

BUSINESS REVIEW

In November 2008 we announced the sale of the Insulators and Alumina businesses, acquired as part of the Argillon Group, for €21 million in cash plus a €2 million vendor loan note. The businesses had been classified as “assets held for sale” in last year’s accounts. The sale resulted in a profit of £0.9 million in discontinued businesses, which is excluded from underlying earnings per share.

Dividend

The board is recommending to shareholders a final dividend of 26.0 pence (unchanged from 2008) making a total dividend for the year of 37.1 pence, an increase of 1%. Cover for 2008/09 would be 2.4 times. The overall percentage increase in the dividend for the full year is slightly greater than the growth in underlying earnings per share as a result of the 5% increase in the interim dividend.

Pensions

At 31st March 2009 the group’s main UK pension scheme was in deficit by £45.2 million (94% funded) on an IFRS basis compared with a surplus of £65.1 million at 31st March 2008. The change mainly reflected the fall in asset values at 31st March 2009 compared with a year earlier, with equity investments in particular adversely affected by the global recession. The valuation was also adjusted for the latest information on mortality for the members of the scheme with expected longevity rates increasing.

Worldwide, including provisions for the group’s post-retirement healthcare schemes, the group had a net deficit of £151.6 million on employee benefit obligations at 31st March 2009 compared with a surplus of £16.4 million at 31st March 2008. In 2009/10 we plan to make an additional payment of US \$30 million into our US schemes to bring the funds closer to balance. The triennial revaluation of our main UK scheme is currently underway and it is likely that the company will need to increase its rate of contributions from 2010. In 2008/09 the company’s contribution to the UK scheme was £22.1 million.

Cash Flow

The group achieved strong cash generation in 2008/09 with a net cash inflow of £96.8 million. After taking into account the impact of exchange translation on foreign currency borrowings the group’s net debt fell by £76.0 million to £534.4 million. Included in cash flow under IFRS is the impact of swap transactions used to manage currency borrowings. If these are added to exchange translation the total translational effect of exchange rate movements on borrowings denominated in foreign currencies was over £110 million and cash generation more than £190 million.

Net cash flow from operating activities increased by £271.8 million to £501.4 million. In response to the fall in demand from the automotive sector and lower precious metal prices we were able to generate £204.2 million from reduced working capital. We invested £209.3 million in capital expenditure and other investments, which was 2.0 times depreciation. Major projects included the construction of the two new ECT facilities

in Macedonia and western Pennsylvania, USA, and new production capacity at Clitheroe, UK to manufacture methanol synthesis catalysts. In November 2008 we completed the planned disposal of Argillon’s Insulators and Alumina businesses for €21 million in cash plus a €2 million vendor loan note.

We plan to reduce capital expenditure to 1.2 times depreciation in 2009/10. Major projects will include completion of ECT’s new facilities in Macedonia and western Pennsylvania and investment in China on manufacturing capacity for plate catalysts used for reducing harmful NOx emissions from power stations.

Capital Structure

In 2008/09 net debt fell by £76.0 million to £534.4 million and equity rose by £15.8 million to £1,176.1 million. Gearing (net debt / equity) fell by 7.2% to 45.4%. The group’s target range for gearing is 50% to 60%. Given the current level of economic uncertainty and more difficult conditions in the credit markets the board is happy to keep gearing below the target range for the time being. Net debt / EBITDA for the year was 1.3 times and interest cover (underlying operating profit / net finance costs) was 9.2 times.

On 31st July 2008 we drew down a five year fixed rate loan of €125 million from the European Investment Bank (EIB) under a facility arranged earlier in the year. The facility is provided to support the group’s investment in research and development. At 31st March 2009 the group had £609.1 million of debt in the form of long term bonds issued in the USA and loans from the EIB. Gross debt (net of related swaps) amounted to £649.6 million offset by £115.2 million of cash and deposits. The group also had £315.0 million of committed bank facilities which are individually negotiated and over half have expiry dates after 31st March 2011 (see note 29b on page 90). There were no drawings under these bank facilities at 31st March 2009.

Treasury Policies

Financial Risk Management and Treasury Policies

The group uses financial instruments, in particular forward currency contracts and currency swaps, to manage the financial risks associated with its underlying business activities and the financing of those activities. The group does not undertake any trading activity in financial instruments. Our treasury department is run as a service centre rather than a profit centre.

Interest Rate Risk

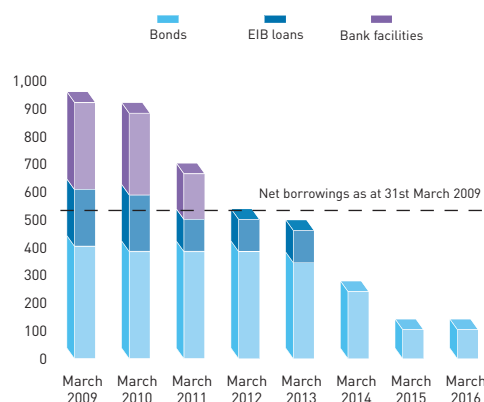
At 31st March 2009 the group had net borrowings of £534.4 million. Some 63% of this debt was at fixed rates with an average interest rate of 5.1%. The remaining 37% of the group’s net borrowings was funded on a floating rate basis. A 1% change in all interest rates would have a 0.7% impact on underlying profit before tax. This is within the range the board regards as acceptable.

Borrowings

	31st March 2009		31st March 2008	
	£ million	%	£ million	%
Five to ten years	242.6	37	256.5	36
Two to five years	268.5	41	261.1	37
One to two years	88.9	14	72.9	10
Within one year	49.6	8	122.0	17
Gross borrowings (net of swaps)	649.6	100	712.5	100
Less: cash and deposits	115.2		102.1	
Net debt	534.4		610.4	

Maturity Profile of Debt Facilities

£ million



Foreign Currency Risk

Johnson Matthey's operations are located in over 30 countries, providing global coverage. The majority of its profits are earned outside the UK. In order to protect the group's sterling balance sheet and reduce cash flow risk the group has financed most of its investment in the USA, Europe and Japan by borrowing US dollars, euros and yen respectively. Although much of this funding is obtained by directly borrowing the relevant currency, a part is achieved through currency swaps which can be more efficient and reduce costs and credit exposure. The group uses forward exchange contracts to hedge foreign exchange exposures arising on forecast receipts and payments in foreign currencies. Currency options are occasionally used to hedge foreign exchange exposures, usually when the forecast receipt or payment amounts are uncertain. Details of the contracts outstanding on 31st March 2009 are shown on pages 89 and 90.

Precious Metal Prices

Fluctuations in precious metal prices can have a significant impact on Johnson Matthey's financial results. Our policy for all manufacturing businesses is to limit this exposure by hedging against future price changes where such hedging can be done at acceptable cost. The group does not take material exposures on metal trading.

All the group's stocks of gold and silver are fully hedged by leasing or forward sales. Currently the majority of the group's platinum stocks are unhedged because of the lack of liquidity in the platinum market.

Liquidity and Going Concern

The group's policy on funding capacity is to ensure that we always have sufficient long term funding and committed bank facilities in place to meet foreseeable peak borrowing requirements. At 31st March 2009 the group had cash and deposits of £115.2 million and £315.0 million of undrawn committed bank facilities available to meet future funding requirements. The group also has a number of uncommitted facilities, including metal leases, and overdraft lines at its disposal.

Gross borrowings (net of related swaps) of £649.6 million at 31st March 2009 included £609.1 million of debt arranged under long term bond issues and long term funding from the European Investment Bank, of which only £19.0 million falls due to be repaid in the 15 months to 30th June 2010 (the going concern period). £265.0 million of the committed bank facilities have expiry dates after 30th June 2010. The maturity dates of the group's debt and borrowing facilities are illustrated in the table and chart above.

The directors have assessed the future funding requirements of the group and the company and compared it to the level of long term debt and committed bank facilities for the 15 months from the balance sheet date. The assessment included a sensitivity analysis on the key factors which could affect future cash flow and funding requirements. Having undertaken this work the directors are of the opinion that the group has adequate resources to fund its operations for the foreseeable future and so determine that it is appropriate to prepare the accounts on a going concern basis.