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News release

London, Wednesday 18 March 2015

For immediate release

Interim results for the six months ended 31 January 2015

	Headline*				Statutory	
	2015 £m	2014 £m	Reported	Underlying#	**2015 £m**	2014 £m
Revenue	**1,416**	1,442	(2)%	1%	**1,416**	1,442
Operating profit	**232**	245	(5)%	(3)%	**164**	170
Operating margin	**16.4%**	17.0%	(60) bps	–	**11.6%**	11.8%
Pre-tax profit	**208**	215	(3)%	0%	**131**	132
Basic EPS	**38.5p**	39.5p	(3)%		**21.8p**	23.7p
Free cash-flow	**58**	30				
Dividend	**13.00p**	12.75p	2%		**13.00p**	12.75p
Return on capital employed	**15.4%**	16.6%	(120) bps			

*In addition to statutory reporting, Smiths Group reports its continuing operations on a headline basis. Headline profit is before exceptional items, impairment of goodwill and amortisation 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.

#Organic growth adjusting for foreign exchange translation.

Highlights

- Underlying revenue growth driven by Smiths Medical, Flex-Tek and John Crane
- Strong growth at Smiths Medical reflecting recent investment in infusion pumps
- John Crane delivered a resilient performance reflecting aftermarket strength
- Performance at Smiths Detection starting to stabilise as a result of initiatives
- Smiths Interconnect faces tough trading conditions; Flex-Tek performed well
- Headline operating margin lower with pressure in Detection and Interconnect
- Strong headline operating cash conversion at 88%; dividend up 2%

"Smiths Group delivered underlying revenue growth. Improvements at Smiths Medical, John Crane and Flex-Tek more than offset revenue declines at Smiths Detection and Smiths Interconnect where tough trading conditions persist. The reported results were held back by adverse foreign exchange.

"We remain focused on repositioning the business to accelerate medium-term revenue growth and have launched a new cross-divisional programme to add further momentum. '*Engineered for Growth*' has four workstreams: sales and marketing effectiveness; bringing new products to market faster through innovation; quality improvement; and increasing our presence in China. Our growth investment is funded by ongoing operational improvements and our '*Fuel for Growth*' programme, which is on track to generate £60m of annual savings by 2017.

"We expect to deliver improved underlying performance in the second half. Smiths Detection will benefit from a prior year comparator affected by one-off charges. John Crane is expected to see a slight easing in trading as upstream customers adjust their expenditure to the lower oil price and as some projects may be deferred. The growth rate at Smiths Medical will slow versus the strong first half performance. Seasonality will bias performance at Smiths Interconnect to the second half but trading in the second half will remain below last year's levels. Flex-Tek should continue to perform well. We are focused on investing to drive sales growth in what are attractive long-term markets, and on delivering further operational improvements, while generating strong cash conversion and returns."

Philip Bowman
Chief Executive

Divisional highlights*

	% of Group revenue	Underlying revenue growth*	Underlying headline operating profit growth*	Headline operating profit margin*		Headline return on capital employed*	
				2015	2014	**2015**	2014
John Crane	32%	**1%**	**0%**	**23.2%**	23.2%	**26.5%**	26.5%
Smiths Medical	29%	**6%**	**9%**	**19.0%**	18.3%	**15.1%**	15.3%
Smiths Detection	16%	**(5)%**	**(15)%**	**10.3%**	11.8%	**3.1%**	8.6%
Smiths Interconnect	14%	**(6)%**	**(33)%**	**9.2%**	13.1%	**12.0%**	12.2%
Flex-Tek	9%	**4%**	**3%**	**18.1%**	18.3%	**33.7%**	32.7%
Group	100%	**1%**	**(3)%**	**16.4%**	17.0%	**15.4%**	16.6%

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

John Crane

- Resilient performance with revenue up 1% driven by its focus on aftermarket services for rotating equipment
- Margins maintained at 23.2%; manufacturing constraints have now been addressed
- Current order book is solid, but project delays are possible in the current environment
- Tougher market conditions in upstream and first fit OEM signal a slight decline in trading for the full year

Smiths Medical

- Revenue up 6% due to strong ambulatory infusion performance and recovery in disposables
- Margins up 70 bps, reflecting higher volumes and efficiencies
- Full year performance is expected to moderate more in line with the market

Smiths Detection

- Revenue down 5% amid continued tough trading conditions; making progress on stabilising operations
- Margins down 150 bps with lower volumes and adverse pricing masking the benefit of efficiency gains
- Full year revenue is expected to be lower than last year; margins should improve against a weak comparator
- Recent order wins have strengthened order book for delivery in FY16

Smiths Interconnect

- Revenue 6% lower with pressures in Microwave and Connectors offsetting growth in Power
- Margins down 390 basis points on lower volumes, adverse operational gearing and mix
- We expect that seasonality will bias performance to the second half but will remain below prior year levels

Flex-Tek

- Revenue up 4% driven by US residential construction, specialty heating elements and aero/automotive hoses
- Margins down 20 bps with increased investment in marketing and new product development
- US construction and heating demand should support growth; margin outlook stable despite increased investment

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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 18 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 0062

International: +44 (0)20 3427 0662

US/Canada toll free: 1 877 841 4559

An audio replay is available for seven days on the following numbers (access PIN 654131#):

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 £131m (2014: £132m) and earnings per share were 21.8p (2014: 23.7p).

See note 3 to the interim report for the definition of headline profit measures and note 4 for an analysis of exceptional items.

Chief Executive's review

Results overview

The results benefited from Smiths Group's strength and breadth as a diversified engineering company, with a portfolio of leading-edge, technology-driven businesses serving a wide range of end markets and geographies. Underlying revenues rose as Smiths Medical saw growth in infusion pumps and a disposables recovery. Both Flex-Tek and John Crane reported further progress. Smiths Detection and Smiths Interconnect continue to face challenging end markets which affected revenues and profit margins. Foreign exchange translation continued to be a headwind to our reported results.

We maintained our programme of operational improvements and efficiencies across the businesses, helping to fund increased investment in high growth markets and new product development to accelerate medium-term revenue growth.

John Crane delivered a resilient performance as a result of its focus on aftermarket services despite the impact of a lower oil price on the wider energy services sector. Underlying revenue grew with higher aftermarket revenues for its rotating equipment more than offsetting pressures from its upstream oil services and first-fit rotating equipment business. Headline operating margins were maintained. Smiths Medical saw strong revenue growth as a result of its strategy to invest in infusion pumps in recent years and a recovery in disposables performance following the US distributor destocking last year. Margins improved on higher volumes and efficiency gains. Revenue and margins at Smiths Detection fell as it continues to trade in difficult markets with volume and price pressures. However, encouraging progress has been made in delivering efficiency gains and restructuring the business, which will deliver benefits over time. They have also secured new orders to strengthen the order book for the next financial year. Smiths Interconnect also experienced a weak first half due to customer spending delays and some programme slowdowns in various markets. Margins fell on the reduced volumes and associated cost absorption issues as well as adverse mix. Flex-Tek revenues benefited from growth from its US residential construction products, specialty heating elements and hoses for aerospace and automotive applications. Margins were stable despite increased investment in marketing and innovation.

Strategy

Our strategy is to continue to grow shareholder value by:

- Delivering revenue growth through investment in organic drivers, including new product development and expansion in high-growth markets, and through targeted acquisitions;
- Enhancing margins through a relentless drive for operational improvement across all our businesses;
- Finding smarter ways of working and having the best people;
- Promoting a culture of responsibility in everything we do;
- Generating strong operating cash-flows with efficient balance sheet management; and
- Allocating capital rigorously across the business, through both organic investment and acquisitions & disposals.

We continued to pursue these objectives and some examples of our progress are set out below. Of these objectives, the area where we see greatest opportunity is revenue growth. This remains a key priority for the Group as we seek to reposition the business.

Investing to accelerate revenue growth – '*Engineered for Growth*'

We have launched a new Group-wide programme – '*Engineered for Growth'* – to accelerate revenue growth, which is focused around four main priority areas: sales and marketing excellence, quality improvement, China, and innovation. This programme is designed to share and leverage our expertise across the divisions and to build momentum in these targeted areas. We expect this multi-year programme to deliver improved results over the medium-term as the initiatives gain traction.

Sales and marketing excellence - We recognise that we have in the past focused more on technology and engineering solutions and not enough on the customer and their needs. We are upgrading our sales and marketing capabilities to become a more customer and market-led business. Group-wide sales and marketing councils have been formed to improve customer insight and market segmentation, ensure better price positioning, drive the changes needed to build a more customer-centred business, and better exploit the Smiths brand. We have also held our first Sales Academy which is designed to improve the capabilities of our sales people.

Quality - We see a significant opportunity to improve quality that will in turn support our growth agenda and help reduce the costs of poor quality. We have developed a suite of metrics for defining the cost of poor quality with the aim of driving out these costs. These are being implemented across the Group. This should also improve customer satisfaction and perceptions.

China - As part of our broader initiative to increase our presence in high-growth emerging markets, we are prioritising resources and investment into China. We are establishing a Smiths Group presence in China that will provide key local expertise in legal, government affairs and commercial practice for all of the divisions. This will provide a focus to co-ordinate and leverage the Group's activities, presence and scale. The divisions are committed to delivering their strategic plans for China. John Crane, for instance, has recently undertaken a major long-term investment in its manufacturing and customer service centre in Tianjin. We continue to concentrate on our wider objective to increase the Group's presence in emerging markets. Emerging market revenues grew 5% at constant currencies and now represent 16.2% of Group revenues, an increase of 100 basis points.

Innovation - Innovation is our lifeblood as a technology company and we have invested consistently in R&D over recent years. Our task is to ensure this is at least matched by the contribution of new products to our revenues. It is also to accelerate the speed to market from the idea generation to the finished product. This workstream is examining ways to improve the effectiveness of our investment. Improved processes and performance yardsticks for new product vitality and attrition across all divisions have been agreed. Greater sharing of technical knowledge is also a priority and an Innovation Summit was held in January to devise the best ways of delivering the ground-breaking solutions our customers demand.

We are focused on improving the effectiveness of our innovation spend. Our company-funded investment in R&D declined 8% to £53m – mainly as a result of recent product launches at Smiths Detection, such as their XCT checked baggage screener, which signals the end of an investment phase on such projects. Smiths Detection has focused its investment more tightly around products that are expected to deliver more certain returns and has cut back on less attractive, non-strategic project areas.

Recent new product launches included John Crane's AURA 220 gas seal, the first of a new family of gas seals to be unveiled, which uses a common global design and patented polymeric sealing device to help cut operating costs. Among products developed and to be unveiled soon by Smiths Interconnect are a tail-mounted airborne antenna targeted at the regional and business jet market and a RF test product to complement its successful PIM (passive intermodulation) offerings. Checkpoint.Evo, a new software solution that greatly enhances inspection and integration capabilities at airport checkpoints, was launched by Smiths Detection in January and has already attracted orders.

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

We are funding investment in these growth initiatives through our *Fuel for Growth* programme, which is expected to generate £60m of annual savings for reinvestment in sales, marketing and new product development. The programme is expected to cost £120m over a three-year period, which will be treated as an exceptional item. There will also be some accompanying capital expenditure. This restructuring focuses on three areas: site rationalisation with a particular emphasis on manufacturing footprint to support future growth at lower costs; organisational effectiveness through delayering and broadening management control spans; and the upgrading of information systems – particularly in John Crane – to improve decision-making and to support the next stage of globalisation. To date, we have incurred costs of £44m across the programme, which has delivered annualised savings of £20m. For the full year, we expect to achieve an annualised savings of around £25m a year and incur £40m of costs which will be treated as exceptional.

	Programme to date		**Total programme expectations**	
	Costs to date	**Annualised savings to date**	**Total costs by end FY 2017**	**Full annual benefits by end FY 2017**
John Crane	8	10	25	13
Smiths Medical	15	5	45	23
Smiths Detection	13	-	34	14
Smiths Interconnect	8	5	12	7
Flex-Tek	-	-	4	3
Total	**44**	**20**	**120**	**60**

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. While the medium-term objective is to maintain this dividend cover, we will operate some flexibility in applying the 2.5 times cover to take account of short-term impacts such as foreign exchange.

The Board has declared an interim dividend of 13.00p per share, an increase of 2% reflecting the strong cash conversion in the period. The interim dividend will be paid on 24 April to shareholders registered at the close of business on 27 March. The ex-dividend date is 26 March.

Outlook

We expect to deliver improved underlying performance in the second half. Smiths Detection will benefit from a prior year comparator affected by one-off charges. John Crane is expected to see a slight easing in trading as upstream customers adjust their expenditure to the lower oil price and as some OE projects may be deferred. The growth rate at Smiths Medical will slow versus the strong first half performance. Seasonality will bias performance at Smiths Interconnect to the second half but trading in the second half will remain below last year's levels. Flex-Tek should continue to perform well. We are focused on investing to drive sales growth in what are attractive long-term markets, and on delivering further operational improvements, while generating strong cash conversion and returns.

Business review

Revenue
Revenue grew 1%, or £9m, on an underlying basis to £1,416m. Including adverse currency translation of £35m, overall reported revenue declined £26m (2%). The £9m underlying increase was driven by growth in Smiths Medical (+£25m), Flex-Tek (+£5m) and John Crane (+£3m), which was partially offset by declines at Smiths Interconnect (-£12m) and Smiths Detection (-£12m).

Profit
Headline operating profit saw an underlying reduction of 3% (£7m) to £232m. On a reported basis, headline operating profit fell £13m (5%) including adverse foreign exchange translation of £6m. Headline operating margin fell to 16.4% (2014: 17.0%), mainly the result of the tough trading conditions in Smiths Interconnect and Smiths Detection. The main drivers of the £7m underlying reduction were higher revenues and efficiencies at Smiths Medical (+£7m) and increased volumes at Flex-Tek (+£1m), which were more than offset by lower volumes, reduced overhead cost recovery and adverse mix at Smiths Interconnect (-£9m), weaker volumes and price at Detection (-£4m) and higher corporate costs (-£2m).

Operating profit on a statutory basis, after taking account of the items excluded from the headline figures, was £164m (2014: £170m) – see notes 3 and 4 for information on the excluded items. The decline was driven mainly by the £26m goodwill impairment on John Crane Production Solutions and the reduced headline operating profit.

The net interest charge on debt was reduced to £24m (2014: £30m), primarily due to the repayment of the $250m 6.05% fixed rate Notes in May 2014. Headline profit before tax decreased £7m to £208m (2014: £215m). On an underlying basis, headline profit before tax was flat.

The Group's tax rate on headline profit for the period was 26.5% (2014: 27.0%). Headline earnings per share decreased by 3% to 38.5p (2014: 39.5p).

On a statutory basis, profit before tax declined £1m to £131m (2014: £132m); it is stated after taking account of exceptional costs, a pensions finance charge of £4m (2014: £5m) and other items excluded from the headline measure.

Cash generation
Operating cash generation remained strong with headline operating cash of £204m (2014: £211m), representing 88% (2014: 86%) 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 increased £28m to £58m (2014: £30m). 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 £112m (2014: £83m).

Dividends paid in the period on ordinary shares amounted to £108m (2014: £225m consisting of final and special dividends).

Net debt at 31 January was £929m, up from £804m at 31 July 2014. The increase in net debt reflects outflows from dividends (£108m) and pension funding (£36m) as well as adverse foreign exchange translation (£47m).

John Crane

	2015 £m	2014 £m	Reported growth	Underlying growth
Revenue	**453**	469	(3)%	1%
Headline operating profit	**105**	109	(3)%	0%
Headline operating margin	**23.2%**	23.2%	0 bps	
Statutory operating profit	**61**	64	(5)%	
Return on capital employed	**26.5%**	26.5%	0 bps	

John Crane's underlying revenue grew 1% against a backdrop of more difficult market conditions in some parts of the energy segment. Reported revenue, including £19m of adverse foreign exchange translation, declined 3%. The underlying revenue growth reflects increased revenue in the aftermarket rotating equipment business, offset by declining sales in the first-fit rotating equipment and upstream oil services businesses. Excluding upstream oil services, revenues showed a 3% underlying increase.

Headline operating profit margin was maintained at 23.2%. Reported headline operating profit declined 3% (£4m), driven by adverse currency translation of £4m. Underlying headline operating profit was flat. The difference between statutory and headline operating profit primarily reflects a £26m goodwill impairment on John Crane Production Solutions as a result the impact of lower oil prices on their customers; the cost of John Crane, Inc. asbestos litigation of £12m and amortisation of acquired intangible assets of £4m. Return on capital employed was maintained at 26.5%.

Overall aftermarket revenues grew 3% on an underlying basis. However, excluding our upstream oil services business, sales rose 7% illustrating the strength of the rotating equipment aftermarket. Consumer demand for oil and gas has remained high and refineries are operating at full capacity, with the US and Latin America particularly strong. Recent contracts include a global framework agreement with a large petrochemical manufacturer based in Saudi Arabia and a new gas seal reliability management contract in Singapore.

John Crane continued to focus on strengthening its aftermarket capabilities in strategic locations, upgrading about 10% of our service centres around the globe in the last two years to give customers additional services, training and technical expertise. In ASEAN, we expanded the service super centre in Singapore and opened two facilities in Malaysia: a sales and service office in Kuala Lumpur and a service centre in Bintulu. In the Middle East, the Dubai service super centre was upgraded, along with service centres in Saudi Arabia, Egypt and Kuwait. Additionally, several new service centres were established across Saudi Arabia and Iraq. The super centres in South Africa and Canada were also expanded. Building on our 2011 acquisition of Turbo Components and Engineering (TCE), we expanded our hydrodynamic bearing service offering by opening or upgrading sites in Canada, Germany, Dubai and Singapore.

Underlying sales of first-fit original equipment fell 2% as market pressures in Europe were partially offset by demand in North America. As in the prior 18 months, the business continues to gain a leading share of large downstream greenfield projects, although we are seeing some projects being delayed and cancelled. However, John Crane recently signed an exclusive framework agreement for part of the Kuwait National Petroleum Company's (KNPC) Clean Fuels Project, a modernisation programme that will upgrade two refineries in Kuwait.

Our rotating equipment manufacturing capacity constraints are now behind us. As previously outlined, we increased internal machining capacity by about 10% during the period, cutting our overall use of outsourced manufacturing. The capacity was added in lower cost, emerging market factories including China, India, the Czech Republic and Mexico.

A decline in our upstream oil services business, reported as part of our aftermarket revenue, continued, as crude oil prices fell. The business remains focused on strengthening local customer service capabilities and expanding to new countries.

Revenue from emerging markets rose 11% and now represents 25% of John Crane sales, with the higher increases resulting from growth in Mexico and Nigeria.

Research and development

John Crane increased investment in R&D by 28% compared to the prior period, illustrating its commitment to address future market needs. During the period we introduced the AURA 220 gas seal, representing the next-generation of advanced gas seal technology and the first to be unveiled as part of a new family of gas seals. The new technology uses a common global design and patented polymeric sealing device with *Active Deflection Control* to help customers reduce operating and transaction costs.

Building on our long engineering heritage, the company has launched "*Engineering U*" an accelerated career development programme for promising entry-level mechanical engineers. The first 12-month US-based pilot is underway and we intend to implement the programme at our global R&D centres in the UK and China in the future.

Outlook

On a constant currency basis, trading may be at slightly lower levels to prior year in the second half. Cost saving initiatives are expected to underpin operating profit margins. Mid- and downstream order book should support modest second half sales growth in this segment, whereas difficult market conditions, directly related to the reduction in crude oil prices, in our upstream segment are expected to persist.

Smiths Medical

	2015 £m	2014 £m	Reported growth	Underlying growth
Revenue	**406**	389	4%	6%
Headline operating profit	**78**	71	9%	9%
Headline operating margin	**19.0%**	18.3%	70 bps	
Statutory operating profit	**68**	63	7%	
Return on capital employed	**15.1%**	15.3%	(20) bps	

Reported revenue grew 4% (£17m). Excluding a currency translation impact of £8m, underlying revenue grew 6%. This growth was driven by our strength and investment focus on ambulatory infusion amid ongoing competitor disruptions, and continued improvement in supply chain reliability. A weak prior year comparator for disposables, affected by distributor destocking, also helped.

Smiths Medical delivered strong profit growth in the first half, driven mainly by higher underlying revenue, tight cost controls and the initial benefits of restructuring. Headline operating profit grew 9%, on a reported and underlying basis, resulting in a 70 basis point increase in operating margins to 19.0%. This improvement stems from higher volumes, operating efficiencies and the benefit of restructuring on lowering overheads. These more than offset price headwinds, input cost inflation, and adverse transactional foreign exchange.

The difference between statutory and headline operating profit principally reflects the amortisation of acquired intangibles and restructuring costs. Return on capital employed declined 20 basis points to 15.1%, as a result of higher inventory and increased capital spending to underpin the restructuring programmes.

Underlying sales of consumables, which represent 81% of total revenue, were up 3%. We saw strong growth in ambulatory infusion disposables on the back of improved sales of our ambulatory pumps, continued robust performance in assisted reproduction products and a return to growth in PIVC, safety needles, and tracheostomy, albeit from a softer comparable period. Underlying sales of hardware rose 24% on the strength of our infusion products.

Medication delivery underlying revenues were up 19% driven by strong ambulatory infusion sales, reflecting the continued success of our CADD product range. A sharper emphasis on this product line is enhancing our already favourable market position. Our targeted sales initiative began producing positive results in the second half of last year and accelerated in this first half. While we expect to continue to perform well in ambulatory infusion, growth rates in the second half will slow against the tougher comparator. Infusions systems growth also reflects the launch of a new infusion pump in China. We continue to invest in interoperability capabilities to support the integration of our devices with electronic medical records and other hospital systems, which will further support future performance in the infusion franchise. We are also building a robust pipeline of new products to ensure our long-term leadership in infusion technologies.

Vital care underlying sales were slightly up despite sluggish procedure volumes and price pressures in developed countries. Assisted reproduction grew strongly and tracheostomy maintained its steady growth. General anaesthesia, respiratory and temperature management all grew, despite difficult market conditions, against a weak prior year comparator affected by distributor destocking.

Safety devices underlying revenue increased 3% with a return to growth in PIVC and safety needles, albeit against a soft prior year period affected by trade inventory reductions. Syringe sales were strong in the US, and PIVC revenue in emerging markets also showed good growth. The recently introduced ViaValve continues to be received positively in the US. Although competitive pressures in Europe have limited the success of our IntuitIV product, launched at the same time, this product positions us well to benefit from the EU directive to improve workplace safety by preventing sharps injuries.

We are maintaining our investment levels in the faster growing emerging markets. After a disappointing performance in China last year, our focus on key product registrations, better sales channel alignment, sales incentives and faster new product introductions are now delivering positive results. Recent product launches in China and the introduction of a strong distribution partner for our infusion business has resulted in first half growth of 17%. Elsewhere, our transition to a direct selling model in India delivered growth of 43%. Sales to our distributor markets have been more challenging with strong sales in South East Asia offset in recent months by the impact of macro-economic factors in Russia and the Middle East. We believe that a focus on expanding our presence in the emerging markets is a sound strategy to counter slower growth in developed markets. While these results are much more encouraging, we clearly have more work to do to deliver consistently high growth in the emerging markets.

Research and Development

Investment in R&D remains a priority. Our first half R&D cash spend of £22m (2014: £19m) grew 13% and amounted to 5.3% of sales (2014: 4.9%). We have continued our initiative to streamline the organisation, upgrade talent and improve processes to accelerate speed-to-market. In particular, we have introduced new processes for prioritising our investment toward new products that will deliver the strongest returns, while supporting a more balanced product strategy across our three segments.

Sales of our CADD Solis PIB pump grew strongly in the US and Europe, supported by solid performances by Medfusion 4000, Jelco IntuitIV and ViaValve. These were all launched in the last 2-3 years, reinforcing the importance and potential of improving our new product development pipeline. Anticipated launches of new products in vascular access, temperature management, pain management and infusion over the next 2-3 years, give us confidence in our ability to accelerate sales in line with or better than market growth

Outlook

We expect the growth rate to slow in the second half compared to the first half, reflecting last year's strong second half comparator. Medication delivery should perform well on the back of recent product launches and effective sales and marketing although the growth rate will slow in the second half. We continue to work on improving performance in vital care and safety devices with increased investment in new product development. Margins are expected to show modest improvement for the full year reflecting the benefit of operational efficiencies and restructuring despite foreign exchange transaction headwinds.

Smiths Detection

	2015 £m	2014 £m	Reported growth	Underlying growth
Revenue	**231**	251	(8)%	(5)%
Headline operating profit	**24**	30	(20)%	(15)%
Headline operating margin	**10.3%**	11.8%	(150) bps	
Statutory operating profit	**14**	28	(50)%	
Return on capital employed	**3.1%**	8.6%	(550) bps	

Faced with an increasingly competitive market, Smiths Detection is implementing a series of initiatives to reshape the business and return to profitable growth. While solid progress has been made on a number of priorities, both sales and profits declined in the first half as trading remained challenging.

Revenue fell 5% on an underlying basis, due partly to delays in a number of major programmes. Weakness in transportation and ports & borders was only partially offset by an encouraging performance in critical infrastructure. Regionally, continuing pressure on government budgets in EMEA was reflected in lower activity in transportation and ports & borders, although major airport contracts were won in Abu Dhabi and the UK.

Headline operating profit declined 14% underlying, driven by lower sales volumes and continued competitive pricing pressure in some end use markets and business mix. Headline operating margin of 10.3% was 150 basis points lower than the same period last year despite stronger control measures, especially in programme management. Including £9m of adverse foreign exchange translation, reported headline operating profit fell 20%.

The difference between statutory and headline operating profit primarily relates to £9m of exceptional restructuring costs arising from the Group's Fuel for Growth programme. Return on capital declined 550 basis points as a result of the lower profitability over the past 12 months.

Value engineering and cost saving actions are continuing alongside the *Fuel for Growth* initiative. This comprehensive business improvement programme initiated in 2014 will deliver annual savings of some £14m at an expected total cost of £34m by the end of FY17. Costs of £9m were incurred in the first half.

Among the major cost-saving measures, three facilities in North America will close this year. The Malaysian hub exceeded output targets ahead of a further ramp-up of production to support sales to the EMEA region in the third quarter. Production of small X-ray machines will cease in Germany and their manufacture is also transferred to Malaysia. Simplifying this global supply chain will enable us to realise substantial long-term benefits.

Transportation sales fell 5% on an underlying basis amid challenging and increasingly competitive market conditions. Last year's revenues also benefited from a large contract to supply airport screening equipment to Doha.

Nevertheless the order book benefited from the award of two significant contracts – to equip a new terminal at Abu Dhabi Airport and to supply London Heathrow its future requirement for out-of-gauge X-ray equipment. Under the contracts, the equipment will be supported by multi-year service agreements. The growing importance of the Middle

East to Smiths Detection is also seen in a major order completed for Emirates Group Security at its cargo handling facility at the new Al Maktoum International Airport.

A number of key contracts were also renewed or extended in the Americas: including a major service contract with Leidos. Revenue also benefited from the delivery of automatic explosives scanners (aTiX) for carry-on baggage screening under an Advanced Technology 2 contract with the US Transport Security Administration. In Asia Pacific, Detection won an important contract from Manila International Airport for 14 eqo body-screening systems.

In Europe, security improvements driven by new legislation are increasingly affecting airport buying decisions. The newly introduced EU Standard 3 covering all automated hold baggage inspection for explosives, has triggered a new replacement cycle. This is generating increased interest in the recently developed HI-SCAN 180180 XCT scanner, which is Standard 3 compliant. Already operating in Germany and Morocco, the new scanner is the main element of the Heathrow contract.

During the period, the HI-SCAN 6040-2is HR became the first dual-view X-ray system in the world to achieve Standard 3 Type C approval as a liquid explosive detection system.

Revenue from critical infrastructure was especially strong, rising 36% on an underlying basis. Sales in the US grew by 30%, principally as a result of increased orders from the New York Court Authority to supply networked X-ray equipment to courthouses and other facilities. Sales in the Middle East expanded strongly from a small base and our X-ray equipment is now used to safeguard a range of Saudi Arabian government ministries, armed forces establishments and royal palaces.

Underlying revenue in ports & borders fell 55% with the decline most noticeable in Europe and the US. It continues to be a challenging market with increased competitive pressures, which has caused the significant drop in volumes. Latin America remains a growth prospect, and orders in the period included cargo inspection systems worth some £14m for Nicaragua and Paraguay.

Underlying military revenues were up 1% as defence budgets remained constrained. Long term contracts underpin this business and we secured an additional order of more than $9m from the US Department of Defense.

The aftermarket, accounting for 36% of total revenue, is an important growth driver, with an 11% increase in sales in the first half. Among new business successes, our support for a major installation at Doha’s new international airport was confirmed with a five-year service/maintenance contract.

Research and development

Smiths Detection continues to focus on developing new products and systems as platforms for its principal technologies. Company-funded R&D fell 31% to £13m, or 6% of sales (2014: 8%), reflecting the decision to focus investment more tightly on fewer projects. Capitalised projects accounted for £2m (2014: £8m) of the funded R&D. Customer and government support for R&D totalled £2m in the period (2014: £2m), bringing total R&D spend to £15m (2014: £21m).

New products, benefiting transportation and critical infrastructure in particular included Checkpoint.Evo, a new software solution that greatly enhances inspection and integration capabilities at aviation checkpoints. It enables real-time data collection, distribution and management to improve both the inspection process and operational efficiency.

Air cargo screening is an expanding market requiring large-scale scanning equipment. To meet global legal requirements for 100% inspection of air cargo on passenger flights, the HI-SCAN 180180-2is pro was launched as an advanced version of its market-leading predecessor.

Outlook

The rate of sales decline seen in the first half is likely to persist during the second half. However, recent contract wins and the strengthening order book are expected to support increased revenue in FY16. Headline operating margins should improve in the second half against a comparator period affected by one-off costs. Excluding these one-off costs, like-for-like margins in the second half will continue to be relatively soft in some markets, partially offset by the benefits of the cost reduction initiatives. Margins in the medium term are expected to improve as the product initiatives such as value engineering and other cost savings take effect.

Smiths Interconnect

	2015 £m	2014 £m	Reported growth	Underlying growth
Sales	**198**	210	(6)%	(6)%
Headline operating profit	**18**	27	(33)%	(33)%
Headline operating margin	**9.2%**	13.1%	(390) bps	
Statutory operating profit	**7**	16	(56)%	
Return on capital employed	**12.0%**	12.2%	(20) bps	

Smiths Interconnect's reported and underlying revenue declined 6%, or £12m, mainly due to delays in customer spending and programme slowdowns in many of our end markets. This was only slightly offset by growth in data centres. While sales in Europe improved marginally, revenue from North America fell slightly and emerging markets, particularly China, were impacted by contract timing with revenue from certain test equipment orders benefiting the prior year. In addition, some major projects, such as the Chinese commercial aircraft programme, are moving from design to qualification with a consequential demand dip before volumes start increasing in the production phase.

Headline operating profit fell 33%, or £9m, on both an underlying and reported basis. Margins declined 390 basis points to 9.2%. The main contributors were adverse mix, reflecting revenue declines in higher margin sectors, and negative operational gearing from lower volumes. Pricing pressure also continued in several sectors. Appropriate restructuring and cost controls have been implemented and will continue for the rest of the financial year. In addition, we continue to drive procurement and operational efficiencies through our lean and value engineering programmes. Return on capital employed fell 20 basis points with the lower profitability. The difference between statutory and headline operating profit reflects amortisation of acquired intangible assets (£9m) and exceptional restructuring costs of (£2m).

Connectors underlying revenues fell 4%. Following a strong close to the prior year, the first half started slowly with shipments to European defence customers cut due to export licence delays and lower demand from two large medical customers. Revenues improved slightly in the second quarter on the back of recovery in defence and medical and strong demand for our new semiconductor test products. The high reliability and harsh environment value proposition of Connectors was highlighted by the use of our products in the Rosetta mission which landed a probe on a comet in deep space last November. We were also awarded a High & New Technology Certification from the Chinese Government for our semiconductor test products. Operationally, Connectors continues to restructure its US presence, consolidating into its mid-West and Mexico facilities.

Microwave sales fell 12% on an underlying basis reflecting significant revenue reductions across all its markets. Wireless telecoms demand declined as the rate of 4G LTE deployments in the US slowed with one operator cutting capex spending significantly. Internationally, demand from Australian operators grew and there was positive progress on opportunities in Indonesia and China which will benefit the second half. The change in timing of certain orders for our high performance cable assemblies, which helped prior year revenue, caused a large reduction in H1 test equipment sales. This cable assembly programme experiences annual surges in demand around the middle of the calendar year and we remain well positioned to secure significant orders in 2015. In commercial aerospace, sales to the main customer for our airborne antenna system fell, but we continue to develop new product offerings and new customers, particularly in Asia. Defence revenues were flat despite further delays and volume reductions on some key programmes such as datalink terminals. Defence budgets have generally stabilised, and demand held up on our larger production programmes. New contracts included an RF filter project for a Canadian government application.

Underlying revenue at Power increased 4%. Data centre sales grew, particularly in the US, due to favourable market conditions, increasing win rates and large project awards from both existing colocation customers and new enterprise customers in financial services and IT. Sales of our industrial products were affected by a significant prior year customer filing for bankruptcy. The power protection markets remained soft, especially US telecoms, because of similar customer dynamics as experienced by the Microwave business. However, new design opportunities with one of the larger US network operators should provide some recovery in the second half and beyond. Margins were constrained as the positive effects of volume and fixed cost reductions from prior year restructuring were offset by pricing pressure due to strong competition on large data centre projects and reinvestment in future growth opportunities.

Research and development

Total R&D expenditure remained at 6.5% of sales (£13m) with the customer-funded portion flat at £1.5m in line with stabilising defence budgets. Business development activities continued to focus R&D investment on commercial markets with higher growth potential. Examples include additional variants of our next generation semiconductor test sockets; a tail-mounted airborne antenna targeted at the regional and business jet market; a value engineered version of our busway range for the high growth emerging markets; and a new RF test product to complement our successful PIM (passive intermodulation) offerings.

Outlook

Looking ahead, market conditions are expected to be largely similar with continued strength in data centre and semiconductor test. Defence is starting to show some signs of modest growth, although individual programme dynamics will be a greater influence on our future performance. US wireless operators are expected to continue to limit infrastructure investment, although there are new network deployments in Asia and Australia that provide opportunity. Other commercial markets such as medical are likely to trend positively. We expect that seasonality will bias performance towards the second half although trading in the second half will remain below prior year levels.

Flex-Tek

	2015 £m	2014 £m	Reported growth	Underlying growth
Revenue	**128**	123	4%	4%
Headline operating profit	**23**	22	3%	3%
Headline operating margin	**18.1%**	18.3%	(20) bps	
Statutory operating profit	**22**	18	22%	
Return on capital employed	**33.7%**	32.7%	100 bps	

Flex-Tek revenues grew 4%, or £5m, on a reported and underlying basis. The increase was driven by the reviving US residential construction market as well as sales growth in specialty heating elements and hoses for aerospace and automotive applications. Headline operating margins at 18.1% were slightly down on increased volumes because of higher investment costs in marketing and new product development. Return on capital employed improved 100 basis points.

The difference between statutory and headline operating profit reflects exceptional litigation costs of £1m.

Fluid Management revenues rose 1% with a better performance in commercial airframe and engine makers only partially offset by lower sales for satellite launch vehicles and military gas turbines. New aircraft project awards are starting to boost revenues, although first half growth was offset by reduced sales in Europe. Major airframe manufacturers, Airbus and Boeing, and engine makers Pratt & Whitney, GE, and Rolls-Royce, won new orders to push the large commercial jet backlog to record levels. Our sales into automotive fuel and brake applications continue to grow.

Sales of flexible gas piping and HVAC ducting to the construction market rose 4%. Revenue growth benefited from greater activity in US residential construction and from our success in cross-selling ducting, flexible gas piping and HVAC heating element product lines to the US distribution market. Our new sales efforts introducing flexible gas piping into the UK market have proved successful and we have plans for expansion.

Heat Solutions revenues rose 13% on the back of strong growth in specialty heating elements and slightly improved sales to the appliance sector. Sales to distributors, via cross-selling efforts with ducting and gas piping, and the growth of heating elements for bespoke applications accounted for most of the improvement. Investments in product development and in new technologies continued at last year's increased levels. Sales in China were flat for the half as growth in specialty applications was offset by weakness in the appliance side of the business.

Underlying revenue at Flexible Solutions fell 2%, reflecting the continued decline of the floor care market. Growth in specialty applications and R&D investment in medical products continue to deliver positive results.

Research and development

Our increased R&D investment aimed at approvals on next-generation airplanes and new heating technologies is proving effective and we continue to seek acquisition opportunities to build on the strength of the businesses and management. R&D investment increased 23% in the period.

In Fluid Management, new product development spend continues to be focused on requirements for the next generation of quieter, more fuel-efficient aircraft, and developments in 3000 psi and 5000 psi hoses are expected to drive future revenues.

Opportunities to develop specialty heating elements that open up higher margin markets and create scope for additional revenue growth are another high priority.

Outlook

US residential housing numbers continue to show modest improvement, although higher interest rates, higher home prices, and stricter lending practices could hinder anticipated growth. Aerospace demand for our Fluid Management business is likely to remain muted as the new programmes benefiting our product lines have yet to ramp up. Improved general economic conditions are expected to benefit Heat Solutions.

Financial review

Earnings per share
Basic headline earnings per share from continuing activities were 38.5p (2014: 39.5p), a decline of 3%. This reflects the lower headline operating profit which has been partly offset by a lower finance charge and tax rate.

On a statutory basis, the basic earnings per share from continuing activities were 21.8p (2014: 23.7p).

Exceptional and other items relating to continuing activities excluded from headline profit before tax
These items amounted to a charge of £77m compared to a charge of £83m in 2014. They comprised:

- Amortisation of intangible assets acquired in business combinations of £18m (2014: £21m) and a £26m goodwill impairment charge for John Crane Production Solutions because of the impact of a lower oil price environment on its customers. The ongoing amortisation charge relates principally to technology and customer relationships;
- £14m charge (2014: £36m) in connection with John Crane, Inc. asbestos litigation;
- £2m charge (2014: £6m) in connection with Titeflex Corporation litigation;
- £19m charge for restructuring (2014: £14m) in respect of the '*Fuel for Growth*' programme;
- £13m gain on changes to post-retirement benefits;
- £4m charge for retirement benefit finance (2014: £5m);
- £5m charge for legacy retirement benefit administration (2014: £3m); and
- £2m of financing losses (2014: nil).

In the period to 31 January 2014, in addition to the above, £2m profit on disposal of businesses; £1m cost of acquisition and disposals and £1m gain on legal settlement of diabetes royalty payments were also excluded from headline performance.

Cash generation and net debt
Operating cash generation remained strong with headline operating cash of £204m (2014: £211m), representing 88% (2014: 86%) 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 increased £28m to £58m (2014: £30m). 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 £112m (2014: £83m).

Dividends paid in the period on ordinary shares amounted to £108m (2014: £225m consisting of final and special dividends).

Net debt at 31 January was £929m, up from £804m at 31 July 2014. The increase in net debt reflects outflows from dividends (£108m) and pension funding (£36m) as well as adverse foreign exchange translation (£47m).

Headline interest and other financing costs
Interest payable on debt, net of interest earned on cash deposits, was £24m (2014: £30m). It reduced as the $250m 6.05% fixed rate Notes were repaid in May 2014. Headline interest costs were covered 9.7 times by headline operating profits.

The Group accounts for pensions using IAS 19. As required by this standard, a finance charge of £4m (2014: £5m) 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 £56m in R&D (2014: £61m), equivalent to 3.9% of revenue (2014: 4.2%). Of that total, £53m was funded by the Company compared with £57m in 2014, a decrease of 8%. This decrease was caused by some long-running programmes coming to an end and as we seek to improve the efficiency of our innovation investment. We actively seek funding from customers to support R&D and this amounted to £3m (2014: £4m). Under IFRS, certain development costs are capitalised, and this amounted to £9m in the period (2014: £15m). 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 £55m (2014: £58m) represented an effective rate of 26.5% on the headline profit before taxation (2014: 27.0%). This rate is expected to be sustained for the full year. On a statutory basis, the tax charge on continuing activities was £44m (2014: £37m).

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 comprises of 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 120 basis points to 15.4% (2014: 16.6%), primarily as a result of lower returns on capital in Smiths Detection and Smiths Interconnect.

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 2015 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 risen to £338m at 31 January 2015 from £242m at 31 July 2014. The increase reflects the impact of lower bond yields and new mortality assumptions for the US plans, partly offset by the benefit of scheme contributions and asset returns.

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 2015	31 July 2014	31 January 2014
Funded plans			
UK plans – funding status	**99%**	99%	99%
US plans – funding status	**73%**	84%	85%
Other plans – funding status	**80%**	79%	80%

	31 January 2015 £m	31 July 2014 £m	31 January 2014 £m
Deficit			
Funded plans	**(224)**	(135)	(132)
Unfunded plans	**(114)**	(107)	(104)
Total deficit	**(338)**	(242)	(236)
Retirement benefit assets	**158**	123	102
Retirement benefit liabilities	**(496)**	(365)	(338)
	(338)	(242)	(236)

In the current year, cash contributions to the schemes are expected to total approximately £85m (2014: £88m). In addition, the Group will invest £24m (2014: £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 2015 is set out in the table below:

Pension scheme membership	**SIPS**	**TIGPS**	**US plans**	**Total**
Deferred active	460	250	2,810	**3,520**
Deferred	11,120	13,600	3,070	**27,790**
Pensioners	13,040	17,350	5,550	**35,940**
Total	**24,620**	**31,200**	**11,430**	**67,250**

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 2015	31 January 2014		31 July 2014
Average rates:				
US dollar	**1.59**	1.61	Dollar strengthened 1%	1.64
Euro	**1.27**	1.19	Euro weakened 7%	1.21
Period end rates:				
US dollar	**1.50**	1.65	Dollar strengthened 9%	1.69
Euro	**1.33**	1.22	Euro weakened 9%	1.26

Risk management

The principal risks and uncertainties affecting the business activities of the Group and relevant mitigating activities were set out on pages 60-65 of the Annual Report for the year ended 31 July 2014, a copy of which is available at the Company's website at www.smiths.com.

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 below and more fully in the Annual Report. Since the Annual Report, the Board has announced that the Chief Executive and Finance Director will both step down during the course of 2015, which increases the possible risks arising from managing this management transition and the potential failure to attract suitably qualified personnel. Currency volatility has continued to prevail 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.

The key risks and uncertainties are summarised below:

Economic outlook and geo-political environment

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.

Compliance with legislation and regulations

A complex legislative and regulatory environment applies to the Group's activities such that failure to comply could have a significant impact on the financial results.

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 and business/process transformation

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.

Programme delivery

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.

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 2014. There have been no changes to the membership of the board.

For and on behalf of the Board of Directors:

Philip Bowman
Chief Executive

Peter Turner
Finance Director

17 March 2015

Independent review report to Smiths Group plc

Report on the condensed interim financial statements

Our conclusion

We have reviewed the condensed interim financial statements, defined below, in the Interim report of Smiths Group plc for the period ended 31 January 2015. Based on our review, nothing has come to our attention that causes us to believe that the condensed interim financial statements are 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.

This conclusion is to be read in the context of what we say in the remainder of this report.

What we have reviewed

The condensed interim financial statements, which are prepared by Smiths Group plc, comprise:

- ·the consolidated balance sheet as at 31 January 2015;
- ·the consolidated income statement and consolidated statement of comprehensive income for the period then ended;
- ·the consolidated cash flow statement for the period then ended;
- ·the consolidated statement of changes in equity for the period then ended; and
- ·the notes to the Interim report.

As disclosed in note 1, the financial reporting framework that has been applied in the preparation of the full annual financial statements of the group is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

The condensed interim financial statements included in the Interim report have been prepared in accordance with International Accounting Standard 34, 'Interim Financial Reporting', as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Conduct Authority.

What a review of condensed interim financial statements involves

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.

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 interim financial statements.

Responsibilities for the condensed interim financial statements and the review

Our responsibilities and those of the directors

The Interim report, including the condensed interim financial statements, 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.

Our responsibility is to express to the company a conclusion on the condensed interim 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 complying with the Disclosure and Transparency Rules of the Financial Conduct Authority and for no other purpose. We do not, in giving this conclusion, 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.

PricewaterhouseCoopers LLP
Chartered Accountants
London

17 March 2015

(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 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Continuing operations				
Revenue	2	**1,416**	1,442	2,952
Cost of sales		**(776)**	(791)	(1,626)
Gross profit		**640**	651	1,326
Sales and distribution costs		**(202)**	(201)	(398)
Administrative expenses	4	**(274)**	(280)	(550)
Operating profit		**164**	170	378
Comprising				
– headline operating profit	3	**232**	245	504
– exceptional items, impairment of goodwill, amortisation of acquired intangibles	3	**(68)**	(75)	(126)
		164	170	378
Interest receivable		**1**	2	3
Interest payable		**(25)**	(32)	(62)
Other financing losses		**(5)**	(3)	(8)
Other finance charges – retirement benefits		**(4)**	(5)	(9)
Finance costs		**(33)**	(38)	(76)
Profit before taxation		**131**	132	302
Comprising				
– headline profit before taxation	3	**208**	215	445
– exceptional items, impairment of goodwill, amortisation of acquired intangibles and other financing gains and losses	3	**(77)**	(83)	(143)
		131	132	302
Taxation	6	**(44)**	(37)	(67)
Profit for the period		**87**	95	235
Attributable to				
Smiths Group shareholders		**86**	94	233
Non-controlling interests		**1**	1	2
		87	95	235
Earnings per share	5			
Basic		**21.8p**	23.7p	59.0p
Diluted		**21.6p**	23.6p	58.4p
Dividends per share (declared)	13			
– interim		**13.00p**	12.75p	12.75p
– final				27.50p
		13.00p	12.75p	40.25p

Consolidated statement of comprehensive income (unaudited)

	Notes	Period ended 31 January 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Profit for the period		**87**	95	235
Other comprehensive income				
Actuarial losses on retirement benefits	7	**(120)**	(37)	(77)
Taxation recognised on actuarial movements		**32**	(3)	6
Other comprehensive income which will not be reclassified to the consolidated income statement		**(88)**	(40)	(71)
Other comprehensive income which will be, or has been, reclassified				
Exchange gains/(losses)		**127**	(186)	(257)
Fair value gains/(losses)				
– on available for sale financial assets		**15**		3
– deferred in the period on cash-flow and net investment hedges		**(64)**	88	119
– reclassified to income statement		**2**	(2)	(3)
Total other comprehensive income		**(8)**	(140)	(209)
Total comprehensive income		**79**	(45)	26
Attributable to				
Smiths Group shareholders		**78**	(45)	25
Non-controlling interests		**1**		1
		79	(45)	26

Consolidated balance sheet (unaudited)

	Notes	31 January 2015 £m	31 January 2014 £m	31 July 2014 £m
Non-current assets				
Intangible assets	8	**1,606**	1,609	1,544
Property, plant and equipment	9	**275**	259	258
Financial assets – other investments		**146**	99	117
Retirement benefit assets	7	**158**	102	123
Deferred tax assets		**238**	174	185
Trade and other receivables		**41**	31	35
Financial derivatives		**9**	13	9
		2,473	2,287	2,271
Current assets				
Inventories		**487**	443	427
Current tax receivable		**43**	25	34
Trade and other receivables		**596**	608	635
Cash and cash equivalents	10	**178**	176	190
Financial derivatives		**24**	11	8
		1,328	1,263	1,294
Total assets		**3,801**	3,550	3,565
Non-current liabilities				
Financial liabilities				
– borrowings	10	**(1,084)**	(894)	(982)
– financial derivatives		**(5)**	(7)	(4)
Provisions for liabilities and charges	12	**(275)**	(256)	(245)
Retirement benefit obligations	7	**(496)**	(338)	(365)
Deferred tax liabilities		**(64)**	(68)	(58)
Trade and other payables		**(29)**	(33)	(28)
		(1,953)	(1,596)	(1,682)
Current liabilities				
Financial liabilities				
– borrowings	10	**(23)**	(183)	(12)
– financial derivatives		**(15)**	(7)	(5)
Provisions for liabilities and charges	12	**(89)**	(73)	(82)
Trade and other payables		**(437)**	(416)	(464)
Current tax payable		**(74)**	(55)	(75)
		(638)	(734)	(638)
Total liabilities		**(2,591)**	(2,330)	(2,320)
Net assets		**1,210**	1,220	1,245
Shareholders' equity				
Share capital		**148**	148	148
Share premium account		**348**	346	346
Capital redemption reserve		**6**	6	6
Revaluation reserve		**1**	1	1
Merger reserve		**235**	235	235
Retained earnings		**583**	565	559
Hedge reserve		**(120)**	(88)	(58)
Total shareholders' equity		**1,201**	1,213	1,237
Non-controlling interest equity		**9**	7	8
Total equity		**1,210**	1,220	1,245

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 2014		494	242	559	(58)	1,237	8	1,245
Profit for the period				86		86	1	87
Other comprehensive income								
Exchange gains				127		127		127
Actuarial losses on retirement benefits and tax				(88)		(88)		(88)
Fair value gains/(losses)				15	(62)	(47)		(47)
Total comprehensive income for the period				140	(62)	78	1	79
Transactions relating to ownership interests								
Exercises of share options		2				2		2
Taxation recognised on share options				(1)		(1)		(1)
Purchase of own shares				(11)		(11)		(11)
Dividends								
– equity shareholders	13			(108)		(108)		(108)
Share-based payment				4		4		4
At 31 January 2015		**496**	**242**	**583**	**(120)**	**1,201**	**9**	**1,210**

	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	242	930	(174)	1,486	7	1,493
Profit for the period				94		94	1	95
Other comprehensive income								
Exchange losses				(185)		(185)	(1)	(186)
Actuarial losses on retirement benefits and tax				(40)		(40)		(40)
Fair value gains/(losses)					86	86		86
Total comprehensive income for the period				(131)	86	(45)		(45)
Transactions relating to ownership interests								
Exercises of share options		6				6		6
Purchase of own shares				(13)		(13)		(13)
Dividends								
– equity shareholders	13			(225)		(225)		(225)
Share-based payment				4		4		4
At 31 January 2014		**494**	**242**	**565**	**(88)**	**1,213**	**7**	**1,220**

Consolidated cash-flow statement (unaudited)

	Notes	Period ended 31 January 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Net cash inflow from operating activities	14	**112**	83	256
Cash-flows from investing activities				
Expenditure on capitalised development		**(8)**	(13)	(23)
Expenditure on other intangible assets		**(8)**	(8)	(17)
Purchases of property, plant and equipment		**(28)**	(24)	(54)
Disposals of property, plant and equipment		**2**	4	5
Investment in financial assets		**(13)**	(12)	(28)
Acquisition of businesses				(1)
Disposals of businesses			3	3
Net cash-flow used in investing activities		**(55)**	(50)	(115)
Cash-flows from financing activities				
Proceeds from exercise of share options		**2**	6	6
Purchase of own shares		**(11)**	(13)	(13)
Dividends paid to equity shareholders		**(108)**	(225)	(275)
Cash (outflow)/inflow from matured derivative financial instruments		**(3)**	3	11
Increase in new borrowings		**91**		138
Reduction and repayment of borrowings		**(53)**		(180)
Net cash-flow used in financing activities		**(82)**	(229)	(313)
Net (decrease)/increase in cash and cash equivalents		**(25)**	(196)	(172)
Cash and cash equivalents at beginning of the period		**189**	387	387
Exchange differences		**13**	(21)	(26)
Cash and cash equivalents at end of the period		**177**	170	189
Cash and cash equivalents at end of the period comprise				
– cash at bank and in hand		**105**	102	115
– short-term deposits		**73**	74	75
– bank overdrafts		**(1)**	(6)	(1)
		177	170	189

Reconciliation of net cash-flow to movement in net debt

	Notes	Period ended 31 January 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Net (decrease)/increase in cash and cash equivalents		**(25)**	(196)	(172)
Net (increase)/decrease in borrowings resulting from cash-flows		**(38)**		42
Movement in net debt resulting from cash-flows		**(63)**	(196)	(130)
Capitalisation, interest accruals and unwind of capitalisation of fees		**(9)**	(8)	3
Movement in fair value hedging		**(6)**	(3)	(3)
Exchange differences		**(47)**	50	70
Movement in net debt in the period		**(125)**	(157)	(60)
Net debt at start of period	10	**(804)**	(744)	(744)
Net debt at end of period	10	**(929)**	(901)	(804)

Notes to the Interim report (unaudited)

1 Basis of preparation

The condensed interim financial statements cover the six month period ended 31 January 2015 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 2014, 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 2015. These accounting policies are consistent with those applied in the preparation of the financial statements for the year ended 31 July 2014.

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 £20m (31 July 2014: £29m) has been recognised in the period in respect of contracts in progress at the period end with a total expected value of £118m (31 July 2014: £113m). A 5% reduction in the proportion of the contract activity recognised in the current period would have reduced operating profit by less than £1m for both Smiths Detection and Smiths Interconnect (31 July 2014: less than £1m).

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 2015 was £22m (31 July 2014: £19m).

Taxation

The Group has recognised deferred tax assets of £26m (31 July 2014: £21m) relating to losses and £103m (31 July 2014: £91m) 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.

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 2015 there is a retirement benefit asset of £158m (31 July 2014: £123m) 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: Employee benefits.

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 2015 the carrying value of inventory incorporates provisions of £73m (31 July 2014: £76m). The inventory turn rate of 3.2 (31 July 2014: 3.8) varies across the five divisions. Smiths Detection has the slowest inventory utilisation with a turn rate of 2.6 (31 July 2014: 3.1).

At 31 January 2015 the gross value of receivables partly provided for or more than 3 months overdue was £61m (31 July 2014: £46m) and there were provisions of £21m (31 July 2014: £18m) against these receivables which were carried at a net value of £40m (31 July 2014: £28m).

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 2014. 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 note 8 and the Annual Report 2014 for details of the critical assumptions made, including the sales and margin volatility in Smiths Detection, Smiths Interconnect Power, and disclosures on the sensitivity of the impairment testing to these key assumptions.

See note 8 for the results of the half year impairment testing for John Crane Production Solutions.

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 £232m (31 July 2014: £204m) 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 £66m (31 July 2014: £61m) 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.

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 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 2015
	John Crane £m	**Smiths Medical £m**	**Smiths Detection £m**	**Smiths Interconnect £m**	**Flex-Tek £m**	**Corporate costs £m**	**Total £m**
Revenue	**453**	**406**	**231**	**198**	**128**		**1,416**
Divisional headline operating profit	**105**	**78**	**24**	**18**	**23**		**248**
Corporate headline operating costs						**(16)**	**(16)**
Headline operating profit/(loss)	**105**	**78**	**24**	**18**	**23**	**(16)**	**232**
Exceptional operating items (note 4)	**(13)**	**(6)**	**(10)**	**(2)**	**(1)**	**13**	**(19)**
Legacy retirement benefits administration costs						**(5)**	**(5)**
Impairment of goodwill and amortisation of acquired intangible assets	**(31)**	**(4)**		**(9)**			**(44)**
Operating profit/(loss)	**61**	**68**	**14**	**7**	**22**	**(8)**	**164**
Exceptional finance costs – adjustment to discounted provision (note 4)	**(2)**				**(1)**		**(3)**
Net finance costs – other							**(30)**
Profit before taxation							**131**

							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	469	389	251	210	123		1,442
Divisional headline operating profit	109	71	30	27	22		259
Corporate headline operating costs						(14)	(14)
Headline operating profit/(loss)	109	71	30	27	22	(14)	245
Exceptional operating items (note 4)	(38)	(3)	(2)	(2)	(4)	(2)	(51)
Legacy retirement benefits administration costs						(3)	(3)
Amortisation of acquired intangible assets	(7)	(5)		(9)			(21)
Operating profit/(loss)	64	63	28	16	18	(19)	170
Exceptional finance costs – adjustment to discounted provision (note 4)	(2)				(1)		(3)
Net finance costs – other							(35)
Profit before taxation							132

	John Crane £m	Smiths Medical £m	Smiths Detection £m	Smiths Interconnect £m	Flex-Tek £m	Corporate costs £m	Total £m
							Year ended 31 July 2014
Revenue	941	804	512	445	250		2,952
Divisional headline operating profit	234	159	25	71	47		536
Corporate headline operating costs						(32)	(32)
Headline operating profit/(loss)	234	159	25	71	47	(32)	504
Exceptional operating items (note 4)	(56)	(8)	(1)	(5)	(10)	(1)	(81)
Legacy retirement benefits administration costs						(6)	(6)
Amortisation and impairment of acquired intangible assets	(12)	(9)	(1)	(17)			(39)
Operating profit/(loss)	166	142	23	49	37	(39)	378
Exceptional finance costs – adjustment to discounted provision (note 4)	(5)				(1)		(6)
Net finance costs – other							(70)
Profit before taxation							302

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

	John Crane £m	**Smiths Medical £m**	**Smiths Detection £m**	**Smiths Interconnect £m**	**Flex-Tek £m**	**Total £m**
						31 January 2015
Property, plant, equipment, development projects and other intangibles	**97**	**181**	**95**	**41**	**21**	**435**
Working capital assets	**358**	**241**	**268**	**163**	**81**	**1,111**
Operating assets	**455**	**422**	**363**	**204**	**102**	**1,546**
Derivatives, tax and retirement benefit assets						**472**
Goodwill and acquired intangibles						**1,432**
Corporate assets						**173**
Cash						**178**
Total assets						**3,801**
Working capital liabilities	**(161)**	**(99)**	**(166)**	**(63)**	**(29)**	**(518)**
Corporate and non-headline liabilities						**(312)**
Derivatives, tax and retirement benefits						**(654)**
Borrowings						**(1,107)**
Total liabilities						**(2,591)**
Average divisional capital employed	**871**	**1,098**	**604**	**519**	**142**	**3,234**
Average corporate capital employed						**(46)**
Average total capital employed						**3,188**

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 £815m (31 July 2014: £815m) 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 2014 Total £m
Property, plant, equipment, development projects and other intangibles	91	159	97	39	19	405
Working capital assets	350	228	275	161	73	1,087
Operating assets	441	387	372	200	92	1,492
Derivatives, tax and retirement benefit assets						359
Goodwill and acquired intangibles						1,382
Corporate assets						142
Cash						190
Total assets						3,565
Working capital liabilities	(143)	(97)	(166)	(70)	(26)	(502)
Corporate and non-headline liabilities						(317)
Derivatives, tax and retirement benefits						(507)
Borrowings						(994)
Total liabilities						(2,320)
Average divisional capital employed	876	1,100	632	518	139	3,265
Average corporate capital employed						(47)
Average total capital employed						3,218

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 2015	**166**	**171**	**39**	**35**	**42**	**453**
Revenue period ended 31 January 2014	176	180	40	33	40	469

Smiths Medical	Medication delivery £m	Vital care £m	Safety devices £m	Total £m
Revenue period ended 31 January 2015	**128**	**159**	**119**	**406**
Revenue period ended 31 January 2014	110	162	117	389

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 2015	**116**	**19**	**26**	**6**	**61**	**3**	**231**
Revenue period ended 31 January 2014	127	44	26	6	47	1	251

Smiths Interconnect	Connectors £m	Microwave £m	Power £m	Total £m
Revenue period ended 31 January 2015	**70**	**80**	**48**	**198**
Revenue period ended 31 January 2014	73	91	46	210

Flex-Tek	Fluid Management £m	Flexible Solutions £m	Heat Solutions £m	Construction £m	Total £m
Revenue period ended 31 January 2015	**33**	**25**	**29**	**41**	**128**
Revenue period ended 31 January 2014 (restated)	33	26	25	39	123

The allocation of Flex-Tek revenue for the period ended 31 January 2014 has been restated following reorganisation which moved a business from Fluid Management to Flexible Solutions.

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;
- impairment of goodwill and amortisation of intangible assets acquired in a business combination – the impairment and amortisation charges are non-cash items, 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 2015 £m**	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Operating profit		**164**	170	378
Exclude				
– exceptional operating items	4	**19**	51	81
– legacy retirement benefits administration costs		**5**	3	6
– impairment of goodwill	8	**26**		
– amortisation of acquired intangible assets	8	**18**	21	39
Non-headline items in operating profit		**68**	75	126
Headline operating profit		**232**	245	504
Finance costs		**(33)**	(38)	(76)
Exclude				
– exceptional finance costs	4	**3**	3	6
– other financing gains and losses		**2**		2
– other finance costs – retirement benefits		**4**	5	9
Non-headline items in finance costs		**9**	8	17
Headline finance costs		**(24)**	(30)	(59)
Profit before taxation		**131**	132	302
Non-headline items in operating profit		**68**	75	126
Non-headline items in finance costs		**9**	8	17
Headline profit before taxation		**208**	215	445
Profit after taxation – continuing operations		**87**	95	235
Exclude				
– non-headline items in profit before taxation		**77**	83	143
– tax on excluded items		**(11)**	(21)	(53)
		66	62	90
Headline profit after taxation – continuing operations		**153**	157	325

Headline earnings before interest, tax depreciation and amortisation

Smiths use the following calculation of Headline EBITDA for the ratio of net debt to EBITDA.

	Notes	**Period ended 31 January 2015 £m**	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Headline operating profit		**232**	245	504
Exclude				
Depreciation	9	**24**	23	46
Amortisation of development costs	8	**10**	10	21
Amortisation of software, patents and intellectual property	8	**6**	7	13
Headline EBITDA		**272**	285	584

4 Exceptional items

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

	Period ended 31 January 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Operating items			
Restructuring programmes	**(19)**	(14)	(29)
Gains on changes to post-retirement benefits	**13**		
Profit on disposals and acquisition and disposal costs		1	4
Resolution of items originally reported as non-headline		1	2
Litigation			
– provision for Titeflex Corporation subrogation claims (note 12)	**(1)**	(5)	(10)
– provision for John Crane, Inc. asbestos litigation (note 12)	**(12)**	(34)	(48)
	(19)	(51)	(81)
Financing items			
Exceptional finance costs – adjustment to discounted provision			
– provision for Titeflex Corporation subrogation claims (note 12)	**(1)**	(1)	(1)
– provision for John Crane, Inc. asbestos litigation (note 12)	**(2)**	(2)	(5)
	(22)	(54)	(87)

Period ended 31 January 2015

Restructuring costs comprise £19m in respect of Fuel for Growth. This programme, which involves redundancy, relocation and consolidation of manufacturing, is considered exceptional by virtue of its size.

Gains of £13m on changes to post-retirement benefits arise from a settlement offer by the US defined benefit pension plans allowing deferred members a one-off option to elect to cash out their retirement entitlements rather than receive a pension at retirement which was completed in September 2014. See note 9 in the Annual Report 2014.

A charge of £1m 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. A reduction in the expected gross cost has been offset by a charge of £2m relating to changes in discounting.

The operating charge in respect of John Crane, Inc. litigation comprises £6m in respect of increased provision for adverse judgments and legal defence costs, £1m in respect of litigation management and legal fees in connection with litigation against insurers, and £5m arising from the decrease in US risk free rates.

5 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 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Profit attributable to equity shareholders for the year – total	**86**	94	233
Average number of shares in issue during the year	**394,695,781**	394,166,825	394,296,986

Diluted earnings per share are calculated by dividing the profit attributable to ordinary shareholders by 398,359,970 (period ended 31 January 2014: 396,377,484; year ended 31 July 2014: 398,399,449) 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 2015 £m		Period ended 31 January 2014 £m		Year ended 31 July 2014 £m	
	£m	**EPS (p)**	£m	EPS (p)	£m	EPS (p)
Profit attributable to equity shareholders of the Parent Company	**86**	**21.8**	94	23.7	233	59.0
Exclude						
Non-headline items and related tax (note 3)	**66**	**16.7**	62	15.8	90	22.8
Headline	**152**	**38.5**	156	39.5	323	81.8
Statutory EPS – diluted (p)		**21.6**		23.6		58.4
Headline EPS – diluted (p)		**38.2**		39.2		81.0

6 Taxation

The interim tax charge of 33.6% is calculated by applying the estimated effective headline tax rate of 26.5% for the year ending 31 July 2015 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 2015 £m		Period ended 31 January 2014 £m		Year ended 31 July 2014 £m	
	Continuing operations £m	**Tax rate**	Continuing operations £m	Tax rate	Continuing operations £m	Tax rate
Profit before taxation	**131**		132		302	
Taxation	**(44)**	**33.6%**	(37)	28.2%	(67)	22.3%
Adjustments						
Non-headline items excluded from profit before taxation (note 3)	**77**		83		143	
Taxation on non-headline items	**(11)**		(21)		(53)	
Headline						
Headline profit before taxation	**208**		215		445	
Taxation on headline profit	**(55)**	**26.5%**	(58)	27.0%	(120)	27.0%

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 2014	(41)	127	86
Foreign exchange gains and losses	1	15	16
(Charge)/credit to income statement	(45)	1	(44)
Credit to reserves		31	31
Tax paid	54		54
At 31 January 2015	**(31)**	**174**	**143**

The deferred tax credit 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.

7 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, this is disclosed on the balance sheet as a retirement benefit asset. The IAS 19 surplus of any one scheme is not available to fund the IAS 19 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.

The amounts recognised in the balance sheet were as follows:

	31 January 2015 £m	31 January 2014 £m	31 July 2014 £m
Market value of funded plan assets	**4,118**	3,716	3,800
Present value of funded scheme liabilities	**(4,342)**	(3,848)	(3,935)
Unfunded pension plans	**(94)**	(85)	(89)
Post retirement healthcare	**(20)**	(19)	(18)
Net retirement benefit liability	**(338)**	(236)	(242)
Retirement benefit assets	**158**	102	123
Retirement benefit obligations	**(496)**	(338)	(365)
Net retirement benefit liability	**(338)**	(236)	(242)

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

	31 January 2015		31 January 2014		31 July 2014	
	UK	**US**	UK	US	UK	US
Rate of increase for active deferred members	**3.6%**	**n/a**	4.2%	n/a	4.2%	n/a
Rate of increase in pensions in payment	**2.7%**	**n/a**	3.3%	n/a	3.3%	n/a
Rate of increase in deferred pensions	**2.7%**	**n/a**	3.3%	n/a	3.3%	n/a
Discount rate	**2.9%**	**3.65%**	4.2%	4.70%	4.0%	4.40%
Inflation rate	**2.7%**	**n/a**	3.3%	n/a	3.3%	n/a
Healthcare cost increases	**5.0%**	**n/a**	5.0%	n/a	4.3%	n/a

The mortality assumptions for the UK schemes are consistent with the 31 July 2014 valuation. However for the US schemes, the mortality tables were updated from RP-2000 projected to 2025 as of 31 July 2014 to RP-2014 projected generationally with scale MP-14 as of 31 January 2015, to reflect the new mortality tables finalised since the year end. The updated US assumptions give the following:

Expected further years of life				US schemes
	Male 31 January 2015	**Female 31 January 2015**	Male 31 July 2014	Female 31 July 2014
Member who retires next year at age 65	**22**	**24**	20	21
Member, currently 45, when they retire in 20 years' time	**23**	**26**	20	21

Present value of funded scheme liabilities and assets for the main UK and US schemes

			31 Jan 2015 £m			31 July 2014 £m
	SIPS	**TIGPS**	**US schemes**	SIPS	TIGPS	US schemes
Present value of funded scheme liabilities						
– Active deferred members	**(80)**	**(81)**	**(130)**	(71)	(74)	(97)
– Deferred members	**(838)**	**(678)**	**(164)**	(714)	(589)	(221)
– Pensioners	**(1,078)**	**(856)**	**(357)**	(999)	(810)	(277)
Present value of funded scheme liabilities	**(1,996)**	**(1,615)**	**(651)**	(1,784)	(1,473)	(595)
Market value of scheme assets	**1,807**	**1,772**	**473**	1,639	1,594	500
Surplus/(deficit)	**(189)**	**157**	**(178)**	(145)	121	(95)

Smiths Industries Pension Scheme has a synthetic equity investment strategy using exchange-traded futures to invest in global equity markets. At 31 January 2015 the aggregate value of these derivatives was a liability of £8m.

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

	31 January 2015 £m	31 January 2014 £m	31 July 2014 £m
At beginning of period	**(242)**	(254)	(254)
Exchange adjustment	**(15)**	12	19
Current service cost	**(1)**	(1)	(3)
Scheme administration costs	**(5)**	(3)	(6)
Past service cost, curtailments and settlements	**13**		
Finance charges – retirement benefits	**(4)**	(5)	(9)
Contributions by employer	**36**	52	88
Actuarial (loss)/gain	**(120)**	(37)	(77)
Net retirement benefit liability	**(338)**	(236)	(242)

Actuarial losses have primarily arisen from lower discount rates in the UK and US and the change in mortality assumptions for the US scheme, partly offset by higher returns on scheme assets.

8 Intangible assets

	Goodwill £m	Development costs £m	Acquired intangibles £m	Software, patents and intellectual property £m	Total £m
Cost					
At 1 August 2014	1,395	216	386	164	2,161
Exchange adjustments	95	19	37	6	157
Additions		9		8	17
Disposals			(2)	(3)	(5)
At 31 January 2015	**1,490**	**244**	**421**	**175**	**2,330**
Amortisation					
At 1 August 2014	86	102	313	116	617
Exchange adjustments	8	9	30	5	52
Charge for the period		10	18	6	34
Impairment charge	26				26
Disposals			(2)	(3)	(5)
At 31 January 2015	**120**	**121**	**359**	**124**	**724**
Net book value at 31 January 2015	**1,370**	**123**	**62**	**51**	**1,606**
Net book value at 31 January 2014	1,352	119	93	45	1,609
Net book value at 31 July 2014	1,309	114	73	48	1,544

Goodwill impairment

John Crane Production Solutions ("JCPS")

JCPS is a business unit of John Crane focused on the servicing and provision of onshore down-hole 'artificial lift' pumping hardware and systems. Goodwill of £6m (31 July 2014: £30m) is allocated to JCPS. An impairment test was carried out because the significant decline in oil prices since 31 July 2014 has adversely affected JCPS' customers. JCPS anticipates that customers will scale back expansion plans and work to reduce running costs. The JCPS goodwill has been impaired by £26m because JCPS is now expected to have lower operating margins and less growth in the future, significantly reducing the value in use of the business.

The impairment loss has been recognised in John Crane administration expenses, and excluded from headline operating profit for the division, as part of "impairment of goodwill and amortisation of acquired intangible assets".

	Period ended 31 January 2015	Year ended 31 July 2014
Impairment loss recognised	**£26m**	
Basis of valuation	**value in use**	value in use
Discount rate used for impairment test	**12.9%**	12.6%
Long-term growth rates	**2.2%**	2.2%

Sales assumptions for JCPS are based on:

- Anticipated levels of maintenance and repair activities based on the current forward curve for oil prices; and
- Expected North American drilling activity.

The gross margins included in the projections are lower than historical due to lower levels of activity. As required by IAS 36: Impairment of assets, margin projections for JCPS are based on the current fixed cost base, and do not incorporate any future restructuring.

Goodwill sensitivity analysis

Smiths Detection

Goodwill of £366m (31 July 2014: £369m) is allocated to Smiths Detection. The impairment testing carried out for Annual Report 2014 has been updated to 31 January 2015. The value in use model incorporates a discount rate of 12.7% (31 July 2014: 12.5%) and assumes long-term growth of 2.2% (31 July 2014: 2.3%). No impairment has been identified, but sensitivity analysis identifies that the following changes in assumptions (in isolation) would cause the value in use to fall below the carrying value:

	Period ended 31 January 2015 Change required to trigger impairment	Year ended 31 July 2014 Change required to trigger impairment
Surplus over carrying value	**£170m**	£165m
Forecast operating cash-flow	**29% reduction**	30% reduction
Discount rate	**300 basis points higher**	300 basis points higher
Long-term growth rates	**690 basis points lower**	690 basis points lower

Sales assumptions for Smiths Detection are based on:

- the current order book and tenders in progress, including airport, cargo scanning and military opportunities;
- expected market growth rates. Market growth drivers considered include
  - passenger numbers for air transportation;
  - global trade for cargo screening;
  - increased regulatory standards to detect a wider range of substances at lower threat mass; and
  - expected rate of replacement for units initially installed following 11 September 2001.
- expected rate of adoption of new products and technologies, including HI-SCAN 10080 XCT for baggage handling systems, HI-SCAN 6040-2is for critical infrastructure and Ace-ID for trace; and
- forecast servicing of the installed product base.

Margin projections for Smiths Detection are based on historical margins, projected margins on tenders in progress and the current fixed cost base.

The directors also reviewed the fair value less costs to sell for the division when considering the results of the impairment testing, which supported the conclusion that the Smiths Detection goodwill was not impaired.

Smiths Interconnect Power

Goodwill of £128m (31 July 2014: £114m) is allocated to Smiths Interconnect Power. The impairment testing carried out for Annual Report 2014 has been updated to 31 January 2015. The value in use model incorporates a discount rate of 12.3% (31 July 2014: 11.4%) and assumes long-term growth of 2.5% (31 July 2014: 2.5%). No impairment has been identified, but sensitivity analysis identifies that the following changes in assumptions (in isolation) would cause the value in use to fall below the carrying value:

	Period ended 31 January 2015 Change required to trigger impairment	Year ended 31 July 2014 Change required to trigger impairment
Surplus over carrying value	**£15m**	£8m
Forecast operating cash-flow	**11% reduction**	6% reduction
Discount rate	**90 basis points higher**	40 basis points higher
Long-term growth rates	**180 basis points lower**	70 basis points 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.

The directors also reviewed the fair value less costs to sell for Smiths Interconnect Power when considering the results of the impairment testing, which supported the conclusion that the goodwill was not impaired.

Other CGUs

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.

9 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 2014	184	520	212	916
Exchange adjustments	12	39	8	59
Additions	3	16	9	28
Disposals	(3)	(6)	(4)	(13)
At 31 January 2015	**196**	**569**	**225**	**990**
Depreciation				
At 1 August 2014	95	393	170	658
Exchange adjustments	7	30	7	44
Charge for the period	4	14	6	24
Disposals	(3)	(4)	(4)	(11)
At 31 January 2015	**103**	**433**	**179**	**715**
Net book value at 31 January 2015	**93**	**136**	**46**	**275**
Net book value at 31 January 2014	93	125	41	259
Net book value at 31 July 2014	89	127	42	258

10 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 2015 £m	31 January 2014 £m	31 July 2014 £m
Cash and cash equivalents			
Net cash and deposits	**178**	176	190
Short-term borrowings			
Bank overdrafts	**(1)**	(6)	(1)
$250m 6.05% US$ Guaranteed notes 2014		(152)	
Bank and other loans	**(1)**	(1)	(1)
Interest accrual	**(21)**	(24)	(10)
	(23)	(183)	(12)
Long-term borrowings			
£150m 7.25% Sterling Eurobond 2016	**(150)**	(150)	(150)
€300m 4.125% Eurobond 2017	**(230)**	(251)	(243)
$175m 7.37% US$ Private placement 2018	**(116)**	(106)	(104)
Revolving Credit Facility 2019	**(155)**		(106)
$250m 7.20% US$ Guaranteed notes 2019	**(166)**	(151)	(147)
$400m 3.625% US$ Guaranteed notes 2022	**(265)**	(235)	(231)
Bank and other loans	**(2)**	(1)	(1)
	(1,084)	(894)	(982)
Borrowings	**(1,107)**	(1,077)	(994)
Net debt	**(929)**	(901)	(804)

Under the terms of the US$800m Revolving Credit Facility dated 19 February 2014, Smiths Group has the option to request that the original maturity date of 19 February 2019 be extended by 12 months. This option was duly exercised and agreed with the lending banks on 4 February 2015. Smiths can request exercise of the remaining uncommitted one-year extension option in December 2015.

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 2014	189	(11)	(982)	(804)
Foreign exchange gains and losses	13		(60)	(47)
Net cash inflow/(outflow)	(25)			(25)
Repayment and drawdown of borrowings		1	(39)	(38)
Capitalisation, interest accruals and unwind of capitalised fees		(9)		(9)
Fair value movement from interest rate hedging		(2)	(4)	(6)
Change in maturity analysis		(1)	1	
At 31 January 2015	**177**	**(22)**	**(1,084)**	**(929)**

11 Fair value of financial instruments

	Carrying value 31 January 2015 £m	**Fair value 31 January 2015 £m**	Carrying value 31 January 2014 £m	Fair value 31 January 2014 £m	Carrying value 31 July 2014 £m	Fair value 31 July 2014 £m
Level 1 valuations						
Financial assets – other investments	**139**	**139**	96	96	111	111
Level 2 valuations						
Financial derivatives - assets	**33**	**33**	24	24	17	17
Borrowings	**(1,107)**	**(1,183)**	(1,077)	(1,153)	(994)	(1,065)
Financial derivatives - liabilities	**(20)**	**(20)**	(14)	(14)	(9)	(9)
Level 3 valuations						
Financial assets – other investments	**7**	**7**	3	3	6	6

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.

12 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 2014	43	204	61	19	327
Exchange adjustments	1	25	7	1	34
Provision charged	10	13	1	8	32
Provision released	(2)	(2)			(4)
Unwind of provision discount		2	1		3
Utilisation	(11)	(10)	(4)	(3)	(28)
At 31 January 2015	**41**	**232**	**66**	**25**	**364**
Current liabilities	33	28	10	18	89
Non-current liabilities	8	204	56	7	275
At 31 January 2015	**41**	**232**	**66**	**25**	**364**

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

Trading

The trading provision includes warranties and product liabilities provisions of £32m (31 July 2014: £35m), £8m (31 July 2014: £7m) in connection with ongoing price audits of overhead cost recovery charges associated with certain historical supply agreements and £1m (31 July 2014: £1m) for 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 government price audits, 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.

John Crane, Inc. litigation provision

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 237,000 claims (31 July 2014: 235,000 claims) against JCI have been dismissed before trial over the last 35 years. JCI is currently a defendant in cases involving approximately 79,000 claims (31 July 2014: 80,000 claims). Despite the large number of claims brought against JCI, since the inception of the litigation it has had final judgments against it, after appeals, in only 132 cases (31 July 2014: 131 cases) over the period, and has had to pay awards amounting to approximately US$150m (31 July 2014: US$149m). JCI has also incurred significant additional defence costs. The litigation involves claims for a number of allegedly asbestos related diseases, with awards, when made, for mesothelioma tending to be larger than those for other diseases. JCI's ability to defend mesothelioma cases successfully is, therefore, likely to have a significant impact on its annual aggregate adverse judgment and defence costs.

The provision is based on past history and 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.

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 2015 £m	31 January 2014 £m	31 July 2014 £m
Gross provision	**249**	231	227
Discount	**(17)**	(24)	(23)
Discounted pre-tax provision	**232**	207	204
Deferred tax	**(78)**	(70)	(68)
Discounted post-tax provision	**154**	137	136

John Crane, Inc. litigation provision sensitivities

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.

Statistical analysis of the provision indicates that there is a 50% probability that the total future expenditure will fall between £235m and £263m, compared to the gross provision value of £249m.

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.

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.

The provision 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.

	31 January 2015 £m	31 January 2014 £m	31 July 2014 £m
Gross provision	**71**	69	67
Discount	**(5)**	(7)	(6)
Discounted pre-tax provision	**66**	62	61
Deferred tax	**(25)**	(23)	(23)
Discounted post-tax provision	**41**	39	38

Titeflex Corporation litigation provision sensitivities

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.

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. The £8m charge in the period relates to projects in the Fuel for Growth programme.

13 Dividends

The following dividends were declared and paid in the period:

	Period ended 31 January 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Ordinary final dividend of 27.50p for 2014 (2013: 27.00p) paid 21 November 2014	**108**	107	107
Special dividend of 30.00p for 2013 paid 22 November 2013		118	118
Ordinary interim dividend of 12.75p for 2014 paid 25 April 2014			50
	108	225	275

An interim dividend of 13.00p per share was declared by the Board on 18 March 2015 and will be paid to shareholders on 24 April 2015. 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 27 March 2015.

14 Cash-flow from operating activities

	Period ended 31 January 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Operating profit – continuing	**164**	170	378
Amortisation of intangible assets	**34**	37	73
Impairment of intangible assets	**26**		
Loss/(profit)on disposal of property, plant and equipment and intangible assets		2	2
Profit on disposal of business		(2)	(3)
Depreciation of property, plant and equipment	**24**	23	46
Share-based payment expense	**4**	4	9
Retirement benefits	**(44)**	(47)	(79)
Increase in inventories	**(38)**	(2)	4
Decrease/(increase) in trade and other receivables	**60**	36	(13)
Decrease in trade and other payables	**(47)**	(65)	(9)
Increase in provisions		15	19
Cash generated from operations	**183**	171	427
Interest	**(17)**	(28)	(76)
Tax paid	**(54)**	(60)	(95)
Net cash inflow from operating activities	**112**	83	256

Headline operating cash-flow

	Period ended 31 January 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Net cash inflow from operating activities	**112**	83	256
Exclude			
Interest	**17**	28	76
Tax paid	**54**	60	95
Cash outflow in respect of exceptional operating items	**29**	36	74
Pension deficit payments	**34**	49	82
Include			
Expenditure on capitalised development, other intangible assets and property, plant and equipment	**(44)**	(45)	(94)
Disposals of property, plant and equipment in the ordinary course of business	**2**		1
Headline operating cash-flow	**204**	211	490

Free cash-flow

	Period ended 31 January 2015 £m	Period ended 31 January 2014 £m	Year ended 31 July 2014 £m
Net cash inflow from operating activities	**112**	83	256
Expenditure on capitalised development, other intangible assets and property, plant and equipment	**(44)**	(45)	(94)
Disposals of property, plant and equipment	**2**	4	5
Investment in financial assets relating to pensions financing	**(12)**	(12)	(24)
Free cash-flow	**58**	30	143
Investment in other financial assets	**(1)**		(4)
Acquisition of businesses			(1)
Disposal of businesses		3	3
Net cash-flow used in financing activities	**(82)**	(229)	(313)
Net increase/(decrease) in cash and cash equivalents	**(25)**	(196)	(172)

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 2014.