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News release

London, Wednesday 19 March 2014
For immediate release

Interim results for the six months ended 31 January 2014

	Headline*				Statutory†	
	2014 £m	2013 £m	Reported	Underlying#	**2014 £m**	2013 £m
Revenue	**1,442**	1,475	(2)%	(1)%	**1,442**	1,475
Operating profit	**245**	253	(3)%	(2)%	**170**	211
Operating margin	**17.0%**	17.1%	(10) bps	–	**11.8%**	14.3%
Pre-tax profit	**215**	223	(4)%	(3)%	**132**	166
Basic EPS	**39.5p**	40.9p	(4)%		**23.7p**	30.7p
Free cash-flow	**30**	71				
Dividend	**12.75p**	12.50p	2%		**12.75p**	12.50p
Return on capital employed	**16.6%**	16.7%	(10) bps			

*In addition to statutory reporting, Smiths Group reports its continuing operations on a headline basis. Headline revenue and profit is before exceptional items, amortisation and impairment of acquired intangible assets, pension charges and financing gains/losses from currency hedging. Free cash-flow and return on capital employed are described in the Financial review.

†The statutory figures for 2013 have been restated for IAS 19 (revised 2011).

#Organic growth at constant currency.

Highlights

- Company-funded investment in new product development up 7% to £57m
- Strong headline operating cash conversion at 86%
- Dividend up 2%; reflecting continued strong cash generation
- Strength in commercial markets offset by challenging healthcare and defence markets
- John Crane and Flex-Tek report underlying revenue and margin growth
- Medical generated strong cash; margin affected by volume, price pressure and device tax
- New divisional medium-term operating ranges for revenue growth and margins

"We made good progress in our businesses that serve commercial customers, while those with significant government and healthcare exposure continued to face challenging trading conditions. Underlying revenue and margins advanced in John Crane and Flex-Tek but were primarily offset by declines in Smiths Medical. Smiths Interconnect and Smiths Detection saw more modest reductions compared against strong prior periods.

"We continue to focus on operational improvements to support investment in both high growth markets and new products to accelerate medium-term revenue growth. We have outlined mid-term operating ranges for revenue growth and headline operating margin for each of the divisions. We also provide further details of our '*Fuel for Growth*' programme scheduled to generate £60m of annual savings by 2017 to reinvest in growth initiatives.

"We anticipate improved underlying trading in the second half driven by a strong John Crane order book, some recovery in Smiths Interconnect and further growth in Flex-Tek. Smiths Detection will continue to be affected by government budget pressures. Smiths Medical is expected to continue to face tough trading. At current rates, foreign exchange headwinds will increase in the second half, with a 4-5% impact on full year earnings. We will maintain our focus on investing to drive sales growth in what are attractive long-term markets, and delivering further operational improvements, while providing strong cash conversion and returns."

Philip Bowman
Chief Executive

Divisional highlights*

	% of Group headline revenue	Underlying headline revenue growth*	Underlying headline operating profit growth*	Headline operating profit margin		Return on capital employed	
				2014	2013	**2014**	2013
John Crane	32%	**2%**	**9%**	**23.2%**	21.8%	**26.5%**	24.3%
Smiths Medical	27%	**(4)%**	**(18)%**	**18.3%**	21.1%	**15.3%**	16.9%
Smiths Detection	17%	**(1)%**	**(7)%**	**11.8%**	12.0%	**8.6%**	12.2%
Smiths Interconnect	15%	**(4)%**	**(7)%**	**13.1%**	13.5%	**12.2%**	12.3%
Flex-Tek	9%	**3%**	**13%**	**18.3%**	16.7%	**32.7%**	29.8%
Group	100%	**(1)%**	**(2)%**	**17.0%**	17.1%	**16.6%**	16.7%

John Crane

- Revenue up 2% driven by original equipment and aftermarket revenue in mid- and downstream segments
- Margins improved 140 bps to 23.2% to record high, driven by higher revenue and cost efficiencies
- Strong order book signals an improving growth rate through the second half

Smiths Medical

- Revenue down 4% driven by volume and price pressure; volume affected by distributor destocking in the US
- Margins down 280 bps, reflecting adverse operational gearing, impact from US medical device tax
- Full year revenue and profit expected to be below the level achieved last year

Smiths Detection

- Revenue down 1% against a strong comparator –critical infrastructure gains offset by transportation declines
- Margins down 20 bps with lower volumes and adverse operational gearing
- Full year revenue expected to be lower than the level achieved last year on a slightly weaker order book

Smiths Interconnect

- Revenue 4% lower against a strong comparator period, constrained by headwinds in defence (c. 28% of sales)
- Margins down 40 basis points with lower volumes and investment for growth offsetting productivity gains
- Second half should benefit from improvements in commercial markets; cost savings support margin recovery

Flex-Tek

- Revenue up 3% driven mainly by US residential construction and specialty heating elements.
- Margins up 160 bps, helped by better volumes, mix and pricing.
- Aerospace and US construction demand should support continued growth; margins geared to volume

**All figures are on a headline basis. Revenue and profit growth are at constant currency and exclude the impact of acquisitions and disposals*

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Presentation

The presentation slides and a live webcast of the presentation to analysts are available at www.smiths.com/results at 09.00 (UK time) on Wednesday 19 March. A recording of the webcast is available later that day. A live audio broadcast of the presentation is also available by dialling (no access code required):

UK toll free: 0808 237 0030

International: +44 (0)20 3139 4830

US/Canada toll free: 1 866 928 7517

Access code: 78370991#

An audio replay is available for seven days on the following numbers (access PIN 645568#):

UK toll free: 0808 237 0026

International: +44 (0)20 3426 2807

US/Canada toll free: 1 866 535 8030

Photography

Original high-resolution photography and broadcast quality video is available to the media from the media contacts above or from http://www.smiths.com/images.aspx.

Statutory reporting

Statutory reporting takes account of all items excluded from headline performance. On a statutory basis, pre-tax profit from continuing operations was £132m (2013: restated £166m) and earnings per share were 23.7p (2013: 30.7p).

The items excluded from headline performance comprise:

- amortisation of acquired intangible assets of £21m (2013: £23m);
- £36m in connection with John Crane, Inc. asbestos litigation (2013: £11m);
- £5m in connection with Titeflex Corporation litigation (2013: £3m);
- £14m of exceptional restructuring costs (2013: £5m);
- £5m for retirement benefit finance charge (2013: restated charge of £12m);
- £4m legacy retirement benefit administration costs (2013: restated £4m)
- £2m profit on disposal of businesses (2013: £1m);
- £1m cost of acquisition and disposals (2013: nil); and
- £1m gain on legal settlements and diabetes royalty payments

In the period to 31 January 2013, in addition to the above, £1m gain on changes to pension plans and £1m of financing losses were also excluded from headline performance.

Chief Executive's review

Results overview

Smiths Group made further progress at John Crane and Flex-Tek, while those divisions that serve the healthcare and defence/security sectors have continued to experience tough trading. The results at Medical were disappointing but reflect difficult trading conditions, particularly in developed markets. We still see opportunities to drive operational efficiencies at Smiths Medical to support margins while continuing to invest more in ongoing growth initiatives. The overall performance benefited from our strength and breadth as a diversified engineering company, our portfolio of leading-edge, technology-driven businesses serving a wide range of end markets and geographies. We continue to drive operational improvements and efficiencies across our businesses while increasing investment in high growth markets and new product development to accelerate medium-term revenue growth.

John Crane grew revenue with continued demand for first-fit OEM applications and aftermarket services to energy customers. Headline operating profit advanced from higher revenues and ongoing productivity efforts resulting in higher margins, more than offsetting cost inflation and our investment in growth opportunities. Smiths Medical saw revenues decline as sluggish procedure volumes, pricing pressure and distributor destocking took effect. Margins also fell, weighed down by the impact of the lower volumes which hit operational gearing and the incremental impact from the US medical device tax introduced last year. At the same time, Smiths Medical had to manage the inevitable disruption caused by the approach last year to acquire the business. Smiths Detection experienced a small reduction in revenue against a strong comparator period. Underlying growth in the critical infrastructure was offset by weakness in transportation, ports & borders and military sectors. As expected, Smiths Interconnect also saw a relatively weak first half against a strong performance last year, primarily due to weaker defence revenues. Margins were down with the reduced volumes, despite the benefit of cost saving initiatives. Flex-Tek delivered strong revenue growth from its construction products, generating higher margins as a result of its strong operational gearing.

Strategy

Our strategy is to continue to grow shareholder value by:

- Delivering sales growth through investment in organic drivers including new product development and expansion in high growth markets
- Enhancing margins through a relentless drive for operational improvement across all our businesses
- Generating strong cash-flows with better balance sheet management
- Implementing a rigorous approach to allocating capital across the businesses through active and disciplined portfolio management and a targeted acquisition strategy
- Improving returns on capital.

We continued to pursue these objectives during the period and some examples are set out below. Clear opportunities remain for Smiths Group to improve performance progressively and generate further value for shareholders.

Investing to accelerate revenue growth – new products

Our firm commitment to new product development, which has given us technology leadership in many areas, is crucial to driving future revenue and margin growth as new products typically command higher margins. We raised company-funded investment in R&D by 7% to £57m and secured a further £4m of customer-funded investment to take our total spend to £61m, or 4.2% of revenue (2013: 4.0%). John Crane was granted a patent for technology that will monitor the condition of a gas seal to improve product performance, extend average product lifespan and aid emission reduction in operation across the energy sector. Smiths Medical's CADD Solis PIB (Programmable Intermittent Bolus) pump, due for launch in the US this year following recent FDA clearance, is expected to provide continued growth opportunities, particularly in labour and delivery wards. New temperature management, pain management, airway and infusion products are also in the pipeline. Smiths Detection has unveiled ACE-ID, a handheld explosives identifier for use by bomb disposal and hazardous materials teams, and two new high-energy scanners for the ports and borders market – one static for checking light vehicles and the other a mobile version designed for rapid deployment in confined spaces. Smiths Interconnect is introducing higher density semiconductor test sockets to enable testing of packaged chips to their full limits. Flex-Tek continues to focus investment on specialist heating elements, medical tubing and aerospace application.

Investing to accelerate revenue growth – high-growth markets

We have continued to invest to expand our presence in emerging markets to improve the Group's growth profile over the medium term. In the first half, revenue from emerging markets was maintained, representing about 15% of Group sales. Increases in John Crane and Smiths Interconnect were offset by declines in Smiths Detection and Smiths Medical. We recognise that it takes time to establish a local sales presence through recruitment, training and brand building. In addition, there are also product registration processes in many markets. However, we believe that this is the right strategy for the Group to accelerate its growth profile and generate improved returns in the medium term. In Smiths Interconnect we saw good growth in Asia for connectors and secured contracts in data centres in India and Brazil. In John Crane, we continued to build infrastructure in select markets and to invest in local technical service capabilities.

'*Fuel for* Growth' – programme to fund growth investment

Over the past six years, we have pursued a series of restructuring programmes across the Group. This has improved the efficiency and effectiveness of the Group as well as benefited margins and provided the funds to invest in growth initiatives such as new product development and expansion in emerging markets. In September 2013, we announced another phase of restructuring, '*Fuel for Growth*', which was expected to generate annual savings of £50m at a cost of £100m by the end of financial year 2017. Further work on this initiative has highlighted more opportunities and the programme is now expected to generate £60m of annual savings for reinvestment in sales, marketing and new product development. The programme is now expected to cost £120m, which will be treated as an exceptional item. There will also be some accompanying capital expenditure. This restructuring will concentrate on three areas: site rationalisation with a particular focus on manufacturing footprint to support future growth while lowering costs; organisational effectiveness through delayering and broadening management spans of control; and the upgrading of information systems - particularly in John Crane - to improve decision-making and to support the next stage of globalisation. In the first half, we incurred costs of £12m across the programme, which delivered savings of £1m in the period.

	Total costs by end FY 2017	Full annual benefits by end FY 2017
John Crane	28	14
Smiths Medical	46	23
Smiths Detection	28	14
Smiths Interconnect	15	7
Flex-Tek	3	2
Total	**120**	**60**

There is also an existing performance improvement initiative that was initiated in 2011 in Smiths Detection, to lower the fixed cost base and enable the business to respond better to variations in demand, while improving customer service. It has continued to make good progress with a further £3m of savings generated in the period, bringing total savings to date to £28m. We expect to deliver a further £1m of savings during the second half. The total programme is expected to generate £33m of annual savings at a cost of £29m by the end of financial year 2015. We will conclude the programme at the end of this financial year and roll any remaining elements into the '*Fuel for Growth*' programme.

Setting medium-term operating ranges

In September 2008, we set out targets for revenue growth and margin improvement. This coincided with the start of a severe and prolonged economic recession. The divisions generally fared well on margins which were more within our control as a result of the programmes we implemented. However, revenue growth proved generally harder to achieve. The continued uncertainty in the world economy and financial markets in recent years made us reluctant to revisit the operating ranges until there was a degree of economic stability and forward visibility.

We announced at our 2013 annual results that we would publish revised operating ranges as part of today's results and, for John Crane, at its capital markets day held last December. These are mid-term operating ranges with average annual growth rates at constant currencies and margin expectations, assuming no discontinuities in the market drivers. It is possible that divisions may operate outside these ranges in any one period. For example, as a government contracting business, Smiths Detection can experience variability in its revenue and margin profile because of the timing of orders and the implementation of new regulations.

	Average annual organic revenue growth		Headline operating margin
John Crane	Mid-single digit	4-6%	22-25%
Smiths Medical	Low-single digit	0-3%	20-24%
Smiths Detection	Variable, averaging mid-single digits	4-6%	14-20%
Smiths Interconnect	Low to mid-single digits	3-5%	16-18%
Flex-Tek	Mid-single digits	3-6%	15-20%

Further details on the underlying market drivers, our divisional strategic initiatives and the dynamics of margin development are provided in the results presentation materials available on www.smiths.com. The revenue growth rates are typically lower than those provided in 2008 while the margin ranges are at a similar or higher level. This reflects that we are operating in a relatively lower growth environment today – particularly given the outlook for government budgets in defence and homeland security and the pressures on the healthcare market in developed markets. However, the objective of the '*Fuel for growth*' programme is to improve the organic growth characteristics over time. At the same time, we will continue to seek acquisitions that accelerate our strategic ambitions and generate value. These acquisitions will augment these organic ranges and will be facilitated by the Group's strong balance sheet.

Enhancing talent throughout the organisation

The successful implementation of our strategic initiatives depends on us having the talent in place throughout the organisation. Our processes to foster and retain the necessary skills have been reinforced at all levels across the Group. Jeff McCaulley joined in March to lead Smiths Medical into its next phase of development. At both senior and junior management levels leadership programmes have been refreshed as we work ever harder to ensure that the appropriate competencies needed to strengthen the organisation are in place.

Dividend

The Board has a progressive dividend policy for future pay-outs while maintaining a dividend cover of around 2.5 times. This policy will enable us to retain sufficient cash-flow to meet our legacy liabilities and finance our investment in the drivers of growth.

The Board has declared an interim dividend of 12.75p per share, an increase of 2% reflecting the strong cash conversion in the period. The interim dividend will be paid on 25 April to shareholders registered at the close of business on 28 March. The ex-dividend date is 26 March.

Outlook

We anticipate improved underlying trading in the second half driven by a strong John Crane order book, some recovery in Smiths Interconnect and further growth in Flex-Tek. Smiths Detection will continue to be affected by government budget pressures. Smiths Medical is expected to continue to face tough trading. At current rates, foreign exchange headwinds will increase sharply in the second half, with a 4-5% impact on full year earnings. We will maintain our focus on investing to drive sales growth in what are attractive long-term markets, and delivering further operational improvements, while providing strong cash conversion and returns.

Business review

Revenue

Revenue declined 1%, or £14m, on an underlying basis to £1,442m. Including adverse currency translation of £19m, overall reported revenue declined £33m (2%). The £14m underlying decline was driven by growth in John Crane (+£10m) and Flex-Tek (+£3m), which was more than offset by declines in Smiths Medical (-£15m), Smiths Interconnect (-£8m) and Smiths Detection (-£4m).

Profit

Headline operating profit saw an underlying reduction of 2% (£6m) to £245m. On a reported basis, headline operating profit fell £8m (3%) including adverse foreign exchange translation of £2m. Headline operating margin fell slightly to 17.0% (2013: 17.1%), mainly the result of the tough trading conditions in Smiths Medical and the incremental cost of the US medical device tax (£3m). The main drivers of the £6m underlying reduction were higher revenues and ongoing productivity efforts at John Crane (+£9m), increased volumes and price at Flex-Tek (+£2m) and lower corporate costs (+£3m) which was more than offset by lower volumes, price and the US device tax at Smiths Medical (-£16m), lower volumes at Detection (-£2m) and Interconnect (-£2m).

Operating profit on a statutory basis, after taking account of the items excluded from the headline figures, was £170m (2013: restated £211m). The decline was in large part a result of increased exceptional costs (see note 4). Statutory profit for 2013 has been restated to take account of the reporting requirements of IAS 19 (Revised 2011).

The net interest charge on debt was up slightly at £31m (2013: £30m). Headline profit before tax decreased £8m to £215m (2013: £223m). On an underlying basis, headline profit before tax declined by 3%.

The Group's tax rate on headline profit for the period was 27.0% (2013: 27.5%). Headline earnings per share decreased by 4% to 39.5p (2013: 40.9p).

On a statutory basis, profit before tax declined £34m to £132m (2013: restated £166m); it is stated after taking account of increased exceptional costs, a pensions finance charge of £5m (2013: restated charge of £12m) and other items excluded from the headline measure.

Cash generation

Operating cash generation remained strong with headline operating cash of £211m (2013: £223m), representing 86% (2013: 88%) of headline operating profit (see note 14 to the accounts for a reconciliation of headline operating cash and free cash-flow to statutory cash-flow measures). Free cash-flow fell £41m to £30m (2013: £71m). Free cash-flow is stated after interest, tax and pensions financing, but before acquisitions, financing activities and dividends.

On a statutory basis, net cash inflow from continuing operations was £83m (2013: £120m).

Dividends paid in the period on ordinary shares amounted to £225m, consisting final and special dividends (2013: £103m).

Net debt at 31 January was £901m, up from £744m at 31 July 2013. The increase in net debt reflects outflows from dividends (£225m) and pension funding (£52m) offset by an exchange translation benefit (£50m).

On 19 February, the Group completed the refinancing of its existing bank facility with a new US$800m committed revolving credit facility that matures in February 2019 with two one-year extension options.

John Crane

	2014 £m	2013 £m	Reported growth	Underlying growth
Revenue	**469**	469	0%	2%
Headline operating profit	**109**	102	6%	9%
Headline operating margin	**23.2%**	21.8%	140 bps	
Statutory operating profit	**64**	87		
Return on capital employed	**26.5%**	24.3%	220 bps	

John Crane delivered solid profit growth in the half, driven by higher underlying revenues and ongoing productivity initiatives. Headline operating profit grew 6% (£7m), driven by a 9% (£9m) underlying increase offset by adverse currency translation of £2m. Headline operating margin grew 140 basis points, or 150 basis points on a constant currency basis. The order book at the end of the period was 9% higher than the prior year, a record high.

The difference between statutory and headline operating profit reflects the £34m expense of John Crane, Inc. asbestos litigation, amortisation of acquired intangible assets of £7m and restructuring costs of £4m. Return on capital employed improved 220 basis points to 26.5% because of increased profitability.

Underlying revenue grew 2% (£10m), offset by £10m of adverse foreign exchange impact, leaving reported revenue flat. This underlying improvement reflects increased revenue in first-fit original equipment and aftermarket, offset by declining sales in our upstream oil services segment. Excluding this upstream segment, overall revenues reported a 4% underlying increase.

Underlying aftermarket revenues, excluding sales from our upstream oil services business, were up 3% on the back of strong activity with energy services customers across the Middle East, Latin America and North America. Including sales to our upstream oil services business, overall aftermarket revenues were flat on an underlying basis. Several renewals and aftermarket service contracts signed in the period with energy customers are expected to bolster the long-term outlook for the business. Performance Plus reliability programmes were secured in Singapore, Colombia, Australia, the US and other countries around the world. A contract covering a significant number of wet seal upgrades was signed with BP Rumaila Iraq, and a large order for slurry seals was won in the Democratic Republic of Congo. Additionally, John Crane was recognised by Petrobras with an award for responsible partnership for the fourth consecutive year, illustrating John Crane's commitment to providing the highest level of service to customers.

While our upstream oil services business, which is reported as part of our aftermarket revenue, benefited from additional projects for an existing OMV Petrom contract in Romania, underlying sales declined overall. This decline in upstream activity was driven by an increasingly competitive operating environment in the US, as well as severe winter weather in North America, which affected activity in the sector for a number of months.

Underlying revenues of first-fit original equipment rose 6% as our customers continue to invest in new capital projects. We continue to see customer confidence in the oil and gas segment, while the power generation segment remains challenging. Commercial activity again expanded in our high-growth markets, with multiple orders secured to supply products for large capital projects. These included the Zubair Project, covering the development of one of Iraq's largest oil fields. A significant order from Rolls Royce was won, reflecting an increase in filtration system orders.

Emerging markets remained a strong platform for growth. In the first half of 2014, emerging market revenue increased about 9% at constant currencies and comprised about 23% of our overall revenue. We continue to build infrastructure in select markets and invest in local technical service capabilities, preparing for future growth in China, ASEAN countries and the Middle East.

Increased revenue during the period resulted in approximately half of the underlying profit growth; the remaining profit growth was the result of ongoing productivity efforts, some of which are part of our '*Fuel for Growth*' programme. This programme is expected to deliver £14m of annualised savings by 2017 at an investment of £28m, which will be reported as exceptional. £4m of exceptional items were incurred during the first half. This revenue growth and these savings initiatives drove margin expansion, despite continued investment in highly competitive first-fit original equipment projects and new product development which we believe will position the company for accelerated medium-term growth.

Research and development

John Crane continues to invest in new product development and engineering, reflecting its commitment to sustain investments in R&D that will address future market needs. The company's focus remains on developing engineered solutions that address customers' growing processing demands while supporting reduced environmental impact and improved energy efficiency. Operating conditions are ever more challenging as customers face increasingly higher pressure and speed criteria while exploiting more difficult environments. As the industry leader in gas seal technology, John Crane remains at the forefront of ultra-high pressure designs capable of meeting the intensifying demands of compression equipment and the new requirements of emerging markets.

Benefits of products in the R&D pipeline range from expanded operating performance limits and lower energy consumption, to extended product life cycles. John Crane anticipates several new product launches over the next few years that will present new market opportunities and improve customers' operating performance and reduce costs. During the period, John Crane was awarded a patent for a breakthrough technology that will monitor the condition of a gas seal to improve product performance, extend average product lifespan and aid emission reduction in operation across the energy sector.

Outlook
Mid- and downstream order growth in the first half and strong order book should support solid second half sales growth. However, we anticipate market conditions in our upstream segment to continue to be challenging. On a constant currency basis, these combined effects should result in a second half sales growth rate within our mid-single digit operating range. Margins in the second half are expected to be at the higher end of our operating range.

Smiths Medical

	2014 £m	2013 £m	Reported growth	Underlying growth
Revenue	**389**	413	(6)%	(4)%
Headline operating profit	**71**	87	(18)%	(18)%
Headline operating margin	**18.3%**	21.1%	(280) bps	
Statutory operating profit	**63**	82		
Return on capital employed	**15.3%**	16.9%	(160) bps	

Smiths Medical saw underlying headline revenue decline by 4%, or £15m, mainly due to consumable product pressures which were slightly offset by strong ambulatory infusion sales. Reported headline revenue fell 6% (£24m), including an adverse currency translation impact of £9m. The underlying decline stems from soft trading conditions in the developed market medical devices sector. These included adverse pricing, capital spending constraints and relatively flat procedure growth rates. The pressures were particularly acute in the US where sales weakened amid stalled procedure volumes and distributor destocking. The last six months has seen an acceleration in destocking, a trend evident among US distributors for the past 18 months, resulting in first half US sales down 6% against the prior half year. Our analysis of revenues to US end-customers indicates more resilient underlying demand, down by 1% over the same period. There has also been inevitable disruption caused by the approach last year to acquire the business.

Underlying sales of consumables, which represent almost 85% of total revenue, were down 4%, reflecting distributor destocking in the first half and weak procedure activity. Pressure was particularly acute in peripheral intravenous catheters (PIVC), safety needles and respiratory products, as well as in European kitting operations as we continue to focus on more profitable product lines. Underlying sales of hardware also fell 3% on the back of declines in infusion systems and temperature management, only partly offset by strong growth in ambulatory infusion revenues.

Headline operating profit declined 18% on both a reported and underlying basis resulting in a 280 basis points fall in margin to 18.3%. This stems from the impact of lower first half volumes on factory performance, the incremental cost (£3m) from the introduction of the US medical device tax last year and approximately £2m of non-recurring insurance proceeds in the prior year. We continue to aim to offset the impact of the medical device tax by focusing on higher margin products and implementing the operational restructuring plans announced in 2013.

The difference between statutory and headline operating profit principally reflects the amortisation of acquired intangibles and restructuring costs. Return on capital employed declined 160 basis points to 15.3% as a result of the lower profits.

Medication delivery underlying revenues were flat, with strong ambulatory infusion sales offset by weaker infusion system and consumables business. Ambulatory infusion sales rose 7%, primarily due to the continued success in the US and Europe of the CADD Solis VIP pump. The CADD Solis PIB (Programmable Intermittent Bolus) pump, which received FDA clearance in December 2013, launched in the US early in the second half and is expected to provide continued growth opportunities, particularly in labour and delivery wards. Following a strong initial launch, sales of our Medfusion 4000 wireless syringe pump have been slower than expected as the squeeze on hospital capital budgets is maintained. We believe our Medfusion 4000 pipeline is well positioned for future growth, and we continue to invest in interoperability capabilities (integration with electronic medical records and other hospital systems), which will further support future performance in the syringe infusion market. We also anticipate that investment in wireless and interoperable ambulatory pumps will speed up future growth, as we leverage our leadership in ambulatory infusion.

Vital care underlying sales declined 3% in the face of continued sluggish procedure volumes and pricing pressures in developed countries. The assisted reproduction and invasive blood pressure management (IBPM) businesses grew strongly, while tracheostomy was relatively flat due to first half supply constraints. The general anaesthesia, respiratory, patient monitoring and temperature management businesses all declined given market pressures.

Respiratory performance, in particular, was impacted by channel inventory movements in the first half and underlying demand for our products remains robust. In contrast to the sluggish developed markets, our investment in emerging markets generated steady regional growth for IBPM, tracheostomy and patient monitoring.

Safety devices underlying revenue declined 8% amid pressures in sharps safety, PIVC and vascular access sales. However, with the emphasis on provider and patient safety, interest in both safety needle and catheter products remains high in developed markets and is growing in emerging markets, where we continue to invest and drive sales productivity. In 2013, we launched two innovative PIVC devices, ViaValve and Jelco IntuitIV. Our new blood control safety PIVC device, ViaValve, has received very positive customer reviews in the US, and we are expanding its launch to select European countries in 2014. In Europe, the Jelco IntuitIV safety catheter remains well placed to benefit from the EU Directive, effective in 2013, to improve workplace safety by preventing sharps injuries.

Developed markets remain challenging and we are maintaining our investment programme to expand in the faster growing emerging markets. As previously signalled, we estimate that it typically takes three to five years to reach target commercial productivity levels as we register and introduce new products and build our presence in these markets. In several territories, progress has been slowed by our efforts to transition to new distributor relationships capable of driving faster long term growth. Overall, emerging market revenue declined 10% as regulatory approvals of a new infusion pump in China were delayed and we experienced lower distributor demand in several smaller markets. Nonetheless, we have seen good growth in Brazil (15%) and India (27%) and total emerging market sales represent over 10% of the business. While the pace of executing this strategy is constrained by lengthy product registration processes in some countries and the time needed to recruit and train staff, we firmly believe that a continued focus on expanding our emerging market exposure is the right strategy to counter the challenges in developed markets.

Research and development

Investment in R&D remains a priority. Our total first half R&D cash spend of £19m (2013: £18m) grew 5% and amounted to 4.9% of sales (2013: 4.4%). At the same time, we have continued our initiative to streamline the organisation, upgrade talent and improve processes to accelerate speed-to-market for new products. We continue to invest in emerging market R&D and now have an established product development team in Shanghai with particular focus on infusion. We have also further increased our investment in clinical research to deliver evidence of effectiveness and economic benefit for our products, as customers increasingly demand proof of performance and value.

We have seen good sales traction of our Graseby 2000/2100 syringe pumps in India, and the CADD Solis VIP pump in the US and Europe. The pipeline for Medfusion 4000, CADD Solis VIP, Jelco IntuitIV and ViaValve, plus the recent clearance of CADD Solis PIB in the US as well as anticipated launches of new temperature management, pain management and infusion products over the next year, leave us well positioned for stronger new product sales. In addition to new launches, we also continue to expand the distribution and penetration of existing products into new regions, broadening our offering particularly in emerging markets.

Outlook

The challenging revenue trends in developed markets are expected to continue in the medium term and we will seek to counter them through the launch of innovative products, offering a broad portfolio, and executing our growth strategy in emerging markets. While we will continue to seek cost saving initiatives and operational enhancements, we expect profitability in the short term to be impacted by the full year effect of the US medical device tax, pricing headwinds, and our increased investment in new product development. At constant currencies, second half revenue and profit are expected to be below the equivalent period last year but with a reduced rate of decline compared with that experienced in the first half.

Smiths Detection

	2014 £m	2013 £m	Reported growth	Underlying growth
Revenue	**251**	255	(1)%	(1)%
Headline operating profit	**30**	31	(3)%	(7)%
Headline operating margin	**11.8%**	12.0%	(20) bps	
Statutory operating profit	**28**	26		
Return on capital employed	**8.6%**	12.2%	(360) bps	

Smiths Detection's revenue declined 1% (£4m) on an underlying basis against a strong comparator prior period. Growth in critical infrastructure was more than offset by weakness in transportation, military, ports and borders, and emergency responders.

Headline operating margins fell 20 basis points to 11.8% as headline operating profit declined 7% on an underlying basis. Profitability was affected by the lower volumes and some lower margin contracts reflecting competitive pressures. These more than offset the benefits of value engineering and cost savings delivered by the performance improvement programme. Announced in 2011, this programme has generated £28m of annual savings to date with costs of £28m against total expected costs of £29m. The programme will conclude at the end of the current financial year and any remaining elements will be rolled into the 'Fuel for Growth' programme. At the same time, we increased our investment in sales and marketing. We also undertook a review of all major contracts following the £15m provision that was made in the second half of last year to meet additional costs arising from technical challenges encountered on contract execution. No significant adjustment to the provision was required as a result of the review, although some further contract losses were incurred in the period. We also continued reviewing working capital requirements and expect that this review will conclude during the second half.

The difference between statutory and headline operating profit includes exceptional restructuring costs of £2m. Return on capital declined 360 basis points reflecting the lower profitability.

Site rationalisation and headcount reduction continued and the restructuring plan in Wiesbaden, Germany, is on track to reduce the workforce by 175 by the end of this calendar year. An R&D facility in Cork, Ireland, is due to close in the second half. Our new Asia Pacific X-ray manufacturing hub in Johor Bahru, Malaysia, was officially opened in January 2014 and its current workforce of 60 are producing up to 100 X-ray units per month. The new site improves our competitive position and benefits aftermarket service by reducing parts shipping time and costs. Its prime location in the fastest growing region for air transportation positions it well for significant growth as a manufacturing centre over the next few years.

Continued focus on the aftermarket has delivered strong underlying revenue growth, up 15% in the first half. This includes the benefit from the start of a two-year, £18m contract for the supply and management of bio-consumables for the UK MOD's fleet of Integrated Biological Detection Systems and $14m in orders for aftermarket support to the US Customs and Border Protection agency. Excluding these large consumables contracts which are unlikely to be repeated in the near term, aftermarket revenues grew to now represent 27% of divisional sales.

Transportation sales fell 3% against a very strong comparator period, which had benefited from several large contracts. However, the US TSA (Transportation Security Administration) has placed a $7m order for the RespondeR bottled liquid scanner, a product that is attracting increased international interest as customers seek fast and efficient ways to scan for liquids and gels. In Europe, the recent adoption of the new liquids regulations for transiting passengers has encouraged customers to pursue cost effective methods for upgrading existing equipment. Products such as our new Threat Identification Module (TIM) meet that need by enabling airports to upgrade existing X-ray units, quickly and cheaply, to achieve the latest standards for liquid detection. Our new HI-SCAN 10080 XCT automatic explosives scanner for checked baggage, developed in conjunction with Analogic, has already passed the EU Standard 3 tests that will be required for all new airport applications from September 2014. The XCT is currently undergoing operational testing with the TSA. The certification of the XCT allows it to be included in airport tenders for what is we expect to be a long-term replacement market over the next decade.

Revenue from critical infrastructure rose 17% on an underlying basis, primarily driven by growth in emerging markets such as Brazil, Singapore, Russia and India. It was also helped by a stabilisation of US Government spending and a greater focus on products specifically designed to meet the needs of customers within this segment.

Although underlying revenue in ports and borders fell 3% due to increased competitive and pricing pressures, we continue to see growing demand for our advanced scanners from customs authorities around the world seeking greater security and the improved tax revenue collection. We recently won a US$8m order from the Canadian Border Services and customer enquiries are generally high, especially for our newer lightweight cargo inspection systems. There is also growing confidence in the outlook for emerging markets, increasingly attracted by the revenue-earning opportunities from efficient tax collection coupled with improved border security.

Underlying military revenues fell 11%, as pressures on defence budgets continued. However, we secured new major US military programs. An additional order of $7m was received for the latest JCAD (Joint Chemical Agent Detector), our main, long-running military contract. We have also continued to deliver the Chemical Biological Protection System mobile shelter to the US Army and National Guard, which will provide a steady revenue stream into 2015.

Research and Development

Smiths Detection is committed to the constant development of its principal technologies, products and systems, the great majority of which are funded and managed internally. Company funded R&D increased 13% to £19m, equivalent to 7.5% of sales (2013: 6.6%). This includes £8m of capitalised projects. We actively seek customer and government support for R&D and total R&D spend was £21m (2013: £20m) or 8.4% of sales.

New products introduced during the period included the HI-SCAN 6040-2is is a compact, next-generation, dual-view X-ray scanner aimed at the transportation and critical infrastructure markets. Its competitive price and new product advantages are already helping win new business.

The ACE-ID is a handheld explosives identifier for use by bomb disposal and hazmat teams. Using RAMAN laser based spectroscopy, it enables the fast and safe identification of potential threats in a small portable unit.

Two new powerful X-ray systems capable of scanning complete vehicles have been launched. The HCVL is a fixed scanner to check light vehicles at checkpoints and border crossings while the HCVMe35 is a mobile truck and container system, designed for rapid deployment in space-restricted areas. Both have already generated significant interest from Customs authorities where excise revenue collection is becoming an increasing important part of their operations.

Outlook

The order book remains slightly behind the same time last year, which points to lower underlying revenue in the second half. However, as a government contracting business, Smiths Detection can experience variability in its revenue and margin profile because of the timing of orders and the implementation of government capital spending. Headline operating margins will benefit from our restructuring initiatives and on-going site rationalisation plans. New product launches and certifications will support expansion into new markets and provide opportunities in existing markets.

Smiths Interconnect

	2014 £m	2013 £m	Reported growth	Underlying growth
Revenue	**210**	218	(4)%	(4)%
Headline operating profit	**27**	30	(7)%	(7)%
Headline operating margin	**13.1%**	13.5%	(40) bps	
Statutory operating profit	**16**	20		
Return on capital employed	**12.2%**	12.3%	(10) bps	

Reported revenue for Smiths Interconnect declined 4%, or £8m, reflecting lower underlying revenue against a strong comparator. Underlying sales fell £8m, or 4%, primarily due to sharply reduced demand on military programmes in Europe, particularly the Eurofighter, and the US, where communications and self-protection programmes were scaled down as a result of the shrinking US presence in Afghanistan. Strong growth in Asia, particularly China and India, and general improvements in commercial markets such as telecoms and data centres softened the defence impact. Foreign exchange had a negative impact of £1m.

Headline operating profit decreased 7%, or £2m, on an underlying basis. Margins fell 40 basis points to 13.1%, mainly because of operational leverage on volume reductions and mix effects due to the end of higher margin programmes. Year on year savings from several ongoing productivity initiatives of almost £2m were reinvested in business development capabilities to support the continued transition to more commercial markets and increased R&D activities to drive future revenue potential. In addition, new cost reduction actions were instigated, including the closure of two further manufacturing facilities, one in the US and the other in Europe. Return on capital employed reduced by 10 basis points due to lower profitability.

The difference between statutory and headline operating profit principally reflects amortisation of acquired intangibles (£9m) and restructuring costs (£3m).

In Connectors, underlying revenue fell by 3%, the net impact of several positives and negatives. In Europe, the continued decline in Eurofighter production and the operational disruption from the closure of the UK manufacturing facility were only partially offset by a general improvement in economic conditions and industrial activity in Germany. While sales of recently launched semiconductor test products started to gain traction, the seasonal ramp up to support the sales of electronic consumer products over the November/December holiday period was lower than in previous years. Defence revenues also weakened on the back of the continued decline in overall spending and delayed funding of new programs such as the Ground Combat Vehicle. Asian revenues continued to grow, fuelled by new sales resources and the creation of a Singapore entity providing local language customer service and engineering support. Commercial aviation and medical revenues remained robust with further successes including a disposable catheter application and an artificial heart system.

Microwave, with approximately one third of revenue to the defence market, saw underlying revenue decline 6% as reductions in major programmes supporting the US war effort in Afghanistan, including Unmanned Aerial Vehicle datalinks and ground vehicle self-protection radar systems, affected activity. The defence focused businesses were restructured appropriately although some margin leakage occurred. While business development and engineering resources were shifted to more commercial opportunities, we continued to win contracts on US strategic defence applications such as ISR (Intelligence, Surveillance, Reconnaissance) with a new programme providing over £2m of revenue in the current fiscal year. Partially offsetting the challenges in defence, wireless telecoms and test & measurement performed strongly. Network optimisation filters revenues grew, particularly from Australian operators and new customers in the Middle East, and our new distributed antenna system product gained traction. Sales of PIM (passive intermodulation) test instruments held up well despite increased competition, and we were selected as the sole source PIM instrument supplier for two network management contractors of a major US wireless operator.

Underlying revenue in the Power business fell 2%. Data centre demand was positive with strong international growth and robust performance in the US, particularly in the colocation sector. Significant contracts were secured in India, Ireland and Brazil, mostly for our Busway and Power Distribution offerings, whilst in the US, focused sales and marketing efforts have significantly increased the value of our quote log. Industrial markets have also shown signs of a rebound with resumption in orders from a previously significant customer for furnace power controllers for LED crystal growth applications. Sales of power protection products continued to decline, particularly in the North America telecoms market, more than offsetting Power's positive trends. This business has now been restructured both commercially and operationally with revenue and margin benefits expected to start accruing in the second half. The commercial team has refocused on enhancing our value proposition and driving new sales opportunities, and we have completed a phased exit from the highly competitive Chinese market.

Research and development

Total R&D increased £1m to £14m or 6.5% of sales. The customer-funded portion, related mainly to the defence market, remained flat at £1.5m as government research budgets continued to be tightly controlled. However, to support the transition to more commercial markets and position the business for future growth, internal investment in R&D increased 8% to £12m or 5.8% of sales.

R&D investment continued to focus on new product innovation for higher growth and budding commercial markets. New higher density semiconductor test sockets were launched which enable testing of the packaged chips to their full limits. Work also continued on products for new applications such as electric vehicles and downhole logging, as well as next generation variants of existing offerings including PIM testing and satellite communications antenna systems.

Outlook

The outlook is for a gradual improvement in commercial market conditions to continue, while defence budgets are starting to stabilise at a lower base level, although specific programme lifecycle variations will drive performance. The strategy to focus resources on both commercial markets and emerging geographies will continue. Generally positive conditions in wireless telecoms, semiconductor test and data centres, together with targeted business development activities, the introduction of new products and a stronger commercial order backlog, are expected to deliver an improved performance in the second half. Margins are expected to improve as the year progresses, benefitting from volume increases, pricing initiatives and restructuring and efficiency savings.

Flex-Tek

	2014 £m	2013 £m	Reported growth	Underlying growth
Revenue	**123**	120	3%	3%
Headline operating profit	**22**	20	13%	13%
Headline operating margin	**18.3%**	16.7%	160 bps	
Statutory operating profit	**18**	17		
Return on capital employed	**32.7%**	29.8%	290 bps	

Flex-Tek's reported and underlying revenues grew 3%, or £3m, reflecting an improvement in the US residential construction market and growth in sales of specialty heating elements and medical hoses. Sales of aerospace components and OEM heating elements were flat compared with the prior year. Headline operating profit margins improved 160 basis points to 18.3%. The £2m (13%) increase in headline operating profit on a reported and underlying basis resulted from higher volumes and pricing which offset raw material inflation. Return on capital employed rose 290 basis points because of the improved profitability.

The difference between statutory and headline operating profit principally reflects exceptional litigation costs of £5m.

Fluid Management revenues were flat as growth in commercial airframe and automotive applications was offset by lower sales for satellite launch vehicles, military gas turbines and development work on next generation engines. Last year's first half revenues had benefited from development programmes for new aerospace engines which did not repeat in the period. However, the business is now well positioned for sales growth when deliveries of the new generation airframes and engines start in 2016. The healthy state of the US automotive market is reflected in our order book.

Construction revenues of HVAC (heating, ventilation & air conditioning) ducting and flexible gas piping products delivered an underlying 10% increase. According to the US Census Bureau, the December 2013 seasonally adjusted annual rate of new single family home starts was 667,000 or 7% higher than the previous December. Low home prices and interest rates continue to support high single digit growth in this market.

Heat Solutions underlying revenues were flat with increased sales of specialty heating elements and HVAC aftermarket applications offset by lower revenues from household appliance and residential HVAC OEM customers. OEM household appliance manufacturers continue to project mid-single digit growth rates in US markets and flat globally. Slow job creation and inflation worries have kept consumer confidence cautious in the US.

Underlying revenues in Flexible Solutions were up 1%, with strong growth in medical sleep apnoea products and slightly better sales of US industrial ducting offsetting continuing weak demand for floorcare applications.

Research and development

Flex-Tek continues to fund new product development for future commercial airframes and engines. Additional spending has been focused on specialist heating elements and medical tubing. Significant progress has been achieved at our Asian facilities; examples include the manufacture of heating elements from China for local applications and serving customers in the Middle East, and Airbus support from our factory in India. We continue to seek new investments to grow our market share, expand our product portfolio, and target potential bolt-on acquisitions to exploit the strength of the management team.

Outlook

Looking to the second half, we expect the positive trends to be maintained on the back of higher content in commercial airframes from new lighter weight, high pressure hydraulic hose assemblies, share gains in the HVAC heating element aftermarket, and continued growth in US residential construction and medical tubing. The gradually improving US economy and growth in Asia will provide further support for these trends. Margins will benefit from higher volumes but face pressure from increased investment in R&D, inflation and competition.

Financial review

Earnings per share
Basic headline earnings per share from continuing activities were 39.5p (2013: 40.9p), a decline of 4%. This reflects the lower headline headline operating profit which has been partly offset by a lower tax rate.

On a statutory basis, the basic earnings per share from continuing activities were 23.7p (2013: 30.7p).

Exceptional and other items relating to continuing activities excluded from headline profit before tax
These items amounted to a charge of £83m compared to a charge of £57m in 2013. They comprised:

- Amortisation of intangible assets acquired in business combinations of £21m (2013: £23m). The charge relates principally to technology and customer relationships;
- £36m charge (2013: £11m) in connection with John Crane, Inc. asbestos litigation;
- £5m charge (2013: £3m) in connection with Titeflex Corporation litigation;
- £14m charge for restructuring (2013: £5m) in respect of the '*Fuel for Growth*' programme and performance improvement programme in Smiths Detection;
- £5m charge for retirement benefit finance (2013: restated charge of £12m);
- £4m charge for legacy retirement benefit administration (2013: £4m)
- £2m profit on disposal of businesses (2013: £1m);
- £1m cost of acquisition and disposals (2013: nil); and
- £1m gain on legal settlement of diabetes royalty payments

In the period to 31 January 2013, in addition to the above, £1m gain on changes to pension plans and £1m of financing losses were also excluded from headline performance.

Cash generation and net debt
Operating cash generation remained strong with headline operating cash of £211m (2013: £223m), representing 86% (2013: 88%) of headline operating profit (see note 14 to the accounts for a reconciliation of headline operating cash and free cash-flow to statutory cash-flow measures). Free cash-flow fell £41m to £30m (2013: £71m). Free cash-flow is stated after interest, tax and pensions financing, but before acquisitions, financing activities and dividends.

On a statutory basis, net cash inflow from continuing operations was £83m (2013: £120m).

Dividends paid in the period on ordinary shares amounted to £225m, consisting of final and special dividends (2013: £103m).

Net debt at 31 January was £901m, up from £744m at 31 July 2013. The increase in net debt reflects outflows from dividends (£225m) and pension funding (£52m) offset by an exchange translation benefit of (£50m).

On 19 February, the Group completed the refinancing of its existing bank facility with a new US$800m committed revolving credit facility that matures in February 2019 with two one-year extension options.

Headline interest and other financing costs
Interest payable on debt, net of interest earned on cash deposits, was £31m (2013: £30m). Interest costs were covered 8.0 times by headline operating profits.

The Group accounts for pensions using IAS19. As required by this standard, a finance charge of £5m (2013: a restated charge of £12m) is recognised reflecting the unwinding of the discount on the net pension liability.

Research and development
Investment in research and development (R&D) drives future performance and is a measure of the Group's commitment to the future organic growth of the business.

We invested a total of £61m in R&D (2013: £59m), equivalent to 4.2% of revenue (2013: 4.0%). Of that total, £57m was funded by the Company compared with £54m in 2013, an increase of 7%. We actively seek funding from customers to support R&D and this amounted to £4m (2013: £5m). Under IFRS, certain development costs are capitalised, and this amounted to £15m in the period (2013: £14m). The gross capitalisation is shown as an intangible asset. Where customers contribute to the costs of development, the contribution is included as deferred income and disclosed within trade and other payables.

Taxation
The headline tax charge of £58m (2013: £61m) represented an effective rate of 27.0% on the headline profit before taxation (2013: 27.5%). This rate is expected to be sustained for the full year. On a statutory basis, the tax charge on continuing activities was £37m (2013: £45m).

The Group continues to take advantage of global manufacturing, research and development and other tax incentives, the tax-efficient use of capital and tax compliance management. The tax rate is expected to be within the range of 26% and 28% over the medium term.

Return on capital employed

The return on capital employed (ROCE) is calculated over a rolling 12-month period and is the percentage that headline operating profit represents monthly average capital employed. Capital employed comprises total equity adjusted for goodwill recognised directly in reserves, post-retirement benefit assets and liabilities net of tax, litigation provisions relating to exceptional items net of tax, and net debt. The ROCE decreased 10 basis points to 16.6% (2013: 16.7%) as a result of reduced profitability in Smiths Medical, Detection and Interconnect offsetting improved profitability in John Crane and Flex-Tek.

Retirement benefits

As required by IFRS, the balance sheet reflects the net surplus or deficit in retirement benefit plans, taking assets at their market values at 31 January 2014 and evaluating liabilities at period-end AA corporate bond interest rates.

The tables below disclose the net status across a number of individual plans. Where any individual plan shows a surplus under IAS 19, this is disclosed on the balance sheet as a retirement benefit asset. The IAS 19 surplus of any one plan is not available to fund the IAS 19 deficit of another plan. The net pension deficit has fallen to £236m at 31 January 2014 from £254m at 31 July 2013. The decrease reflects the benefit of scheme contributions, while the asset returns and foreign exchange broadly offset the increase in liabilities caused by a slight decrease in the discount rates upon which the liability is calculated.

The accounting basis under IAS 19 does not necessarily reflect the funding basis agreed with the Trustees and, should the schemes be wound up while they had members, they would need to buy out the benefits of all members. The buyouts would cost significantly more than the present value of scheme liabilities calculated in accordance with IAS 19.

The retirement benefit position was:

	31 January 2014	31 July 2013	31 January 2013
Funded plans			
UK plans – funding status	**99%**	99%	97%
US plans – funding status	**85%**	81%	74%
Other plans – funding status	**80%**	80%	71%

	31 January 2014 £m	31 July 2013 £m	31 January 2013 £m
Deficit			
Funded plans	**(132)**	(147)	(276)
Unfunded plans	**(104)**	(107)	(106)
Total deficit	**(236)**	(254)	(382)
Retirement benefit assets	**102**	121	83
Retirement benefit liabilities	**(338)**	(375)	(465)
	(236)	(254)	(382)

In the current year, cash contributions to the schemes are expected to total approximately £90m (2013: £78m). In addition, the Group will invest £24m (2013: £24m) in an escrow account as part of the 10-year funding plan agreed with the Smiths Industries Pension Scheme (SIPS).

The approximate pension membership for the three main schemes in January 2014 is set out in the table below:

Pension scheme membership	**SIPS**	**TIGPS**	**US plans**	**Total**
Deferred active	540	270	3,220	**4,030**
Deferred	11,580	14,010	6,400	**31,990**
Pensioners	13,070	17,900	5,520	**36,490**
Total	**25,190**	**32,180**	**15,140**	**72,510**

Exchange rates

The results of overseas operations are translated into sterling at average exchange rates. The net assets are translated at period-end rates. The principal exchange rates, expressed in terms of the value of sterling, are shown in the following table.

	31 January 2014	31 January 2013		31 July 2013
Average rates:				
US dollar	**1.61**	1.60	Dollar weakened 1%	1.57
Euro	**1.19**	1.24	Euro strengthened 4%	1.20
Period end rates:				
US dollar	**1.65**	1.59	Dollar weakened 4%	1.52
Euro	**1.22**	1.17	Euro weakened 4%	1.14

Risk management

The principal risks and uncertainties affecting the business activities of the Group and relevant mitigating activities were set out on pages 56 to 61 of the Annual Report for the year ended 31 July 2013, a copy of which is available at the Company's website at www.smiths.com. The key risks and uncertainties are summarised below:

Economic outlook

Economic and financial market conditions may lead to recession and may cause adverse effects on customers or suppliers with consequential capacity or cash-flow implications for Smiths Group.

***Eurozone* break-up**

Political and economic structural weaknesses in the single currency framework may result in the Eurozone breaking up which could affect our business through currency devaluations and a wider economic uncertainty.

Compliance with legislation and regulations

A complex legislative and regulatory environment applies to the Group's activities such that failure to comply could lead to financial penalty.

Pension funding

Defined benefit pension scheme obligations are funded by Group companies based on actuarial assumptions. Changes in discount rates, inflation, returns or mortality could lead to material changes in funding requirements.

Financial risks

Financial risk, whether from foreign exchange fluctuations, availability of funding, changes in tax rates or availability of insurance cover may cause adverse effects on the Group's net assets, earnings or liquidity.

Product liability and litigation

Product liability claims and litigation, particularly given the Group's significant sales exposure to the US market, may have a significant impact on the financial results.

Global supply chain/concentration of manufacturing

Reliance on sole suppliers or concentration of manufacturing in the supply chain – especially in areas exposed to natural catastrophe – may result in disruption to the supply of products.

Government customers

Over 35% of revenues are from governments or influenced by governments. Many such governments are reducing expenditure in the present economic environment with consequential risks to revenue.

Technology and innovation

Product innovation is key to long-term revenue growth. Failure of the Group to innovate its products and services could materially affect market share and sales growth.

Talent and succession planning

Suitably qualified personnel are an important asset that underpins the Group's success. Failure to attract or retain such personnel may result in weaker growth and returns.

Contractual liabilities

Failure to deliver products and services according to contractual obligations may lead to higher costs, liquidated damages or other penalties.

Acquisitions and disposals

Acquisitions are subject to execution risk and may be more difficult to integrate than expected so that the full benefits are not realised.

Information technology and cyber-security

Information systems are subject to security risk and play an important part in business processes, both internally and externally.

Developments since the Annual Report

In the view of the Board, the risks and uncertainties affecting the Group for the remaining six months of the financial year continue to be those set out briefly above and more fully in the Annual Report. Since the Annual Report, continued constraints on government budgets are likely to put pressure on public sector spending in areas such as healthcare, defence and homeland security in markets in which the Group operates. Currency volatility has also increased since the Annual Report which could cause variations in the Group's reported results as average exchange rates fluctuate and variations in the value of the Group's reported net assets as exchange rates change.

Statement of directors' responsibilities

The Interim report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the Interim report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority. The Disclosure and Transparency Rules ("DTR") require that the accounting policies and presentation applied to the half-yearly figures must be consistent with those applied in the latest published annual accounts, except where the accounting policies and presentation are to be changed in the subsequent annual accounts, in which case the new accounting policies and presentation should be followed, and the changes and the reasons for the changes should be disclosed in the Interim report, unless the United Kingdom Financial Conduct Authority agrees otherwise.

The directors confirm that this condensed set of financial statements has been prepared in accordance with International Accounting Standard 34, 'Interim Financial Reporting' as adopted by the European Union, and that the interim management report herein includes a fair review of:

- the important events that have occurred during the first six months of the financial year and their impact on the condensed set of financial statements as required by DTR 4.2.7;
- the principal risks and uncertainties for the remaining six months of the year as required by DTR 4.2.7; and
- related party transactions that have taken place in the first six months of the current financial year and changes in the related party transactions described in the previous annual report that have materially affected the financial position or performance of the group during the first six months of the current financial year as required by DTR 4.2.8.

The directors of Smiths Group plc are listed in the Smiths Group plc Annual Report for the year ended 31 July 2013. Donald Brydon retired as planned on 19 November 2013. There have been no other changes to the membership of the board.

For and on behalf of the Board of Directors:

Philip Bowman
Chief Executive

Peter Turner
Finance Director

18 March 2014

Independent review report to Smiths Group plc

Introduction

We have been engaged by the Company to review the condensed set of financial statements in the Interim report for the period ended 31 January 2014, which comprises the consolidated income statement, consolidated statement of comprehensive income, consolidated balance sheet, consolidated statement of changes in equity, consolidated cash flow statement and related notes. We have read the other information contained in the Interim report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

Directors' responsibilities

The Interim report is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the Interim report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

As disclosed in note 1, the annual financial statements of the Group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this Interim report has been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting", as adopted by the European Union.

Our responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the Interim report based on our review. This report, including the conclusion, has been prepared for and only for the Company for the purpose of the Disclosure and Transparency Rules of the Financial Conduct Authority and for no other purpose. We do not, in producing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the Interim report for the period ended 31 January 2014 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

PricewaterhouseCoopers LLP
Chartered Accountants
London
18 March 2014

(a) The maintenance and integrity of the Smiths Group plc website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

(b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Consolidated income statement (unaudited)

	Notes	**Period ended 31 January 2014 £m**	Period ended 31 January 2013 (restated) £m	Year ended 31 July 2013 (restated) £m
Continuing operations				
Revenue	2	**1,441.8**	1,475.2	3,108.6
Cost of sales		**(790.5)**	(799.4)	(1,694.0)
Gross profit		**651.3**	675.8	1,414.6
Sales and distribution costs		**(201.1)**	(214.0)	(425.6)
Administrative expenses		**(282.7)**	(251.6)	(503.4)
Profit on disposal of businesses	4	**2.3**	0.7	0.9
Operating profit		**169.8**	210.9	486.5
Comprising				
– headline operating profit	3	**245.2**	252.7	559.7
– exceptional items, amortisation of acquired intangibles	3	**(75.4)**	(41.8)	(73.2)
		169.8	210.9	486.5
Interest receivable		**1.5**	1.2	2.6
Interest payable		**(32.2)**	(31.4)	(64.3)
Other financing losses		**(2.9)**	(2.9)	(6.1)
Other finance charges – retirement benefits		**(4.7)**	(12.1)	(23.0)
Finance costs		**(38.3)**	(45.2)	(90.8)
Profit before taxation		**131.5**	165.7	395.7
Comprising				
– headline profit before taxation	3	**214.5**	222.5	498.0
– exceptional items, amortisation of acquired intangibles and other financing gains and losses	3	**(83.0)**	(56.8)	(102.3)
		131.5	165.7	395.7
Taxation	5	**(37.1)**	(44.5)	(79.1)
Profit after taxation – continuing operations		**94.4**	121.2	316.6
(Loss)/profit after taxation – discontinued operations		**0.1**		
Profit for the period		**94.5**	121.2	316.6
Attributable to				
Smiths Group shareholders		**93.4**	120.5	315.0
Non-controlling interests		**1.1**	0.7	1.6
		94.5	121.2	316.6
Earnings per share	7			
Basic		**23.7p**	30.7p	80.1p
Diluted		**23.6p**	30.4p	79.3p
Dividends per share (declared)	6			
– interim		**12.75p**	12.50p	12.50p
– final				27.00p
– special				30.00p
		12.75p	12.50p	69.50p

Consolidated statement of comprehensive income (unaudited)

	Notes	Period ended 31 January 2014 £m	Period ended 31 January 2013 (restated) £m	Year ended 31 July 2013 (restated) £m
Profit for the period		**94.5**	121.2	316.6
Other comprehensive income				
Actuarial (losses)/gains on retirement benefits	8	**(37.3)**	212.6	326.6
Taxation recognised on actuarial movements		**(3.1)**	(21.5)	(39.0)
Other comprehensive income which will not be reclassified to the consolidated income statement		**(40.4)**	191.1	287.6
Other comprehensive income which will be, or has been, reclassified				
Exchange gains/(losses)		**(185.4)**	29.0	99.8
Fair value gains/(losses)				
– on available for sale financial assets		**0.3**	3.4	0.1
– deferred in the period on cash-flow and net investment hedges		**88.3**	(2.0)	(44.7)
– reclassified to income statement		**(2.1)**	(1.5)	(4.3)
Taxation recognised on fair value gains and losses				(1.0)
Total other comprehensive income		**(139.3)**	220.0	337.5
Total comprehensive income		**(44.8)**	341.2	654.1
Attributable to				
Smiths Group shareholders		**(44.9)**	342.0	654.2
Non-controlling interests		**0.1**	(0.8)	(0.1)
		(44.8)	341.2	654.1

Consolidated balance sheet (unaudited)

	Notes	31 January 2014 £m	31 January 2013 £m	31 July 2013 £m
Non-current assets				
Intangible assets	9	**1,608.6**	1,710.6	1,746.0
Property, plant and equipment	10	**259.3**	266.7	280.0
Financial assets – other investments		**98.9**	76.8	86.1
Retirement benefit assets	8	**102.5**	83.0	121.7
Deferred tax assets		**174.0**	181.1	185.4
Trade and other receivables		**30.7**	28.0	34.1
Financial derivatives		**12.5**	10.8	6.4
		2,286.5	2,357.0	2,459.7
Current assets				
Inventories		**442.7**	480.7	475.6
Current tax receivable		**24.7**	17.3	33.4
Trade and other receivables		**608.6**	626.0	695.5
Cash and cash equivalents	11	**175.9**	275.5	393.8
Financial derivatives		**11.2**	11.8	8.1
		1,263.1	1,411.3	1,606.4
Total assets		**3,549.6**	3,768.3	4,066.1
Non-current liabilities				
Financial liabilities				
– borrowings	11	**(893.9)**	(1,084.2)	(951.1)
– financial derivatives		**(6.7)**	(3.9)	(11.0)
Provisions for liabilities and charges	13	**(255.7)**	(253.1)	(258.1)
Retirement benefit obligations	8	**(338.1)**	(464.9)	(375.3)
Deferred tax liabilities		**(67.9)**	(68.8)	(73.1)
Trade and other payables		**(33.2)**	(37.4)	(31.0)
		(1,595.5)	(1,912.3)	(1,699.6)
Current liabilities				
Financial liabilities				
– borrowings	11	**(182.8)**	(46.3)	(187.1)
– financial derivatives		**(7.1)**	(3.3)	(5.8)
Provisions for liabilities and charges	13	**(72.6)**	(76.2)	(78.1)
Trade and other payables		**(416.4)**	(443.3)	(521.8)
Current tax payable		**(54.7)**	(67.3)	(80.1)
		(733.6)	(636.4)	(872.9)
Total liabilities		**(2,329.1)**	(2,548.7)	(2,572.5)
Net assets		**1,220.5**	1,219.6	1,493.6
Shareholders' equity				
Share capital		**147.9**	147.5	147.7
Share premium account		**345.9**	336.5	340.8
Capital redemption reserve		**5.8**	5.8	5.8
Revaluation reserve		**1.7**	1.7	1.7
Merger reserve		**234.8**	234.8	234.8
Retained earnings		**564.9**	614.7	929.2
Hedge reserve		**(87.9)**	(128.3)	(174.0)
Total shareholders' equity		**1,213.1**	1,212.7	1,486.0
Non-controlling interest equity		**7.4**	6.9	7.6
Total equity		**1,220.5**	1,219.6	1,493.6

Consolidated statement of changes in equity (unaudited)

	Notes	Share capital and share premium £m	Other reserves £m	Retained earnings £m	Hedge reserve £m	Equity shareholders' funds £m	Non-controlling Interest £m	Total equity £m
At 31 July 2013		488.5	242.3	929.2	(174.0)	1,486.0	7.6	1,493.6
Profit for the period				93.4		93.4	1.1	94.5
Other comprehensive income								
Exchange losses				(184.3)	(0.1)	(184.4)	(1.0)	(185.4)
Actuarial losses on retirement benefits and tax				(40.4)		(40.4)		(40.4)
Fair value gains				0.3	86.2	86.5		86.5
Total comprehensive income for the period				(131.0)	86.1	(44.9)	0.1	(44.8)
Transactions relating to ownership interests								
Exercises of share options		5.3				5.3		5.3
Purchase of own shares				(12.8)		(12.8)		(12.8)
Dividends								
– equity shareholders	6			(224.7)		(224.7)		(224.7)
– non-controlling interest							(0.3)	(0.3)
Share-based payment				4.2		4.2		4.2
At 31 January 2014		**493.8**	**242.3**	**564.9**	**(87.9)**	**1,213.1**	**7.4**	**1,220.5**

	Notes	Share capital and share premium £m	Other reserves £m	Retained earnings £m	Hedge reserve £m	Equity shareholders' funds £m	Non-controlling Interest £m	Total equity £m
At 31 July 2012		479.2	242.3	376.1	(124.8)	972.8	8.0	980.8
Profit for the period				120.5		120.5	0.7	121.2
Other comprehensive income								
Exchange gains/(losses)				30.5		30.5	(1.5)	29.0
Actuarial losses on retirement benefits net of tax				191.1		191.1		191.1
Fair value gains/(losses)				3.4	(3.5)	(0.1)		(0.1)
Total comprehensive income for the period				345.5	(3.5)	342.0	(0.8)	341.2
Transactions relating to ownership interests								
Exercises of share options		4.8				4.8		4.8
Purchase of own shares				(11.0)		(11.0)		(11.0)
Dividends								
– equity shareholders	6			(103.2)		(103.2)		(103.2)
– non-controlling interest							(0.3)	(0.3)
Share-based payment				7.3		7.3		7.3
At 31 January 2013		**484.0**	**242.3**	**614.7**	**(128.3)**	**1,212.7**	**6.9**	**1,219.6**

Consolidated cash-flow statement (unaudited)

	Notes	Period ended 31 January 2014 £m	Period ended 31 January 2013 £m	Year ended 31 July 2013 £m
Net cash inflow from operating activities	14	**83.2**	119.9	353.4
Cash-flows from investing activities				
Expenditure on capitalised development		**(13.6)**	(13.0)	(28.4)
Expenditure on other intangible assets		**(8.0)**	(3.0)	(11.1)
Purchases of property, plant and equipment		**(24.1)**	(23.1)	(56.5)
Disposals of property, plant and equipment		**4.3**	2.0	3.9
Investment in financial assets		**(12.1)**	(12.1)	(24.3)
Acquisition of businesses			(0.5)	(0.5)
Disposals of businesses		**3.0**	0.7	0.3
Net cash-flow used in investing activities		**(50.5)**	(49.0)	(116.6)
Cash-flows from financing activities				
Proceeds from exercise of share options		**5.3**	4.8	9.3
Purchase of own shares		**(12.8)**	(11.0)	(11.0)
Dividends paid to equity shareholders		**(224.7)**	(103.2)	(152.4)
Dividends paid to non-controlling interests		**(0.3)**	(0.3)	(0.3)
Cash inflow/(outflow) from matured derivative financial instruments		**4.3**	(2.0)	(0.4)
Increase in new borrowings		**0.1**	247.2	247.2
Reduction and repayment of borrowings		**(0.4)**	(158.8)	(159.1)
Net cash-flow used in financing activities		**(228.5)**	(23.3)	(66.7)
Net (decrease)/increase in cash and cash equivalents		**(195.8)**	47.6	170.1
Cash and cash equivalents at beginning of the period		**386.5**	203.7	203.7
Exchange differences		**(20.9)**	3.2	12.7
Cash and cash equivalents at end of the period		**169.8**	254.5	386.5
Cash and cash equivalents at end of the period comprise				
– cash at bank and in hand		**101.8**	191.1	164.2
– short-term deposits		**74.1**	84.4	229.6
– bank overdrafts		**(6.1)**	(21.0)	(7.3)
		169.8	254.5	386.5

Reconciliation of net cash-flow to movement in net debt

	Notes	Period ended 31 January 2014 £m	Period ended 31 January 2013 £m	Year ended 31 July 2013 £m
Net (decrease)/increase in cash and cash equivalents	14	**(195.8)**	47.6	170.1
Net (increase)/decrease in borrowings resulting from cash-flows		**0.3**	(88.4)	(88.1)
Movement in net debt resulting from cash-flows		**(195.5)**	(40.8)	82.0
Capitalisation, interest accruals and unwind of capitalisation of fees		**(8.3)**	(11.3)	(3.8)
Movement in fair value hedging		**(3.2)**	2.0	9.7
Exchange differences		**50.6**	(13.5)	(40.9)
Movement in net debt in the period		**(156.4)**	(63.6)	47.0
Net debt at start of period		**(744.4)**	(791.4)	(791.4)
Net debt at end of period		**(900.8)**	(855.0)	(744.4)

Notes to the Interim report (unaudited)

1 Basis of preparation

The condensed interim financial information covers the six month period ended 31 January 2014 and has been prepared under International Financial Reporting Standards (IFRS) as adopted by the European Union, in accordance with International Accounting Standard 34 'Interim Financial Reporting' and the Disclosure and Transparency Rules of the Financial Services Authority. It is unaudited but has been reviewed by the auditors and their report is attached to this document.

The interim financial information does not constitute statutory accounts within the meaning of Section 434 of the Companies Act 2006. It should be read in conjunction with the statutory accounts for the year ended 31 July 2013, which were prepared in accordance with IFRS as adopted by the European Union and have been filed with the Registrar of Companies. The auditors' report on these statutory accounts was unqualified and did not contain a statement under Section 498(2) or (3) of the Companies Act 2006.

Accounting policies

The condensed interim financial information has been prepared on the basis of the accounting policies applicable for the year ending 31 July 2014. These accounting policies are consistent with those applied in the preparation of the financial statements for the year ended 31 July 2013, except for the adoption of:

- 'IAS 19 (Revised 2011): Employee benefits'. The consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and related notes have been restated to reflect the recognition requirements of this standard;
- 'IAS 28: Investments in Associates and Joint Ventures' which has not led to any changes in reported figures or disclosures;
- Amendments to IFRS 7 'Disclosures – Offsetting financial assets and financial liabilities'. The additional disclosures required will be included in the statutory accounts for the year ended 31 July 2014;
- 'IFRS 10: Consolidated financial statements' which has not led to any changes in reported figures or disclosures;
- 'IFRS 11: Joint Arrangements' which has not led to any changes in reported figures or disclosures;
- 'IFRS 12: Disclosed of Interests in Other Entities' which has not led to any changes in reported figures or disclosures; and
- 'IFRS 13: Fair value measurement'. Adopting this new accounting requirement has increased the disclosure included in the notes to the interim report.

Significant judgements, key assumptions and estimates

The preparation of the accounts in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the accounts and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from these estimates. The key estimates and assumptions used in these consolidated financial statements are set out below.

Revenue recognition

The timing of revenue recognition on contracts depends on the assessed stage of completion of contract activity at the balance sheet date. This assessment requires the expected total contract revenues and costs to be estimated based on the current progress of the contract. Revenue of £25.8m (31 July 2013: £53.0m) has been recognised in the period in respect of contracts in progress at the period end with a total expected value of £132.6m (31 July 2013: £149.7m). A 5% reduction in the proportion of the contract activity recognised in the current period would have reduced operating profit by an estimated £0.1m (31 July 2013: £0.5m) for Smiths Detection and £0.1m (31 July 2013: £0.3m) for Smiths Interconnect.

In addition to contracts accounted for on a percentage of completion basis, Smiths Detection also has long-term contractual arrangements for the sale of goods and services. Margins achieved on these contracts can reflect the impact of commercial decisions made in different economic circumstances. In addition, contract delivery is subject to commercial and technical risks which can affect the outcome of the contract.

Smiths Medical has rebate arrangements in place with some distributors in respect of sales to end customers where sales prices have been negotiated by Smiths Medical. Rebates are estimated based on the level of discount derived from sales data from distributors, the amount of inventory held by distributors and the time lag between the initial sale to the distributor and the rebate being claimed. The rebate accrual at 31 January 2014 was £16.6m (31 July 2013: £17.0m).

Working capital provisions

For inventory and receivables, if the carrying value is higher than the expected recoverable value, the Group makes provisions writing down the assets to their recoverable value. The recoverable value of inventory is estimated using historical selling prices, sales activity and customer contracts. The recoverable value of receivables is considered individually for each customer and incorporates past experience and progress with collecting receivables.

At 31 January 2014 the carrying value of inventory incorporates provisions of £70.5m (31 July 2013: £74.4m). The inventory turn rate of 3.6 (31 July 2013: 3.6) varies across the five divisions. Smiths Detection has the slowest inventory utilisation with a turn rate of 2.6 (31 July 2013: 2.4).

At 31 January 2014 the gross value of receivables partly provided for or more than 3 months overdue was £55.1m (31 July 2013: £53.4m) and there were provisions of £15.9m (31 July 2013: £17.8m) against these receivables which were carried at a net value of £39.2m (31 July 2013: £35.6m).

Impairment
Goodwill is tested at least annually for impairment and intangible assets acquired in business combinations are tested if there are any indications of impairment, in accordance with the accounting policy set out in the Annual Report 2013. The recoverable amounts of cash generating units and intangible assets are determined based on value in use calculations. These calculations require the use of estimates including projected future cash-flows and other future events.

See the Annual Report 2013 for details of the critical assumptions made, including the sales and margin volatility in Smiths Detection and Smiths Interconnect and disclosures on the sensitivity of the impairment testing to these key assumptions. See note 9 for details of the changes in assumptions required to trigger an impairment in Smiths Interconnect Power Management.

Provisions for liabilities and charges
As previously reported, John Crane, Inc., a subsidiary of the Group, is currently one of many co-defendants in litigation relating to products previously manufactured which contained asbestos. Provision of £207.0m (31 July 2013: £210.0m) has been made for the future defence costs which the Group is expected to incur and the expected costs of future adverse judgments against John Crane, Inc. Whilst published incidence curves can be used to estimate the likely future pattern of asbestos related disease, John Crane, Inc.'s claims experience is significantly impacted by other factors which influence the US litigation environment. These can include: changing approaches on the part of the plaintiffs' bar; changing attitudes amongst the judiciary at both trial and appellate levels; and legislative and procedural changes in both the state and federal court systems. Therefore, because of the significant uncertainty associated with the future level of asbestos claims and of the costs arising out of the related litigation, there can be no guarantee that the assumptions used to estimate the provision will result in an accurate prediction of the actual costs that may be incurred. John Crane, Inc. takes account of the advice of an expert in asbestos liability estimation in quantifying the expected costs.

As previously reported, Titeflex Corporation, a subsidiary of the Group in the Flex-Tek division, has received a number of claims from insurance companies seeking recompense on a subrogated basis for the effects of damage allegedly caused by lightning strikes in relation to its flexible gas piping product. It has also received a number of product liability claims regarding this product, some in the form of purported class actions. Titeflex Corporation believes that its products are a safe and effective means of delivering gas when installed in accordance with the manufacturer's instructions and local and national codes, however some claims have been settled on an individual basis without admission of liability. Provision of £62.3m (31 July 2013: £65.6m) has been made for the costs which the Group is expected to incur in respect of these claims. However, because of the significant uncertainty associated with the future level of claims, there can be no guarantee that the assumptions used to estimate the provision will result in an accurate prediction of the actual costs that may be incurred.

The Group has on occasion been required to take legal action to protect its intellectual property and other rights against infringement. It has also had to defend itself against proceedings brought by other parties, including product liability and insurance subrogation claims. Provision is made for any expected costs and liabilities in relation to these proceedings where appropriate, though there can be no guarantee that such provisions (which may be subject to potentially material revision from time to time) will accurately predict the actual costs and liabilities that may be incurred.

All provisions may be subject to potentially material revisions from time to time if new information becomes available as a result of future events.

Retirement benefits
The consolidated financial statements include costs in relation to, and provision for, retirement benefit obligations. The costs and the present value of any related pension assets and liabilities depend on such factors as life expectancy of the members and the discount rate used to calculate the present value of the liabilities. The Group uses previous experience and independent actuarial advice to select the values of critical estimates.

At 31 January 2014 there is a retirement benefit asset of £102.5m (31 July 2013: £121.7m) which arises from the rights of the employers to recover the surplus at the end of the life of the scheme. If the pension schemes were wound up while they still had members, the schemes would need to buy out the benefits of all members. The buy outs would cost significantly more than the present value of the scheme liabilities calculated in accordance with IAS 19 (Revised 2011): Employee benefits.

Taxation
The Group has recognised deferred tax assets of £24.7m (31 July 2013: £28.1m) relating to losses and £85.2m (31 July 2013: £85.6m) relating to the John Crane, Inc. and Titeflex Corporation litigation provisions. The recognition of assets pertaining to these items involves judgement by management as to the likelihood of realisation of these deferred tax assets and this is based on a number of factors, which seek to assess the expectation that the benefit of these assets will be realised, including appropriate taxable temporary timing differences and it has been concluded that there will be sufficient taxable profits in future periods to support recognition.

2 Segment information

Analysis by operating segment

The Group is organised into five divisions: John Crane, Smiths Medical, Smiths Detection, Smiths Interconnect and Flex-Tek. These divisions design and manufacture the following products:

- John Crane – mechanical seals, seal support systems, engineered bearings, power transmission couplings and specialist filtration systems;
- Smiths Medical – medication delivery systems, vital care products and safety devices that prevent needlestick injuries and reduce cross-infection;
- Smiths Detection – sensors that detect and identify explosives, narcotics, weapons, chemical agents, biohazards and contraband;
- Smiths Interconnect – specialised electronic and radio frequency components and sub-systems that connect, protect and control critical systems;
- Flex-Tek – engineered components that heat and move fluids and gases, flexible hosing and rigid tubing.

The position and performance of each division is reported monthly to the Board of Directors. This information is prepared using the same accounting policies as the consolidated financial information except that the Group uses headline operating profit to monitor divisional results and operating assets to monitor divisional position. See note 3 for an explanation of which items are excluded from headline measures. Intersegment sales and transfers are charged at arm's length prices.

							Period ended 31 January 2014
	John Crane £m	**Smiths Medical £m**	**Smiths Detection £m**	**Smiths Interconnect £m**	**Flex-Tek £m**	**Corporate costs £m**	**Total £m**
Revenue	**468.8**	**388.9**	**251.4**	**209.5**	**123.2**		**1,441.8**
Divisional headline operating profit	**108.6**	**71.1**	**29.6**	**27.4**	**22.6**		**259.3**
Corporate headline operating costs						**(14.1)**	**(14.1)**
Headline operating profit	**108.6**	**71.1**	**29.6**	**27.4**	**22.6**	**(14.1)**	**245.2**
Exceptional operating items (note 4)	**(38.2)**	**(3.3)**	**(1.6)**	**(2.7)**	**(4.7)**	**(0.8)**	**(51.3)**
Legacy retirement benefits					**(0.1)**	**(3.4)**	**(3.5)**
Amortisation of acquired intangible assets	**(6.6)**	**(4.9)**	**(0.1)**	**(8.9)**	**(0.1)**		**(20.6)**
Operating profit/(loss)	**63.8**	**62.9**	**27.9**	**15.8**	**17.7**	**(18.3)**	**169.8**
Exceptional finance costs – adjustment to discounted provision (note 4)	**(2.3)**				**(0.6)**		**(2.9)**
Net finance costs – other							**(35.4)**
Profit before taxation							**131.5**

							Period ended 31 January 2013
	John Crane £m	Smiths Medical £m	Smiths Detection £m	Smiths Interconnect £m	Flex-Tek £m	Corporate costs £m	Total £m
Revenue	469.5	412.9	254.6	218.5	119.7		1,475.2
Divisional headline operating profit	102.1	87.1	30.5	29.6	20.0		269.3
Corporate headline operating costs						(16.6)	(16.6)
Headline operating profit	102.1	87.1	30.5	29.6	20.0	(16.6)	252.7
Exceptional operating items (note 4)	(8.1)	0.3	(4.2)		(2.6)	(0.2)	(14.8)
Legacy retirement benefits (restated)						(4.1)	(4.1)
Amortisation of acquired intangible assets	(7.1)	(5.6)	(0.6)	(9.5)	(0.1)		(22.9)
Operating profit/(loss) (restated)	86.9	81.8	25.7	20.1	17.3	(20.9)	210.9
Exceptional finance costs – adjustment to discounted provision (note 4)	(1.4)				(0.4)		(1.8)
Net finance costs – other (restated)							(43.4)
Profit before taxation (restated)							165.7

							Year ended 31 July 2013
	John Crane £m	Smiths Medical £m	Smiths Detection £m	Smiths Interconnect £m	Flex-Tek £m	Corporate costs £m	Total £m
Revenue	985.7	850.4	559.0	460.6	252.9		3,108.6
Divisional headline operating profit	230.5	189.1	58.0	68.8	43.2		589.6
Corporate headline operating costs						(29.9)	(29.9)
Headline operating profit/(loss)	230.5	189.1	58.0	68.8	43.2	(29.9)	559.7
Exceptional operating items (note 4)	(10.8)	1.2	(4.9)	(0.2)	(7.0)	1.8	(19.9)
Legacy retirement benefits (restated)						(6.7)	(6.7)
Amortisation and impairment of acquired intangible assets	(14.2)	(11.4)	(1.1)	(19.7)	(0.2)		(46.6)
Operating profit/(loss) (restated)	205.5	178.9	52.0	48.9	36.0	(34.8)	486.5
Exceptional finance costs – adjustment to discounted provision (note 4)	(3.3)				(0.9)		(4.2)
Net finance costs – other (restated)							(86.6)
Profit before taxation (restated)							395.7

The net operating assets of the five divisions are set out below:

						31 January 2014
	John Crane £m	Smiths Medical £m	Smiths Detection £m	Smiths Interconnect £m	Flex-Tek £m	Total £m
Property, plant, equipment, development projects and other intangibles	**91.1**	**154.3**	**104.1**	**35.6**	**18.9**	**404.0**
Working capital assets	**336.5**	**219.3**	**302.3**	**135.7**	**70.0**	**1,063.8**
Operating assets	**427.6**	**373.6**	**406.4**	**171.3**	**88.9**	**1,467.8**
Derivatives, tax and retirement benefit assets						**324.9**
Goodwill and acquired intangibles						**1,444.5**
Corporate assets						**136.5**
Cash						**175.9**
Total assets						**3,549.6**
Working capital liabilities	**(133.8)**	**(87.2)**	**(162.3)**	**(54.3)**	**(22.5)**	**(460.1)**
Corporate and non-headline liabilities						**(317.8)**
Derivatives, tax and retirement benefits						**(474.5)**
Borrowings						**(1,076.7)**
Total liabilities						**(2,329.1)**
Average divisional capital employed	**895.9**	**1,135.4**	**663.4**	**543.4**	**140.5**	**3,378.6**
Average corporate capital employed						**(46.8)**
Average total capital employed						**3,331.8**

Non-headline liabilities comprise provisions and accruals relating to exceptional items, acquisitions and disposals.

Capital employed is a non-statutory measure of invested resources. It comprises statutory net assets adjusted to add goodwill recognised directly in reserves in respect of subsidiaries acquired before 1 August 1998 of £815.2m (31 July 2013: £815.2m) and eliminate post retirement benefit assets and liabilities and litigation provisions relating to exceptional items, both net of related tax, and net debt.

	John Crane £m	Smiths Medical £m	Smiths Detection £m	Smiths Interconnect £m	Flex-Tek £m	31 July 2013 Total £m
Property, plant, equipment, development projects and other intangibles	100.8	163.8	108.7	36.7	20.4	430.4
Working capital assets	363.0	245.2	343.1	159.5	78.1	1,188.9
Operating assets	463.8	409.0	451.8	196.2	98.5	1,619.3
Derivatives, tax and retirement benefit assets						355.0
Goodwill and acquired intangibles						1,576.9
Corporate assets						121.1
Cash						393.8
Total assets						4,066.1
Working capital liabilities	(166.8)	(96.8)	(202.0)	(69.5)	(28.5)	(563.6)
Corporate and non-headline liabilities						(325.4)
Derivatives, tax and retirement benefits						(545.3)
Borrowings						(1,138.2)
Total liabilities						(2,572.5)
Average divisional capital employed	897.9	1,141.4	657.4	554.4	140.2	3,391.3
Average corporate capital employed						(29.6)
Average total capital employed						3,361.7

Analysis of revenue

The revenue for the main product and service lines for each division is:

John Crane	Original equipment manufacture £m	Aftermarket: Oil, gas and petrochemical £m	Aftermarket: Chemical and pharmaceutical £m	Aftermarket: Distributors £m	Aftermarket: General industry £m	Total £m
Revenue period ended 31 January 2014	**176.4**	**180.4**	**39.8**	**32.6**	**39.6**	**468.8**
Revenue period ended 31 January 2013	168.5	184.8	40.2	33.1	42.9	469.5

Smiths Medical	Medication delivery £m	Vital care £m	Safety devices £m	Total £m
Revenue period ended 31 January 2014	**110.1**	**162.3**	**116.5**	**388.9**
Revenue period ended 31 January 2013	111.8	173.3	127.8	412.9

Smiths Detection	Transportation £m	Ports and borders £m	Military £m	Emergency responders £m	Critical infrastructure £m	Non-security £m	Total £m
Revenue period ended 31 January 2014	**127.2**	**44.1**	**25.6**	**6.2**	**47.3**	**1.0**	**251.4**
Revenue period ended 31 January 2013 (restated)	131.1	44.5	29.0	8.1	41.0	0.9	254.6

The split of Smiths Detection's revenue has been restated to consistently classify product sales. There is no impact on total reported revenue.

Smiths Interconnect	Connectors £m	Microwave £m	Power £m	Total £m
Revenue period ended 31 January 2014	**73.0**	**90.9**	**45.6**	**209.5**
Revenue period ended 31 January 2013	74.9	97.1	46.5	218.5

Flex-Tek	Fluid Management £m	Flexible Solutions £m	Heat Solutions £m	Construction £m	Total £m
Revenue period ended 31 January 2014	**41.1**	**17.5**	**25.2**	**39.4**	**123.2**
Revenue period ended 31 January 2013	41.2	17.5	25.0	36.0	119.7

3 Headline profit measures

The Company seeks to present a measure of underlying performance which is not impacted by exceptional items or items considered non-operational in nature. This measure of profit is described as 'headline' and is used by management to measure and monitor performance.

The following items have been excluded from the headline measure:

- exceptional items, including income and expenditure relating to material litigation in respect of products no longer in production;
- costs of operating retirement benefit schemes which have been closed so that no future benefits are accrued, which are referred to below as legacy schemes, and financing credits and charges relating to retirement benefits;
- amortisation of intangible assets acquired in a business combination – the amortisation charge is a non-cash item, and the directors believe that it should be added back to give a clearer picture of underlying performance; and
- other financing gains and losses, which represent the potentially volatile gains and losses on derivatives and other financial instruments which do not fall to be hedge accounted under IAS 39.

The excluded items are referred to as 'non-headline' items.

	Notes	**Period ended 31 January 2014 £m**	Period ended 31 January 2013 £m	Year ended 31 July 2013 £m
Operating profit (restated)		**169.8**	210.9	486.5
Exclude				
– exceptional operating items	4	**51.3**	14.8	19.9
– legacy retirement benefits (restated)		**3.5**	4.1	6.7
– amortisation of acquired intangible assets	9	**20.6**	22.9	46.6
Non-headline items in operating profit		**75.4**	41.8	73.2
Headline operating profit		**245.2**	252.7	559.7
Finance costs (restated)		**(38.3)**	(45.2)	(90.8)
Exclude				
– exceptional finance costs	4	**2.9**	1.8	4.2
– other financing gains and losses			1.1	1.9
– other finance income – retirement benefits (restated)		**4.7**	12.1	23.0
Non-headline items in finance costs		**7.6**	15.0	29.1
Headline finance costs		**(30.7)**	(30.2)	(61.7)
Profit before taxation (restated)		**131.5**	165.7	395.7
Non-headline items in operating profit (restated)		**75.4**	41.8	73.2
Non-headline items in finance costs (restated)		**7.6**	15.0	29.1
Headline profit before taxation		**214.5**	222.5	498.0
Profit after taxation – continuing operations (restated)		**94.4**	121.2	316.6
Exclude				
– non-headline items in profit before taxation (restated)		**83.0**	56.8	102.3
– tax on excluded items (restated)		**(20.8)**	(16.6)	(52.9)
		62.2	40.2	49.4
Headline profit after taxation – continuing operations		**156.6**	161.4	366.0

Statutory operating profit and finance costs and retirement benefits charges have been restated to reflect the adoption of IAS 19 (Revised 2011): Employee benefits. There is no impact on any headline measures because the principal defined benefit schemes have been closed.

Headline earnings before interest, tax depreciation and amortisation

Headline EBITDA, calculated as follows, is used to calculate the ratio of net debt to EBITDA.

	Notes	**Period ended 31 January 2014 £m**	Period ended 31 January 2013 £m	Year ended 31 July 2013 £m
Headline operating profit		**245.2**	252.7	559.7
Exclude				
Depreciation	10	**23.4**	27.1	52.3
Amortisation of development costs	9	**9.5**	10.0	21.3
Amortisation of software, patents and intellectual property	9	**6.9**	6.5	13.2
Headline EBITDA		**285.0**	296.3	646.5

4 Exceptional items

An analysis of the amounts presented as exceptional items in these financial statements is given below:

	Period ended 31 January 2014 £m	Period ended 31 January 2013 £m	Year ended 31 July 2013 £m
Operating items			
Restructuring programmes	**(14.3)**	(4.8)	(7.8)
Sale of intellectual property relating to diabetes	**0.5**		1.2
Resolution of legacy litigation	**0.6**		
Gains on changes to post retirement benefits		1.7	3.5
Profit on disposal of businesses	**2.3**	0.7	0.9
Profit on disposal of property			5.0
Adjustment to contingent consideration provided on acquisitions	**(0.5)**		1.4
Costs of acquisitions, disposals and aborted transactions	**(1.1)**		(3.0)
Litigation			
– provision for Titeflex Corporation subrogation claims (note 13)	**(4.7)**	(2.6)	(6.8)
– provision for John Crane, Inc. asbestos litigation (note 13)	**(34.1)**	(9.8)	(14.3)
	(51.3)	(14.8)	(19.9)
Financing items			
Exceptional finance costs – adjustment to discounted provision			
– provision for Titeflex Corporation subrogation claims (note 13)	**(0.6)**	(0.4)	(0.9)
– provision for John Crane, Inc. asbestos litigation (note 13)	**(2.3)**	(1.4)	(3.3)
	(54.2)	(16.6)	(24.1)

Period ended 31 January 2014

Restructuring costs include £12.4m in respect of fuel for growth and £1.7m in respect of the improvement programme in Smiths Detection announced in September 2011. These programmes, which involve redundancy, relocation and consolidation of manufacturing, are considered exceptional by virtue of their size.

Profit on disposal of businesses includes the expiry of certain warranties on the disposal of Cross Match Technologies, Inc which has generated an additional profit of £2.5m.

A charge of £4.7m has been made by Titeflex Corporation in respect of changes to the estimated cost of future claims including those from insurance companies seeking recompense for damage allegedly caused by lightning strike, net of gains of £0.2m relating to changes in discounting.

The operating charge in respect of John Crane, Inc. litigation comprises £36.8m in respect of increased provision for adverse judgments and legal defence costs, £0.5m in respect of legal fees in connection with litigation against insurers, less £3.2m arising from the increase in US risk free rates.

5 Taxation

The interim tax charge of 28.2% is calculated by applying the estimated effective headline tax rate of 27.0% for the year ended 31 July 2014 to headline profit before tax and then taking into account the tax effect of non-headline items in the interim period.

A reconciliation of total and headline tax charge is as follows:

	Period ended 31 January 2014 £m		Period ended 31 January 2013 (restated) £m		Year ended 31 July 2013 (restated) £m	
	Continuing operations £m	Tax rate	Continuing operations £m	Tax rate	Continuing operations £m	Tax rate
Profit before taxation	**131.5**		165.7		395.7	
Taxation	**(37.1)**	**28.2%**	(44.5)	26.9%	(79.1)	20.0%
Adjustments						
Non-headline items excluded from profit before taxation (note 3)	**83.0**		56.8		102.3	
Taxation on non-headline items	**(20.8)**		(16.6)		(52.9)	
Headline						
Headline profit before taxation	**214.5**		222.5		498.0	
Taxation on headline profit	**(57.9)**	**27.0%**	(61.1)	27.5%	(132.0)	26.5%

Taxation on non-headline items includes a credit of £1.8m (31 January 2013: £2.0m; 31 July 2013: £4.5m) relating to tax relief on the change in accounting for retirement benefit costs following the adoption of IAS 19 (Revised 2011).

The changes in the value of the net tax liability in the period were:

	Current tax £m	Deferred tax £m	Net tax balance £m
At 31 July 2013	(46.7)	112.3	65.6
Foreign exchange gains and losses	(0.2)	(9.1)	(9.3)
(Charge)/credit to income statement	(43.1)	6.0	(37.1)
Charge to reserves		(3.1)	(3.1)
Tax paid	60.0		60.0
At 31 January 2014	**(30.0)**	**106.1**	**76.1**

The deferred tax charge to reserves relates to actuarial gains on the US pension plans. No deferred tax credit has been recognised in respect of the actuarial losses on the UK pension plans, because the deferred tax asset has not been recognised due to uncertainty as to its recoverability.

6 Dividends

The following dividends were declared and paid in the period:

	Period ended 31 January 2014 £m	Period ended 31 January 2013 £m	Year ended 31 July 2013 £m
Ordinary final dividend of 27.00p for 2013 (2012: 26.25p) paid 22 November 2013	**106.4**	103.2	103.2
Special dividend of 30.00p for 2013 paid 22 November 2013	**118.3**		
Ordinary interim dividend of 12.50p for 2013 paid 26 April 2013			49.2
	224.7	103.2	152.4

An interim dividend of 12.75p per share was declared by the Board on 18 March 2014 and will be paid to shareholders on 25 April 2014. This dividend has not been included as a liability in these accounts and is payable to all shareholders on the register of Members at close of business on 28 March 2014.

7 Earnings per share

Basic earnings per share are calculated by dividing the profit for the year attributable to equity shareholders of the Parent Company by the average number of ordinary shares in issue during the year.

	Period ended 31 January 2014 £m	Period ended 31 January 2013 (restated) £m	Year ended 31 July 2013 (restated) £m
Profit attributable to equity shareholders for the year			
– continuing	**93.3**	120.5	315.0
– total	**93.4**	120.5	315.0
Average number of shares in issue during the year	**394,166,825**	393,075,730	393,323,206

Diluted earnings per share are calculated by dividing the profit attributable to ordinary shareholders by 396,377,484 (period ended 31 January 2013: 396,725,564; year ended 31 July 2013: 397,467,678) ordinary shares, being the average number of ordinary shares in issue during the year adjusted by the dilutive effect of employee share schemes.

A reconciliation of basic and headline earnings per share – continuing is as follows:

	Period ended 31 January 2014 £m		Period ended 31 January 2013 (restated) £m		Year ended 31 July 2013 (restated) £m	
	£m	**EPS (p)**	£m	EPS (p)	£m	EPS (p)
Profit attributable to equity shareholders of the Parent Company	**93.3**	**23.7**	120.5	30.7	315.0	80.1
Exclude						
Non-headline items and related tax (note 3)	**62.2**	**15.8**	40.2	10.2	49.4	12.6
Headline	**155.5**	**39.5**	160.7	40.9	364.4	92.7
Headline EPS – diluted (p)		**39.2**		40.5		91.7

8 Post retirement benefits

Smiths provides post retirement benefits to employees in a number of countries throughout the world. The arrangements include defined benefit and defined contribution plans and, mainly in the United Kingdom (UK) and United States of America (US), post retirement healthcare. The principal defined benefit pension plans are in the UK and in the US and these have been closed so that no future benefits are accrued.

Where any individual scheme shows a surplus under IAS 19 (Revised 2011), this is disclosed on the balance sheet as a retirement benefit asset. The IAS 19 (Revised 2011) surplus of any one scheme is not available to fund the IAS 19 (Revised 2011) deficit of another scheme. The retirement benefit asset arises from the rights of the employers to recover the surplus at the end of the life of the scheme. If the pension schemes were wound up while they had members, the schemes would need to buy out the benefits of all members. The buy outs would cost significantly more than the present value of scheme liabilities calculated in accordance with IAS 19 (Revised 2011).

The principal assumptions used in updating the valuations are set out below:

	31 January 2014		31 January 2013		31 July 2013	
	UK	**US**	UK	US	UK	US
Rate of increase for active deferred members	**4.2%**	**n/a**	4.3%	n/a	4.3%	n/a
Rate of increase in pensions in payment	**3.3%**	**n/a**	3.4%	n/a	3.4%	n/a
Rate of increase in deferred pensions	**3.3%**	**n/a**	3.4%	n/a	3.4%	n/a
Discount rate	**4.2%**	**4.7%**	4.5%	4.2%	4.4%	4.8%
Inflation rate	**3.3%**	**n/a**	3.4%	n/a	3.4%	n/a
Healthcare cost increases	**5.0%**	**n/a**	5.0%	n/a	5.0%	n/a

The amounts recognised in the balance sheet were as follows:

	31 January 2014 £m	31 January 2013 £m	31 July 2013 £m
Market value of funded plan assets	**3,715.9**	3,516.6	3,696.2
Present value of funded scheme liabilities	**(3,847.5)**	(3,792.1)	(3,842.6)
Unfunded pension plans	**(84.6)**	(84.7)	(86.1)
Post retirement healthcare	**(19.4)**	(21.6)	(21.1)
Unrecognised asset due to surplus restriction		(0.1)	
Net retirement benefit liability	**(235.6)**	(381.9)	(253.6)
Retirement benefit assets	**102.5**	83.0	121.7
Retirement benefit obligations	**(338.1)**	(464.9)	(375.3)
Net retirement benefit liability	**(235.6)**	(381.9)	(253.6)

The changes in the present value of the net pension liability in the period were:

	31 January 2014 £m	31 January 2013 (restated) £m	31 July 2013 (restated) £m
At beginning of period	**(253.6)**	(620.2)	(620.2)
Exchange adjustment	**13.3**	0.9	(8.1)
Current service cost	**(1.4)**	(2.1)	(4.1)
Scheme administration costs	**(3.5)**	(4.1)	(6.7)
Past service cost, curtailments and settlements		2.1	4.3
Finance charges – retirement benefits	**(4.7)**	(12.1)	(23.0)
Contributions by employer	**51.6**	41.0	77.5
Actuarial (loss)/gain	**(37.3)**	212.6	326.6
Movement in surplus restriction			0.1
Net retirement benefit liability	**(235.6)**	(381.9)	(253.6)

Actuarial gains and losses have primarily arisen from increases in the value of US scheme assets offset by losses due to lower discount rates in the UK and US.

Adopting IAS 19 (Revised 2011) has had the following impact on reported results:

	31 January 2014 £m	31 January 2013 (restated) £m	31 July 2013 (restated) £m
Additional charge to operating profit	**(3.5)**	(4.1)	(6.7)
Increased finance charges	**(27.3)**	(18.0)	(39.4)
Impact on profit before tax	**(30.8)**	(22.1)	(46.1)
Change to actuarial gains and losses recognised	**30.8**	22.1	46.1

9 Intangible assets

	Goodwill £m	Development costs £m	Acquired intangibles £m	Software, patents and intellectual property £m	Total £m
Cost					
At 1 August 2013	1,553.3	217.4	430.2	155.7	2,356.6
Exchange adjustments	(109.8)	(16.8)	(32.5)	(6.1)	(165.2)
Additions		14.7		8.0	22.7
Disposals	(2.7)	(1.1)	(1.7)	(0.3)	(5.8)
At 31 January 2014	**1,440.8**	**214.2**	**396.0**	**157.3**	**2,208.3**
Amortisation					
At 1 August 2013	98.6	93.5	308.0	110.5	610.6
Exchange adjustments	(7.0)	(7.5)	(23.5)	(5.3)	(43.3)
Charge for the period		9.5	20.6	6.9	37.0
Disposals	(2.7)		(1.7)	(0.2)	(4.6)
At 31 January 2014	**88.9**	**95.5**	**303.4**	**111.9**	**599.7**
Net book value at 31 January 2014	**1,351.9**	**118.7**	**92.6**	**45.4**	**1,608.6**
Net book value at 31 January 2013	1,412.1	114.3	140.5	43.7	1,710.6
Net book value at 31 July 2013	1,454.7	123.9	122.2	45.2	1,746.0

Goodwill sensitivity analysis

Goodwill of £117.1m (31 July 2013: £126.9m) is allocated to Smiths Interconnect Power. The Annual Report 2013 disclosed that reasonable changes in the calculation assumptions would cause the value in use of Smiths Interconnect Power to fall below its carrying value. This impairment testing has been updated to 31 January 2014. No impairment has been identified, but sensitivity analysis identifies the following risks:

	Period ended 31 January 2014 Change required to trigger impairment	Year ended 31 July 2013 Change required to trigger impairment
Forecast operating cash-flow	**9% reduction**	4% reduction
Discount rate	**0.9% higher**	0.5% higher
Long-term growth rates	**1.8% lower**	0.9% lower

Sales assumptions for Smiths Interconnect Power are based on:

- the current order book;
- proportion of recent tenders which have been successful; and
- independent projections of the expected growth of the data centre market in North America.

Margin projections for Smiths Interconnect Power are based on current variable costs and production capacity, and the expected costs of increasing capacity to support higher levels of sales.

For the other cash generating units, nothing has occurred since the year end which would require additional review of carrying values before the annual testing is carried out.

10 Property, plant and equipment

	Land and buildings £m	Plant and machinery £m	Fixtures, fittings, tools and equipment £m	Total £m
Cost or valuation				
At 1 August 2013	199.6	553.9	229.6	983.1
Exchange adjustments	(14.2)	(38.7)	(18.5)	(71.4)
Additions	2.6	15.5	6.0	24.1
Disposals	(0.7)	(5.5)	(2.2)	(8.4)
At 31 January 2014	**187.3**	**525.2**	**214.9**	**927.4**
Depreciation				
At 1 August 2013	98.3	419.7	185.1	703.1
Exchange adjustments	(6.9)	(28.7)	(15.4)	(51.0)
Charge for the period	3.6	13.5	6.3	23.4
Disposals	(0.5)	(4.9)	(2.0)	(7.4)
At 31 January 2014	**94.5**	**399.6**	**174.0**	**668.1**
Net book value at 31 January 2014	**92.8**	**125.6**	**40.9**	**259.3**
Net book value at 31 January 2013	100.2	124.7	41.8	266.7
Net book value at 31 July 2013	101.3	134.2	44.5	280.0

11 Borrowings and net debt

This note sets out the calculation of net debt, an important measure in explaining our financing position. The net debt figure includes accrued interest and the fair value adjustments relating to hedge accounting.

	31 January 2014 £m	31 January 2013 £m	31 July 2013 £m
Cash and cash equivalents			
Net cash and deposits	**175.9**	275.5	393.8
Short-term borrowings			
Bank overdrafts	**(6.1)**	(21.0)	(7.3)
$250m 6.05% US$ Guaranteed notes 2014	**(151.8)**		(164.5)
Bank and other loans	**(1.0)**	(1.1)	(1.2)
Interest accrual	**(23.9)**	(24.2)	(14.1)
	(182.8)	(46.3)	(187.1)
Long-term borrowings			
$250m 6.05% US$ Guaranteed notes 2014		(157.2)	
£150m 7.25% Sterling Eurobond 2016	**(149.7)**	(149.5)	(149.6)
€300m 4.125% Eurobond 2017	**(251.0)**	(261.8)	(267.5)
$175m 7.37% US$ Private placement 2018	**(106.3)**	(110.2)	(115.3)
$250m 7.20% US$ Guaranteed notes 2019	**(151.1)**	(156.5)	(163.8)
$400m 3.625% US$ Guaranteed notes 2022	**(234.6)**	(247.3)	(253.4)
Bank and other loans	**(1.2)**	(1.7)	(1.5)
	(893.9)	(1,084.2)	(951.1)
Borrowings	**(1,076.7)**	(1,130.5)	(1,138.2)
Net debt	**(900.8)**	(855.0)	(744.4)

On 19 February 2014 Smiths completed the refinancing of its existing $800m Revolving Credit Facility which was due to mature in December 2015. The new $800m Revolving Credit Facility matures in February 2019 with two uncommitted one-year extension options.

Movements in net debt

	Net cash and cash equivalents £m	Other short-term borrowing £m	Long-term borrowings £m	Net debt £m
At 31 July 2013	386.5	(179.8)	(951.1)	(744.4)
Foreign exchange gains and losses	(20.9)	12.9	58.6	50.6
Net cash inflow/(outflow)	(195.8)			(195.8)
Repayment and drawdown of borrowings		0.3		0.3
Capitalisation, interest accruals and unwind of capitalised fees		(7.9)	(0.4)	(8.3)
Fair value movement from interest rate hedging		(2.0)	(1.2)	(3.2)
Change in maturity analysis		(0.2)	0.2	
At 31 January 2014	**169.8**	**(176.7)**	**(893.9)**	**(900.8)**

12 Fair value of financial instruments

	Carrying value 31 January 2014 £m	**Fair value 31 January 2014 £m**	Carrying value 31 January 2013 £m	Fair value 31 January 2013 £m	Carrying value 31 July 2013 £m	Fair value 31 July 2013 £m
Level 1 valuations						
Financial assets – other investments	**95.5**	**95.5**	74.2	74.2	83.0	83.0
Level 2 valuations						
Financial derivatives - assets	**23.7**	**23.7**	22.6	22.6	14.5	14.5
Borrowings	**(1,076.7)**	**(1,152.7)**	(1,130.5)	(1,231.8)	(1,138.2)	(1,225.5)
Financial derivatives - liabilities	**(13.8)**	**(13.8)**	(7.2)	(7.2)	(16.8)	(16.8)
Level 3 valuations						
Financial assets – other investments	**3.4**	**3.4**	2.6	2.6	3.1	3.1

Investments with level 1 valuations comprise quoted government bonds.

Derivatives are valued at the net present value of the future cash-flows calculated using market exchange rates and yield curves at the balance sheet date. Borrowings are valued at the net present value of the future cash-flows using credit spreads and yield curves derived from market data.

Cash, trade receivables and trade payables are excluded from this table because carrying value is a reasonable approximation to fair value for all these assets and liabilities.

13 Provisions and contingent liabilities

	Trading	Exceptional and legacy			Total
	£m	John Crane, Inc. litigation £m	Titeflex Corporation litigation £m	Other £m	£m
At 31 July 2013	40.7	210.0	65.6	19.9	336.2
Exchange adjustments	(2.9)	(16.7)	(5.2)	(1.0)	(25.8)
Provision charged	11.2	33.6	4.7	5.2	54.7
Provision released	(1.8)			(0.4)	(2.2)
Unwind of provision discount		2.3	0.6		2.9
Utilisation	(9.0)	(22.2)	(3.4)	(2.9)	(37.5)
At 31 January 2014	**38.2**	**207.0**	**62.3**	**20.8**	**328.3**

The John Crane, Inc. and Titeflex Corporation litigation provisions are the only provisions which are discounted.

Trading

The trading provision primarily relates to warranties £37.6m (31 July 2013: £40.0m) but also includes product liabilities and litigation in respect of current products or on-going business activities.

Contingent liabilities

In the ordinary course of its business, the Group is subject to commercial disputes and litigation such as product liability claims, employee disputes and other kinds of lawsuits, and faces different types of legal issues in different jurisdictions. The high level of activity in the US, for example, exposes the Group to the likelihood of various types of litigation commonplace in that country, such as 'mass tort' and 'class action' litigation, legal challenges to the scope and validity of patents, and product liability and insurance subrogation claims. These types of proceedings (or the threat of them) are also used to create pressure to encourage negotiated settlement of disputes. Any claim brought against the Group (with or without merit), could be costly to defend. These matters are inherently difficult to quantify. In appropriate cases a provision is recognised based on best estimates and management judgement but there can be no guarantee that these provisions (which may be subject to potentially material revision from time to time) will result in an accurate prediction of the actual costs and liabilities that may be incurred. There are also contingent liabilities in respect of litigation for which no provisions are made.

John Crane, Inc.

John Crane, Inc. ("JCI") is one of many co-defendants in numerous lawsuits pending in the United States in which plaintiffs are claiming damages arising from alleged exposure to, or use of, products previously manufactured which contained asbestos. Until 2006, the awards, the related interest and all material defence costs were met directly by insurers. In 2007, JCI secured the commutation of certain insurance policies in respect of product liability. While JCI has excess liability insurance, the availability of such insurance and scope of the cover are currently the subject of litigation in the United States. Pending the outcome of that litigation, JCI has met defence costs directly. Provision is made in respect of the expected costs of defending known and predicted future claims and of adverse judgments in relation thereto, to the extent that such costs can be reliably estimated. No account has been taken of recoveries from insurers as their nature and timing are not yet sufficiently certain to permit recognition as an asset for these purposes.

The JCI products generally referred to in these cases consist of industrial sealing product, primarily packing and gaskets. The asbestos was encapsulated within these products in such a manner that causes JCI to believe, based on tests conducted on its behalf, that the products were safe. JCI ceased manufacturing products containing asbestos in 1985.

JCI continues to actively monitor the conduct and effect of its current and expected asbestos litigation, including the most efficacious presentation of its 'safe product' defence, and intends to continue to resist these asbestos claims based upon this defence. Approximately 232,000 claims (31 July 2013: 230,000) claims against JCI have been dismissed before trial over the last 34 years. JCI is currently a defendant in cases involving approximately 81,000 claims (31 July 2013: 81,000 claims). Despite the large number of claims brought against JCI, it has had final judgments against it, after appeals, in only 127 cases (31 July 2013: 121 cases) over the period, and has had to pay awards amounting to approximately US$138m (31 July 2013: US$120m). JCI has also incurred significant additional defence costs and, whilst the number of claims being filed against JCI and other defendants has been declining, the proportion of mesothelioma claims has increased, and JCI's ability to defend these cases successfully is likely to have a significant impact on its annual aggregate adverse judgment and defence costs.

John Crane, Inc. litigation provision

The provision is based on past history and allows for decreasing levels of new claims based on published tables of asbestos incidence projections and is determined using asbestos valuation experts, Bates White LLC. Whilst published incidence curves can be used to estimate the likely future pattern of asbestos related disease, John Crane, Inc.'s claims experience is significantly impacted by other factors which influence the US litigation environment. These can include: changing approaches on the part of the plaintiffs' bar; changing attitudes amongst the judiciary at both trial and appellate levels; and legislative and procedural changes in both the state and federal court systems. The projections use a 10 year time horizon on the basis that Bates White LLC consider that there is substantial uncertainty in the asbestos litigation environment so probable expenditures are not reasonably estimable beyond this time horizon.

The assumptions made in assessing the appropriate level of provision include:

- The period over which the expenditure can be reliably estimated.
- The future trend of legal costs.
- The rate of future claims filed.
- The rate of successful resolution of claims.
- The average amount of judgments awarded.

However, because of the significant uncertainty associated with the future level of asbestos claims and of the costs arising out of related litigation, there can be no guarantee that the assumptions used to estimate the provision will result in an accurate prediction of the actual costs that may be incurred and, as a result, the provision may be subject to potentially material revision from time to time if new information becomes available as a result of future events.

The provision in respect of JCI is a discounted pre-tax provision using discount rates, being the risk-free rate on US debt instruments for the appropriate period. The deferred tax asset related to this provision is shown within the deferred tax balance. Set out below is the gross, discounted and post-tax information relating to this provision:

	31 January 2014 £m	31 January 2013 £m	31 July 2013 £m
Gross provision	**231.1**	226.4	232.8
Discount	**(24.1)**	(17.7)	(22.8)
Discounted pre-tax provision	**207.0**	208.7	210.0
Deferred tax	**(69.6)**	(49.8)	(60.7)
Discounted post-tax provision	**137.4**	158.9	149.3

John Crane, Inc. contingent liabilities

Provision has been made for future defence costs and the cost of adverse judgments expected to occur. JCI's claims experience is significantly impacted by other factors which influence the US litigation environment. These can include: changing approaches on the part of the plaintiffs' bar; changing attitudes amongst the judiciary at both trial and appellate levels; and legislative and procedural changes in both the state and federal court systems. As a result, whilst the Group anticipates that asbestos litigation will continue beyond the period covered by the provision, the uncertainty surrounding the US litigation environment beyond this point is such that the costs cannot be reliably estimated.

Titeflex Corporation

In recent years Titeflex Corporation, a subsidiary of the Group in the Flex-Tek division, has received a number of claims from insurance companies seeking recompense on a subrogated basis for the effects of damage allegedly caused by lightning strikes in relation to its flexible gas piping product. It has also received a number of product liability claims regarding this product, some in the form of purported class actions. Titeflex Corporation believes that its products are a safe and effective means of delivering gas when installed in accordance with the manufacturer's instructions and local and national codes, however some subrogation claims have been settled on an individual basis without admission of liability. Equivalent third-party products in the US marketplace face similar challenges with the profile of legal activity appearing to increase in recent times.

Titeflex Corporation litigation provision

The continuing progress of claims and the pattern of settlement, together with the recent market place activity, provide sufficient evidence to recognise a liability in the accounts. Therefore provision has been made for the costs which the Group is expected to incur in respect of future claims to the extent that such costs can be reliably estimated. Titeflex Corporation sells flexible gas piping with extensive installation and safety guidance (revised in 2008) designed to assure the safety of the product and minimise the risk of damage associated with lightning strikes.

The assumptions made in assessing the appropriate level of provision, which are based on past experience, include:

- The period over which expenditure can be reliably estimated.
- The number of future settlements.
- The average amount of settlements.

The projections use a rolling 10 year time horizon on the basis that there is substantial uncertainty in the US litigation environment so probable expenditures are not reasonably estimable beyond this time horizon.

However, because of the significant uncertainty associated with the future level of claims and of the costs arising out of related litigation, there can be no guarantee that the assumptions used to estimate the provision will result in an accurate prediction of the actual costs that may be incurred and, as a result, the provision may be subject to potentially material revision from time to time if new information becomes available as a result of future events.

The provision of £62.3m (31 July 2013: £65.6m) is a discounted pre-tax provision using discount rates, being the risk-free rate on US debt instruments for the appropriate period.

Titeflex Corporation contingent liabilities

The Group anticipates that litigation might continue beyond the period covered by the provision. However, the uncertainty surrounding the US litigation environment beyond this point (which reflects factors such as changing approaches on the part of the plaintiffs' bar; changing attitudes amongst the judiciary at both trial and appellate levels; and legislative and procedural changes in both the state and federal court systems) is such that the costs cannot be reliably estimated.

Other exceptional and legacy

Legacy provisions comprise provisions relating to former business activities and properties no longer used by Smiths. Exceptional provisions comprise all provisions which were disclosed as exceptional items when they were charged to the income statement.

These provisions cover exceptional reorganisation, vacant properties, disposal indemnities and litigation in respect of old products and discontinued business activities.

14 Cash-flow from operating activities

	Period ended 31 January 2014 £m	Period ended 31 January 2013 (restated) £m	Year ended 31 July 2013 (restated) £m
Operating profit – continuing	**169.8**	210.9	486.5
Amortisation of intangible assets	**37.0**	39.4	81.1
Loss/(profit)on disposal of property, plant and equipment and intangible assets	**2.0**	0.5	(4.3)
Profit on disposal of business	**(2.3)**	(0.7)	(0.9)
Depreciation of property, plant and equipment	**23.4**	27.1	52.3
Share-based payment expense	**4.2**	7.3	12.1
Retirement benefits	**(46.7)**	(36.9)	(71.0)
Increase in inventories	**(1.6)**	(35.7)	(20.3)
Decrease/(increase) in trade and other receivables	**35.8**	22.9	(30.3)
(Decrease)/increase in trade and other payables	**(65.0)**	(30.3)	31.8
Increase/(decrease) in provisions	**14.6**	(1.4)	(9.9)
Cash generated from operations	**171.2**	203.1	527.1
Interest	**(28.0)**	(19.9)	(59.6)
Tax paid	**(60.0)**	(63.3)	(114.1)
Net cash inflow from operating activities	**83.2**	119.9	353.4

Headline operating cash-flow

	Period ended 31 January 2014 £m	Period ended 31 January 2013 £m	Year ended 31 July 2013 £m
Net cash inflow from operating activities	**83.2**	119.9	353.4
Exclude			
Interest	**28.0**	19.9	59.6
Tax paid	**60.0**	63.3	114.1
Cash outflow in respect of exceptional operating items	**36.7**	18.9	43.9
Pension deficit payments	**49.0**	37.9	71.4
Include			
Expenditure on capitalised development, other intangible assets and property, plant and equipment	**(45.7)**	(39.1)	(96.0)
Disposals of property, plant and equipment in the ordinary course of business	**0.2**	2.0	1.5
Headline operating cash-flow	**211.4**	222.8	547.9

Free cash-flow

	Period ended 31 January 2014 £m	Period ended 31 January 2013 £m	Year ended 31 July 2013 £m
Net cash inflow from operating activities	**83.2**	119.9	353.4
Expenditure on capitalised development, other intangible assets and property, plant and equipment	**(45.7)**	(39.1)	(96.0)
Disposals of property, plant and equipment	**4.3**	2.0	3.9
Investment in financial assets relating to pensions financing	**(12.0)**	(12.0)	(24.0)
Free cash-flow	**29.8**	70.8	237.3
Investment in other financial assets	**(0.1)**	(0.1)	(0.3)
Acquisition of businesses		(0.5)	(0.5)
Disposal of businesses	**3.0**	0.7	0.3
Net cash-flow used in financing activities	**(228.5)**	(23.3)	(66.7)
Net increase/(decrease) in cash and cash equivalents	**(195.8)**	47.6	170.1

15 Related party transactions

The related party transactions in the period were consistent with the nature and size of transactions disclosed in the Annual Report for the year ended 31 July 2013.