

Chairman and Chief Executive's statement



David Gawler
Chairman and Chief Executive

Summary of results

	Year ended 31 December	
	2004 £m	2003 £m
Turnover		
Continuing operations	870.4	842.4
Discontinued operations	-	28.8
	<u>870.4</u>	<u>871.2</u>
Operating profit		
Continuing operations:		
Adjusted operating profit ⁽ⁱ⁾	54.3	30.0
Goodwill amortisation	(1.2)	(1.2)
Operating exceptional items	(19.2)	(9.9)
	<u>33.9</u>	<u>18.9</u>
Discontinued operations	0.6	10.1
Operating exceptional items	-	(0.9)
Operating profit	<u>34.5</u>	<u>28.1</u>
Non-operating exceptional items	5.2	(1.0)
Profit before interest	<u>39.7</u>	<u>27.1</u>
Net interest	(11.6)	(16.8)
Exceptional financing costs	-	(6.5)
Profit before tax	<u>28.1</u>	<u>3.8</u>
Net debt	<u>66.5</u>	<u>136.8</u>
Earnings/(loss) per share - basic		
Headline	10.4p	(6.2)p
Adjusted ⁽ⁱ⁾	16.0p	9.9p

*(i) before exceptional items and amortisation of goodwill
Earnings per share calculations for 2003 have been restated for the rights issue*

Financial overview

I am pleased to report that 2004 has been a highly successful year for the Company. After four years of restructuring and cost cutting, asset and business disposals, together with unremitting renegotiations with lenders, Charter has emerged as a healthier and much transformed company. In 2004 it achieved an adjusted operating profit of £54.3 million, an 81 per cent improvement over the level of last year, halved net debt from £136.8 million to £66.5 million and generated free cash flow for the second year in succession. The Company also settled a dispute with US loan note holders and completed a rights issue, which raised £44.6 million net of costs. Such actions have strengthened the Company's balance sheet, enabled the Group to resume its restructuring programme and to invest in the core businesses.

Since the year end, the Company cancelled the onerous syndicated banking facility, which it replaced with a new bank facility provided by HSBC on conventional banking terms.

Overview of Group results

In the year ended 31 December 2004 turnover from continuing businesses increased to £870.4 million (2003: £842.4 million).

The adjusted operating profit from continuing businesses, before exceptional items and amortisation of goodwill, increased by 81 per cent to £54.3 million (2003: £30.0 million).

The welding and cutting business ("Esab") produced excellent results during the year, with adjusted operating profits of £48.7 million, compared with £31.8 million in 2003, an increase of 53 per cent. Particularly pleasing was the significant improvement in operating margins to 7.8 per cent, as compared with 5.5 per cent in 2003.

During the year the air and gas handling business ("Howden") also produced excellent results, with adjusted operating profits of £15.1 million, compared with £6.3 million in 2003, an increase of 140 per cent. Operating profit of £11.1 million in the second half of 2004 was excellent and £7.1 million better than was achieved in the first half of the year. Although turnover declined in the year to £241.6 million

(2003: £256.9 million), operating margins improved satisfactorily from 2.5 per cent in 2003 to 6.3 per cent in 2004. Howden's order intake during the year was stronger than in previous years and orders in hand at year end were £181.0 million, 57 per cent ahead of last year.

During the year the continuing specialised engineering businesses comprised two small non-core businesses that generated turnover of £7.3 million (2003: £8.4 million) and recorded operating losses of £2.1 million (2003: losses of £1.3 million).

The operating profit on discontinued operations of £0.6 million is in respect of Esab's 50 per cent interest in GCE Gas Control Equipment AB ("GCE"), which was sold in February 2004 for £14.3 million.

Central costs were £7.4 million in 2004 compared with £6.8 million last year.

During the year the net charge for exceptional items totalled £14.0 million before taxation and minority interests (2003: £18.3 million). These charges were incurred mainly in connection with restructuring initiatives, but were partially offset by profits on disposals of assets.

The charge for operating exceptional items in 2004 was £19.2 million (2003: £10.8 million) and comprised £12.8 million of restructuring costs, £4.5 million (net) in respect of unauthorised payments and £1.9 million of legal and environmental costs, offset in part by a £5.2 million non-operating exceptional credit arising on disposals. Non-operating exceptional gains of £5.2 million arose on disposals (2003: a non-exceptional charge of £1.0 million). There were no exceptional financing costs in 2004 (2003: £6.5 million). A full analysis of exceptional items appears on page 4.

The group's profit on ordinary activities before tax amounted to £28.1 million (2003: £3.8 million), its ordinary tax charge was £13.6 million (2003: £7.1 million) and the tax credit attributable to the exceptional items was £0.5 million (2003: £0.2 million). During the year an exceptional tax credit of £6.6 million arose following settlement of certain specific tax issues. After charging minority interests of £6.8 million (2003: £4.3 million), the retained profit for the year was £14.8 million (2003: a retained loss of £7.4 million).

Adjusted earnings per share increased by 62 per cent to 16.0 pence (2003: 9.9 pence) and the headline earnings per share amounted to 10.4 pence (2003: loss per share of 6.2 pence). The comparative earnings per share for 2003 have been adjusted for the rights issue.

During the course of the year equity shareholders' funds rose to £75.7 million, an increase of £71.3 million.

Cash flow and borrowings

A rights issue in February 2004 raised £44.6 million, net of costs, and the sale of Esab's 50 per cent interest in GCE was completed for a consideration of £14.3 million.

The cash inflow from operating activities for the year was £47.5 million (2003: £54.9 million), which was after expenditures on restructuring of £15.2 million (2003: £19.2 million). Capital expenditure was £10.0 million (2003: £7.1 million). The depreciation and amortisation charge was £17.4 million (2003: £19.9 million). Net proceeds from the sale of fixed assets amounted to £2.9 million (2003: £16.6 million). Excluding the sale of GCE, net expenditure of £4.7 million was incurred on acquisitions and disposals in the year whereas in 2003 disposals of subsidiary undertakings generated £26.5 million.

Net debt, which was £136.8 million at 31 December 2003, had been reduced to £66.5 million by 31 December 2004 reflecting a net cash inflow of £70.3 million, including an exchange gain of £2.8 million.

As a result of lower average daily borrowing levels during the year, the interest charge (excluding exceptional financing costs) was £11.6 million, which was £5.2 million lower than the £16.8 million incurred in 2003. Exceptional financing costs were £nil (2003: £6.5 million).

Refinancing

During 2004, the group met its day to day working capital requirements through borrowings under a syndicated revolving credit facility. At 31 December 2004, £73.3 million was available under the syndicated facility, of which £37.3 million was drawn.

On 21 March 2005 the Company cancelled the syndicated facility and replaced it with a two year £50 million credit facility, expiring on 31 March 2007, with an option to extend for a further three months.

US loan notes

In February 2004 the Company settled its dispute with the 2007 and 2009 US loan note holders, who had initiated proceedings in April 2003 against the Company and one of its subsidiaries. The 2007 loan notes of US\$85.0 million (£44.3 million) and the 2009 loan notes of US\$35.0 million (£18.2 million) are scheduled for repayment on 21 October 2007 and 21 October 2009 respectively and, following the settlement, the respective coupon rates payable under these notes are 7.38 per cent and 7.46 per cent.

South American business venture

On 2 September 2004 Esab concluded an agreement under which its effective interest in its South American business venture was increased from 41.7 per cent to 51.0 per cent. The purchase consideration of this incremental interest was US\$4.12 million (£2.25 million), of which US\$1.37 million (£0.75 million) was paid on completion. The balance is payable in instalments, the last of which is due in September 2007. As a result of this transaction the ownership, management and operations of the South American business venture have been simplified. The remaining business partner, Mercoweld S.A., with whom the Company has an excellent relationship, increased its shareholding from 38.0 per cent to 49.0 per cent on the same date.

Chairman and Chief Executive's statement

continued

Exceptional items

The exceptional items resulted in an overall charge in the year of £14.0 million (2003: £18.3 million) before tax and minority interests and comprised:

	Year ended 31.12.04 £m	Year ended 31.12.03 £m
Operating		
Continuing operations		
Restructuring		
Welding and cutting	(12.8)	(5.0)
Air and gas handling	-	(4.1)
Specialised engineering	-	(0.4)
	<u>(12.8)</u>	<u>(9.5)</u>
Unauthorised payments	(4.5)	-
Legal and environmental costs	(1.9)	(0.4)
	<u>(19.2)</u>	<u>(9.9)</u>
Discontinued operations		
Restructuring costs	-	(0.9)
	<u>(19.2)</u>	<u>(10.8)</u>
Non-operating		
Continuing operations		
Net (loss)/profit on sale of fixed assets	(0.3)	4.7
Profit/(loss) on sale or termination of operations	3.6	(0.3)
	<u>3.3</u>	<u>4.4</u>
Discontinued operations		
Profit on sale of operations before reinstatement of goodwill	5.7	18.8
Associated goodwill	(6.0)	(20.2)
Loss on sale of operations	(0.3)	(1.4)
Goodwill provision on discontinued operations	-	(4.0)
Additional costs in respect of disposals in prior years	(2.0)	-
Release of provisions in respect of disposals in prior years	4.2	-
	<u>1.9</u>	<u>(5.4)</u>
	5.2	(1.0)
Exceptional financing costs	-	(6.5)
Total exceptional items before tax and minority interests	<u>(14.0)</u>	<u>(18.3)</u>

Restructuring costs

The restructuring of Esab's businesses and the rationalisation of its global manufacturing capacity have continued during 2004.

Restructuring costs in Esab of £12.8 million were provided in 2004 in connection with the full cost of its restructuring and reorganisation of certain of its European businesses. The greater part of this project was implemented during the year and will be completed in 2005. The improvements to operational efficiencies and business processes

in Europe have resulted in reduced operating costs of around £3.9 million in the second half of 2004 and it is expected that further costs savings of £6.6 million should occur in the 2005 financial year.

There were no restructuring costs in Howden during 2004.

Unauthorised payments

On 20 August 2004 the Company announced that an employee had been involved in a fraud against the group by making a series of unauthorised payments of some £9.2 million. The Company's insurance provider, AIG Europe (UK) Limited, accepted the Company's claim and, subsequent to the year end, paid the Company £5.0 million, being the limit under the Company's fidelity insurance policy. The exceptional charge of £4.5 million in 2004 (2003: £nil) therefore comprises the net cost of £4.2 million in respect of the unauthorised payments, together with professional fees. Of the £9.2 million of unauthorised payments, £5.0 million were made prior to 1 January 2004 and this amount has been treated as a credit in the Statement of Total Recognised Gains and Losses.

The Company brought proceedings and obtained judgement against the employee and is in the process of realising his assets, which are unlikely to produce in excess of £100,000 after costs. The employee was convicted of theft on 10 December 2004 and sentenced on 25 January 2005 to five years imprisonment.

There are a number of other potential sources of recovery available to the Company, which it is pursuing.

Under the terms of its fidelity insurance policy, the Company is entitled to recover the balance of its costs and uninsured losses before its insurance provider is entitled, by subrogation, to recover what it has paid to the Company.

During the year, the Company strengthened its financial controls at both the corporate and subsidiary levels.

Legal and environmental costs

A provision has been made of £1.9 million in respect of costs of environmental remediation regarding a vacant property in the United States, which has not been used by Howden for many years.

Non-operating exceptional items

The exceptional loss on the sale of fixed assets amounted to £0.3 million (2003: profit £4.7 million).

During the year a non-operating exceptional credit of £3.6 million arose (2003: a charge of £0.3 million). The 2004 credit arose on the release of a disposal provision no longer required.

The sale of the group's 50 per cent interest in GCE was completed on 26 February 2004. A non-operating exceptional profit of £5.7 million arose on the sale of this business, which was offset by the write back of the balance of goodwill on the acquisition of GCE of £6.0 million. A provision of £4.0 million in 2003 had also been made against the write back of goodwill of GCE.

In respect of prior year disposals, additional provisions of £2.0 million have been made, offset by a release of provisions of £4.2 million.

Taxation

The effective adjusted tax rate for the year is 31.5 per cent (2003: 30.5 per cent). Following the settlement of certain specific

outstanding tax issues with the Inland Revenue, an exceptional tax credit of £6.6 million arose in 2004. The tax credit attributable to exceptional items amounted to £0.5 million (2003: £0.2 million).

Retirement benefits

At 31 December 2004, the group's balance sheet reflected net provisions of £32.8 million (2003: £31.4 million) in respect of unfunded pension liabilities. There was a further net provision of £17.5 million (2003: £26.7 million) in respect of the group's liability for estimated future overseas medical costs.

If provision for the group's net pension deficit of £106.7 million (2003: £96.8 million) and that for the group's estimated future overseas medical costs of £22.9 million (2003: £26.7 million), calculated in accordance with FRS17, had been incorporated in the consolidated balance sheet at year end, net assets would have decreased by £79.3 million (2003: £65.4 million). The increase in this provision arose principally from changes in mortality rate assumptions.

Contingent liabilities

As disclosed in the Company's annual report and accounts in recent years The ESAB Group Inc. ("Esab"), a subsidiary of the Company, in common with other companies in the welding products industry, has been named as a defendant in a number of lawsuits in State and Federal courts in the United States alleging personal injuries from exposure to manganese in the fumes of welding consumables, some of which are due to be tried this year. Whilst litigation is notoriously uncertain, on the advice of Esab's counsel in the United States, the directors believe that Esab has meritorious defences to these claims, most of which should be covered in whole or in part by insurance, and Esab is defending these claims vigorously.

International Financial Reporting Standards ('IFRS')

The group is required to adopt IFRS in the preparation of its consolidated financial statements with effect from 1 January 2005. Therefore the group will issue its interim results for the period ending 30 June 2005 in accordance with IFRS. Comparative figures will be restated accordingly and the restated 2004 results and financial position will be issued during the second quarter of 2005.

The Standards that are expected to have the most impact on the group are:

- IAS 19 ('Employee Benefits') which will lead to the recognition of additional pension and other post retirement liabilities on a basis similar, but not identical, to those currently disclosed under FRS 17;
- IAS 21 ('The Effects of Changes in Foreign Exchange Rates') which may lead to certain gains and losses on foreign exchange currently recognised in reserves affecting the profit and loss account and might mean greater profit volatility in the future;
- IAS 38 ('Intangible Assets') which will lead to the recognition on the balance sheet of internal development costs that meet the recognition criteria of the standard; and
- IFRS 3 ('Business Combinations'), which does not allow an annual charge for the amortisation of goodwill.

In addition certain options available under IFRS 1 ('First-time Adoption of International Financial Reporting Standards') remain under review. In particular the Group may choose to revalue certain properties on transition to IFRS, with such revaluations treated as deemed cost in the future.

The analysis of the impact of IFRS is being prepared on the basis of the knowledge of the expected standards and interpretations expected to be effective, and the accounting policies expected to be adopted, when the first set of IFRS financial statements are prepared for 2005. Therefore as these interpretations develop there is a possibility that this analysis may evolve further.

Dividends

The Board has decided not to declare a dividend for the year ended 31 December 2004.

Board

There were a number of changes to the Charter Board during the year. Robert Careless was appointed Finance Director on 22 April 2004, replacing David Eilbeck who resigned on that date. Michael Foster, who had been a Non-Executive Director since December 2001, was appointed Commercial Director on 1 January 2005. Homi Mullan, the Senior Non-Executive Director and Chairman of the Audit and Remuneration Committees resigned on 6 December 2004 and was succeeded in these roles by the Hon. James Bruce on that date. Subsequent to the year end, the Company has appointed three new Non-Executive Directors. Grey Denham and Andrew Osborne joined the Board on 8 February 2005 and, as announced separately today, John Biles will join the Board with effect from 1 April 2005.

Prospects

Restructuring and cost cutting initiatives over the past four years have resulted in improved operational efficiencies as evidenced by the significant increases in operating margins at Esab and Howden. These core businesses are now better placed to benefit from the improving conditions and opportunities in their key markets. Net debt was reduced by £70.3 million and the Company ended the year in a much stronger financial condition than it has enjoyed in the recent past.

In the light of the 2004 results, trading to date and the incremental restructuring benefits expected this year, the Board views the outlook for 2005 with confidence.

David Gawler
Chairman and Chief Executive
23 March 2005