6 | **26.7** | 41.4 | **0.9** | 4.2 | **93.2** | 113.5 |
| Unallocated costs | | | | | | | | | **(4.2)** | (4.7) |
| **Group EBITA[2]** | | | | | | | | | **89.0** | 108.8 |
| Restructuring costs and other one-off items | | | | | | | | | **(12.0)** | (10.6) |
| **Underlying operating profit[3]** | | | | | | | | | **77.0** | 98.2 |
| Amortisation of intangible assets | | | | | | | | | **(16.3)** | (3.2) |
| **Operating profit** | | | | | | | | | **60.7** | 95.0 |
| Finance income | | | | | | | | | **24.4** | 34.3 |
| Finance expense | | | | | | | | | **(53.7)** | (47.0) |
| Loss on disposal of business | | | | | | | | | **–** | (0.7) |
| Share of profit of associate (net of income tax) | | | | | | | | | **–** | 1.2 |
| **Profit before taxation** | | | | | | | | | **31.4** | 82.8 |

1. Divisional EBITA is defined as segment operating profit before restructuring costs, other one-off items and amortisation of intangible assets.
2. Group EBITA is defined as operating profit before restructuring costs, other one-off items and amortisation of intangible assets.
3. Underlying operating profit is defined as operating profit before amortisation of intangible assets.

The above measures of profit are shown because the Directors use them to measure the underlying performance of the business, as referred to in the Business review section of the Annual Report.

The Group did not have any significant inter-segment revenue between reportable operating segments in 2009 and 2008.

## 2. Segment reporting continued

| | Carbon 2009 £m | Carbon 2008 £m | Technical Ceramics 2009 £m | Technical Ceramics 2008 £m | Insulating Ceramics – Thermal Ceramics 2009 £m | Insulating Ceramics – Thermal Ceramics 2008 £m | Insulating Ceramics – Molten Metal Systems 2009 £m | Insulating Ceramics – Molten Metal Systems 2008 £m | Consolidated 2009 £m | Consolidated 2008 £m |
|---|---|---|---|---|---|---|---|---|---|---|
| Segment assets | **384.4** | 254.6 | **220.9** | 274.6 | **258.2** | 359.2 | **31.6** | 44.1 | **895.1** | 932.5 |
| Unallocated assets | | | | | | | | | **146.1** | 146.2 |
| Total assets | | | | | | | | | **1,041.2** | 1,078.7 |
| Segment liabilities | **78.5** | 60.1 | **32.9** | 59.2 | **64.9** | 131.4 | **7.4** | 16.4 | **183.7** | 267.1 |
| Unallocated liabilities | | | | | | | | | **642.9** | 603.6 |
| Total liabilities | | | | | | | | | **826.6** | 870.7 |
| Investment in associates | **1.5** | 6.4 | **–** | – | **–** | – | **–** | – | **1.5** | 6.4 |
| Segment capital expenditure | **5.0** | 13.0 | **6.1** | 6.8 | **5.9** | 9.1 | **0.9** | 4.0 | **17.9** | 32.9 |
| Unallocated capital expenditure | | | | | | | | | **0.2** | 0.5 |
| Total capital expenditure | | | | | | | | | **18.1** | 33.4 |

| | Carbon 2009 £m | Carbon 2008 £m | Technical Ceramics 2009 £m | Technical Ceramics 2008 £m | Insulating Ceramics – Thermal Ceramics 2009 £m | Insulating Ceramics – Thermal Ceramics 2008 £m | Insulating Ceramics – Molten Metal Systems 2009 £m | Insulating Ceramics – Molten Metal Systems 2008 £m | Consolidated 2009 £m | Consolidated 2008 £m |
|---|---|---|---|---|---|---|---|---|---|---|
| Segment depreciation | **9.9** | 8.0 | **9.1** | 8.2 | **11.5** | 10.5 | **1.2** | 0.9 | **31.7** | 27.6 |

| | Europe 2009 £m | Europe 2008 £m | Americas 2009 £m | Americas 2008 £m | Far East & Australia 2009 £m | Far East & Australia 2008 £m | Middle East & Africa 2009 £m | Middle East & Africa 2008 £m | Consolidated 2009 £m | Consolidated 2008 £m |
|---|---|---|---|---|---|---|---|---|---|---|
| Revenue from external customers | **453.3** | 328.0 | **325.1** | 359.6 | **140.1** | 135.1 | **24.1** | 12.3 | **942.6** | 835.0 |
| Non-current assets (excluding deferred tax and financial instruments) | **285.0** | 204.3 | **216.9** | 253.6 | **78.8** | 86.6 | **1.7** | 2.7 | **582.4** | 547.2 |

Revenue from external customers attributed to the UK (the Group's country of domicile) was £252.7 million (2008: £83.6 million).

### Major customer

Revenues from one customer of the Group's Carbon Division represent £161.1 million of the Group's total revenues.

# Notes to the consolidated financial statements
continued

## 3. Acquisitions
### Acquisitions in 2009
Clearpower

In 2007 the Group acquired 49% of the Ordinary share capital of Clearpower Limited, a company that, via two intermediary holding companies, owns 100% of NP Aerospace Limited. On 5 January 2009 the Group acquired the remaining 51% of the Ordinary share capital of Clearpower Limited for a total of £56.8 million, an amount contingent on the future performance of Clearpower Limited. This comprised £12.2 million in cash for 11% of the Ordinary share capital and £44.6 million in discounted deferred contingent consideration for 40% of the Ordinary share capital.

The discounted deferred contingent consideration takes the form of four synthetic forwards each to acquire 10% of the Ordinary share capital of Clearpower Limited at future dates from 2010 onwards, the amount of which are based on a fixed EBITDA multiple of Clearpower Limited. In accordance with IAS 32 *Financial Instruments: Presentation*, the Group has recognised a liability representing the estimated present value of the redemption amount in respect of its obligation to acquire these shares and has treated them as if they were acquired by the Group on 5 January 2009. Since this consideration is contingent on the future performance of Clearpower the liability is remeasured at each reporting date with any adjustments recorded through goodwill, in accordance with IFRS 3 *Business Combinations*. It is possible that the carrying amount of this liability will increase or decrease if the future performance of Clearpower varies from current expectations. At 3 January 2010 this liability to purchase the remaining 40% of the Ordinary share capital of Clearpower Limited was remeasured and increased to £46.0 million. In addition amounts payable in respect of the acquisition of 11% of the Ordinary share capital were increased by £8.1 million based on the actual performance of Clearpower Limited in 2009. The £8.1 million deferred contingent consideration in respect of the acquisition of 11% of the Ordinary share capital will be paid after the balance sheet date.

At 3 January 2010 the Group carries a total liability of £54.1 million in respect of deferred consideration. This is included within current and non-current non-trade payables (see note 22). The unwinding of the discount on this liability of £2.2 million is recorded as a finance expense (see note 6). The adjustment through goodwill since the date of acquisition as a result of the remeasurement is £7.3 million.

The principal activity of NP Aerospace Limited is the development, manufacture and marketing of ballistic and non-ballistic products in the defence and civil sectors. In the 12 months to 3 January 2010 Clearpower Limited and its subsidiaries contributed an operating profit before amortisation of intangible assets of £28.8 million to the consolidated net profit.

The details of the transaction, result and fair value adjustments arising from the change in ownership are shown below:

| | Acquiree's carrying amount 2009 £m | Fair value to the Group 2009 £m |
|---|---|---|
| **Clearpower** | | |
| **The figures in the table below represent a 100% interest in Clearpower Limited** | | |
| Intangible assets | – | 51.5 |
| Property, plant and equipment | 2.9 | 2.9 |
| Other working capital | 0.1 | 0.1 |
| Derivative financial liabilities | (0.8) | (0.8) |
| Interest-bearing loans and other borrowings | (58.3) | (58.3) |
| Non-controlling interest | (1.2) | (1.2) |
| Deferred taxation | 0.3 | (14.1) |
| **Net liabilities acquired** | (57.0) | (19.9) |
| Goodwill | | 96.7 |
| **Fair value of net liabilities acquired and goodwill arising** | | 76.8 |

| | |
|---|---|
| **Components of cost of acquisition** | |
| Fair value of consideration for initial 49% shareholding in 2007 | 0.5 |
| Fair value of consideration for remaining 51% shareholding in 2009 | 64.1 |
| Total cost of acquisition | 64.6 |
| Earnings under equity method of initial 49% shareholding (while Clearpower Limited was an associate) | 1.4 |
| Revaluation surplus arising on step acquisition | 10.8 |
| **Fair value of net liabilities acquired and goodwill arising** | 76.8 |

| | |
|---|---|
| Cash paid on acquisition of 11% of the Ordinary share capital | 12.2 |
| Acquisition costs | 0.1 |
| **Net cash outflow to the Group in 2009** | 12.3 |

**3. Acquisitions** continued

Provisional fair value adjustments were made to reflect the fair value of the assets/liabilities acquired and principally represent the recognition of the fair value of non-contractual customer relationships, order book and technology and the associated deferred tax on the temporary timing difference created by the fair value adjustments. No adjustments to fair value were made.

Recognised goodwill comprises £22.5 million arising on the initial purchase of the 49% interest in 2007 and £74.2 million arising on the effective acquisition of the remaining 51% interest on 5 January 2009.

Excluding goodwill a total of £51.5 million of intangible assets has been recognised comprising £23.9 million of customer relationships, £18.3 million of technology and an order book of £9.3 million. These have been recognised within operating intangibles arising on acquisition (see note 11).

Goodwill represents future economic benefits arising from assets that are not capable of being identified individually or recognised as separate assets. This includes acquirer-specific synergies such as cross-selling opportunities and the enhancement of technologies and processes between existing and acquired sites.

The fair value of the purchase consideration, which is dependent on future results, represents management's best estimate of the likely final purchase consideration.

The revaluation surplus, recorded in the statement of other comprehensive income, reflects the increase in the fair value of the Group's original 49% interest in Clearpower Limited from the date of its original acquisition to 5 January 2009 excluding goodwill and to the extent not previously recognised as the Group's share of the results of Clearpower Limited.

## Other acquisitions

On 6 April 2009, the Group acquired a 50% stake in Integrated Survivability Technologies Limited. The principal activity of Integrated Survivability Technologies Limited is acting as prime contractor for delivery of military vehicles and provision of related support services. This company did not trade prior to the date of acquisition.

During the year the Company acquired a further 9% of the Ordinary share capital and voting rights of Carbo San Luis SA for £1.1 million, resulting in a total shareholding of 84.6% at 3 January 2010.

## Acquisitions in 2008

On 31 March 2008 the Group acquired 100% of the shares in the Technical Ceramics business of Carpenter Technology Corporation, known as Certech and Carpenter Advanced Ceramics, for £74.6 million. The principal activity of Certech is the manufacture of complex injection-moulded ceramic components. The principal activity of Carpenter Advanced Ceramics is the manufacture of engineered ceramic products. In the nine months to 4 January 2009 these subsidiaries contributed an operating profit before amortisation of intangible assets of £6.6 million to the consolidated net profit for the period. The Group revenue and profit from operations before amortisation of intangible assets for 2008, had the acquisition taken place at the beginning of the period, are £849.2 million and £100.4 million respectively.

## Effect of acquisitions

The acquisitions had the following effect on the assets and liabilities of the Group:

| | Carrying values before acquisition 2008 £m | Fair value to the Group 2008 £m |
|---|---|---|
| Certech and Carpenter Advanced Ceramics | | |
| Intangible assets | 3.2 | 32.2 |
| Property, plant and equipment | 8.3 | 9.0 |
| Other working capital | 11.9 | 11.3 |
| Provisions | – | (1.7) |
| Deferred taxation | – | (11.3) |
| Net identifiable assets and liabilities | 23.4 | 39.5 |
| Goodwill on acquisition | | 38.6 |
| Consideration payable, excluding acquisition costs, satisfied in cash | | 74.6 |
| Acquisition costs | | 3.5 |
| Net cash outflow | | 78.1 |

Goodwill represents future economic benefits arising from assets that are not capable of being identified individually or recognised as separate assets. This will include acquirer-specific synergies such as cross-selling opportunities and the enhancement of technologies and processes between existing and acquired sites.

# Notes to the consolidated financial statements
continued

**3. Acquisitions** continued
Excluding goodwill a total of £32.2 million of intangible assets have been recognised, which comprise customer relationships. These have been recognised within operating intangibles arising on acquisition (see note 11).

During the year the Company acquired a further 6% of the Ordinary share capital and voting rights of Carbo San Luis SA for £0.7 million, resulting in a shareholding of 75.6%.

**4. Operating costs**

| | 2009 £m | 2008 £m |
|---|---|---|
| Change in stocks of finished goods and work in progress | **(0.7)** | 4.8 |
| Raw materials and consumables | **302.3** | 204.6 |
| Other external charges | **148.3** | 143.2 |
| Total | **449.9** | 352.6 |
| Employee costs: | | |
| Wages and salaries | **214.3** | 209.7 |
| Share-based payments | **2.0** | 2.5 |
| Social security costs | **45.1** | 41.1 |
| Other pension costs | **7.1** | 8.9 |
| Total | **268.5** | 262.2 |
| Depreciation: | | |
| Owned assets | **30.5** | 27.3 |
| Assets held under finance leases | **1.2** | 0.3 |
| Total | **31.7** | 27.6 |
| Rentals under operating leases: | | |
| Hire of plant and machinery | **3.0** | 1.9 |
| Other operating leases | **8.7** | 5.0 |
| Total | **11.7** | 6.9 |
| Other operating charges and income: | | |
| Foreign exchange losses | **3.9** | 2.2 |
| Other operating charges | **97.3** | 87.0 |
| Foreign exchange gains | **(6.1)** | (8.7) |
| Other operating income | **(3.3)** | (3.6) |
| Total | **91.8** | 76.9 |
| Total operating costs before restructuring costs, other one-off items and amortisation of intangible assets | **853.6** | 726.2 |
| Restructuring costs and other one-off items: | | |
| Employment termination costs | **11.3** | 1.0 |
| Non-cash write-off of assets | **1.5** | 4.2 |
| Other site rationalisation and closure costs | **2.1** | 5.3 |
| Costs (recovered)/incurred associated with settlement of prior period anti-trust litigation | **(0.9)** | 0.9 |
| Profit on disposal of property | **(2.0)** | (0.8) |
| Total | **12.0** | 10.6 |
| Amortisation of intangible assets | **16.3** | 3.2 |
| Total operating costs | **881.9** | 740.0 |

The Group recognised £13.9 million in expense in respect of research and development (2008: £9.8 million).

## 4. Operating costs continued

A summary of the audit and non-audit fees in respect of services provided by KPMG Audit plc charged to operating profit in the year ended 3 January 2010 is set out below:

| | 2009 £m | 2008 £m |
|---|---|---|
| Fees payable to the Company's auditor for the audit of the Company's annual accounts | **0.4** | 0.4 |
| Fees payable to the Company's auditor and its associates for other services: | | |
| The audit of the Company's subsidiaries pursuant to legislation and other services | **1.6** | 1.4 |
| Tax services | **0.1** | 0.1 |
| | **2.1** | 1.9 |

In addition, in 2008 KPMG Audit plc was paid £0.1 million in respect of the acquisition of Certech and Carpenter Advanced Ceramics.

## 5. Staff numbers

The average number of persons employed by the Group (including Directors) during the year, analysed by category, was as follows:

| | Number of employees 2009 | 2008 |
|---|---|---|
| United Kingdom | **1,484** | 1,394 |
| Rest of Europe | **1,738** | 1,868 |
| The Americas | **3,632** | 4,051 |
| Far East and Australia | **2,692** | 3,064 |
| Middle East and Africa | **242** | 244 |
| | **9,788** | 10,621 |
| Carbon | **3,548** | 3,868 |
| Technical Ceramics | **2,698** | 2,843 |
| Thermal Ceramics | **3,032** | 3,354 |
| Molten Metal Systems | **502** | 548 |
| Corporate | **8** | 8 |
| | **9,788** | 10,621 |

# Notes to the consolidated financial statements
continued

## 6. Net finance income and expense

| | 2009 £m | 2008 £m |
|---|---|---|
| **Recognised in profit or loss** | | |
| Interest income on bank deposits | **2.3** | 3.0 |
| Interest income from associate | **–** | 4.1 |
| Expected return on IAS 19 scheme assets | **22.1** | 25.7 |
| Foreign exchange gains recognised on net investment hedge | **–** | 1.5 |
| Finance income | **24.4** | 34.3 |
| Interest expense on financial liabilities measured at amortised cost | **(25.1)** | (21.4) |
| Interest on IAS 19 obligations | **(26.4)** | (25.6) |
| Interest expense on unwinding of discount on deferred consideration | **(2.2)** | – |
| Finance expense | **(53.7)** | (47.0) |
| Net financing costs recognised in profit or loss | **(29.3)** | (12.7) |

The above finance income and expense include the following in respect of assets/(liabilities) not at fair value through profit or loss:

| | 2009 £m | 2008 £m |
|---|---|---|
| Total interest income on financial assets | **2.3** | 7.1 |
| Total interest expense on financial liabilities | **(25.1)** | (21.4) |

| | 2009 £m | 2008 £m |
|---|---|---|
| **Recognised directly in equity** | | |
| Net change in fair value of available-for-sale financial assets | **1.0** | (3.8) |
| Cash flow hedges: | | |
| Effective portion of changes in fair value of cash flow hedges | **0.2** | (4.6) |
| Transferred to profit or loss | **4.6** | 1.2 |
| Effective portion of change in fair value of net investment hedge | **9.1** | (42.8) |
| Foreign currency translation differences for foreign operations | **(8.9)** | 61.6 |
| | **6.0** | 11.6 |
| Recognised in: | | |
| Fair value reserve | **1.0** | (3.8) |
| Translation reserve | **0.2** | 18.8 |
| Hedging reserve | **4.8** | (3.4) |
| | **6.0** | 11.6 |

## 7. Taxation - income tax expense

### Recognised in the income statement

| | 2009 £m | 2008 £m |
|---|---|---|
| **Current tax expense** | | |
| Current year | **17.3** | 15.7 |
| Adjustments for prior years | **(0.8)** | (1.7) |
| | **16.5** | 14.0 |
| **Deferred tax expense** | | |
| Origination and reversal of temporary differences | **(7.8)** | 4.8 |
| Benefit of losses recognised | **–** | 1.3 |
| | **(7.8)** | 6.1 |
| Total income tax expense in income statement | **8.7** | 20.1 |

### Reconciliation of effective tax rate

| | 2009 £m | 2009 % | 2008 £m | 2008 % |
|---|---|---|---|---|
| Profit before tax | **31.4** | | 82.8 | |
| Income tax using the domestic corporation tax rate | **8.8** | **28.0** | 23.2 | 28.0 |
| Non-deductible expenses | **6.4** | **20.4** | 0.8 | 1.0 |
| Temporary differences not equalised in deferred tax | **(4.3)** | **(13.7)** | (10.6) | (12.8) |
| (Over)/under-provided in prior years | **(0.2)** | **(0.6)** | 2.3 | 2.8 |
| Other (including the impact of overseas tax rates) | **(2.0)** | **(6.4)** | 4.4 | 5.3 |
| | **8.7** | **27.7** | 20.1 | 24.3 |

| | 2009 £m | 2008 £m |
|---|---|---|
| **Income tax recognised directly in equity** | | |
| Actuarial gains and losses | **–** | 5.4 |
| Tax effect on components of other comprehensive income | **5.5** | – |
| Other | **(0.2)** | – |
| Total income tax recognised directly in equity | **5.3** | 5.4 |

## 8. Restructuring costs and costs associated with settlement of prior period anti-trust litigation

Costs of restructuring were £14.9 million (2008: £10.5 million). During the period net legal costs of £0.9 million were recovered relating to the settlement of anti-trust litigation (2008: £0.9 million net legal costs charge).

## 9. Earnings per share

### Basic earnings per share

The calculation of basic earnings per share at 3 January 2010 was based on the profit attributable to equity holders of The Morgan Crucible Company plc of £19.0 million (4 January 2009: £59.2 million) and a weighted average number of Ordinary shares outstanding during the period ended 3 January 2010 of 268,070,252 (4 January 2009: 266,882,370) calculated as follows:

| | 2009 £m | 2008 £m |
|---|---|---|
| **Profit attributable to equity holders of The Morgan Crucible Company plc** | **19.0** | 59.2 |
| **Weighted average number of Ordinary shares** | | |
| Issued Ordinary shares at the beginning of the period | **270,206,256** | 276,414,074 |
| Effect of shares issued in period and treasury shares held by the Company | **(2,136,004)** | (9,531,704) |
| Weighted average number of Ordinary shares during the period | **268,070,252** | 266,882,370 |
| Basic earnings per share (pence) | **7.1p** | 22.2p |

# Notes to the consolidated financial statements
continued

### 9. Earnings per share continued

#### Diluted earnings per share

The calculation of diluted earnings per share at 3 January 2010 was based on the profit attributable to equity holders of The Morgan Crucible Company plc of £19.0 million (4 January 2009: £59.2 million) and a weighted average number of Ordinary shares outstanding during the period ended 3 January 2010 of 279,724,482 (4 January 2009: 274,229,467), calculated as follows:

| | **2009 £m** | 2008 £m |
|---|---|---|
| **Profit attributable to equity holders of The Morgan Crucible Company plc** | **19.0** | 59.2 |
| **Weighted average number of Ordinary shares:** | | |
| Weighted average number of Ordinary shares during the period | **268,070,252** | 266,882,370 |
| Effect of share options/incentive schemes | **11,654,230** | 7,347,097 |
| Diluted weighted average number of Ordinary shares | **279,724,482** | 274,229,467 |
| Diluted earnings per share (pence) | **6.8p** | 21.6p |

#### Underlying earnings per share

The calculation of underlying earnings per share at 3 January 2010 was based on operating profit and share of profit of associate before amortisation, less net financing costs, loss on disposal of business, income tax expense and non-controlling interests of £35.3 million (4 January 2009: £62.4 million) and a weighted average number of Ordinary shares outstanding during the period ended 3 January 2010 of 268,070,252 (4 January 2009: 266,882,370) calculated as follows:

| | **2009 £m** | 2008 £m |
|---|---|---|
| **Operating profit and share of profit of associate before amortisation, less net financing costs, loss on disposal of business, income tax expense and non-controlling interests** | **35.3** | 62.4 |
| Issued Ordinary shares at the beginning of the period | **270,206,256** | 276,414,074 |
| Effect of shares issued in period and treasury shares held by the Company | **(2,136,004)** | (9,531,704) |
| Weighted average number of Ordinary shares during the period | **268,070,252** | 266,882,370 |
| Earnings per share before amortisation of intangible assets (pence) | **13.2p** | 23.4p |

#### Diluted underlying earnings per share

The calculation of diluted underlying earnings per share at 3 January 2010 was based on operating profit and share of profit of associate before amortisation, less net financing costs, loss on disposal of business, income tax expense and non-controlling interests of £35.3 million (4 January 2009: £62.4 million) and a weighted average number of Ordinary shares outstanding during the period ended 3 January 2010 of 279,724,482 (4 January 2009: 274,229,467), calculated as follows:

| | **2009 £m** | 2008 £m |
|---|---|---|
| **Operating profit and share of profit of associate before amortisation, less net financing costs, loss on disposal of business, income tax expense and non-controlling interests** | **35.3** | 62.4 |
| Weighted average number of Ordinary shares during the period | **268,070,252** | 266,882,370 |
| Effect of share options/incentive schemes | **11,654,230** | 7,347,097 |
| Diluted weighted average number of Ordinary shares during the period | **279,724,482** | 274,229,467 |
| Diluted earnings per share before amortisation of intangible assets (pence) | **12.6p** | 22.8p |

## 10. Property, plant and equipment

| | Land and buildings £m | Plant and equipment and fixtures £m | Total £m |
|---|---|---|---|
| **Cost** | | | |
| Balance at 5 January 2008 | 135.9 | 407.5 | 543.4 |
| Acquisitions through business combinations | 2.0 | 9.0 | 11.0 |
| Additions | 6.5 | 30.9 | 37.4 |
| Disposals | (1.5) | (18.2) | (19.7) |
| Effect of movement in foreign exchange | 38.5 | 100.1 | 138.6 |
| Balance at 4 January 2009 | 181.4 | 529.3 | 710.7 |
| Balance at 5 January 2009 | **181.4** | **529.3** | **710.7** |
| Acquisitions through business combinations | **1.5** | **1.4** | **2.9** |
| Additions | **1.4** | **12.6** | **14.0** |
| Disposals | **(4.3)** | **(11.0)** | **(15.3)** |
| Transfer to assets classified as held for sale | **(4.1)** | **(0.6)** | **(4.7)** |
| Effect of movement in foreign exchange | **(13.2)** | **(36.1)** | **(49.3)** |
| **Balance at 3 January 2010** | **162.7** | **495.6** | **658.3** |
| **Depreciation and impairment losses** | | | |
| Balance at 5 January 2008 | 38.4 | 258.4 | 296.8 |
| Depreciation charge for the year | 3.9 | 23.7 | 27.6 |
| Impairment loss | 1.6 | 2.2 | 3.8 |
| Disposals | (0.7) | (15.0) | (15.7) |
| Effect of movement in foreign exchange | 13.2 | 65.4 | 78.6 |
| Balance at 4 January 2009 | 56.4 | 334.7 | 391.1 |
| Balance at 5 January 2009 | **56.4** | **334.7** | **391.1** |
| Depreciation charge for the year | **4.5** | **27.2** | **31.7** |
| Impairment loss | **0.3** | **–** | **0.3** |
| Disposals | **(1.0)** | **(9.0)** | **(10.0)** |
| Transfer to assets classified as held for sale | **(2.8)** | **(0.5)** | **(3.3)** |
| Effect of movement in foreign exchange | **(4.4)** | **(23.3)** | **(27.7)** |
| **Balance at 3 January 2010** | **53.0** | **329.1** | **382.1** |
| **Carrying amounts** | | | |
| At 5 January 2008 | 97.5 | 149.1 | 246.6 |
| At 4 January 2009 | 125.0 | 194.6 | 319.6 |
| **At 3 January 2010** | **109.7** | **166.5** | **276.2** |

### Assets pledged as security for liabilities

At 3 January 2010 assets with a carrying amount of £4.3 million (2008: £4.2 million) are subject to registered debentures to secure bank loans and other liabilities (see note 18).

### Assets classified as held for sale

| | **2009 £m** | 2008 £m |
|---|---|---|
| Land and buildings | **1.3** | – |
| Plant and equipment | **0.1** | – |
| | **1.4** | – |

# Notes to the consolidated financial statements
continued

### 11. Intangible assets

| | Goodwill £m | Operating intangibles arising on acquisition £m | Capitalised development costs £m | Computer software £m | Total £m |
|---|---|---|---|---|---|
| **Cost** | | | | | |
| Balance at 5 January 2008 | 57.1 | 10.8 | – | 9.5 | 77.4 |
| Acquisitions through business combinations | 38.6 | 32.2 | – | – | 70.8 |
| Additions - externally purchased | – | – | 1.6 | 0.9 | 2.5 |
| Disposals | (1.2) | – | – | (0.1) | (1.3) |
| Effect of movement in foreign exchange | 23.9 | 14.9 | – | 2.1 | 40.9 |
| Balance at 4 January 2009 | 118.4 | 57.9 | 1.6 | 12.4 | 190.3 |
| Balance at 5 January 2009 | **118.4** | **57.9** | **1.6** | **12.4** | **190.3** |
| Acquisitions through business combinations | **96.8** | **51.5** | **–** | **–** | **148.3** |
| Additions - externally purchased | **–** | **–** | **0.7** | **0.9** | **1.6** |
| Disposals | **(0.2)** | **–** | **–** | **(0.7)** | **(0.9)** |
| Effect of movement in foreign exchange | **(8.2)** | **(5.6)** | **(0.1)** | **(0.9)** | **(14.8)** |
| **Balance at 3 January 2010** | **206.8** | **103.8** | **2.2** | **11.7** | **324.5** |
| **Amortisation and impairment losses** | | | | | |
| Balance at 5 January 2008 | – | 1.3 | – | 6.3 | 7.6 |
| Amortisation charge for the year | – | 2.2 | 0.1 | 0.9 | 3.2 |
| Disposals | – | – | – | (0.1) | (0.1) |
| Effect of movement in foreign exchange | – | 1.0 | – | 1.6 | 2.6 |
| Balance at 4 January 2009 | – | 4.5 | 0.1 | 8.7 | 13.3 |
| Balance at 5 January 2009 | **–** | **4.5** | **0.1** | **8.7** | **13.3** |
| Amortisation charge for the year | **–** | **14.8** | **0.3** | **1.2** | **16.3** |
| Disposals | **–** | **–** | **–** | **(0.7)** | **(0.7)** |
| Effects of movement in foreign exchange | **–** | **(0.4)** | **–** | **(0.9)** | **(1.3)** |
| **Balance at 3 January 2010** | **–** | **18.9** | **0.4** | **8.3** | **27.6** |
| **Carrying amounts** | | | | | |
| At 5 January 2008 | 57.1 | 9.5 | – | 3.2 | 69.8 |
| At 4 January 2009 | 118.4 | 53.4 | 1.5 | 3.7 | 177.0 |
| **At 3 January 2010** | **206.8** | **84.9** | **1.8** | **3.4** | **296.9** |

Operating intangibles arising on acquisition include an order book, customer relationships and technology. On 5 January 2009 the Group recognised a £9.3 million order book on acquisition of Clearpower Limited. This has been amortised over a period of 12 months, being the period over which the associated orders are fulfilled. For further details of acquired operating intangible assets see note 3. No order book was recognised in 2008.

## 11. Intangible assets continued

### Impairment test for cash-generating units containing goodwill

In accordance with the requirements of IAS 36 *Impairment of Assets*, goodwill is allocated to the Group's cash-generating units that are expected to benefit from the synergies of the business combination that gave rise to the goodwill. The most significant elements of the Group's total consolidated goodwill of £206.8 million at 3 January 2010 are allocated to the Carbon cash-generating unit.

Goodwill is attributed to each cash-generating unit as follows:

| | **2009 £m** | 2008 £m |
|---|---|---|
| Carbon | **117.0** | 21.5 |
| Technical Ceramics | **67.2** | 72.1 |
| Thermal Ceramics | **20.5** | 22.5 |
| Molten Metal Systems | **2.1** | 2.3 |
| | **206.8** | 118.4 |

Each cash-generating unit is assessed for impairment annually and whenever there is an indication of impairment.

As part of the annual impairment test review the carrying value of goodwill has been assessed with reference to its value in use reflecting the projected cash flows of each cash-generating unit.

The key assumptions on which the cash flow projections are based relate to growth rates and discount rates.

The cash flow projections in year one are based on budgeted operating results for the forthcoming year. The budget for 2010 was approved in December 2009.

Growth rates for the period not covered by budgets are specific to each operating Division, ranging from 4.4% to 6.9% (2008: 4.4% to 6.9%). These growth rates reflect the products, industries and countries in which the Divisions operate. These medium- to long-term growth rates have been reviewed by management during 2009 and are considered to remain appropriate.

Given the similar risk profiles of each of the operating Divisions, together with common funding from the central Group Treasury function, a standard pre-tax discount rate of 12.9% (2008: 13%), based on the Group's weighted average cost of capital, has been used in discounting the projected cash flows and calculating the terminal value at the end of year five. This discount rate has been used as the Group believes it suitably approximates the rate used by end-market participants.

The Directors have considered the following individual sensitivities and are confident that no impairment would arise in any of the following three circumstances:

- if the pre-tax discount rate was increased by 300bps to 15.9%;
- if no growth was assumed for years two to five; and
- if the cash flow projections of all businesses were reduced by 25%.

# Notes to the consolidated financial statements
continued

## 12. Other investments

| | 2009 £m | 2008 £m |
|---|---|---|
| Non-current investments | | |
| Investment in associate | **1.5** | 6.4 |
| Equity securities available-for-sale | **5.7** | 5.2 |
| | **7.2** | 11.6 |

### Investment in associates

Integrated Survivability Technologies Limited

During the year the Group acquired a 50% stake in Integrated Survivability Technologies Limited. The principal activity of Integrated Survivability Technologies Limited is acting as prime contractor for delivery of military vehicles and provision of related support services. Total consideration paid including fees was £1.5 million.

The Group's share of profit after tax in Integrated Survivability Technologies Limited was £nil.

Summary 2009 financial information for the Group's investment in Integrated Survivability Technologies Limited, not adjusted for the 50% ownership held by the Group:

| | 2009 £m |
|---|---|
| Current assets | **15.3** |
| Non-current assets | **0.1** |
| Total assets | **15.4** |
| Current liabilities | **12.4** |
| Non-current liabilities | **–** |
| Total liabilities | **12.4** |
| Revenues | **44.0** |
| Profit | **–** |

Clearpower Limited

As described in note 3, during 2009 the Group acquired the remaining 51% of the Ordinary share capital of Clearpower Limited. As a result its results are fully consolidated in the results for the year ended 3 January 2010. In 2008 the Group had accounted for its investment in Clearpower Limited as an associate. In 2008, the Group's share of profit after tax in its associate for the year was £1.2 million.

Equity securities available-for-sale

The equity securities available-for-sale represent an investment in a mutual fund. A 10% increase in the unit price would increase the fair value of the investments by £0.4 million.

## 13. Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

| | Assets 2009 £m | Assets 2008 £m | Liabilities 2009 £m | Liabilities 2008 £m | Net 2009 £m | Net 2008 £m |
|---|---|---|---|---|---|---|
| Property, plant and equipment | **–** | – | **23.3** | 23.5 | **23.3** | 23.5 |
| Intangible assets | **–** | (0.7) | **24.2** | 16.8 | **24.2** | 16.1 |
| Employee benefits | **(19.8)** | (24.1) | **–** | – | **(19.8)** | (24.1) |
| Provisions | **(5.4)** | (6.6) | **–** | – | **(5.4)** | (6.6) |
| Tax value of loss carried forward recognised | **(7.5)** | (3.2) | **–** | – | **(7.5)** | (3.2) |
| Other items | **(4.5)** | (2.0) | **–** | 0.5 | **(4.5)** | (1.5) |
| | **(37.2)** | (36.6) | **47.5** | 40.8 | **10.3** | 4.2 |

## 13. Recognised deferred tax assets and liabilities continued

### Unrecognised deferred tax assets

Deferred tax assets have not been recognised in respect of the following items:

| | 2009 £m | 2008 £m |
|---|---|---|
| Deductible temporary differences | **(38.9)** | (40.0) |
| Tax losses | **(43.9)** | (33.6) |
| | **(82.8)** | (73.6) |

### Movements in temporary differences during the year

| | Balance 4 January 2008 £m | Recognised in income £m | Acquired in business combinations £m | Recognised directly in equity £m | Balance 4 January 2009 £m | **Recognised in income £m** | **Acquired in business combinations £m** | **Recognised directly in equity £m** | **Balance 3 January 2010 £m** |
|---|---|---|---|---|---|---|---|---|---|
| Property, plant and equipment | 18.4 | 5.1 | – | – | 23.5 | **(0.2)** | **–** | **–** | **23.3** |
| Intangible assets | 0.5 | 5.9 | 9.7 | – | 16.1 | **(6.0)** | **14.1** | **–** | **24.2** |
| Employee benefits | (12.6) | (6.1) | – | (5.4) | (24.1) | **4.3** | **–** | **–** | **(19.8)** |
| Provisions | (6.0) | (0.6) | – | – | (6.6) | **1.2** | **–** | **–** | **(5.4)** |
| Tax value of loss carried forward recognised | (6.3) | 3.1 | – | – | (3.2) | **(4.3)** | **–** | **–** | **(7.5)** |
| Others | (0.6) | (0.9) | – | – | (1.5) | **(2.8)** | **–** | **(0.2)** | **(4.5)** |
| | (6.6) | 6.5 | 9.7 | (5.4) | 4.2 | **(7.8)** | **14.1** | **(0.2)** | **10.3** |

No deferred income tax is provided on the unremitted earnings of overseas subsidiary undertakings as the Group is able to control the remittance of such earnings and currently has no intention of making any such remittance, where such remittance would incur additional tax liabilities.

## 14. Inventories

| | 2009 £m | 2008 £m |
|---|---|---|
| Raw materials and consumables | **56.9** | 43.9 |
| Work in progress | **32.4** | 36.0 |
| Finished goods | **57.0** | 64.0 |
| | **146.3** | 143.9 |

| | | |
|---|---|---|
| Inventories stated at fair value less costs to sell | **2.5** | 1.9 |
| Carrying amount of inventories subject to retention of title clauses | **2.0** | 2.3 |

The Group holds consignment inventory amounting to £24.5 million (2008: £13.0 million) which is not reflected in the balance sheet. The majority of this balance is for precious metals which are held on consignment by a subsidiary and for which it is invoiced only when the material is required.

During the year provisions of £4.4 million were made against inventories and recognised in operating expenses (2008: £4.6 million). The Group did not reverse any provisions against inventory during 2009 and 2008.

# Notes to the consolidated financial statements
continued

## 15. Trade and other receivables

| | 2009 £m | 2008 £m |
|---|---|---|
| **Non-current** | | |
| Loan to associate | – | 36.0 |
| Non-trade receivables and prepayments | 2.1 | 3.0 |
| | 2.1 | 39.0 |
| **Current** | | |
| Trade receivables due from associate | 7.3 | 0.3 |
| Other trade receivables | 137.2 | 164.2 |
| Loans and receivables | 144.5 | 164.5 |
| Non-trade receivables due from associate | – | 5.7 |
| Other non-trade receivables and prepayments | 21.3 | 26.1 |
| | 165.8 | 196.3 |

The Group's exposure to credit and currency risks related to trade and other receivables is disclosed in note 19.

## 16. Cash and cash equivalents/bank overdrafts

| | 2009 £m | 2008 £m |
|---|---|---|
| Bank balances | 92.9 | 100.4 |
| Cash deposits | 14.7 | 54.1 |
| Cash and cash equivalents per consolidated balance sheet | 107.6 | 154.5 |
| Bank balances subject to cash pooling arrangements | – | (15.1) |
| Cash and cash equivalents per consolidated statement of cash flows | 107.6 | 139.4 |
| Bank overdrafts subject to cash pooling arrangements | – | (15.1) |
| Other bank overdrafts | (1.2) | (2.2) |
| Total bank overdrafts | (1.2) | (17.3) |

For 2008, in accordance with IAS 32 *Financial Instruments: Presentation*, bank overdrafts subject to cash pooling arrangements were not offset against cash and cash equivalents as the Group did not intend to settle on a net basis. During 2009, this position was reviewed and the Group would now intend to settle the pooled balances on a net basis.

### Reconciliation of cash and cash equivalents to net debt*

| | 2009 £m | 2008 £m |
|---|---|---|
| Opening net borrowings | (429.8) | (209.8) |
| Net new borrowings | 35.5 | (127.2) |
| Payment of finance lease liabilities | 0.6 | 0.3 |
| Effect of movements in foreign exchange on borrowings | 33.4 | (93.1) |
| Closing borrowings | (360.3) | (429.8) |
| Cash and cash equivalents per consolidated statement of cash flows | 107.6 | 139.4 |
| Closing net debt | (252.7) | (290.4) |

* Net debt is defined as interest-bearing loans and borrowings, bank overdrafts less cash and cash equivalents.

## 17. Capital and reserves

### Translation reserve

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations, as well as from the translation of liabilities that hedge the Company's net investment in a foreign subsidiary and forward contracts used for net investment hedging.

### Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

### Fair value reserve

The fair value reserve includes the cumulative net change in the fair value of available-for-sale investments until the investment is derecognised.

### Special reserve

A Special Resolution to cancel the Share Premium Account was passed at the Annual General Meeting of the Company held on 11 June 1993. This cancellation was confirmed by an Order of the High Court of Justice, Chancery Division, on 14 July 1993. The amount of £88.9 million standing to the credit of the Share Premium Account on 14 July 1993 was transferred to the special reserve against which goodwill on consolidation can be written off. This reserve, together with the amounts standing to the credit of the Share Premium Account on 12 October 1990 of £71.5 million, on 19 June 1987 of £38.9 million and on 27 July 1989 of £12.3 million which were transferred following previous Orders of the High Court, becomes distributable to the extent of subsequent increases in issued share capital and share premium account.

### Capital redemption reserve

The capital redemption reserve arose when the Company redeemed Preference shares wholly out of distributable profits. The movement in 2008 relates to the cancellation of Ordinary shares as a result of the share buy-back programme.

### Other reserves

The other reserves includes the £10.8 million increase in the fair value of the Group's original 49% interest in Clearpower Limited from the date of its original acquisition to 5 January 2009 excluding goodwill and to the extent not previously recognised as the Group's share of the results of Clearpower Limited. See note 3 for further details.

### Retained earnings

The Company has acquired own shares under a share buy-back programme. The Company has also acquired own shares to satisfy the requirements of the various share option incentive schemes. The number of treasury shares held by the Company at the year end was 1,984,022 (2008: 2,593,799); 1,984,022 shares were held by The Morgan General Employee Benefit Trust (2008: 2,593,799) and nil shares were held by the Company (2008: nil). All rights conferred by those shares are suspended until they are reissued.

### Dividends

The following Ordinary dividends were declared and paid by the Company:

| | Per share **2009** **Pence** | Per share 2008 Pence | **2009** **£m** | Total 2008 £m |
|---|---|---|---|---|
| 2007 final | – | 4.50 | – | 12.1 |
| 2008 interim | – | 2.50 | – | 6.7 |
| 2008 final | **4.50** | – | **12.1** | – |
| Total | **4.50** | 7.00 | **12.1** | 18.8 |

The Company also declared the following Ordinary dividend:

| | **Per share 2009 Pence** | **Total 2009 £m** |
|---|---|---|
| 2009 interim | **2.50** | **6.8** |
| | **2.50** | **6.8** |

# Notes to the consolidated financial statements
continued

**17. Capital and reserves** continued
This Ordinary dividend had not been paid by the Company as at 3 January 2010 and has not been provided for at the year end.

In addition to the above, the Company also declared and paid dividends on the 5.5% Cumulative First Preference shares and 5.0% Cumulative Second Preference shares.

After 3 January 2010 the following dividends were proposed by the Directors for 2009. These dividends have not been provided for and there are no income tax consequences.

| | £m |
|---|---|
| 4.5 pence per qualifying Ordinary share | 12.2 |
| 5.5% Cumulative First Preference shares (see note 30) | – |
| 5.0% Cumulative Second Preference shares (see note 30) | – |
| | 12.2 |

| Called up share capital | Authorised<br>**2009**<br>**£m** | Authorised<br>2008<br>£m | Issued<br>**2009**<br>**£m** | Issued<br>2008<br>£m |
|---|---|---|---|---|
| **Equity share capital** | | | | |
| 434,650,876 (2008: 434,650,876) Ordinary shares of 25 pence each | **108.7** | 108.7 | | |
| Fully paid: 270,206,256 (2008: 270,206,256) Ordinary shares of 25 pence each | | | **67.5** | 67.5 |
| | **108.7** | 108.7 | **67.5** | 67.5 |
| **Preference share capital** | | | | |
| 125,327 authorised and issued 5.5% Cumulative First Preference shares of £1 each, fully paid | **0.1** | 0.1 | **0.1** | 0.1 |
| 311,954 authorised and issued 5.0% Cumulative Second Preference shares of £1 each, fully paid | **0.3** | 0.3 | **0.3** | 0.3 |
| Total Preference share capital | **0.4** | 0.4 | **0.4** | 0.4 |
| **Total share capital** | **109.1** | 109.1 | **67.9** | 67.9 |

| Number of shares in issue | Ordinary shares<br>**2009** | Ordinary shares<br>2008 | Preference shares<br>**2009** | Preference shares<br>2008 |
|---|---|---|---|---|
| In issue at beginning of period | **270,206,256** | 276,414,074 | **437,281** | 437,281 |
| Exercise of options under the various Morgan Crucible share option schemes | **–** | 42,182 | **–** | – |
| Cancelled as a result of share buy-back programme | **–** | (6,250,000) | **–** | – |
| In issue at end of period | **270,206,256** | 270,206,256 | **437,281** | 437,281 |

As at the date of this report 270,206,256 Ordinary shares have been issued (2008: 270,206,256).

The holders of Ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

**17. Capital and reserves** continued

The following options were outstanding in respect of Ordinary shares:

| Number of shares | | Exercise price(s) | Normal exercise dates ranging from | to |
|---|---|---|---|---|
| 340,734 | The Morgan Executive Share Option Scheme 1995 | 180.08p-208.12p | 19 June 2003 | 22 November 2011 |
| 2,664,743 | The Morgan Crucible Sharesave Scheme 2004 | 128.00p-249.00p | 1 March 2010 | 31 May 2013 |
| 248,274 | The Morgan Crucible Savings Related Share Options Scheme for Employees in Germany | €1.64 | 1 December 2011 | 31 May 2012 |
| 1,625,391 | The Morgan Crucible Executive Share Option Scheme 2004 | 129.05p-256.00p | 22 June 2007 | 20 December 2016 |
| 6,148,623 | The Morgan Crucible Bonus Deferral Share Matching Plan | 0.00p-197.62p | 10 March 2011 | 6 March 2012 |
| 9,091,427 | The Morgan Crucible Long Term Incentive Plan 2004 | 0.00p | 13 June 2010 | 2 July 2012 |

The 5.5% Cumulative First Preference shares of £1 each and the 5.0% Cumulative Second Preference shares of £1 each confer on the holders thereof the right to receive a cumulative preferential dividend at the rate of 5.5% and 5.0% respectively, calculated up to 30 June and 31 December respectively in every year.

The First and Second Cumulative Preference shares shall not entitle the holders thereof to attend or vote at any general meeting unless either:

(i) the meeting is convened to consider any resolutions for reducing the capital, or authorising any issue of debentures or debenture stock, or increasing the borrowing powers of the Board under the Articles of Association of the Company, or winding up, or sanctioning a sale of the undertaking, or altering the Articles in any manner affecting their respective interests, or any other resolutions directly altering their respective rights and privileges; or

(ii) at the date of the notice convening the general meeting the Preference dividend is upwards of one month in arrears from the payment date of any half-yearly instalment.

On a return of capital on a winding-up the assets of the Company available for distribution shall be applied:

First, in payment to the holders of the First Preference shares of the amounts paid up on such shares, together with interest at the rate of 5.5%pa.

Second, in payment to the holders of the Second Preference shares of the amounts paid up on such shares, together with interest at the rate of 5.0%pa.

Third, in repaying the capital paid up or credited as paid up on the Ordinary shares.

Fourth, any surplus shall be distributed rateably amongst the holders of the Ordinary shares in proportion to the nominal amount paid up on their respective holdings of shares in the Company.

**18. Interest-bearing loans and borrowings**

This note provides information about the contractual terms of the Group's interest-bearing loans and borrowings which are measured at amortised cost. For more information about the Group's exposure to interest rate and foreign currency risk, see note 19.

| | **2009 £m** | 2008 £m |
|---|---|---|
| **Non-current liabilities** | | |
| US Dollar Senior Notes | **233.7** | 273.2 |
| Multicurrency revolving facility | **105.4** | 136.1 |
| Bank and other loans | **6.6** | 0.1 |
| Obligations under finance leases | **0.9** | 1.5 |
| | **346.6** | 410.9 |
| **Current liabilities** | | |
| US Dollar Senior Notes | **10.9** | 12.0 |
| Bank and other loans | **0.9** | 3.9 |
| Obligations under finance leases | **0.7** | 0.8 |
| | **12.5** | 16.7 |

# Notes to the consolidated financial statements
continued

### 18. Interest-bearing loans and borrowings continued

**Terms and debt repayment schedule**

The terms and conditions of outstanding loans were as follows:

| | Currency | Nominal interest rate | Year of maturity | Carrying amount 2009 £m | Carrying amount 2008 £m |
|---|---|---|---|---|---|
| 6.84% US Dollar Senior Notes 2013 | US$ | 6.84% | 2013 | **23.1** | 31.6 |
| 6.23% US Dollar Senior Notes 2010 | US$ | 6.23% | 2010 | **5.1** | 11.4 |
| 5.70% US Dollar Senior Notes 2014 | US$ | 5.70% | 2014 | **61.8** | 69.2 |
| 6.12% US Dollar Senior Notes 2017 | US$ | 6.12% | 2017 | **108.2** | 121.1 |
| 6.26% US Dollar Senior Notes 2019 | US$ | 6.26% | 2019 | **46.4** | 51.9 |
| Multicurrency revolving facility | EUR | 3.46% | 2012 | **38.6** | 96.1 |
| Multicurrency revolving facility | GBP | 3.81% | 2012 | **66.8** | 40.0 |
| Bank and other loans | Various | 4.00%-8.00% | up to 2013 | **7.5** | 4.0 |
| Obligations under finance leases | Various | 6.00% | up to 2014 | **1.6** | 2.3 |
| Total interest-bearing loans and borrowings | | | | **359.1** | 427.6 |

**Finance lease liabilities**

Finance lease liabilities are payable as follows:

| | **Minimum lease payments 2009 £m** | **Interest 2009 £m** | **Principal 2009 £m** | Minimum lease payments 2008 £m | Interest 2008 £m | Principal 2008 £m |
|---|---|---|---|---|---|---|
| Less than one year | **0.8** | **0.1** | **0.7** | 0.9 | 0.1 | 0.8 |
| Between one and five years | **0.9** | **–** | **0.9** | 1.4 | 0.1 | 1.3 |
| More than five years | **–** | **–** | **–** | 0.2 | – | 0.2 |
| | **1.7** | **0.1** | **1.6** | 2.5 | 0.2 | 2.3 |

Bank and other loans include £0.2 million (2008: £0.9 million) of loans secured on the assets of the Group.

As at 3 January 2010 the Group had available headroom under the bank syndication of £171.4 million (2008: £154.5 million).

### 19. Financial risk management

**Overview**

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk.

This note presents information about the Group's exposure to each of the above risks, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

The Board delegates the establishment and implementation of the systems for internal control and risk management to the operating Divisions which are responsible for the identification and evaluation of significant risks applicable to their area of business together with the design and operation of suitable internal controls. The Board delegates the monitoring and review of the internal control and risk management systems to the Audit Committee assisted by the Risk Management Committee. The Risk Management Committee, which is chaired by the Chief Financial Officer, reviews the full range of risks faced by Morgan Crucible as a Group, ensures there are adequate systems in place and evaluates their effectiveness. Where necessary, the Risk Management Committee will initiate action to improve the systems and ensure compliance.

## 19. Financial risk management continued

### Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and investment securities.

The Group has set up notional cash pooling agreements with a number of banks. Under the notional cash pooling agreement the Group has the legal right to offset liabilities on undrawn bank accounts against surplus balances.

### Trade and other receivables

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. The demographics of the Group's customer base, including the default risk of the industry and country in which customers operate, has less of an influence on credit risk.

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. The Group does not require collateral in respect of financial assets.

The Group serves thousands of customers. Many of these have purchased the same product for several years and in some cases decades. Others have modified and enhanced designs or adopted the same components into new products, extending the lifecycle of the components that the Group supplies. The Group's level of customer retention is very high, particularly with its major accounts, and, although the top 20 ranking will alter from year to year, many of the names remain consistent over time.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables and investments. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a general loss component established for groups of similar assets in respect of losses that have been incurred but not yet identified. The general loss allowance is determined based on historical data of payment statistics for similar financial assets.

### Investments

The Group limits its exposure to credit risk by only investing in liquid securities and only with counterparties that have a sound credit rating. Given these high credit ratings, management does not expect any counterparty to fail to meet its obligations.

### Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

| | Carrying amount | |
|---|---|---|
| | **2009 £m** | 2008 £m |
| Available-for-sale financial assets | **5.7** | 5.2 |
| Loan to associate | **–** | 36.0 |
| Loans and receivables | **144.5** | 164.5 |
| Cash and cash equivalents | **107.6** | 154.5 |
| | **257.8** | 360.2 |

The maximum exposure to credit risk for trade receivables at the reporting date by Division was:

| | Carrying amount | |
|---|---|---|
| | **2009 £m** | 2008 £m |
| Carbon | **53.1** | 44.0 |
| Technical Ceramics | **25.9** | 33.5 |
| Thermal Ceramics | **60.5** | 81.3 |
| Molten Metal Systems | **5.0** | 5.7 |
| | **144.5** | 164.5 |

# Notes to the consolidated financial statements
continued

**19. Financial risk management** continued

The maximum exposure to credit risk for trade receivables at the reporting date by geographic region was:

| | Carrying amount 2009 £m | 2008 £m |
|---|---|---|
| Europe | **67.5** | 68.3 |
| Americas | **44.3** | 60.5 |
| Far East and Australasia | **28.7** | 34.3 |
| Middle East and Africa | **4.0** | 1.4 |
| | **144.5** | 164.5 |

## Impairment losses

The ageing of trade receivables at the reporting date was:

| | 2009 £m | 2008 £m |
|---|---|---|
| Not past due | **111.6** | 127.2 |
| Past due 0-30 days | **21.4** | 28.7 |
| Past due 31-60 days | **5.6** | 7.0 |
| Past due 61-90 days | **8.3** | 3.0 |
| Past due more than 90 days | **7.8** | 9.1 |
| | **154.7** | 175.0 |
| Impairment allowance | **(10.2)** | (10.5) |
| | **144.5** | 164.5 |

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

| | 2009 £m | 2008 £m |
|---|---|---|
| Balance at beginning of period | **10.5** | 4.4 |
| (Decrease)/increase in allowance for impairment | **(0.3)** | 6.1 |
| Balance at end of period | **10.2** | 10.5 |

Based on past experience, the Group believes that no impairment allowance is necessary in respect of trade receivables not past due. A specific impairment allowance may be created in respect of an individual trade receivable for which full recovery is doubtful. As at 3 January 2010 and 4 January 2009 there were no specific impairment allowances that were significant to the Group. In addition, local management may create a general impairment allowance to reflect their experience of the historical recoverability of trade receivables past due in the respective markets in which their businesses operate.

The allowances in the accounts in respect of trade receivables are used to record impairment losses unless the Group is satisfied that no recovery of the amount owing is possible; at the point the amount is considered irrecoverable it is written off against the financial asset directly.

## 19. Financial risk management continued

### Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by cash. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions.

The Group seeks a balance between certainty of funding and a flexible, cost-effective borrowing structure. The policy is to ensure that the Group has sufficient liquidity available to meet all foreseeable needs.

The following are the undiscounted contracted maturities of financial liabilities, including interest payments:

| | Effective interest rate | Carrying amount £m | Contractual cash flows £m | Less than 1 year £m | 1-2 years £m | 2-5 years £m | 2009 More than 5 years £m |
|---|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities** | | | | | | | |
| 6.84% US Dollar Senior Notes 2013 | **6.84%** | **23.1** | **25.7** | **7.0** | **6.6** | **12.1** | **–** |
| 6.23% US Dollar Senior Notes 2010 | **6.23%** | **5.1** | **5.1** | **5.1** | **–** | **–** | **–** |
| 5.70% US Dollar Senior Notes 2014 | **5.70%** | **61.8** | **79.5** | **3.5** | **3.5** | **72.5** | **–** |
| 6.12% US Dollar Senior Notes 2017 | **6.12%** | **108.2** | **161.4** | **6.6** | **6.6** | **19.9** | **128.3** |
| 6.26% US Dollar Senior Notes 2019 | **6.26%** | **46.4** | **75.5** | **2.9** | **2.9** | **8.7** | **61.0** |
| Multicurrency revolving facility | **3.69%** | **105.4** | **110.7** | **2.1** | **–** | **108.6** | **–** |
| Bank and other loans | **4.00%-8.00%** | **7.5** | **7.5** | **3.0** | **–** | **4.5** | **–** |
| Bank overdrafts | **3.50%** | **1.2** | **1.2** | **1.2** | **–** | **–** | **–** |
| Obligations under finance leases | **6.00%** | **1.6** | **1.7** | **0.9** | **0.3** | **0.5** | **–** |
| **Derivative financial liabilities** | | | | | | | |
| Forward exchange contracts as cash flow hedges | | **0.1** | **0.1** | **0.1** | **–** | **–** | **–** |
| Forward exchange contracts as fair value hedges | | **0.4** | **0.4** | **0.4** | **–** | **–** | **–** |
| Forward exchange contracts as net investment hedges | | **8.8** | **8.8** | **4.7** | **4.1** | **–** | **–** |
| Interest rate swaps not designated | | **0.5** | **0.5** | **0.5** | **–** | **–** | **–** |
| | | **370.1** | **478.1** | **38.0** | **24.0** | **226.8** | **189.3** |

| | Effective interest rate | Carrying amount £m | Contractual cash flows £m | Less than 1 year £m | 1-2 years £m | 2-5 years £m | 2008 More than 5 years £m |
|---|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities** | | | | | | | |
| 6.84% US Dollar Senior Notes 2013 | 6.84% | 31.6 | 37.0 | 8.3 | 7.8 | 20.9 | – |
| 6.23% US Dollar Senior Notes 2010 | 6.23% | 11.4 | 12.1 | 6.2 | 5.9 | – | – |
| 5.70% US Dollar Senior Notes 2014 | 5.70% | 69.2 | 92.7 | 3.9 | 3.9 | 11.8 | 73.1 |
| 6.12% US Dollar Senior Notes 2017 | 6.12% | 121.1 | 187.7 | 7.4 | 7.4 | 22.2 | 150.7 |
| 6.26% US Dollar Senior Notes 2019 | 6.26% | 51.9 | 87.5 | 3.2 | 3.2 | 9.7 | 71.4 |
| Multicurrency revolving facility | 4.94% | 136.1 | 136.2 | 0.1 | 136.1 | – | – |
| Bank and other loans | 4.00%-8.00% | 4.0 | 4.3 | 4.3 | – | – | – |
| Bank overdrafts | 6.75% | 17.3 | 18.4 | 18.4 | – | – | – |
| Obligations under finance leases | 6.0% | 2.3 | 2.5 | 0.9 | 0.7 | 0.7 | 0.2 |
| **Derivative financial liabilities** | | | | | | | |
| Forward exchange contracts as cash flow hedges | | 4.9 | 4.9 | 4.1 | 0.8 | – | – |
| Forward exchange contracts as net investment hedges | | 11.1 | 11.1 | 11.1 | – | – | – |
| | | 460.9 | 594.4 | 67.9 | 165.8 | 65.3 | 295.4 |

# Notes to the consolidated financial statements
continued

**19. Financial risk management** continued
Loans drawn under the £280 million multicurrency revolving facility are repayable within 12 months, but have been classified as non-current as the relevant committed facilities are available until 1 May 2012.

The following table indicates the periods in which cash flows associated with cash flow hedges are expected to occur. This is matched with the periods in which cash flows associated with cash flow hedges are expected to impact profit or loss.

| | **Carrying amount £m** | **Contractual cash flows £m** | **Less than 1 year £m** | **1-2 years £m** | **2-5 years £m** | **2009 More than 5 years £m** |
|---|---|---|---|---|---|---|
| **Cash flows associated with derivatives that are cash flow hedges:** | | | | | | |
| Forward exchange contracts – Assets | **0.2** | **2.8** | **2.8** | **–** | **–** | **–** |
| Forward exchange contracts – Liabilities | **(0.1)** | **(2.5)** | **(2.5)** | **–** | **–** | **–** |
| | **0.1** | **0.3** | **0.3** | **–** | **–** | **–** |

| | Carrying amount £m | Contractual cash flows £m | Less than 1 year £m | 1-2 years £m | 2-5 years £m | 2008 More than 5 years £m |
|---|---|---|---|---|---|---|
| **Cash flows associated with derivatives that are cash flow hedges:** | | | | | | |
| Forward exchange contracts – Assets | 0.2 | 25.7 | 21.7 | 4.0 | – | – |
| Forward exchange contracts – Liabilities | (4.9) | (30.2) | (25.4) | (4.8) | – | – |
| | (4.7) | (4.5) | (3.7) | (0.8) | – | – |

### Market risk
Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices, will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

The Group buys and sells derivatives in the ordinary course of business, and also incurs financial liabilities, in order to manage market risks. All such transactions are carried out within the guidelines set by the Risk Management Committee. Generally the Group seeks to apply hedge accounting in order to manage volatility in profit or loss.

### Interest rate risk
Profile
At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

| | Carrying amount **2009 £m** | 2008 £m |
|---|---|---|
| **Fixed rate instruments** | | |
| Financial liabilities | **(250.8)** | (287.5) |
| **Variable rate instruments** | | |
| Financial assets | **107.6** | 154.4 |
| Financial liabilities | **(109.5)** | (157.3) |
| | **(1.9)** | (2.9) |

The Group adopts a policy of ensuring that between 30% and 70% of its exposure to changes in interest rates on borrowings is on a fixed rate basis.

## 19. Financial risk management continued

### Fair value sensitivity analysis for fixed rate instruments

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit or loss.

### Cash flow sensitivity analysis for variable rate instruments

A change of 100 basis points in interest rates on the outstanding bank syndication debt at the reporting date would have increased/(decreased) profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. The analysis is performed on the same basis for 2008.

| | | Profit or loss |
|---|---|---|
| | 100 bps increase £m | 100 bps decrease £m |
| **3 January 2010** | | |
| Variable rate instruments | **1.1** | **(0.5)** |
| Cash flow sensitivity (net) | **1.1** | **(0.5)** |
| **4 January 2009** | | |
| Variable rate instruments | 1.4 | (1.4) |
| Cash flow sensitivity (net) | 1.4 | (1.4) |

### Foreign currency risk

The table below shows the Group's currency exposures, being exposures on currency transactions that give rise to net currency gains and losses recognised in the income statement. Such exposures comprise the monetary assets and liabilities of the Group that are not denominated in the functional currency of the operating company involved, other than certain non-sterling borrowings treated as hedges of net investments in overseas entities.

| | | | **2009** | | | 2008 |
|---|---|---|---|---|---|---|
| Functional currency of Group operations | **GBP £m** | **US$ £m** | **Euro £m** | GBP £m | US$ £m | Euro £m |
| Trade receivables | **4.1** | **0.2** | **3.2** | 0.9 | 11.9 | 7.3 |
| Cash and cash equivalents | **8.9** | **0.2** | **1.9** | 0.6 | 21.4 | 12.0 |
| Trade payables | **(1.9)** | **(1.0)** | **(1.7)** | (5.3) | (7.5) | (3.3) |
| Net balance sheet exposure | **11.1** | **(0.6)** | **3.4** | (3.8) | 25.8 | 16.0 |

The amounts shown in the table take into account the effect of the forward contracts entered into to manage these currency exposures.

| | | Average rate | | Year-end rate |
|---|---|---|---|---|
| | **2009** | 2008 | **2009** | 2008 |
| US$ | **1.5687** | 1.8552 | **1.6149** | 1.4450 |
| Euro | **1.1249** | 1.2582 | **1.1255** | 1.0408 |

The Group aims to hedge all material trade receivables and trade payables denominated in a foreign currency. At any point in time the Group also hedges up to 75% of its estimated foreign currency exposure in respect of forecasted sales and purchases over the following 12 months. The Group uses forward exchange contracts to hedge its foreign currency risk. Most of the forward exchange contracts have maturities of less than one year after the balance sheet date.

In respect of other monetary assets and liabilities held in currencies other than the currency of the reporting unit, the Group ensures that the net exposure is kept to an acceptable level, by buying or selling foreign currencies at spot rates where necessary to address short-term imbalances.

### Forecasted transactions

The Group classifies its forward exchange contracts hedging forecasted transactions as cash flow hedges and states them at fair value. The net fair value of forward exchange contracts used as hedges of forecasted transactions at 3 January 2010 was a loss of £0.4 million (2008: loss £4.6 million), comprising assets of £0.1 million (2008: £0.2 million) and liabilities of £0.5 million (2008: £4.8 million) that were recognised in fair value derivatives.

### Cash flow hedges

The contractual cash flows associated with the forward exchange contracts that are designated as cash flow hedges are shown in the section on liquidity risk. The impact on profit or loss is expected to occur at the same time as the associated cash flows.

# Notes to the consolidated financial statements
continued

**19. Financial risk management** continued

### Hedge of net investment in foreign subsidiaries

The Group manages the translation exposure of overseas net assets by seeking to match the currency of borrowings with the currency in which the net assets are denominated. The objectives are to maintain a low cost of borrowing, whilst maintaining a balanced portfolio of net assets by currency.

The Group enters into forward contracts to hedge net investments in overseas subsidiaries. The Group also designates the Euro drawdowns under the US$280 million multicurrency revolving credit facility as a hedge of the Group's investment in subsidiaries in Europe. Euro drawdowns during the year amounted to €43.5 million (2008: €100.0 million).

### Sensitivity analysis

The Group's sensitivity to changes in foreign exchange rates on financial assets and liabilities as at 3 January 2010 is set out in the table below. The impact of a weakening in sterling on the Group's financial assets and liabilities would be more than offset in equity and income by its impact on the Group's overseas net assets and earnings respectively. Sensitivity on Group assets other than financial assets and liabilities is not included in this analysis.

The amounts generated from the sensitivity analysis are forward-looking estimates of market risk assuming certain adverse market conditions occur. Actual results in the future may differ materially from those projected results due to developments in the global financial markets which may cause fluctuations in interest and exchange rates to vary from the hypothetical amounts disclosed in the table below, which therefore should not be considered a projection of likely future events and losses.

The estimated changes for foreign exchange rates are based on an instantaneous 10% weakening or strengthening in sterling against all other currencies from the levels applicable at 3 January 2010, with all other variables remaining constant. Such analysis is for illustrative purposes only - in practice market rates rarely change in isolation.

| | **10% weakening in sterling** | |
|---|---|---|
| **3 January 2010** | **Equity £m** | **Profit before tax £m** |
| US$ | **(20.5)** | **(1.6)** |
| Euro | **(5.5)** | **(0.2)** |
| Other | **1.2** | **–** |

| | 10% weakening in sterling | |
|---|---|---|
| 4 January 2009 | Equity £m | Profit before tax £m |
| US$ | (26.4) | (1.8) |
| Euro | (8.0) | (1.3) |
| Other | 6.9 | – |

The impact of a one cent movement in the US$ exchange rate on results that are reported in US$ (including those currencies that track the US$) would be circa £1.9 million of revenue and £0.2 million of underlying operating profit.

### Other market price risk

Equity price risk arises from available-for-sale equity securities held for meeting partially the unfunded portion of the Group's defined benefit pension obligations. The primary goal of the Group's investment strategy is to maximise returns in order to meet partially the Group's unfunded defined benefit obligations.

### Capital management

The Board's policy is to maintain a strong capital base (total equity) so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Board uses a number of measures, identified as key performance indicators (KPI), to ensure the continued success of the Group. The main KPI for the Group is the underlying profit margin. The aim is to achieve mid-teen margins in good times and double-digit margins when the environment is more challenging. Another measure, the economic value-added ratio (EVA), compares the returns made by our Divisions with the notional cost of investing in them. The Group uses this ratio to ascertain where to make capital investments within the Group. The basic calculation deducts the cost of capital from the net operating profit after allowing for a notional medium-term tax charge.

The Board encourages employees of the Group to hold the Company's Ordinary shares. The Group operates a number of employee share and share option schemes. From time to time the Company purchases its own shares on the market; the timing of these purchases depends on market prices. Primarily the shares are intended to be used for issuing shares under the Group's various share option incentive schemes. The Company may also acquire its own shares under a share buy-back programme.

## 19. Financial risk management continued

The Board seeks to maintain a balance between the advantages and security afforded by a sound capital position, and the higher returns that might be possible with higher levels of borrowings.

The Group's debt to adjusted capital ratio at the end of the reporting period was as follows:

| | 2009 £m | 2008 £m |
|---|---|---|
| Total interest-bearing loans and borrowings | **359.1** | 427.6 |
| Less: cash and cash equivalents and overdrafts | **(106.4)** | (137.2) |
| Net debt | **252.7** | 290.4 |
| Total equity | **214.6** | 208.0 |
| Less: amounts accumulated in equity relating to cash flow hedges | **(0.2)** | 4.6 |
| Adjusted capital | **214.4** | 212.6 |
| Debt to adjusted capital ratio | **1.2** | 1.4 |

There were no changes in the Group's approach to capital management during the year.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

### Fair values

The fair values of financial assets and liabilities, together with the carrying amounts shown in the balance sheet are as follows:

| | Carrying amount 2009 £m | Fair value 2009 £m | Carrying amount 2008 £m | Fair value 2008 £m |
|---|---|---|---|---|
| **Financial assets and liabilities at amortised cost** | | | | |
| 6.84% US Dollar Senior Notes 2013 | **(23.1)** | **(23.8)** | (31.6) | (34.3) |
| 6.23% US Dollar Senior Notes 2010 | **(5.1)** | **(5.1)** | (11.4) | (11.7) |
| 5.70% US Dollar Senior Notes 2014 | **(61.8)** | **(63.3)** | (69.2) | (79.5) |
| 6.12% US Dollar Senior Notes 2017 | **(108.2)** | **(110.0)** | (121.1) | (147.6) |
| 6.26% US Dollar Senior Notes 2019 | **(46.4)** | **(46.2)** | (51.9) | (65.0) |
| Bank syndication | **(105.4)** | **(105.4)** | (136.1) | (136.1) |
| Bank and other loans | **(7.5)** | **(7.5)** | (4.0) | (4.0) |
| Bank overdrafts | **(1.2)** | **(1.2)** | (17.3) | (17.3) |
| Obligations under finance leases | **(1.6)** | **(1.6)** | (2.3) | (2.3) |
| Trade and other payables | **(151.2)** | **(151.2)** | (94.3) | (94.3) |
| Loan to associate | **–** | **–** | 36.0 | 36.0 |
| Loans and receivables | **144.5** | **144.5** | 164.5 | 164.5 |
| Cash and cash equivalents | **107.6** | **107.7** | 154.5 | 154.5 |
| | **(259.4)** | **(263.1)** | (184.2) | (237.1) |
| **Available-for-sale financial instruments** | | | | |
| Available-for-sale financial assets | **5.7** | **5.7** | 5.2 | 5.2 |
| **Derivatives and other items at fair value** | | | | |
| Forward exchange contracts used for hedging: | | | | |
| Assets | **0.5** | **0.5** | 0.2 | 0.2 |
| Liabilities | **(9.8)** | **(9.8)** | (16.0) | (16.0) |
| | **(9.3)** | **(9.3)** | (15.8) | (15.8) |
| | **(263.0)** | **(266.7)** | (194.8) | (247.7) |
| Unrecognised profit/(loss) | | **(3.7)** | | (52.9) |

# Notes to the consolidated financial statements
continued

**19. Financial risk management** continued

### Estimation of fair values

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the preceding table.

### Equity securities

Fair value is based on quoted market prices at the balance sheet date.

### Derivatives

Forward exchange contracts are marked to market either using listed market prices or by discounting the contractual forward price and deducting the current spot rate.

### Interest-bearing loans and borrowings

Fair value is calculated based on discounted expected future principal and interest cash flows.

### Finance lease liabilities

The fair value is estimated as the present value of future cash flows, discounted at market interest rates for homogeneous lease agreements. The estimated fair values reflect changes in interest rates.

### Trade and other receivables/payables

For receivables/payables with a remaining life of less than one year, the notional amount is deemed to reflect the fair value. All other receivables/payables are discounted to determine the fair value.

### Interest rates used for determining fair value

The interest rates used to determine the fair value of loans and borrowings and finance leases are as follows:

| | **2009 %** | 2008 % |
|---|---|---|
| Loans and borrowings | **2.7-6.3** | 2.0-4.0 |
| Finance leases | **6.0** | 6.0 |

### Fair value hierarchy

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (ie as prices) or indirectly (ie derived from prices)

Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

| **3 January 2010** | **Level 1 £m** | **Level 2 £m** | **Level 3 £m** | **Total £m** |
|---|---|---|---|---|
| Available-for-sale financial assets | **5.7** | **–** | **–** | **5.7** |
| Derivative financial assets | **–** | **0.5** | **–** | **0.5** |
| | **5.7** | **0.5** | **–** | **6.2** |
| Derivative financial liabilities | **–** | **(9.8)** | **–** | **(9.8)** |
| | **5.7** | **(9.3)** | **–** | **(3.6)** |

| 4 January 2009 | Level 1 £m | Level 2 £m | Level 3 £m | Total £m |
|---|---|---|---|---|
| Available-for-sale financial assets | 5.2 | – | – | 5.2 |
| Derivative financial assets | – | 0.2 | – | 0.2 |
| | 5.2 | 0.2 | – | 5.4 |
| Derivative financial liabilities | – | (16.0) | – | (16.0) |
| | 5.2 | (15.8) | – | (10.6) |

There have been no transfers between level 1 and level 2 during 2009 and 2008.

## 20. Employee benefits

Morgan Crucible operates a number of defined benefit arrangements as well as defined contribution plans. The defined benefit plans are primarily in the UK, USA and Europe and predominately provide pensions based on service and career average pay. In addition post-retirement medical plans are operated in the USA.

| | 2009 UK £m | 2009 USA £m | 2009 Europe £m | 2009 Rest of world £m | 2009 Total £m |
|---|---|---|---|---|---|
| **Pension plans and employee benefits** | | | | | |
| Present value of unfunded defined benefit obligations | – | (8.7) | (22.5) | (2.1) | (33.3) |
| Present value of funded defined benefit obligations | (333.4) | (111.4) | (1.0) | (10.0) | (455.8) |
| Fair value of plan assets | 298.9 | 73.9 | 0.5 | 9.7 | 383.0 |
| **Deficit** | (34.5) | (46.2) | (23.0) | (2.4) | (106.1) |
| Unrecognised past service costs | – | – | 0.2 | – | 0.2 |
| **Net obligations** | (34.5) | (46.2) | (22.8) | (2.4) | (105.9) |
| **Movements in present value of defined benefit obligation** | | | | | |
| At 5 January 2009 | (278.5) | (131.6) | (25.0) | (11.2) | (446.3) |
| Current service cost | (1.4) | (2.0) | (0.4) | (1.4) | (5.2) |
| Interest cost | (17.7) | (7.3) | (1.1) | (0.3) | (26.4) |
| Actuarial losses | (50.1) | (1.5) | (0.7) | (0.7) | (53.0) |
| Benefits paid | 15.8 | 7.2 | 1.3 | 1.6 | 25.9 |
| Contributions by members | (1.5) | – | – | – | (1.5) |
| Past service costs | – | – | (0.2) | – | (0.2) |
| Curtailments and settlements | – | 1.3 | 0.7 | – | 2.0 |
| Exchange adjustments | – | 13.8 | 1.9 | (0.1) | 15.6 |
| **At 3 January 2010** | (333.4) | (120.1) | (23.5) | (12.1) | (489.1) |
| **Movements in fair value of plan assets** | | | | | |
| At 5 January 2009 | 265.4 | 70.2 | 0.6 | 8.3 | 344.5 |
| Expected return on plan assets | 17.7 | 4.1 | – | 0.3 | 22.1 |
| Actuarial gains | 25.4 | 7.6 | – | 1.3 | 34.3 |
| Contributions by employer | 4.7 | 6.7 | 1.2 | 1.4 | 14.0 |
| Contributions by members | 1.5 | – | – | – | 1.5 |
| Benefits paid | (15.8) | (7.2) | (1.3) | (1.6) | (25.9) |
| Exchange adjustments | – | (7.5) | – | – | (7.5) |
| **At 3 January 2010** | 298.9 | 73.9 | 0.5 | 9.7 | 383.0 |
| Actual return on assets | 43.1 | 11.7 | – | 1.6 | 56.4 |

| | 2009 UK £m | 2009 USA £m | 2009 Europe £m | 2009 Rest of world £m | 2009 Total £m |
|---|---|---|---|---|---|
| **Pension plans and employee benefits** | | | | | |
| **Expense recognised in the consolidated income statement** | | | | | |
| Current service cost and past service cost | (1.4) | (2.0) | (0.4) | (1.4) | (5.2) |
| Interest on defined benefit pension plan obligation | (17.7) | (7.3) | (1.1) | (0.3) | (26.4) |
| Expected return on defined benefit pension plan assets | 17.7 | 4.1 | – | 0.3 | 22.1 |
| Gain on curtailment of US and French employee benefit schemes | – | 1.3 | 0.7 | – | 2.0 |
| **Total expense** | (1.4) | (3.9) | (0.8) | (1.4) | (7.5) |

# Notes to the consolidated financial statements
continued

**20. Employee benefits** continued

The expense is recognised in the following line items in the consolidated income statement:

| | 2009 £m | 2008 £m |
|---|---|---|
| Operating costs | **(3.2)** | (6.7) |
| Finance income | **22.1** | 25.7 |
| Finance expense | **(26.4)** | (25.6) |
| | **(7.5)** | (6.6) |

The Group has adopted the policy of recognising actuarial gains and losses immediately in the balance sheet through other comprehensive income. Cumulative actuarial losses recorded in other comprehensive income since 5 January 2004, the date of transition to Adopted IFRSs, are £95.7 million.

The fair value of the plan assets were as follows:

| | 2009 UK £m | 2009 USA £m | 2009 Europe £m | 2009 Rest of world £m | 2009 Total £m |
|---|---|---|---|---|---|
| Equities | **125.0** | **39.7** | **–** | **–** | **164.7** |
| Bonds | **6.4** | **33.8** | **–** | **–** | **40.2** |
| Matching insurance policies | **167.5** | **–** | **0.5** | **1.7** | **169.7** |
| Other | **–** | **0.4** | **–** | **8.0** | **8.4** |
| **Total** | **298.9** | **73.9** | **0.5** | **9.7** | **383.0** |

Principal actuarial assumptions were:

| | | UK % | USA % | Europe % |
|---|---|---|---|---|
| Discount rate | | **5.80** | **6.10** | **5.20** |
| Expected rate of return on plan assets | – Equities | **8.40** | **9.00** | **n/a** |
| | – Bonds | **5.30** | **5.70** | **n/a** |
| | – Matching insurance | **5.80** | **n/a** | **5.20** |
| Salary increase | | **n/a** | **2.70** | **2.50** |
| Inflation | | **3.50** | **2.20** | **2.00** |
| Pensions increase | | **3.40/3.40** | **n/a** | **2.00** |
| Mortality – post-retirement: | | | | |
| Life expectancy of a male retiring at age 60 in 2009 | | **25.8 years** | **21.2 years** | **22.5 years** |
| Life expectancy of a male retiring at age 60 in 2029 | | **27.1 years** | **21.0 years** | **25.0 years** |

Expected rates of return on plan assets are determined by reference to relevant indices. The overall expected rate of return is calculated by weighting the individual rates in accordance with the anticipated balance in the plan's investment portfolio.

| | 2009 £m | 2008 £m | 2007 £m | 2006 £m | 2005 £m |
|---|---|---|---|---|---|
| **Balance sheet** | | | | | |
| Present value of defined benefit obligation | **(489.1)** | (446.3) | (450.7) | (446.1) | (466.3) |
| Fair value of plan assets | **383.0** | 344.5 | 403.0 | 403.4 | 342.1 |
| Deficit | **(106.1)** | (101.8) | (47.7) | (42.7) | (124.2) |
| Unrecognised past service costs | **0.2** | – | – | – | – |
| Net obligations | **(105.9)** | (101.8) | (47.7) | (42.7) | (124.2) |

## 20. Employee benefits continued

| | 2009 £m | 2008 £m | 2007 £m | 2006 £m | 2005 £m |
|---|---|---|---|---|---|
| **Experience (losses)/gains** | | | | | |
| Experience (losses)/gains on defined benefit obligation | **(2.2)** | 1.7 | (0.2) | (2.0) | (8.6) |
| Experience gains/(losses) on plan assets | **34.3** | (104.7) | (17.5) | 7.2 | 26.0 |

The sensitivities regarding the principal assumptions used to measure the scheme liabilities are:

| | Change in assumption | 2009 Increase effect £m | 2008 Increase effect £m |
|---|---|---|---|
| Discount rate | Decrease by 0.1% | **5.8** | 4.9 |
| Rate of increase in salaries | Increase by 0.1% | **0.1** | 0.1 |
| Inflation | Increase by 0.1% | **3.6** | 2.8 |
| Mortality – post-retirement | Pensioners live 1 year longer | **8.8** | 8.2 |

The 2009 expense recognised in the consolidated income statement includes a £1.3 million gain on curtailment of US employee benefit schemes. The curtailment gain of £0.7 million in Europe arose as a result of two European employee benefit schemes being withdrawn. The unrecognised past service cost in France was as a result of a change in future benefit accrual. This will be amortised over 13 years.

| | 2008 UK £m | 2008 USA £m | 2008 Europe £m | 2008 Rest of world £m | 2008 Total £m |
|---|---|---|---|---|---|
| **Pension plans and employee benefits** | | | | | |
| Present value of unfunded defined benefit obligations | – | (10.1) | (23.9) | (2.1) | (36.1) |
| Present value of funded defined benefit obligations | (278.5) | (121.5) | (1.1) | (9.1) | (410.2) |
| Fair value of plan assets | 265.4 | 70.2 | 0.6 | 8.3 | 344.5 |
| Net obligations | (13.1) | (61.4) | (24.4) | (2.9) | (101.8) |
| **Movements in present value of defined benefit obligation** | | | | | |
| At 5 January 2008 | (325.1) | (95.0) | (20.1) | (10.5) | (450.7) |
| Current service cost | (2.6) | (1.9) | (0.5) | (1.5) | (6.5) |
| Interest cost | (18.4) | (5.9) | (1.0) | (0.3) | (25.6) |
| Actuarial gains | 55.2 | 1.1 | 1.2 | 0.2 | 57.7 |
| Benefits paid | 14.3 | 5.6 | 1.3 | 1.2 | 22.4 |
| Contributions by members | (1.7) | – | – | – | (1.7) |
| Curtailments and settlements | (0.2) | – | – | – | (0.2) |
| Exchange adjustments | – | (35.5) | (5.9) | (0.3) | (41.7) |
| At 4 January 2009 | (278.5) | (131.6) | (25.0) | (11.2) | (446.3) |
| **Movements in fair value of plan assets** | | | | | |
| At 5 January 2008 | 322.6 | 71.2 | 0.5 | 8.7 | 403.0 |
| Expected return on plan assets | 20.1 | 5.3 | – | 0.3 | 25.7 |
| Actuarial losses | (71.1) | (33.1) | – | (0.5) | (104.7) |
| Contributions by employer | 6.4 | 5.0 | 1.3 | 1.0 | 13.7 |
| Contributions by members | 1.7 | – | – | – | 1.7 |
| Benefits paid | (14.3) | (5.6) | (1.3) | (1.2) | (22.4) |
| Exchange adjustments | – | 27.4 | 0.1 | – | 27.5 |
| At 4 January 2009 | 265.4 | 70.2 | 0.6 | 8.3 | 344.5 |
| Actual return on assets | (51.0) | (27.8) | – | (0.2) | (79.0) |

# Notes to the consolidated financial statements
continued

**20. Employee benefits** continued

| | 2008 UK £m | 2008 USA £m | 2008 Europe £m | 2008 Rest of world £m | 2008 Total £m |
|---|---|---|---|---|---|
| **Expense recognised in the consolidated income statement** | | | | | |
| Current service costs | (2.8) | (1.9) | (0.5) | (1.5) | (6.7) |
| Interest on defined benefit pension plan obligation | (18.4) | (5.9) | (1.0) | (0.3) | (25.6) |
| Expected return on defined benefit pension plan assets | 20.1 | 5.3 | – | 0.3 | 25.7 |
| Total expense | (1.1) | (2.5) | (1.5) | (1.5) | (6.6) |

The fair values of the plan assets were as follows:

| | 2008 UK £m | 2008 USA £m | 2008 Europe £m | 2008 Rest of world £m | 2008 Total £m |
|---|---|---|---|---|---|
| Equities | 97.8 | 35.3 | – | – | 133.1 |
| Bonds | 7.1 | 34.5 | – | – | 41.6 |
| Matching insurance policies | 153.3 | – | 0.6 | 1.6 | 155.5 |
| Other | 7.2 | 0.4 | – | 6.7 | 14.3 |
| Total | 265.4 | 70.2 | 0.6 | 8.3 | 344.5 |

Principal actuarial assumptions were:

| | | UK % | USA % | Europe % |
|---|---|---|---|---|
| Discount rate | | 6.50 | 6.10 | 5.60 |
| Expected rate of return on plan assets | – Equities | 8.00 | 8.00 | n/a |
| | – Bonds | 5.00 | 4.70 | n/a |
| | – Matching insurance | 6.50 | n/a | 5.60 |
| Salary increase | | n/a | 2.50 | 2.50 |
| Inflation | | 2.80 | 2.00 | 2.00 |
| Pensions increase | | 2.60/3.15 | n/a | 2.00 |
| Mortality - post-retirement: | | | | |
| Life expectancy of a male retiring at age 60 in 2008 | | 25.7 years | 21.2 years | 22.5 years |
| Life expectancy of a male retiring at age 60 in 2028 | | 27.1 years | 21.2 years | 25.4 years |

The actual liability in respect of global employee benefits will not be known until the last payments have been made. In placing a current estimate on the Company's past service benefit obligations, a number of assumptions about the future are required. For defined benefit schemes, the Directors make annual estimates and assumptions in respect of discount rates, future changes in salaries, employee turnover, inflation rates and life expectancy. In making these estimates and assumptions, the Directors consider advice provided by external advisers, such as actuaries.

### Defined contribution plans

The Group operates a number of defined contribution pension plans. The total expense relating to these plans in the current year was £3.9 million (2008: £2.6 million).

### Share-based payments

During 2004, the Group established a new Long Term Incentive Plan and a new Executive Share Option Scheme. During 2004, the Company also renewed its all-Employee Sharesave Scheme and took the opportunity to extend a similar scheme to employees in Germany.

During 2005, 2006, 2007, 2008 and 2009 the Group made awards under the 2004 Long Term Incentive Plan. During 2005 and 2006 the Group made awards under the 2004 Executive Share Option Scheme. Also in 2005, 2007, 2008 and 2009 the Company granted options under the UK all-Employee Sharesave Scheme and in 2008 the Company granted options under the German all-Employee Sharesave Scheme.

During 2008, the Group established The Morgan Crucible Bonus Deferral Share Matching Plan and awards were made under this plan in 2008 and 2009.

Additionally, equity-settled share option grants and awards made under the Executive Share Option Scheme 1995 are outstanding. In accordance with the transitional provisions under IFRS 1, the recognition and measurement principles in IFRS 2 have not been applied to these grants.

**20. Employee benefits** continued

The terms and conditions of all awards and grants made since 7 November 2002 are as follows:

| Grant date/Employees entitled | Number of instruments | Vesting conditions | Contractual life of option |
|---|---|---|---|
| Awards granted to senior employees in 2009 under The Morgan Crucible Bonus Deferral Share Matching Plan | 3,426,473 | Three years of service plus satisfaction of performance criteria | 3 years |
| Options granted to UK employees in 2009 under the Employee Sharesave Scheme 2004 | 1,937,568 | Three years of service | 3 years |
| Awards granted to senior employees in 2009 under the Long Term Incentive Plan 2004 | 5,085,721 | Three years of service plus satisfaction of performance criteria | 3 years |
| Awards granted to senior employees in 2008 under The Morgan Crucible Bonus Deferral Share Matching Plan | 2,888,005 | Three years of service plus satisfaction of performance criteria | 3 years |
| Options granted to UK employees in 2008 under the Employee Sharesave Scheme 2004 | 1,089,783 | Three years of service | 3 years |
| Options granted to German employees in 2008 under The Morgan Crucible Savings Related Share Option Scheme for Employees in Germany | 278,451 | Three years of service | 3 years |
| Awards granted to senior employees in 2008 under the Long Term Incentive Plan 2004 | 2,691,123 | Three years of service plus satisfaction of performance criteria | 3 years |
| Options granted to UK employees in 2007 under the Employee Sharesave Scheme 2004 | 856,885 | Three years of service | 3 years |
| Awards granted to senior employees in 2007 under the Long Term Incentive Plan 2004 | 1,540,000 | Three years of service plus satisfaction of performance criteria | 3 years |
| Options granted to senior employees in 2006 under the Directors' Share Option Plan 2006 | 1,000,000 | Three years of service plus satisfaction of performance criteria | 10 years |
| Options granted to senior employees in 2006 under the Executive Share Option Scheme 2004 | 398,500 | Three years of service plus satisfaction of performance criteria | 10 years |
| Awards granted to senior employees in 2006 under the Long Term Incentive Plan 2004 | 477,500 | Three years of service plus satisfaction of performance criteria | 3 years |
| Options granted to UK employees in 2005 under the Employee Sharesave Scheme 2004 | 976,614 | Three years of service | 3 years |
| Awards granted to senior employees in 2005 under the Long Term Incentive Plan 2004 | 3,804,820 | Three years of service plus satisfaction of performance criteria | 3 years |
| Awards granted to senior employees in 2004 under the Long Term Incentive Plan 2004 | 5,084,031 | Three years of service plus satisfaction of performance criteria | 3 years |
| Options granted to senior employees in 2005 under the Executive Share Option Scheme 2004 | 2,097,000 | Three years of service plus satisfaction of performance criteria | 10 years |
| Options granted to senior employees in 2004 under the Executive Share Option Scheme 2004 | 3,157,500 | Three years of service plus satisfaction of performance criteria | 10 years |
| Options granted to UK employees in 2004 under the Employee Sharesave Scheme 2004 | 521,884 | Three years of service | 3 years |
| Options granted to German employees in 2004 under The Morgan Crucible Savings Related Share Option Scheme for Employees in Germany | 516,844 | Three years of service | 3 years |
| Options granted to UK employees in 2003 under the Employee Sharesave Scheme 1995 | 779,421 | Three years of service | 3 years |
| Options granted to senior employees in 2004 under the Executive Share Option Scheme 1995 | 263,000 | Three years of service plus satisfaction of performance criteria | 10 years |
| Options granted to senior employees in 2002 under the Executive Share Option Scheme 1995 | 1,780,000 | Three years of service plus satisfaction of performance criteria | 10 years |

# Notes to the consolidated financial statements
continued

**20. Employee benefits** continued

**Performance criteria for Long Term Incentive Plan 2004, Directors' Share Option Plan 2006 and Executive Share Option Scheme 2004**

For awards granted from 2004 to 2006 inclusive, the extent to which awards vested depended on the Company's Total Shareholder Return ('TSR') ranking against the TSR of the other companies in the FTSE 350 measured over the performance period.

If the Company's TSR placed it at the median, then 30% of the awards would vest on the third anniversary of the date of the grant.

If the Company's TSR placed it at the upper quartile, then 100% of the option would vest on the third anniversary of the date of grant. Between the median and upper quartile, the option would vest on a straight-line basis. Below the median, none of the shares would vest.

In 2007 additional performance criteria were attached to the Long Term Incentive Plan 2004. The TSR performance criteria referred to above now only relate to 50% of awards made. The extent to which the other 50% of these awards vest will depend on the Company's earnings per share ('EPS') compared with the Retail Price Index ('RPI'). The full 50% will vest if, over the three-year performance period, the Company's EPS increases by more than the sum of the annual RPI increase and 10% per annum. If the Company's EPS increases by more than the sum of the annual RPI increase and between 4% and 10% per annum then the proportion of awards vesting will be interpolated between 15% and 50%. If the Company's EPS increases by more than the sum of the annual RPI increase and 4% per annum then 15% of the awards will vest. If the Company's EPS increases by less than the sum of the RPI increase and 4% per annum then 0% of the awards will vest.

In 2008 further changes were made to the performance criteria attached to the Long Term Incentive Plan 2004 for awards made in 2008 and onwards. For all participants excluding executive Directors the TSR performance criteria referred to above now only relate to 33.3% of awards made. The extent to which the other 66.7% of these awards vest will depend on the Company's EPS compared with the RPI. The full 66.7% will vest if, over the three-year performance period, the Company's EPS increases by more than the sum of the annual RPI increase and 10% per annum. If the Company's EPS increases by more than the sum of the annual RPI increase and between 4% and 10% per annum then the proportion of awards vesting will be interpolated between 15% and 50%. If the Company's EPS increases by more than the sum of the annual RPI increase and 4% per annum then 15% of the awards will vest. If the Company's EPS increases by less than the sum of the RPI increase and 4% per annum then 0% of the awards will vest. For executive Director participants the conditions remain unchanged from 2007.

In 2009 further changes were made to the performance criteria attached to the Long Term Incentive Plan 2004. For all participants the TSR performance criteria referred to above now relate to 100.0% of awards made.

In addition, an improvement must be shown in the Company's underlying financial performance.

**Performance criteria for The Morgan Crucible Bonus Deferral Share Matching Plan**

The extent to which awards will vest will depend on the Company's EPS compared with the RPI. Participants are able to defer up to 75% of their annual bonus into Company shares, subject to approval by the Remuneration Committee. Under the 2008 grant, the Remuneration Committee allowed participants to defer up to 50% of their annual bonus into Company shares. Participants must hold the deferred shares for three years to be eligible for a matching award. Matching shares may be earned at the end of three years in the event that a stretching EPS target has been met. If the Company's EPS increases by more than the sum of the annual RPI increase and 15% per annum then matching shares equal to three times the deferred shares will be earned. If the Company's EPS increases by more than the sum of the annual RPI increase and between 4% and 10% per annum then the proportion of awards will be interpolated between 0.25x deferred shares and 1.75x deferred shares. If the Company's EPS increases by more than the sum of the annual RPI increase and 4% per annum then matching shares equal to 0.25x deferred shares will be earned. If the Company's EPS increases by less than the sum of the RPI increase and 4% per annum then 0% of the awards will vest.

In 2009 additional criteria were attached to the Bonus Deferral Share Matching Plan. Under the 2009 grant, the Remuneration Committee allowed participants to defer up to 50% of their annual bonus into Company shares. Participants must hold the deferred shares for three years to be eligible for a matching award. Matching shares may be earned at the end of three years in the event that a stretching EPS target has been met. If the Company's EPS increases by more than 15% per annum then matching shares equal to three times the deferred shares will be earned. If the Company's EPS increases by between 4% and 10% per annum then the proportion of awards will be interpolated between 0.25x deferred shares and 1.75x deferred shares. If the Company's EPS increases by more than 4% per annum then matching shares equal to 0.25x deferred shares will be earned. If the Company's EPS increases by less than 4% per annum then 0% of the awards will vest.

## 20. Employee benefits continued

### Performance criteria for the Executive Share Option Scheme 1995

The diluted earnings per share for the Company must grow by at least 2% per annum in excess of RPI over the period of date of grant to date of vesting.

The fair values of services received are in return for awards made and share options granted. The estimate of the fair value of the services received is measured based on an appropriate model as shown in accounting policy note 'n'. In the case of the Binomial Lattice model and Monte Carlo model the contractual life of the options and awards are used as an input. Expectations of early exercise are incorporated into both of these models.

### Long Term Incentive Plan 2004

| | 2009 awards |
|---|---|
| Fair value at measurement date | **45.37p** |
| Share price | **89.85p** |
| Exercise price | **n/a** |
| Expected volatility (expressed as weighted average volatility used in the model) | **40%** |
| Option life (expressed as weighted average life used in the model) | **3 years** |
| Expected dividends | **7.00%** |
| Risk-free interest rate | **4.3%** |

### The Morgan Crucible Bonus Deferral Share Matching Plan

| | 2009 awards |
|---|---|
| Fair value at measurement date | **80.75p** |
| Share price | **80.75p** |
| Exercise price | **n/a** |
| Expected volatility (expressed as weighted average volatility used in the model) | **40%** |
| Option life (expressed as weighted average life used in the model) | **3 years** |
| Expected dividends | **n/a** |
| Risk-free interest rate | **n/a** |

### Executive Share Option Scheme 2004

There were no awards during 2009.

### Employee Sharesave Schemes UK

| | 2009 awards |
|---|---|
| Fair value at measurement date | **56.03p** |
| Share price | **160.00p** |
| Exercise price | **128.00p** |
| Expected volatility (expressed as weighted average volatility used in the model) | **40%** |
| Option life (expressed as weighted average life used in the model) | **3 years** |
| Expected dividends | **2.5%** |
| Risk-free interest rate | **2.1%** |

### The Morgan Crucible Savings Related Share Options Scheme for Employees in Germany

There were no awards during 2009.

### Employee Share Option Scheme 1995

There were no awards during 2009.

The expected volatility is based on the historic volatility (calculated based on the weighted average remaining life of the share options) adjusted for any expected changes to future volatility due to publicly available information.

# Notes to the consolidated financial statements
continued

## 20. Employee benefits continued

The number and weighted average exercise prices of share options are as follows:

| | **Weighted average exercise price 3 January 2010** | **Number of options 3 January 2010** | Weighted average exercise price 4 January 2009 | Number of options 4 January 2009 |
|---|---|---|---|---|
| Outstanding at the beginning of the period | **94.08p** | **13,455,505** | 99.86p | 11,803,800 |
| Granted during the period | **28.33p** | **10,449,762** | 51.24p | 6,947,362 |
| Forfeited during the period | **149.95p** | **(1,283,019)** | 153.89p | (895,840) |
| Exercised during the period | **0.00p** | **–** | 27.09p | (4,160,580) |
| Lapsed during the period | **181.21p** | **(2,503,056)** | 76.34p | (239,237) |
| Outstanding at the end of the period | **45.53p** | **20,119,192** | 94.08p | 13,455,505 |
| Exercisable at the end of the period | **153.71p** | **1,625,391** | 157.39p | 2,449,879 |

The weighted average share price at the date of share options exercised during the period was nil pence (2008: 216.52 pence). The options outstanding at the year end have an exercise price in the range nil to 256.00 pence and a weighted average contractual life of 0.7 years.

The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. The estimates of the fair value of the services received is measured based on either a Monte Carlo model, a Binomial Lattice option pricing model or a Black-Scholes Merton model. The choice of model takes into account the terms and conditions upon which the options were granted.

The IFRS 2 fair value charge expensed to the income statement was £2.0 million (2008: £2.2 million).

## 21. Provisions

| | **Closure and restructuring provisions £m** | **Other provisions £m** | **Environmental provisions £m** | **Total £m** |
|---|---|---|---|---|
| Balance at 4 January 2009 | **5.1** | **10.3** | **4.3** | **19.7** |
| Provisions made during the year | **8.7** | **4.0** | **1.3** | **14.0** |
| Provisions used during the year | **(6.2)** | **(5.3)** | **(1.3)** | **(12.8)** |
| Provisions reversed during the year | **(0.2)** | **(2.8)** | **(0.5)** | **(3.5)** |
| Effect of movements in foreign exchange | **(0.1)** | **(0.4)** | **(0.5)** | **(1.0)** |
| **Balance at 3 January 2010** | **7.3** | **5.8** | **3.3** | **16.4** |
| Current | **4.2** | **3.8** | **2.9** | **10.9** |
| Non-current | **3.1** | **2.0** | **0.4** | **5.5** |
| | **7.3** | **5.8** | **3.3** | **16.4** |

Closure and restructuring provisions are based on the Group's restructuring programmes and represent committed expenditure at the balance sheet date. The amounts provided are based on the costs of terminating relevant contracts, under the contract terms, and management's best estimate of other associated restructuring costs including professional fees, most of which are expected to be incurred over the next year. The amounts provided also include the obligation for discounted future payments under a non-cancellable lease for the offices of the Company's former headquarters, net of expected rental income under sub-leases. The lease expires in 2016.

Other provisions include the settlement of European class actions, together with the associated legal costs. The estimated costs are based on the Group's assessment of the probable future costs of these activities. The Group expects to incur most of the liability in more than one year.

Environmental provisions are for known environmental issues which the Group will rectify over the next few years. In a number of jurisdictions companies have a constructive obligation to remedy any known environmental problems. The estimated costs are based on management's best estimate of the costs required to remedy these problems. The Group expects to incur most of the liability over the next five years.

## 22. Trade and other payables

| | 2009 £m | 2008 £m |
|---|---|---|
| Non-current | | |
| Other trade payables | **0.5** | 0.4 |
| Non-trade payables | **31.2** | 3.6 |
| | **31.7** | 4.0 |
| Current | | |
| Other trade payables | **96.6** | 93.9 |
| Non-trade payables and accrued expenses | **153.7** | 127.0 |
| | **250.3** | 220.9 |

Included in current non-trade payables and accrued expenses and non-current non-trade payables is £26.6 million and £27.5 million respectively of deferred contingent consideration on purchase of 51% of the Ordinary share capital of Clearpower Limited. For further details see note 3.

## 23. Operating leases

### Leases as lessee

Non-cancellable operating lease rentals are payable as follows:

| | 2009 £m | 2008 £m |
|---|---|---|
| Less than one year | **7.9** | 6.1 |
| Between one and five years | **19.6** | 18.2 |
| More than five years | **32.0** | 34.6 |
| | **59.5** | 58.9 |

The Group leases a number of properties under operating leases of varying duration. In some cases, during the life of the lease, the rental payable is reviewed after a fixed period to reflect market rentals.

### Leases as lessor

The total of future minimum sub-lease income under non-cancellable sub-leases is £2.8 million (2008: £5.3 million).

## 24. Capital commitments

Commitments for property, plant and equipment and computer software expenditure for which no provision has been made in these accounts amount to £2.7 million (2008: £3.8 million) for the Group.

## 25. Contingencies

There are contingent liabilities on bills discounted by the Group amounting to £0.8 million (2008: £0.8 million).

The Group has been subject to legal claims in the USA, Canada and Europe. Settlements for the majority of these have been agreed. There remain provisions in respect of these claims of £0.7 million (2008: £2.3 million). The Board, having taken legal advice, is of the opinion that the remainder of these actions will not have a material impact on the Group’s financial position.

In an international group of companies a variety of claims arise from time to time. Provision has been made in these accounts against those claims which the Directors consider meet the requirements of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and are likely to result in significant liabilities.

# Notes to the consolidated financial statements
continued

## 26. Related parties

### Identification of related parties

The Group has related party relationships with its subsidiaries (a list of principal subsidiary undertakings is shown in note 43), with its associates (see note 12) and with its Directors and executive officers.

### Transactions with key management personnel

The Company has written service contracts or letters of appointment with each of its Directors, under which the Directors receive a salary or a fee and other emoluments.

The key management of the Group and parent Company consists of the Board of Directors and members of the Executive Committee.

Their compensation charged in the year was:

| | **2009 £m** | 2008 £m |
|---|---|---|
| Short-term employee benefits | **2.4** | 3.1 |
| Pension and other post-employment costs | **0.3** | 0.3 |
| Share-based payments | **0.7** | 0.8 |
| Termination payments | **–** | 0.4 |
| Non-executive Directors' fees and benefits | **0.3** | 0.3 |
| Total compensation of key management personnel | **3.7** | 4.9 |

Information on executive Directors' remuneration is given in the Remuneration report on pages 77 to 85.

### Transactions in connection with former Directors

During the year the Group made payments on behalf of former Chief Executive Ian Norris of £1.5 million (2008: £1.0 million) to cover the costs of his legal defence against extradition to stand trial in the USA. In addition, the Group recovered fees of £1.6 million (2008: £nil million) in respect of court cost awards relating to legal costs expended on behalf of Ian Norris in prior periods. The Group also made payments to former Chief Executive Warren Knowlton to reimburse him for US employer social costs in respect of his time with the Group.

### Other related party transactions

| | **2009 £m** | 2008 £m |
|---|---|---|
| Sales to associates | **12.4** | 3.6 |
| Interest income from associate | **–** | 4.1 |

The balances with our associates are shown in note 15.

During the year, the Group acquired a controlling interest in Clearpower Limited. As a result, Clearpower Limited ceased to be an associate and is accounted for as a subsidiary from the date control was attained. The Group had related party relationships with Clearpower Limited, as an associate, in the comparative year.

In 2009 the Group acquired a significant interest in Integrated Survivability Technologies Limited and started to account for it as an associate. The transactions with associates reported in 2009 refer to Integrated Survivability Technologies Limited.

## 27. Subsequent events

There have been no material events since the year end.

# Company balance sheet
## as at 3 January 2010

| | Note | 2009 £m | 2008 £m |
|---|---|---|---|
| **Fixed assets** | | | |
| Tangible assets | 31 | **1.8** | 2.2 |
| Investment in subsidiary undertakings | 32 | **790.7** | 693.8 |
| Other investments | 33 | **–** | 5.1 |
| | | **792.5** | 701.1 |
| **Current assets** | | | |
| Debtors – due within one year | 34 | **36.9** | 63.2 |
| – due after one year | 34 | **–** | 37.3 |
| Total debtors | | **36.9** | 100.5 |
| Cash at bank and in hand | | **8.5** | 27.6 |
| | | **45.4** | 128.1 |
| **Creditors – amounts falling due within one year** | 35 | **63.5** | 42.5 |
| **Net current assets** | | **(18.1)** | 85.6 |
| **Total assets less current liabilities** | | **774.4** | 786.7 |
| **Creditors – amounts falling due after more than one year** | | | |
| Amounts payable to subsidiary undertakings | | **178.7** | 196.0 |
| Other creditors, including deferred consideration | 35 | **27.6** | – |
| Derivative financial liabilities | 35 | **4.1** | 0.8 |
| Borrowings | 36 | **105.4** | 136.1 |
| | | **315.8** | 332.9 |
| **Provisions for liabilities and charges** | 37 | **2.8** | 4.7 |
| | | **318.6** | 337.6 |
| **Net assets** | | **455.8** | 449.1 |
| **Capital and reserves** | | | |
| Equity shareholders' funds | | | |
| Called up share capital | 17 | **67.5** | 67.5 |
| Share premium account | 38 | **85.3** | 85.3 |
| Merger reserve | 38 | **17.0** | 17.0 |
| Capital redemption reserve | 38 | **35.7** | 35.7 |
| Profit and loss account | 38 | **249.9** | 243.2 |
| | | **455.4** | 448.7 |
| Non-equity shareholders' funds | | | |
| Called up share capital | | **0.4** | 0.4 |
| **Shareholders' funds** | | **455.8** | 449.1 |

The financial statements were approved by the Board of Directors on 18 February 2010 and were signed on its behalf by:

**Mark Robertshaw,** Chief Executive Officer
**Kevin Dangerfield,** Chief Financial Officer

# Notes to the Company balance sheet

## 28. Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements.

### Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards, and under the historical cost accounting rules.

Under Section 408(4) of the Companies Act 2006 the Company is exempt from the requirement to present its own profit and loss account.

Under FRS 1 *Cash Flow Statements* the Company is exempt from the requirement to prepare a cash flow statement on the grounds that the cash flows of the Company are included within the published consolidated financial statement.

### Fixed assets and depreciation

Depreciation is provided to write off the cost less the estimated residual value of tangible fixed assets by equal instalments over their estimated useful economic lives as follows:

| | |
|---|---|
| Buildings | – 50 years |
| Motor vehicles | – 3 years |
| Fixtures | – 10-20 years |
| Computer software | – 3-6 years |

### Foreign currency

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction or, if hedged forward, at the rate of exchange under the related forward currency contract. Monetary assets and liabilities denominated in foreign currencies are translated using the contracted rate or the rate of exchange ruling at the balance sheet date and the gains or losses on translation are included in the profit and loss account.

### Leases

Rentals payable under operating leases are charged in the profit and loss account on a straight-line basis over the lease term.

### Post-retirement benefits

The Company participates in a Group-wide pension scheme providing benefits based on career average pensionable pay. The assets of the scheme are held separately from those of the Company. The Company is unable to identify its share of the underlying assets and liabilities of the scheme on a consistent and reasonable basis and therefore, as required by FRS 17 *Retirement Benefits*, accounts for the scheme as if it were a defined contribution scheme. As a result, the amount charged to the profit and loss account represents the contributions payable to the scheme in respect of the accounting period. Refer to note 40 for the additional disclosures required by FRS 17.

### Taxation

The charge for taxation is based on the result for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19 *Deferred Tax*.

### Classification of financial instruments issued by the Company

Following the adoption of FRS 25 *Financial Instruments: Disclosure and Presentation*, financial instruments issued by the Company are treated as equity (ie forming part of shareholders' funds) only to the extent that they meet the following two conditions:

a) they include no contractual obligations upon the Company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Company; and

b) where the instrument will or may be settled in the Company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the Company's own equity instruments or is a derivative that will be settled by the Company exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the Company's own shares, the amounts presented in these financial statements for called up share capital and share premium account exclude amounts in relation to those shares.

Finance payments associated with financial liabilities are dealt with as part of interest payable and similar charges. Finance payments associated with financial instruments that are classified as part of shareholders' funds (see dividend policy) are dealt with as appropriations in the reconciliation of movements in shareholders' funds.

## 28. Accounting policies continued

Hedging instruments and hedged items are accounted for separately in the balance sheet. Gains and losses on both are included in profit for the year when they arise (fair value hedges) or when the hedged transaction occurs, having first recorded those on the hedging instrument in equity (cash flow hedges, to the extent effective).

Certain financial assets and liabilities have been designated as fair value through profit or loss and are recognised in the balance sheet at fair value. Changes in the fair value of such instruments during the year were recognised immediately in the profit and loss account.

### Own shares held by ESOP trust

Transactions of the Group-sponsored ESOP trust are treated as being those of the Company and are therefore reflected in the Company's financial statements. In particular, the trust's purchases and sales of shares in the Company are debited and credited to equity.

### Share-based payments

The share option programme allows employees to acquire shares of the Company. The fair value of options granted after 7 November 2002 and those not yet vested as at 4 January 2005 is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employee becomes unconditionally entitled to the options. The fair value of the options granted is measured using an option pricing model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest except where forfeiture is only due to share prices not achieving the threshold for vesting. For details of share-based payments made and the assumptions used in measuring the fair value see note 20.

Share-based payments recharged to subsidiary undertakings are recorded via the inter-company loan account.

### Dividends on shares presented within shareholders' funds

Dividends unpaid at the balance sheet date are only recognised as a liability at that date to the extent that they are appropriately authorised and are no longer at the discretion of the Company. Unpaid dividends that do not meet these criteria are disclosed in the notes to the financial statements.

### Financial guarantee contracts

Where the Company enters into financial guarantee contracts to guarantee the indebtedness of other companies within its group, the Company considers these to be insurance arrangements, and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee.

## 29. Staff numbers and costs

The average number of persons employed by the Company (including Directors) during the year, analysed by category, was as follows:

| | Number of employees 2009 | 2008 |
|---|---|---|
| Directors and head office staff | **23** | 21 |
| Global business units' staff | **13** | 14 |
| | **36** | 35 |

The majority of the Directors and head office staff devote a proportion of their time to global business duties. Of the 23 Directors and head office staff, the average number who spent all or a proportion of their time on corporate duties was eight (2008: eight) as shown in note 5.

The aggregate payroll costs of these persons were as follows:

| | 2009 £m | 2008 £m |
|---|---|---|
| Wages and salaries | **4.9** | 6.0 |
| Share-based payments (see note 20) | **2.0** | 2.2 |
| Social security costs | **1.1** | 1.4 |
| Other pension costs | **0.6** | 0.8 |
| Total overhead employee cost | **8.6** | 10.4 |

# Notes to the Company balance sheet
continued

### 30. Dividends

Dividends payable for the First and Second Preference shares were £22,491 (2008: £22,491) of which £11,245 (2008: £11,244) was outstanding at the balance sheet date.

For proposed Ordinary dividends see the consolidated income statement on page 88.

### 31. Tangible assets

| | Plant, equipment and fixtures £m |
|---|---|
| **Cost** | |
| At 5 January 2009 | **4.0** |
| Additions | **0.1** |
| **At 3 January 2010** | **4.1** |
| **Accumulated depreciation** | |
| At 5 January 2009 | **1.8** |
| Amount provided for in the year | **0.5** |
| **At 3 January 2010** | **2.3** |
| **Net book amounts at 3 January 2010** | **1.8** |
| Net book amounts at 4 January 2009 | 2.2 |

### 32. Investment in subsidiary undertakings

| | Shares £m | Loans £m | Total £m |
|---|---|---|---|
| **Cost** | | | |
| At 5 January 2009 | **587.8** | **155.4** | **743.2** |
| Additions | **66.6** | **81.9** | **148.5** |
| Less: disposals/loan repayments/liquidations | **(10.8)** | **(39.2)** | **(50.0)** |
| **At 3 January 2010** | **643.6** | **198.1** | **841.7** |
| **Amounts provided** | | | |
| At 5 January 2009 | **45.7** | **3.7** | **49.4** |
| Provided in the year | **1.6** | **–** | **1.6** |
| **At 3 January 2010** | **47.3** | **3.7** | **51.0** |
| **Net book amounts at 3 January 2010** | **596.3** | **194.4** | **790.7** |
| Net book amounts at 4 January 2009 | 542.1 | 151.7 | 693.8 |

A list of principal subsidiary undertakings is shown in note 43.

## 33. Other investments

| | £m |
|---|---|
| At 5 January 2009 | **5.1** |
| Amounts received from subsidiary undertakings | **(5.1)** |
| **At 3 January 2010** | **–** |

## 34. Debtors

| | 2009 £m | 2008 £m |
|---|---|---|
| **Due within one year:** | | |
| Other debtors | **1.9** | 0.6 |
| Interest receivable from associate | **–** | 5.6 |
| Derivative financial assets | **1.0** | 4.2 |
| Prepayments and accrued income | **0.7** | 0.7 |
| Amounts receivable from subsidiary undertakings | **33.3** | 52.1 |
| | **36.9** | 63.2 |
| **Due after one year:** | | |
| Loan to associate | **–** | 36.0 |
| Prepayments and accrued income | **–** | 0.5 |
| Derivative financial assets | **–** | 0.8 |
| | **–** | 37.3 |

## 35. Creditors

| | 2009 £m | 2008 £m |
|---|---|---|
| **Due within one year:** | | |
| Bank overdrafts | **8.5** | 8.6 |
| Trade creditors | **1.0** | 1.9 |
| Amounts payable to subsidiary undertakings | **14.7** | 8.1 |
| Other creditors, including deferred consideration | **29.0** | 0.6 |
| Accruals and deferred income | **4.8** | 7.9 |
| Derivative financial liabilities | **5.5** | 15.4 |
| | **63.5** | 42.5 |
| **Due after one year:** | | |
| Other creditors, including deferred consideration | **27.6** | – |
| Derivative financial liabilities | **4.1** | 0.8 |
| | **31.7** | 0.8 |

## 36. Borrowings

| | 2009 £m | 2008 £m |
|---|---|---|
| Bank and other loans | **105.4** | 136.1 |
| Bank overdrafts | **8.5** | 8.6 |
| | **113.9** | 144.7 |
| Less: amount repayable within one year included within current liabilities | **(8.5)** | (8.6) |
| Total repayable after more than one year | **105.4** | 136.1 |

# Notes to the Company balance sheet
continued

### 37. Provisions for liabilities and charges

| | Closure and restructuring provisions £m | Other provisions £m | Environmental provisions £m | Total £m |
|---|---|---|---|---|
| At 5 January 2009 | **2.4** | **0.9** | **1.4** | **4.7** |
| Provided in the year | **–** | **0.7** | **–** | **0.7** |
| Utilised in the year | **(0.3)** | **(0.9)** | **–** | **(1.2)** |
| Released in the year | **–** | **–** | **(1.4)** | **(1.4)** |
| **At 3 January 2010** | **2.1** | **0.7** | **–** | **2.8** |

Closure and restructuring provisions relate mainly to an onerous lease provision for Morgan House, the Company's previous registered address.

Other provisions include the settlement of European class actions, together with the associated legal costs.

### 38. Share premium and reserves

| | Share premium £m | Merger reserve £m | Capital redemption reserve £m | Profit and loss account £m |
|---|---|---|---|---|
| At 5 January 2009 | **85.3** | **17.0** | **35.7** | **243.2** |
| Charges and transfers in relation to share-based payments for the year | **–** | **–** | **–** | **2.3** |
| Dividends | **–** | **–** | **–** | **(12.1)** |
| Retained profit for the year | **–** | **–** | **–** | **16.5** |
| | **85.3** | **17.0** | **35.7** | **249.9** |

HSBC Trustee (C.I.) Limited administer a Trust in which shares are held to satisfy awards granted under the Company's share plans. The shares are distributed in a discretionary settlement governed by the rules of the Trust deed dated 1 March 1996 (as amended).

The total number of own shares held by the Trust at 3 January 2010 is 1,984,022 (2008: 2,593,799) and at that date had a market value of £3,194,275 (2008: £3,157,950).

The amount of reserves of The Morgan Crucible Company plc that may not be distributed under Section 831(4) of the Companies Act 2006 is £139.7 million (2008: £139.7 million).

### 39. Leasing commitments

Operating lease commitments falling due during the next year, for which no provision has been made in these accounts, are:

| | Land and buildings 2009 £m | 2008 £m |
|---|---|---|
| Less than one year | **–** | 0.1 |
| Between one and five years | **0.2** | 0.2 |
| More than five years | **0.5** | 0.5 |
| | **0.7** | 0.8 |

### 40. Pension costs

**The Morgan Pension Scheme and The Morgan Senior Staff Pension and Life Assurance Scheme**

The Company participates in two defined benefit schemes in the UK. The assets of these schemes are held in separate trustee-administered funds, The Morgan Pension Scheme ('MPS') and The Morgan Group Senior Staff Pension and Life Assurance Scheme ('SSS'). Given that the Company is unable to identify its share of the scheme assets and liabilities on a consistent and reasonable basis, as permitted by FRS 17 *Retirement Benefits*, the schemes have been accounted for in these financial statements as if they were defined contribution schemes.

## 40. Pension costs continued

The latest actuarial valuations of the MPS and the SSS were carried out as at 6 April 2006 and 1 April 2006 respectively, and updated for FRS 17 purposes to 31 December 2009 by a qualified independent actuary. The results for these schemes in respect of the Group are shown below:

| | 2009 % | 2008 % |
|---|---|---|
| **Assumptions:** | | |
| RPI inflation | **3.50** | 2.80 |
| Discount rate | **5.80** | 6.50 |
| Pension increases in payment | **3.40/3.40** | 2.60/3.15 |
| General salary increases | **n/a** | n/a |

The assets in the scheme and the expected rates of return were:

| | 2009 Expected return % | 2009 £m | 2008 Expected return % | 2008 £m |
|---|---|---|---|---|
| **Asset distribution and balance sheet reconciliation:** | | | | |
| Equities | **8.4** | **125.0** | 8.0 | 97.8 |
| Bonds | **5.3** | **6.4** | 5.0 | 7.1 |
| Property | **6.4** | **–** | 5.8 | 4.9 |
| Other | **5.8** | **167.5** | 3.8 | 155.6 |
| Total market value of assets | | **298.9** | | 265.4 |
| Present value of liability | | **(333.4)** | | (278.5) |
| Deficit in the scheme | | **(34.5)** | | (13.1) |
| Employer contributions due within one year | | **(0.1)** | | (0.1) |

Other assets include an insurance policy as described in note 20.

The contribution for the year was £4.7 million (2008: £6.4 million).

## 41. Contingent liabilities

Where the Company enters into financial guarantee contracts to guarantee the indebtedness of other companies within its Group, the Company considers these to be insurance arrangements, and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee.

There are no other contingent liabilities in the Company as at 3 January 2010.

The Group has been subject to legal claims in the USA, Canada and Europe. Settlements for the majority of these have been agreed. There remain provisions in respect of these claims of £0.7 million (2008: £2.3 million). The Board, having taken legal advice, is of the opinion that the remainder of these actions will not have a material impact on the Group's financial position.

## 42. Related parties

The Company's transactions with non-wholly owned subsidiaries are as follows:

| | 2009 £m | 2008 £m |
|---|---|---|
| Amounts invoiced to non-wholly owned subsidiaries | **0.7** | 0.7 |
| Amounts receivable from non-wholly owned subsidiaries | **4.1** | 0.8 |

The Directors have reviewed transactions with related parties (as defined in FRS 8 *Related Party Disclosures*) and have concluded that there are no other material transactions which require disclosure which have not been acknowledged elsewhere in the Annual Report and Accounts.

# Notes to the Company balance sheet
continued

### 43. Principal subsidiary undertakings

| | | Country of incorporation and principal place of business |
|---|---|---|
| **Carbon companies** | | |
| | Shanghai Morgan Carbon Co. Ltd. | China |
| | Shanghai Morganite Electrical Carbon Co. Ltd. | China |
| | Morganite Electrical Carbon Limited | England |
| * | NP Aerospace Limited | England |
| * | Morgan Rekofa GmbH | Germany |
| * | Morgan Materials Hungary Kft. | Hungary |
| * | Assam Carbon Products Ltd. | India |
| * | Morgan Carbon Italia s.r.l. | Italy |
| * | Morganite Carbon Kabushiki Kaisha | Japan |
| * | Morganite Luxembourg S.A. | Luxembourg |
| * | National Electrical Carbon B.V. | Netherlands |
| * | Morganite South Africa Pty. Limited | South Africa |
| * | Morgan Advanced Materials and Technology Inc. | USA |
| * | National Electrical Carbon Products Inc. | USA |
| * | Graphite Die Mold Inc. | USA |
| **Insulating Ceramics companies** | | |
| * | Carbo San Luis S.A. | Argentina |
| | Dalian Morgan Refractories Limited | China |
| | Morgan Thermal Ceramics International Trading (Shanghai) Co. Ltd. | China |
| | Morgan Thermal Ceramics Shanghai Ltd. | China |
| | Yixing Morgan Thermal Ceramics Co. Ltd. | China |
| | Morganite Crucible Limited | England |
| | Thermal Ceramics UK Limited | England |
| * | Thermal Ceramics de France S.A.S. | France |
| * | Carl Nolte Söhne GmbH | Germany |
| * | Thermal Ceramics Deutschland GmbH & Co. K.G. | Germany |
| * | Ciria India Ltd. | India |
| * | Morganite Crucible (India) Limited | India |
| | Murugappa Morgan Thermal Ceramics Limited | India |
| * | Thermal Ceramics Italiana s.r.l. | Italy |
| | Shin-Nippon Thermal Ceramics Corporation | Japan |
| * | Limited Liability Company Morgan Thermal Ceramics Sukhoy Log | Russia |
| | Thermal Ceramics Asia Pte. Ltd. | Singapore |
| * | Thermal Ceramics South Africa Pty. Limited | South Africa |
| * | Thermal Ceramics Espana S.L. | Spain |
| * | Morganite Crucible Inc. | USA |
| * | Thermal Ceramics Inc. | USA |
| **Technical Ceramics companies** | | |
| * | Morgan Technical Ceramics Australia Pty. Ltd. | Australia |
| * | Yixing Haldenwanger Fine Ceramic Co. Ltd. | China |
| | Certech International Limited | England |
| | Morgan Advanced Ceramics Limited | England |
| | Morgan Electro Ceramics Limited | England |
| * | W. Haldenwanger Technische Keramik GmbH & Co. K.G. | Germany |
| | Wesgo Ceramics GmbH | Germany |
| * | Morgan Technical Ceramics S.A. de C.V. | Mexico |
| * | Certech Inc. | USA |
| * | Morgan Advanced Ceramics Inc. | USA |
| * | Morgan Technical Ceramics Auburn Inc. | USA |

* Denotes companies some or all of whose shares are owned by a subsidiary.

## 43. Principal subsidiary undertakings continued

| | Country of incorporation and principal place of business |
|---|---|
| **Other subsidiary undertakings** | |
| * Morganite Australia Pty Limited | Australia |
| * Morganite Brasil Limitada | Brazil |
| * Morganite Canada Corporation | Canada |
| Grupo Industrial Morgan S.A. de C.V. | Mexico |
| Morgan Korea Company Limited | South Korea |
| Morganite Industries Inc. | USA |

* Denotes companies some or all of whose shares are owned by a subsidiary.

In 2009 and 2008 the following German subsidiaries, which are included in the Group consolidated accounts, utilised article 264b of the German Commercial Code to be liberated from preparing and disclosing audited statutory accounts:

- W Haldenwanger Technische Keramik GmbH & Co K.G.
- Technische Keramik & Co K.G.
- Thermal Ceramics Deutschland GmbH & Co K.G.

## 44. Company reconciliation of movements in shareholders' funds
for the year ended 3 January 2010

| | **2009 £m** | 2008 £m |
|---|---|---|
| **Retained profit/(loss) for the financial year** | **16.5** | (23.5) |
| Dividends | **(12.1)** | (18.7) |
| Purchase of shares for share incentive schemes | **–** | 0.4 |
| Charge in relation to share-based payments | **2.3** | 3.2 |
| Share buy-back | **–** | (12.1) |
| **Net increase/(decrease) in shareholders' funds** | **6.7** | (50.7) |
| Opening shareholders' funds | **449.1** | 499.8 |
| **Closing shareholders' funds** | **455.8** | 449.1 |

# Group statistical information
## Under adopted IFRSs

| | 2005 £m | 2006 £m | 2007 £m | 2008 £m | **2009 £m** |
|---|---|---|---|---|---|
| **Revenue** | 745.7 | 677.8 | 693.2 | 835.0 | **942.6** |
| **Profit from operations before restructuring costs, other one-off items and amortisation of intangible assets** | 67.3 | 74.9 | 88.1 | 108.8 | **89.0** |
| **Restructuring costs and other one-off items:** | | | | | |
| Restructuring costs and costs associated with settlement of prior period anti-trust litigation | (32.0) | (27.7) | (9.0) | (11.4) | **(14.0)** |
| Gain on curtailment of UK employee benefit schemes | – | 11.0 | – | – | **–** |
| Terminated bid approach costs | – | (2.1) | – | – | **–** |
| Profit/(loss) on disposal of property | (0.4) | 0.3 | (0.2) | 0.8 | **2.0** |
| **Profit from operations before amortisation of intangible assets** | 34.9 | 56.4 | 78.9 | 98.2 | **77.0** |
| Amortisation of intangible assets | (1.3) | (1.2) | (1.6) | (3.2) | **(16.3)** |
| **Operating profit** | 33.6 | 55.2 | 77.3 | 95.0 | **60.7** |
| Net financing costs | (13.1) | (3.4) | (5.5) | (12.7) | **(29.3)** |
| Loss on disposal of businesses | (0.1) | (1.5) | (0.3) | (0.7) | **–** |
| Share of profit of associate (net of income tax) | – | – | 0.2 | 1.2 | **–** |
| **Profit before taxation** | 20.4 | 50.3 | 71.7 | 82.8 | **31.4** |
| Income tax expense | (8.8) | (10.6) | (15.2) | (20.1) | **(8.7)** |
| **Profit after taxation but before gain on sale of discontinued operations** | 11.6 | 39.7 | 56.5 | 62.7 | **22.7** |
| Gain on sale of discontinued operations, net of tax | 42.6 | – | – | – | **–** |
| **Profit for the period** | 54.2 | 39.7 | 56.5 | 62.7 | **22.7** |
| **Assets employed** | | | | | |
| Property, plant and equipment | 235.3 | 230.2 | 246.6 | 319.6 | **276.2** |
| Intangible assets | 46.6 | 66.4 | 69.8 | 177.0 | **296.9** |
| Investments and other receivables | 6.4 | 8.4 | 49.5 | 50.6 | **9.3** |
| Deferred tax assets | 27.4 | 28.8 | 25.8 | 36.6 | **37.2** |
| Net current assets | 94.2 | 44.0 | 74.4 | 189.9 | **136.5** |
| **Total assets less current liabilities** | 409.9 | 377.8 | 466.1 | 773.7 | **756.1** |
| Employee benefits | 124.2 | 42.7 | 47.7 | 101.8 | **105.9** |
| Provisions and other items | 61.9 | 103.6 | 202.9 | 423.1 | **388.1** |
| Deferred tax liabilities | 28.1 | 28.4 | 19.2 | 40.8 | **47.5** |
| | 195.7 | 203.1 | 196.3 | 208.0 | **214.6** |
| **Equity** | | | | | |
| Total equity attributable to equity holders of the parent Company | 182.3 | 186.7 | 176.2 | 177.8 | **184.6** |
| Minority interest | 13.4 | 16.4 | 20.1 | 30.2 | **30.0** |
| Total equity | 195.7 | 203.1 | 196.3 | 208.0 | **214.6** |
| **Ordinary dividends per share (paid)** | 2.5p | 4.5p | 6.75p | 7.0p | **4.5p** |
| **Earnings per share** | | | | | |
| Basic | 18.1p | 12.9p | 19.1p | 22.2p | **7.1p** |
| Diluted | 17.2p | 12.3p | 18.5p | 21.6p | **6.8p** |
| Basic before amortisation of intangible assets | 18.6p | 13.3p | 19.7p | 23.4p | **13.2p** |
| Diluted before amortisation of intangible assets | 17.7p | 12.7p | 19.1p | 22.8p | **12.6p** |

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**The Morgan Crucible Company plc**
Quadrant, 55-57 High Street
Windsor, Berkshire SL4 1LP
Tel: +44 (0)1753 837000
Fax: +44 (0)1753 850872

www.morgancrucible.com