

Business Review

Financial performance

Net finance cost

Net finance cost for the year was £3.1m (2008: income of £4.3m) with the increase attributable to a £5.2m increase in the net finance cost on post-employment benefit liabilities and a significant reduction in the interest receivable on short-term deposits as global interest rates have reduced during the year. The net finance cost will increase further in 2009/10 as the impact of changing assumptions for discount rates and lower asset values on the IAS 19 pension deficit interest take effect. Interest receivable on our net funds will also be impacted by the low interest rates.

Taxation

The Group's income tax expense for the year, on continuing operations, was £18.5m (2008: £23.3m). This included a one-off £7.0m benefit from the purchase of prior year consortium relief credits from the Metronet companies, giving a normalised effective tax rate of 18.5% (2008: 25.7%). Excluding that one-off benefit, the Group's normalised effective tax rate would have been 25.4%, slightly higher than anticipated due to the impact of the lower share price on the tax deductions available from the Group's share incentive plans. Looking forward, the Group's effective tax rate is expected to continue to benefit from R&D tax credits and the proportion of profits earned in jurisdictions with lower tax rates than the UK.

Earnings per share (EPS)

Basic EPS was 86.1p (2008: 98.9p). Normalised diluted EPS, which is considered to be a more representative measure of underlying trading and relates to continuing operations, was 82.3p (2008: 66.7p), an increase of 23.4%. Excluding the benefit of acquired tax losses, normalised diluted earnings per share would have been 75.2p, an increase of 12.7%.

Pensions Funding

The latest actuarial valuation of the defined benefit Atkins Pension Plan (the Plan) carried out as at 1 April 2007 indicated that the Plan had an actuarial deficit of approximately £215m. Accelerated contributions of £44.5m were made during the year and the Group has agreed to contribute a further £32m per year for the next five years. The next actuarial valuation will take place as at 1 April 2010 and is likely to be completed in late 2010 or early 2011.

Charges

The Group accounts for pension costs under IAS 19, *Employee benefits*. The total charge to the income statement in respect of defined benefit schemes reduced to £14.8m (2008: £17.8m), comprising total service cost of £8.9m (2008: £16.7m) and net finance cost of £5.9m (2008: £1.1m). The charge relating to defined contribution schemes increased to £28.2m (2008: £19.0m), reflecting the closure of the defined benefit schemes to future accrual and the transfer of staff to the defined contribution scheme.

IAS 19 valuation and accounting treatment

The Group assesses pension scheme funding with reference to actuarial valuations but for reporting purposes uses IAS 19. Under IAS 19, the Group recognised a much-increased post-tax retirement benefit liability of £215.4m at 31 March 2009 (2008: £153.9m) reflecting the adverse impact of the investment markets on fund assets. The actuarial loss recognised through equity amounted to £88.5m (2008: Gain of £6.4m which became a loss of £1.0m after taking into account the impact of the change in UK tax rates).

The assumptions used in the IAS 19 valuation are detailed in note 29 to the Financial Statements.

Cash

Net funds at 31 March 2009 were £234.2m (2008: £168.4m) made up as follows:

	2009 £m	2008 £m
Cash and cash equivalents	209.7	154.5
Loan notes receivable	12.9	5.6
Financial assets at fair value through profit or loss	28.7	29.7
Borrowings due within one year	(2.8)	(4.2)
Borrowings due after one year	(0.6)	(3.2)
Finance leases	(13.7)	(14.0)
Net funds	234.2	168.4

£234.2m

Net funds

Cash generated from continuing operations was £125.5m (2008: £80.9m), representing 122% of operating profit, and can be summarised as follows:

	2009 £m	2008 £m
EBITDA	136.5	117.1
Additional outflow relating to pensions	(40.6)	(29.1)
Movement in working capital	10.9	(7.3)
Movement in provisions	9.2	(5.5)
Other non-cash items	9.5	5.7
	125.5	80.9

Operating cash flow remained strong as we continued to optimise the cash position on our contracts. Proactive working capital management resulted in a net working capital inflow of £10.9m which was achieved despite a lengthening of debtor days in the Middle East in the last quarter of the year. The accruals for redundancy and bonus payments increased this year and will result in an outflow in the first half of 2009/10.

The movement in provisions includes the additional onerous contract provisions recognised in the Asset Management segment and a net increase in the Group's vacant property provision, where we took a more conservative view in light of the current environment for letting surplus office space, both of which will result in a cash outflow in the coming financial years.

Net tax paid amounted to £12.8m (2008: £14.7m) which includes payments of £0.4m (2008: £11.8m) to Metronet for consortium relief. The cash flows associated with this year's consortium relief benefit of £7m will be incurred in 2009/10.

Net capital expenditure in the year, including the purchase of computer software licences, amounted to £27.6m (2008: £25.7m). This was less than originally anticipated as we reduced discretionary items in this time of economic uncertainty.

An amount of £12.3m (2008: £34.0m) was paid out in respect of the share buyback programme.

Capital structure

As at 31 March 2009, the Group had a shareholders' deficit of £43.5m (2008: £23.4m) and the Company had shareholders' funds of £108.8m (2008: £126.9m).

The Company had 104.5m fully paid ordinary shares in issue at 31 March 2009 (2008: 104.5m). The Company commenced a share buyback programme in November 2007 and by 31 March 2009 had bought 4.3m of its own shares in the market for a total consideration, including commission and stamp duty, of £46.4m. These shares are held within treasury. During the year the Company bought 1.1m shares (2008: 3.2m) at a total cost of £11.5m (2008: £34.9m) with the last purchase occurring in July 2008.

Treasury policies and objectives

The Group's treasury function manages and monitors external funding and investment requirements and financial risks in support of the Group's corporate objectives. The Board reviews and agrees policies and authority levels for treasury activities.

The Group's financial instruments, other than derivatives, comprise borrowings, cash and liquid resources and various items, such as trade receivables and trade payables, which arise directly from its operations. The main purpose of these financial instruments is to finance the Group's activities. The Group also enters into derivative transactions, principally forward foreign currency contracts, in order to manage foreign exchange risk on material commercial transactions undertaken in currencies other than the local functional currency. The Group does not trade in financial instruments.

The main risks arising from the Group's financial instruments are market risk (including foreign exchange risk, interest rate risk and price risk), credit risk and liquidity risk, along with the risks arising from the financing of the Group's activities in the Public Private Partnership (PPP) and Private Finance Initiative (PFI) sectors. The Group's exposures to and management of each of these risks, together with sensitivities and risk concentrations, are described in detail in note 2 to the Financial Statements.

The Group funds its ongoing activities through cash generated from its operations and, where necessary, bank borrowings and finance leases. The Group's banking facilities are described in note 25 to the Financial Statements; utilisation of the facility mainly relates to letters of credit issued in respect of individual projects undertaken by the Group's operating businesses. As at 31 March 2009 the Group had £75.0m undrawn committed borrowing facility available (2008: £58.8m).

There have been no significant changes to the Group's treasury policies during the year.

Business Review

Financial performance

Continued

Critical accounting policies

The Group's principal accounting policies are described in note 1 to the Financial Statements. The Financial Statements for the year ended 31 March 2009 have been prepared under IFRS as adopted by the EU.

The preparation of Financial Statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the Financial Statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. Material estimates applied across the Group's businesses and Joint Ventures are reviewed to a common standard and adjusted where appropriate to ensure that consistent treatment of similar and related issues that require judgement is achieved upon consolidation. Any revisions to estimates are recognised prospectively.

The accounting policies and areas that require the most significant estimates and judgements to be used in the preparation of the Financial Statements are in relation to contract accounting and defined benefit pension schemes.

Contract accounting

Profit is recognised on contracts on a percentage completion basis, provided the outcome of the project can be reasonably foreseen. Full provision is made for estimated losses. Where contracts span more than two accounting periods profit is not generally recognised until the project is 50% complete.

The projected outcome of any given contract is necessarily based on estimates of revenues and costs to completion. Whilst the assumptions made are based on professional judgements, subsequent events may mean that estimates calculated prove inaccurate, with a consequent effect on the reporting of results.

Defined benefit pension schemes

Accounting for pensions involves judgement about uncertain events in the future such as inflation, salary levels at retirement, longevity rates, rates of return on plan assets and discount rates. Assumptions in respect of pensions and post-retirement benefits are set after consultation with independent qualified actuaries. Management believes the assumptions are appropriate. However, a change in the assumptions used would impact the Group's results and net assets. Any differences between the assumptions and the actual outcome will affect results in future years. An estimate of the sensitivity is disclosed in note 29 to the Financial Statements.