

MACFARLANE GROUP PLC
REPORT AND FINANCIAL STATEMENTS
31 DECEMBER 2005

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OUR BUSINESSES – PACKAGING DISTRIBUTION AND MANUFACTURING OPERATIONS

■ PACKAGING DISTRIBUTION

The Macfarlane Packaging Distribution business is the leading UK distributor of a comprehensive range of packaging consumable products. We enable customers to cost effectively package their products by providing a broad product range, single source supply, just in time delivery from any of our 15 Regional Distribution Centres and tailored stock management programmes.

□ LABELS

Macfarlane Labels design and produce high quality self-adhesive and re-sealable labels for consumer packs. The customer base is primarily leading FMCG companies. The business operates from two plants, one in Kilmarnock and one in Dublin as well as a European sales office for re-sealable labels based in Sweden.

□ PLASTICS

Macfarlane Plastics design and produce injection-moulded closures and dispensers primarily for powdered consumer products for major FMCG customers across Europe. The business operates from a production plant in Wicklow in Ireland.

■ INTERNATIONAL

Macfarlane Group's four International packaging manufacturing and assembly operations are in California and Mexico. These plants provide a range of packaging solutions primarily for the electronics, medical and gift markets.

■ PACKAGING MANUFACTURE

Macfarlane's Packaging Manufacture business operates from Grantham and Westbury, producing a range of low volume, custom designed packaging solutions using corrugate, timber and foam materials. The product range is focussed on the electronics, medical and automotive markets where product protection, for both storage and transportation are key requirements.

CHAIRMAN'S STATEMENT

ARCHIE HUNTER
Chairman

"I am very glad to report that after four years of losses, Macfarlane Group has returned to profit in 2005."

I am very glad to report that after four years of losses, Macfarlane Group has returned to profit in 2005.

After trading losses of	£ (10.4)million	in 2003 *
and	£ (2.4)million	in 2004 **
we have recorded a trading profit of	£ 2.6 million	in 2005 **

Earnings per share from all businesses in 2005 were 3.01p and group turnover from continuing businesses has increased in the year by £5 million to £127 million.

The turn-around in trading and asset disposals has had the expected positive impact on our cash position. The Group generated cash of £7 million in 2005 and as a result there has been further significant reduction in group borrowings, which stood at £6 million at 31 December 2005 compared to a high point of £32 million at 30 September 2003. The Board anticipates further cash generation from trading in 2006.

All of this has been achieved by disciplined executive action to a demanding plan set by the Board two years ago. The platform has now been created for further profitable development and the payment of dividends to our shareholders.

TRADING

The results improvement has been achieved in the face of a difficult market for Packaging Distribution in the UK. The highlights have been the retention of margins and the return to profitability. The drive for profitable growth is now our priority. Future sales growth in this business should be accompanied by strong profit generation given the levels of operational gearing in our UK wide network.

In 2005, within our Manufacturing Operations, our Labels business had to respond to increasingly demanding customer requirements. Significant raw material price increases had an inevitable impact on our Plastics business, which showed improvements but continued to be loss making. The Group's operations in California and Mexico returned to profit in 2005. They show good potential with strong customer and supplier relationships. Both our UK Packaging Manufacturing locations produced profits in 2005 and further improvement is expected this year.

In line with the Group's strategy to concentrate on and develop its core businesses, Macfarlane Group announced an agreement in January 2006 to sell its Hungarian packaging manufacture and assembly operation. The directors estimate that the disposal will produce a realised gain of £0.9 million in the financial year to 31 December 2006.

More detailed trading comments are set out in the operations review, following my statement.

* Loss from continuing and discontinued operations before property gains per UK GAAP
** Profit/(loss) from continuing and discontinued trading operations

INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRSs")

These are the first annual accounts requiring to be prepared in line with IFRSs. These new standards have a significant impact on the balance sheet.

In common with many companies we had to incorporate a net pension scheme deficit on the balance sheet, which at 31 December 2005 amounted to £16 million, net of attributable deferred taxation of £7 million. Without taking action, the incorporation of this deficit would have prevented the payment of dividends by the Company in the short-term. In 2005 therefore the Board sought and received the agreement of shareholders and the court to restructure the company's capital base and the effect of the restructuring is shown in the parent company balance sheet. I would like to emphasise that it is out of the distributable reserves of the parent company that dividends are paid to shareholders and at 31 December 2005, these amounted to £4.4 million.

A plan of payments to fund the deficit over future years has been agreed with the Trustees of the pension scheme. The Board is considering what further steps should be taken to address the pension deficit and mitigate the future effect on the Group's distributable reserves.

CASH AND DIVIDENDS

For the past two years the Board has been clear that alongside the restoration of profitable trading, a significant reduction in group borrowings was a priority. With these objectives now realised, this allows the Board to address the establishment of an appropriate pattern of dividend payment to our shareholders. The Board believes that shareholders can expect to hear now of the Board's intentions in this regard.

Subject to continued satisfactory trading, the Board plans to establish the payment of an interim dividend in October of each year and a final dividend in June each year, following the Annual General Meeting. In my statement dated 6 September 2005, I indicated that no further dividend would be declared in respect of 2005. In respect of 2006, the Board's current intention is that the dividend should be at the rate of 2p per share, 1p for each of the interim and final dividend. However in view of the interval since the last dividend payment in September last year, the Board intends acceleration of the 2006 interim payment from October to June 2006, with the final dividend of 1p being declared and approved by shareholders at the Annual General Meeting in 2007.

The Board intends to present a special resolution to shareholders at the forthcoming AGM to restore the authority to buy-back shares of the Company in the market. The Board has no present intention to use this authority but we believe that it is now appropriate for the Company to have the authority in case specific circumstances develop, where it would be in the best interests of shareholders for the Company to purchase its own shares. If passed, it is the intention of the Board that this authority would be used sparingly.

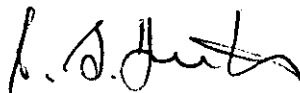
FUTURE PROSPECTS

I am glad to report a positive start to 2006 and the Board anticipates for the full year a significant advance in profits over 2005.

Our objectives for 2006 are profitable growth in our major businesses. We intend to achieve this by playing to our strengths. Our Packaging Distribution business is the UK leader, almost three times the size of our nearest competitor. We intend to use that strength to further develop our presence, which we estimate currently to be about 10% of the UK market. In each of our other businesses we have created opportunities and we plan to take advantage of them.

Having come through a most difficult period the challenge facing our staff is now a very different one. Through their efforts, the reputation and standing of Macfarlane Group has been very significantly restored. The platform we asked for has been created. The challenge will not diminish but it is one that is now exciting and uplifting. On behalf of the Board I thank them all for what has been achieved.

I am confident we have in the business the leadership and the determination that we need.



ARCHIE S. HUNTER
Chairman
28 March 2006

OPERATIONS REVIEW AND FINANCIAL REVIEW

OPERATIONS REVIEW

Trading performance

Group Segment	Revenue 2005 £000	Revenue 2004 £000	Result 2005 £000	Result 2004 £000
Packaging Distribution	73,915	74,095	661	(769)
Manufacturing Operations	53,332	48,610	2,267	864
Continuing activities	127,247	122,705	2,928	95
Discontinued activities (Manufacturing Operations)	3,618	4,634	750	(845)
	130,865	127,339	3,678	(750)
Net interest payable			(1,054)	(1,678)
Profit/(loss) from continuing & discontinued trading operations			2,624	(2,428)
Gain on disposal of properties			1,048	3,566
Loss on disposal of discontinued operations			-	(1,400)
Profit/(loss) before taxation			3,672	(262)
Tax Continuing activities			(161)	26
Discontinued activities			(126)	-
Profit/(loss) for the year			3,385	(236)

Our objective in 2005 was to return Macfarlane Group to profitability following four years of losses. The results for 2005 show the Group recording profits from trading operations of £2.6 million, an improvement of £5.1 million on the previous year. The return to profitability combined with good cash generation and lower levels of debt reflect favourably on the actions we have taken across all group businesses to grow sales, improve margins, lower costs and increase productivity.

All businesses within the Group, with the exception of our Plastics business in Ireland, were profitable in 2005. The return to profitability was achieved despite unfavourable market conditions in the majority of the markets in which we operate and increasing cost pressures on raw materials, fuel and energy.

We have demonstrated in 2005 our ability to implement the relevant action plans to return Macfarlane Group to profitability and a solid foundation has now been established. The focus of our plans for 2006 and beyond is to build on this base and grow the business both organically and through acquisition.

PACKAGING DISTRIBUTION

The Macfarlane Packaging Distribution business is the leading UK distributor of a comprehensive range of packaging consumable products. In a highly fragmented market, Macfarlane currently has a 10% market share and through its 15 Regional Distribution Centres (RDCs) supplies customers on a local, regional and national basis. The business enables customers to cost effectively package their products by providing them with a comprehensive product range, single source supply, just in time delivery and tailored stock management programmes.

In 2005 Macfarlane Packaging Distribution recorded a profit of £0.7m, an improvement of £1.4m on the previous year. There were a number of factors that contributed to the improvement in results:

- Although sales revenue was flat on 2004, our 2005 sales performance from the top 10 RDCs showed 5.3% growth versus the previous year in a market that by common consent in 2005 was at best flat;
- In 2005 our On-Time-In-Full ("OTIF") deliveries averaged 92% compared with 85% in 2004 and only 71% in 2003. This clearly demonstrates the progress we are making in improving the service to our customers;
- In 2005 we increased product range penetration in our existing customer base to an average 8.2 lines per customer compared with 8.0 in 2004 and 7.0 in 2003;

- During 2005 we opened 2,875 new customers, an increase of 12% vs. 2004;

- We commenced in 2005 a programme to rationalise our supplier base to more cost-effectively source products. Our current supplier base consists of 670 companies, a reduction of 90 vs. 2004;

- Our headcount in 2005 stabilised at 400 and our overhead to sales ratio reduced by 1.8% from 2004;

- In 2005, 30 major customers commenced trading with us electronically using our new Customer Connect service; and

- Our 2005 customer satisfaction survey showed 79% of customers rating our service above average (2004 - 74%) and of these, 27% rating our service as excellent (2004 - 24%).

During 2005 we had stable trading patterns in 12 of our 15 RDCs. These RDCs have experienced and capable management leading effective teams with low staff turnover. Collectively the profit improvement from the stable RDCs was £1.2 million over 2004. However there remain 3 RDCs, which did not perform to the expected levels during 2005. Actions have been taken to strengthen and focus management in these RDCs and we are expecting significant performance improvement in 2006.

The plan for 2006 is to focus our management actions on growing the business, with a particular emphasis on extending the range of products and services supplied to our existing customers and the winning of new customers. During 2006 we will create a dedicated new team focused on winning new business. We will also increase our accessibility to new customers through our web-based service Packaging2U. Our intention is also to enable a wider range of our customers to benefit from trading with us electronically through the Customer Connect service.

We will maintain our attention to cost control and through the ongoing programme of supplier rationalisation and the strength of our strategic supplier relationships expect to maintain our gross margin in 2006.

Our current RDC network allows us to effectively access 85% of the UK market and we are currently operating at ca. 70% of the RDC network capacity. During 2006 we will evaluate potential acquisition opportunities to improve market access and make more effective use of our existing capacity.

MANUFACTURING OPERATIONS

In 2005 Macfarlane Group's Manufacturing Operations recorded a profit of £2.3 million, an improvement of £1.4 million on the previous year. All operations showed improvements on 2004.

Both Macfarlane Labels and Macfarlane Plastics businesses supply major FMCG customers primarily, but not exclusively, based in the UK and Ireland. Labels operate from two plants, Kilmarnock and Dublin, supplying design and production of high quality self-adhesive and re-sealable labels for consumer packs. Plastics operate from Wicklow in Ireland designing and producing injection-moulded closures and dispensers primarily used in the packaging of powdered consumer products.

The key features of the Labels performance in 2005 were:

- A profit performance broadly in line with 2004 despite the market for self-adhesive labels being particularly competitive with strong retail pressure for supplier price reductions;
- Good volume growth of 27% in re-sealable labels and self-adhesive label volumes at last year's levels;
- Cost reductions and programmes to improve productivity were implemented at both our plants with the aim of offsetting the selling price pressures;
- There have been initial moves to develop the re-sealable labels business in the USA, following encouraging feedback from potential customers; and
- There are new versions of the re-sealable label being trialled which will enable its use in a number of additional product sectors.

Packaging Distribution

Our current RDC network allows us to effectively access 85% of the UK market.

Our priorities in 2006 are to continue to improve operational efficiencies in order to offset retail price pressure, to broaden the appeal of the re-sealable label offering and to accelerate our growth plans in our chosen sectors of the self-adhesive label market. We also see potential opportunities to accelerate growth through acquisition.

The Plastics business reduced its operating losses significantly in 2005 but did not achieve the break-even level that was targeted. The key features of the 2005 performance were:

- Sales volume growth vs. 2004 and the operating loss was reduced versus 2004;
- Continued rises in raw material prices, which were not fully recovered, from the customer base;
- We experienced increased cost pressures particularly on transport and energy; and
- Towards the end of 2005 a number of senior management changes were implemented.

The strengthened management team is now fully focused on building on the improvements achieved in 2005 to restore a break-even position in 2006.

Macfarlane had packaging manufacturing and assembly operations in California, Hungary and Mexico during 2005. These plants provided corrugate, foam and timber packaging solutions primarily to the electronics sector.

The US operations focus particularly on foam based products in relation to their position in the electronics sector and have recently diversified into the healthcare and fresh produce display sectors of the market.

The US business had a particularly successful year in 2005.

- During 2005 the US business suffered major raw material price increases both as a result of the oil price pressure and also due to supply chain issues with certain key vendors following the extraordinary weather conditions. However both of these difficulties were effectively managed and had no material impact on the business in 2005;
- The sales momentum created in the second half of 2004 was maintained throughout the year resulting in annual sales growth of 27%;
- The business returned to profitability following losses in 2004;
- The absorption of the foam packaging activities of a key customer that took place at the end of 2004 was successfully integrated in 2005 and contributed 12% of the sales growth;
- We also created and strengthened a number of significant major customer relationships during 2005 in both the medical and electronics sectors and these provide a solid platform for further growth in 2006; and
- At the end of 2005 we made the decision to establish a new facility in Tijuana, to enable us to more cost-effectively service our customers in Southern California and give access to new customers in Northern Mexico.

Our priorities in 2006 are to build on our current strong market position and our key customer relationships in California in the medical and electronics sectors. The opening of the new facility in Tijuana will enable us to enhance our production capacity while at the same time becoming more cost-effective and more accessible to key local markets and customers particularly in the Northern Mexico region.

OPERATIONS REVIEW AND FINANCIAL REVIEW

Labels

Macfarlane Labels demonstrates a commitment to quality and customer service that is recognised by its brand leading customers.

OPERATIONS REVIEW (continued)

The decision to establish a business in Hungary was made in 2000, when IBM, a key customer of our Westbury facility relocated to Budapest. Although our business in Hungary continued to be successful in 2005, we became increasingly concerned at the over-dependence on this one customer. In 2005 Nefab AB, a Swedish based company, expressed an interest in acquiring our business in Hungary. Following a strategic review the decision was made to sell the business. The transaction was completed early in January 2006 at a price of £2.3m, a £0.9m premium to net asset value and the activities have been disclosed as discontinued in the financial statements.

Macfarlane's Packaging Manufacture business operates from two UK sites in Grantham and Westbury. The business produces a range of low volume, custom-designed packaging solutions using corrugate, timber and foam materials. The range of products is particularly focused on the electronics, medical and automotive markets where product protection, for both storage and transportation are key requirements.

The highlights of the 2005 performance were:

- Both sites returning to profitability in 2005 following losses in 2004;
- At Grantham the introduction of a "lean manufacturing programme" produced cost reductions and improved productivity;
- Customer retention levels increased through improved customer service; and
- At Westbury the profit recovery was primarily driven by good sales growth.

The priority for 2006 is to improve the returns from this business. At Grantham the focus in 2006 will be on growing sales particularly through the Macfarlane Packaging Distribution network. Our Westbury location is focused on maintaining sales momentum while at the same time introducing a number of the productivity improvement initiatives that were effective at Grantham in 2005.

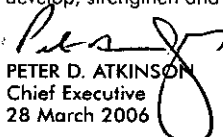
FUTURE OUTLOOK

During 2005 we have demonstrated our ability to return the Group to profitability. We have also improved cash generation and significantly strengthened the balance sheet. Our priority is now to continue the process of giving greater focus to the Group's activities, accelerating growth in the key businesses and continuing to improve financial performance in the niche businesses.

The Group has a range of businesses, all of which have good potential and operate in highly fragmented markets with opportunities for consolidation. Our market positions particularly in UK Packaging Distribution and Labels are sound and can be strengthened through both organic and acquisition-lead growth. In addition we have a number of other good geographic and product niches, most of which are now profitable and offer continued potential for profit improvement.

The businesses are all developing their operational capability and cost-effectiveness. We consistently see our customer service improving dramatically and our key customer and supplier relationships are strengthening. A key component of our future plans is to accelerate the efforts of all our businesses to become more customer-focused.

Following a particularly difficult period over the last three years, Macfarlane Group has now established a strong foundation. Management is now focused on using this foundation to further develop, strengthen and grow the Group's key businesses.


PETER D. ATKINSON
Chief Executive
28 March 2006

FINANCIAL REVIEW

2005 RESULTS

	Continuing £000	Discontinued £000	2005 £000	Continuing £000	Discontinued £000	2004 £000
Turnover	127,247	3,618	130,865	122,705	4,634	127,339
Cost of sales	(85,122)	(2,082)	(87,204)	(82,200)	(2,540)	(84,740)
Gross profit	42,125	1,536	43,661	40,505	2,094	42,599
Net operating expenses	(39,197)	(786)	(39,983)	(40,410)	(2,939)	(43,349)
Profit/(loss) before property transactions	2,928	750	3,678	95	(845)	(750)
Gain on property disposals	1,048	–	1,048	3,566	–	3,566
Operating profit/(loss)	3,976	750	4,726	3,661	(845)	2,816
Net interest cost	(1,086)	32	(1,054)	(1,678)	–	(1,678)
Profit/(loss) after interest	2,890	782	3,672	1,983	(845)	1,138
Loss on disposal of business	–	–	–	–	(1,400)	(1,400)
Profit/(loss) before tax	2,890	782	3,672	1,983	(2,245)	(262)

Group turnover from continuing activities in 2005 increased from £122.7 million to £127.2 million, a £4.5 million increase. Turnover from continuing and discontinued activities increased to £130.9 million from the previous year's figure of £127.3 million.

Profits before tax were £3.7 million compared to a loss of £0.3 million in 2004, with major trading improvements in 2005 recorded in our Packaging Distribution and Manufacturing Operations. In February 2005 the Company's vacant property at Govan, near Glasgow, was sold, realising a significant gain.

Further improvements are anticipated in 2006 by continuing the focus on sales growth and cost reduction.

CONTINUING AND DISCONTINUED OPERATIONS

In January 2006, the Company's Hungarian subsidiary was sold. Consequently the results of the subsidiary for 2005 and 2004 are classified as discontinued operations in the consolidated income statement. The component parts of the balance sheet sold in January 2006 are classified as non-current assets and current liabilities held for sale at 31 December 2005.

The results from the former trading subsidiary Tom Brands Electrical Services Limited are also classified as discontinued operations in the 2004 consolidated income statement.

INTEREST AND BORROWINGS

Net finance costs less investment income amounted to £1.1 million compared to £1.7 million in 2004. The reduced interest charge reflects a considerable reduction in the levels of bank borrowings during the year. The Board remains firmly committed to reducing debt further during 2006.

TAXATION

The total tax charge for the year was £0.3 million on the profit before tax as shown above of £3.7 million compared with a tax credit of £0.1 million on pre-tax losses of £0.3 million in the previous year. The majority of the 2005 tax charge related to overseas operations. The rate varied significantly from the standard UK rate of 30% due to UK gains on property assets, which were not taxable and the utilisation of corporation tax losses from previous years.

The balance of UK tax losses totalling approximately £10.0m have been carried forward and are available for offset against future taxable profits.

EARNINGS PER SHARE AND DIVIDENDS

Basic earnings per share from continuing operations totalled 2.43p per share in the year to 31 December 2005 compared to 1.79p in the previous year.

An interim dividend of 0.75p was paid on 27 September 2005. No final dividend will be recommended in respect of the 2005 results.

OPERATIONS REVIEW AND FINANCIAL REVIEW

FINANCIAL REVIEW (continued)

PROPERTY

In the five years since January 2001, we have fully exited over 54 sites, a mixture of owned and leased properties, all surplus to our requirements, and ensured that no further liabilities will attach to Macfarlane Group. Our existing property portfolio comprises 19 trading sites in the UK and 7 trading sites overseas. We also hold 15 non-trading sites in the UK, of which 12 are assigned or sub-let recovering all the property cost, ensuring that there is only a modest vacant property cost accruing to Macfarlane Group.

CASH FLOW AND NET DEBT

Cash inflow from operating activities was £2.0 million (2004 – £2.2 million) and the Group's financing requirements have been met by short-term borrowings. Access to adequate funds is ensured by maintaining committed levels of borrowing facilities. Bank facilities are in place to meet the Group's future anticipated financing requirements.

The Group spent £0.9 million on capital expenditure in 2005 (2004 – £3.9 million) and will continue to invest where there are needs or opportunities to meet future growth plans although the levels of investment will continue to be carefully monitored. Capital expenditure in 2006 is expected to continue to be well below the annual depreciation charge, reflecting the well-invested nature of the majority of our businesses.

The Group had net debt of £6.4 million at 31 December 2005, a decrease of £6.7 million from £13.1 million the previous year. A key feature in 2005 was that the Group was strongly cash generative from its trading operations. This will be a key focus in future years to ensure that profit generation is at the very minimum, matched by cash generation.

The Group will be prudent in its assessment of the likely returns from capital expenditure and potential acquisitions. The aim would be to seek short-term returns in excess of our weighted-average cost of capital.

FINANCIAL INSTRUMENTS

The Group's principal financial instruments comprise borrowings, cash and short-term deposits, and other items, such as trade receivables and trade payables that arise directly from its operations. The main purpose of these financial instruments is to raise finance for the Group's operations. It is, and has been throughout the period under review, the Group's policy that no trading in financial instruments shall be undertaken. The main risks arising are interest rate risk, liquidity risk and currency risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below. These policies have remained unchanged since the beginning of 2005.

Interest rate risk

The Group finances its business through a mixture of reserves and bank borrowings. The Group borrows in the desired currencies at floating rates of interest. Interest rate exposures are reviewed regularly and financial instruments considered. At present it is not deemed necessary to cover interest rate exposures by the use of financial instruments.

Liquidity risk

The Group's policy with regard to liquidity remains ensuring adequate access to funds by maintaining appropriate levels of committed short-term overdraft facilities, which are then reviewed on a regular basis. The maturity profile of debt outstanding at 31 December 2005 is set out in notes 19 and 20 to the financial statements. The Group's exposure to Credit Risk is managed by dealing only with banks and financial institutions with strong credit ratings.

Currency risk

The Group now has five overseas subsidiaries, two operating in Ireland and the others operating in US, Mexico and Sweden. Revenues and expenses are denominated exclusively in Euros, US dollars and Swedish krone respectively. As a result, movements in the Euro, US dollar and Swedish krone to sterling exchange rates, could affect the Group's sterling balance sheet. The Group's policy during 2005 has been to review the need to hedge exposures on a monthly basis and it was not deemed necessary to cover any currency exposures by the use of financial instruments. For 2006 onwards the Group's policy will continue to be to review the need to hedge exposures on a monthly basis.

IMPLEMENTATION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS

2005 has seen the adoption of International Financial Reporting Standards for the first time. The main impact of including the pension scheme deficit in the financial statements is discussed in the following section.

PENSION SCHEME DEFICIT

The Group recognised the full pension deficit at the date of transition to IFRS, namely 1 January 2004. The impact of recognising the pension deficit, net of incorporating the related deferred tax asset, was a reduction in net assets of £12.1 million at 31 December 2003 and £12.2 million at 31 December 2004. Actuarial gains and losses have been recognised in full in the consolidated statement of recognised income and expense.

Our UK defined benefits pension scheme has assets at current market value of £40.8 million (2004 – £35.1 million) and liabilities discounted using specified bond yields of £63.8 million (2004 – £52.5 million). On this valuation basis at 31 December 2005, there is a deficit of £23.0 million (2004 – £17.4 million), which is partially offset by a deferred tax asset of £6.9 million (2004 – £5.2 million) giving a net deficit of £16.1 million (2004 – £12.2 million).

MOVEMENT IN PENSION SCHEME DEFICIT

	2005 £000	2004 £000
At 1 January	(17,424)	(17,312)
Current service cost	(298)	(438)
Contributions	746	621
Other financial charges	(448)	(517)
Actual return less expected return on scheme assets	4,093	814
Experience gains & losses arising on scheme liabilities	(490)	338
Changes in assumptions underlying the present value of the scheme's liabilities	(9,156)	(930)
At 31 December	(22,977)	(17,424)

Ongoing contributions to the scheme in 2005 covered current service costs and the costs of financing the deficit, but were not at a level to cause the deficit to reduce. The pension scheme's assets saw a significant benefit of over £4.1 million from higher than expected equity returns in 2005. However this benefit was more than offset by changes to two of the major actuarial assumptions in determining the pension scheme's liabilities, firstly significant reductions in the bond yields used to value pension liabilities and secondly the move to more up-to-date mortality tables used to value liabilities. Both of these factors increased the pension scheme's liabilities by nearly £9.2 million.

Following the completion of a triennial actuarial valuation in May 2005, the Group agreed with the pension scheme trustees to make additional contributions of approximately £0.7 million to reduce the deficit over the next three years until the next triennial valuation in May 2008.

CAPITAL RESTRUCTURING

During the year, the Company applied to the Court of Session to have its Capital Redemption Reserve and Share Premium Account cancelled. Approval was given on 1 September 2005 and thereafter the Capital Redemption Reserve and Share Premium Account were effectively reclassified as distributable reserves.

SHAREHOLDERS' FUNDS

	2005 £000	2004 £000
Profit/(loss) for the year	3,385	(236)
Dividends to equity holders in the year	(844)	(844)
Exchange differences on translation of foreign operations	144	(180)
Actuarial (losses)/gains on pension schemes	(5,553)	222
Taxation on items taken direct to equity	1,666	(67)
Movements in equity in the year	(1,202)	(1,105)
Opening equity	26,641	27,746
Closing equity	25,439	26,641

Shareholders' funds have decreased from £26.6 million to £25.4 million, a reduction of £1.2 million. Profit for the year totalled £3.4 million and dividends of £0.8 million were paid during 2005. The net pension deficit increased by £3.9 million, representing an actuarial loss of £5.6 million offset by related deferred taxation of £1.7 million. Foreign exchange retranslation gains totalled £0.1 million.

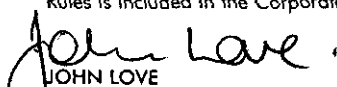
At the year-end the Company's market capitalisation was £38.2 million, compared with £34.5 million last year. The share price at 31 December 2005 was 33¼p, compared with 30p at 31 December 2004. The Group has continued to deliver positive shareholder returns in 2005.

ACCOUNTING POLICIES

The Group continues to comply with all mandatory International Financial Reporting Standards.

GOING CONCERN

The directors' statement on going concern as required by the Listing Rules is included in the Corporate Governance Report on page 20.


JOHN LOVE
Finance Director
28 March 2006

DIRECTORS AND ADVISERS

1. ARCHIE HUNTER

Chairman

Appointed as a non-executive director on 1 October 1998, becoming Chairman on 1 November 2003. Aged 62, Archie was formerly the senior partner of KPMG in Scotland and a member of KPMG's UK Governing Body from 1992 until 1999. He is a past President of The Institute of Chartered Accountants of Scotland. Archie is a non-executive director of The Royal Bank of Scotland plc, The Edinburgh US Tracker Trust PLC and The Beatson Cancer Research Institute and chairs the Court of Strathclyde University. He is Chairman of the Nominations Committee.

2. PETER ATKINSON

Chief Executive

Aged 49, Peter joined Macfarlane Group as Chief Executive on 6 October 2003. He has a strong sales and marketing background through his career at Procter & Gamble and S. C. Johnson. Peter also has significant general management experience gained during his time at GKN PLC and its joint venture partners where he worked from 1988 to 2001 in a number of senior executive roles in their business-to-business operations. He has a successful track record of both business turnarounds and business development with extensive exposure to international business, having worked in the UK, Continental Europe and the USA. From 2000 to 2003, he was responsible for the US automotive and materials handling businesses of Brambles Industries PLC. Peter was appointed a non-executive director of Speedy Hire plc during 2005.

3. GRAEME BISSETT

Non-Executive Director

Graeme Bissett joined the Board on 11 May 2004 as a non-executive director. Aged 48, Graeme has considerable financial experience, having previously been the finance director of Kwik-Fit plc. Prior to this he was a partner with Arthur Andersen. Graeme is currently Chairman or non-executive director of a number of private companies and is a member of Court and Convenor of the Finance Committee at Heriot-Watt University. Having been recruited due to his relevant financial experience, Graeme assumed the chair of the Audit Committee during 2004 and is also a member of the Nominations Committee and the Remuneration Committee.

4. GRAHAM CASEY

Executive Director

Aged 46, Graham joined Macfarlane Group's Labels business in 1976. He became Managing Director of the business in 1999 and joined the Group Board on 1 June 2001. Graham is Joint Managing Director – Sales & Marketing within Macfarlane Labels Limited and is responsible for leading the strategic development of the Labels' business.

5. JOHN LOVE

Finance Director

A member of the Institute of Chartered Accountants of Scotland, John has been with the Group for ten years and was appointed Finance Director on 12 July 1999. Aged 45, he was with Deloitte & Touche and its predecessor firms for sixteen years before joining Macfarlane Group in 1996.

6. KEVIN MELLOR

Non-Executive Director (Senior Independent Director)

Aged 59, Kevin Mellor joined the Board on 11 May 2004 as a non-executive director and is the Group's nominated Senior Independent Director. He is currently President of Bax Global for Europe, Middle East and Africa. Kevin adds significant operations experience to the Board, having previously held senior executive positions at Exxon, B.E.T. PLC, Tibbett & Britten Group plc and Transport Development Group. He chairs the Remuneration Committee and is a member of the Nominations Committee and the Audit Committee.

7. ANDREW COTTON

Company Secretary

Andrew joined Macfarlane Group in 1999 as Finance Director of the Labels' business. He then moved to Macfarlane Group's office in Glasgow in 2001 where he is now part of the Executive Team leading corporate development, acquisitions and disposals. Andrew was appointed Company Secretary on 3 August 2001.

REGISTRATION NUMBER

No. 4221 Registered in Scotland

REGISTERED OFFICE

21 Newton Place, Glasgow G3 7PY
Telephone: 0141 333 9666 Fax: 0141 333 1988

PRINCIPAL BANKERS

Bank of Scotland, Corporate Banking Scotland,
123 St. Vincent Street, Glasgow G2 5EA

SOLICITORS

Dundas & Wilson CS LLP, 191 West George Street, Glasgow G2 2LD

Wright Johnston & Mackenzie LLP, 302 St Vincent Street, Glasgow G2 5RZ

STOCKBROKERS

KBC Peel Hunt Ltd, 111 Old Broad Street, London EC2N 1PH

Speirs & Jeffrey Limited, 36 Renfield Street, Glasgow G2 1NA

INDEPENDENT AUDITORS

Deloitte & Touche LLP, Glasgow

REGISTRARS

Lloyds TSB Registrars Scotland, PO Box 28448, Finance House,
Orchard Brae, Edinburgh EH4 1WQ

REPORT OF THE DIRECTORS

The directors present their annual report and the audited financial statements of the Group for the year ended 31 December 2005.

PRINCIPAL ACTIVITIES

There were no significant changes in the activities of the Company and its subsidiaries during 2005, which continue to be the distribution of packaging and manufacturing operations comprising specialist printing, the manufacture of packaging and the provision of storage and warehousing services. Details of the principal subsidiary companies and their activities are set out on page 61.

REVIEW OF THE BUSINESS

A review of the business during and following the end of the financial year and comments on future developments in the Group are contained in the Chairman's Statement and the Operations Review and Financial Review on pages 2 to 9.

RESULTS AND DIVIDENDS

The Group's profit before tax from continuing activities was £2,890,000 after recording a profit on disposal of fixed assets of £1,048,000 and before recording a profit on discontinued operations of £656,000. (2004 – profit before tax was £1,983,000 after recording a profit on disposal of fixed assets of £3,566,000, and before recording a loss on discontinued operations of £845,000 and a loss on disposal of business of £1,400,000). This results in a profit for the year of £3,385,000 (2004 – loss for the year of £236,000).

The directors declared an interim dividend of 0.75p, which was paid on 27 September 2005. (2004 – 0.75p per share) The directors do not recommend the payment of a final dividend for the year ended 31 December 2005 (2004 – Nil).

SHARE CAPITAL AND RESERVES

At the last Annual General Meeting on 10 May 2005, the directors were given authority to allot further ordinary shares for cash beyond those committed to the share option schemes up to an aggregate amount of £1,437,738. That authority expires at the conclusion of the forthcoming Annual General Meeting. A resolution will be put to shareholders to renew for a further year the authority over the existing unissued and uncommitted ordinary share capital. This authority is limited to a maximum nominal amount of £1,437,738. As in previous years, the directors have no current intention of exercising that authority.

During the year, the Company applied to the Court of Session to have its Capital Redemption Reserve and Share Premium Account cancelled. Approval was given on 1 September 2005 and thereafter the Capital Redemption Reserve and Share Premium Account were cancelled and reclassified as distributable reserves.

An ordinary resolution will be proposed at the forthcoming Annual General Meeting to seek authority to enable the Company to purchase up to 10% of its own shares. The authority will only be exercised when it is deemed to be in the best interests of shareholders and would be expected to lead to an increase in earnings per share.

SUBSTANTIAL HOLDINGS OF SHARES IN THE COMPANY

The Company has received notification that at 28 March 2006 the following members held more than 3 per cent of the ordinary share capital of the Company.

	Holding	Percentage
Funds managed or advised by	11,158,185	9.70%
Hermes Pensions Management Limited		
Funds managed or advised by	11,131,779	9.68%
Credit Suisse Asset Management Limited		
Funds managed or advised by	7,229,292	6.29%
Deutsche Bank AG/ DWS GmbH		
Funds managed by	6,101,000	5.30%
F&C Asset Management Limited		
Funds managed or advised by	5,750,000	5.00%
Prudential/M&G Investment Management		
Lord Macfarlane of Bearsden KT and Lady Macfarlane	4,033,170	3.51%

BOARD OF DIRECTORS

The names of the directors in office at 31 December 2005, who served throughout the year together with short biographical details are set out on page 10.

In accordance with the Articles of Association, J. Love and PD. Atkinson retire by rotation at the Annual General Meeting in 2006 and in accordance with the Articles of Association offer themselves for re-election. J. Love has a service contract with the Company dated 11 October 1999 with a standard notice period of one year. PD. Atkinson has a service contract with the Company dated 6 October 2003 with a standard notice period of one year.

R.G.T. Stenhouse stepped down from the Board at the conclusion of the Annual General Meeting on 10 May 2005.

No director, either during or at the end of the financial year, had an interest in any contract relating to the business of the Company or any of its subsidiaries. The statement of directors' interests in the ordinary share capital of Macfarlane Group PLC is contained in the Board Report on Directors' Remuneration on page 14.

REPORT OF THE DIRECTORS

DIRECTORS' AND OFFICERS' LIABILITY INSURANCE

The Company has maintained directors' and officers' liability insurance cover throughout the financial year.

EMPLOYEE SHARE SCHEMES

During the year no ordinary shares were issued on the exercise of options under the Group's share option schemes. Options previously granted over 203,898 ordinary shares in the Company's share option schemes lapsed during 2005.

Details relating to options granted to parent company directors are set out in the Directors' Remuneration Report on page 15. All remaining options outstanding under the Company's share option schemes at 31 December 2005 are set out in note 32 on page 44.

Share options over 170,000 ordinary shares at a price of 35p per share were granted to both G.H. Casey and J. Love on 14 September 2005 under the Macfarlane Group PLC Executive Share Option Scheme 2000. These options are exercisable between 15 September 2008 and 14 September 2015, subject to the satisfactory completion of the scheme's conditions. The performance condition relating to these options requires total shareholder return of between 10% and 15% per annum over three years from the date of grant for vesting between 40% and 100% of the value of these options respectively. No re-testing of these options will be undertaken.

The Remuneration Committee supervises the grant of options, which are only capable of being exercised if the performance condition to which they are subject has been satisfied. The Remuneration Committee will specify the performance condition at the time of the grant of the option, having regard to the objectives of the Company and to market practice at the relevant time. The Remuneration Committee has decided to move away from purely EPS growth given the recent historic performance and felt that TSR would provide a simple and understandable basis, which clearly aligns the interest of option holders with shareholders. The Remuneration Committee proposed that performance conditions attached to grants for 2005 would be based on growth in TSR at the time the options were granted.

The Board and Remuneration Committee have completed a review of the Company's remuneration policy in light of current market practice. A resolution will be proposed at the forthcoming Annual General Meeting to seek authority for a Performance Share Plan to provide appropriate long-term incentives for the senior management. Further detail is given in the Board Report on Directors' Remuneration on page 16.

PROPERTY, PLANT AND EQUIPMENT

The movements in property, plant and equipment are set out in note 12 on page 36.

FINANCING POLICY AND FINANCIAL INSTRUMENTS

The Group's policies are set out in the Financial Review on page 8.

HEALTH, SAFETY AND THE ENVIRONMENT

In Macfarlane Group our goal is to ensure that we have a safe working environment for the benefit of our employees, customers, shareholders and the communities around us, in each country in which we operate. Good Health Safety and Environmental ("HSE") management not only protects our stakeholders and the environment, it also makes a positive contribution to our business. We are committed to continuous improvement in our HSE performance.

Site ownership of health and safety, fire safety and environmental responsibilities rests with our local teams who are encouraged to adhere to the Group's objectives for HSE. We shall support our staff by assisting them to develop their understanding of the implications of their actions and guiding them to take appropriate steps to improve matters.

It is the Group's policy to attempt to minimise the impact of our activities on the environment whilst seeking to safeguard it. The Group is a member of Valpak, a legal compliance scheme which aims to recycle packaging and develop markets for recycled products. An increasing number of the Group's manufactured products contain a high proportion of recycled material.

EMPLOYMENT OF DISABLED PERSONS

The Group policy is to encourage the employment of disabled persons where the disabilities do not hinder these persons in the performance of their duties. Where an employee becomes disabled every effort is made to ensure that their employment with the Group continues and that appropriate training is arranged. Registered disabled persons, once employed, receive equal opportunities for training, career development and promotion.

EMPLOYEE INVOLVEMENT

The Group recognises the importance of meaningful communication and consultation in maintaining good employee relations. The Group's policy of having efficient autonomous units facilitates the involvement of employees in the businesses in which they work, either through joint committees or less formal but equally effective methods of communication and consultation.

SUPPLIER PAYMENT POLICY

The Group recognises the importance of maintaining good business relationships with its suppliers. The Group's policy is to negotiate terms with suppliers and settle liabilities in accordance with these terms. All companies in the Group follow this policy and the staff who deal with payments to suppliers are made aware of it. Further details of the policy are made known to suppliers on request. At 31 December 2005 the Company had an average of 37 days purchases outstanding in trade creditors (2004 – 39 days).

POLITICAL AND CHARITABLE CONTRIBUTIONS

£5,000 was donated to the Kelvingrove Refurbishment Appeal during 2005. A contribution of £1,800 was made to BBC Children in Need as part of a sales promotion exercise in the final quarter of 2004. No political donations were made in either year.

CLOSE COMPANY STATUS

The Company is not a close company within the provisions of the Income and Corporation Taxes Act 1988.

POST BALANCE SHEET EVENT

On 11 January 2006, the Group concluded an agreement to sell its Hungarian packaging manufacture and assembly operation, Macfarlane Packaging Kft to Nefab AB, a Swedish based company, for a total cash consideration of £2.3 million after attributable expenses. The directors estimate that the disposal will produce a realised gain of £0.9 million in the year to 31 December 2006.

AUDITORS

A resolution to re-appoint Deloitte & Touche LLP as the Company's auditors will be proposed at the forthcoming Annual General Meeting.

By Order of the Board



ANDREW COTTON
Company Secretary
28 March 2006

BOARD REPORT ON DIRECTORS' REMUNERATION

INTRODUCTION

This report is prepared in accordance with the Directors' Remuneration Report Regulations 2002 and also meets the relevant requirements of the Listing Rules of the Financial Services Authority. It describes how the Board has applied the Principles of Good Governance relating to directors' remuneration. As required by the Regulations a resolution to approve this report will be proposed at the Annual General Meeting on 9 May 2006 at which the financial statements will be approved.

AUDITED INFORMATION

The emoluments of the parent company directors are shown below:

(i) Emoluments

	Fees/ salaries £000	Annual bonus £000	Benefits in kind £000	2005 £000	2004 £000
Chairman					
A.S. Hunter	58	–	–	58	55
Executive Directors					
P.D. Atkinson	275	41	16	332	286
G.H. Casey	121	–	15	136	131
J. Love	128	–	8	136	133
Non-Executive Directors					
K.D. Mellor	25	–	–	25	15
(2004 – eight months)					
G. Bissett	25	–	–	25	15
(2004 – eight months)					
R.G.T. Stenhouse	10	–	–	10	25
(2005 – five months)					
M. Clark	–	–	–	–	10
(2004 – five months)					
	642	41	39	722	670
Pension contributions				119	101
				841	771

The emoluments of executive directors and the structure of bonus schemes are determined by the Remuneration Committee. Bonuses are based on performance targets as set out on page 16 for the year to 31 December 2005. A bonus of £41,000 was payable to P.D. Atkinson for the year (2004 – £20,000).

Fees to Messrs G. Bissett and R.G.T. Stenhouse were paid to their firm and company respectively.

(ii) Directors' pension entitlements

The following executive directors are members of Macfarlane Group PLC Pension & Life Assurance Scheme (1974), a defined benefit pension scheme. Details of benefits accruing under the scheme are shown below:

	Years of service	Accrued pension 31 December 2005 £000 p.a.	Increase in accrued pension in 2005 £000 p.a.	Accrued pension 31 December 2004 £000 p.a.
G.H. Casey	30	39	2	37
J. Love	10	16	2	14

	Transfer value 31 December 2005 £000	Contributions made by the director in 2005 £000	Increase in 2005 transfer value net of contributions £000	Transfer value 31 December 2004 £000
G.H. Casey	287	8	32	247
J. Love	111	8	15	88

The Company made pension contributions for P.D. Atkinson during 2005 totalling £68,750 (2004 – £62,500).

(iii) Shareholdings

The directors at 31 December 2005 and their interests in ordinary shares of Macfarlane Group PLC were as follows:

	2005		2004	
	Beneficial	Option	Beneficial	Option
A.S. Hunter	150,500	–	150,500	–
P.D. Atkinson	251,000	1,861,538	191,000	1,861,538
G. Bissett	151,000	–	91,000	–
G.H. Casey	67,444	537,408	67,444	367,408
J. Love	406,732	566,915	322,332	396,915
K.D. Mellor	80,000	–	–	–

G.H. Casey and J. Love's beneficial holdings include 7,444 and 22,332 shares respectively held by nominees in The Macfarlane Group PLC Bonus Deferral Plan. None of the directors has any non-beneficial holdings in the Company. No changes occurred in the beneficial holdings between 1 January and 28 March 2006.

(iv) Directors' share options

	2004	Granted	2005	Exercise price	Details below	Exercise period
P.D. Atkinson	800,000	–	800,000	30p	5	26 January 2007 – 25 January 2014
	100,000	–	100,000	30p	5	26 January 2007 – 25 January 2014
	961,538	–	961,538	26p	6	29 October 2007 – 28 October 2014
	<u>1,861,538</u>		<u>1,861,538</u>			
G.H. Casey	35,000	–	35,000	220p	1	26 January 1999 – 25 January 2006
	95,339	–	95,339	59p	2	22 March 2003 – 21 March 2010
	75,274	–	75,274	68½p	3	15 March 2004 – 14 March 2011
	43,795	–	43,795	68½p	3	15 March 2004 – 14 March 2011
	118,000	–	118,000	88p	4	5 April 2005 – 4 April 2012
	–	170,000	170,000	35p	7	15 September 2008 – 14 September 2015
	<u>367,408</u>	<u>170,000</u>	<u>537,408</u>			
J. Love	144,915	–	144,915	59p	2	22 March 2003 – 21 March 2010
	96,205	–	96,205	68½p	3	15 March 2004 – 14 March 2011
	43,795	–	43,795	68½p	3	15 March 2004 – 14 March 2011
	112,000	–	112,000	88p	4	5 April 2005 – 4 April 2012
	–	170,000	170,000	35p	7	15 September 2008 – 14 September 2015
	<u>396,915</u>	<u>170,000</u>	<u>566,915</u>			

1. This option lapsed on 25 January 2006.
2. Macfarlane Group (Clonsman) PL.C. 1995 Executive Share Option Scheme. The performance condition relating to these options requires earnings per share growth of between 5% and 10% over a three-year period.
3. Macfarlane Group PLC Company Share Option Plan 2000 and The Macfarlane Group PLC Executive Share Option Scheme 2000. The performance condition relating to these options requires earnings per share growth of between 3% and 8% over a three-year period.
4. The Macfarlane Group PLC Executive Share Option Scheme 2000. The performance condition relating to these options requires earnings per share growth of 3% over a three-year period.
5. Macfarlane Group PLC Company Share Option Plan and The Macfarlane Group PLC Executive Share Option Scheme 2000. The performance condition relating to these options is that Group earnings before taxation in 2006 must exceed £7.5m. No re-testing of the option will be undertaken.
6. The Macfarlane Group PLC Executive Share Option Scheme 2000. The performance condition relating to this option requires total shareholder return of between 10% and 15% per annum over three years from the date of grant for vesting between 40% and 100% of the value of the option respectively. No re-testing of the option will be undertaken.
7. The Macfarlane Group PLC Executive Share Option Scheme 2000. The performance condition relating to these options requires total shareholder return of between 10% and 15% per annum over three years from the date of grant for vesting between 40% and 100% of the value of the option respectively. No re-testing of these options will be undertaken.

(iv) Directors' share options

No other share options were granted or exercised during the year. Messrs A.S. Hunter, G. Bissett and K.D. Mellor are non-executive directors of the Company and do not hold share options in the Company. The market value of Macfarlane Group PLC ordinary shares at 31 December 2005 was 33½p per share (2004 – 30p). The range of share prices during 2005 was 29p to 40½p for each ordinary share of 25p.

BOARD REPORT ON DIRECTORS' REMUNERATION

UNAUDITED INFORMATION

Remuneration Committee

The Company has a Remuneration Committee, constituted in accordance with the recommendations of the Combined Code. Since 10 May 2005, the Remuneration Committee has comprised two independent non-executive directors namely, Kevin Mellor (Chairman) and Graeme Bissett. Prior to 10 May 2005 the Committee comprised Kevin Mellor (Chairman), Graeme Bissett and Guy Stenhouse. None of the members of the Remuneration Committee during 2005 has any personal financial interests, other than as a shareholder, in the matters to be decided, conflicts of interests arising from cross-directorships or any day-to-day involvement in running the business.

The remuneration of executive directors is determined by the Remuneration Committee. The Chairman of the Company normally attends the meetings of the Committee, except when matters concerning his own remuneration are concerned. The Committee makes recommendations to the Board on its proposals and has access to professional advice both from inside and outside the Company. During 2005 the Committee used the services of New Bridge Street Consultants LLP to advise on certain aspects of directors' remuneration. New Bridge Street Consultants LLP do not provide any other services to the Company.

The Remuneration Committee meets routinely twice each year with other meetings convened as considered necessary. Individual attendance details can be found within the Corporate Governance Report. The Committee's terms of reference are available on the Group web site (www.macfarlanegroup.net) and its responsibilities include:

- (i) Setting, reviewing and recommending to the Board the Group's overall remuneration policy and strategy;
- (ii) Setting, reviewing and approving individual remuneration packages for the executive directors and the Chairman;
- (iii) Considering the provisions of the service agreements of the executive directors, in particular the terms of any notice periods;
- (iv) Reviewing the salary structure and terms, conditions and benefits of employment for the Chief Executive's direct reports;
- (v) Approving share options grants and the performance conditions under which the options are granted;
- (vi) Reviewing the design of all share incentive plans for approval by shareholders; and
- (vii) Ensuring that all provisions regarding disclosure of remuneration and pensions, as set out in the Directors' Remuneration Report Regulations 2002 and the Combined Code are fulfilled.

The Remuneration Committee Chairman will be available to answer questions on any aspect of remuneration policy at the Annual General Meeting.

Remuneration policy

It is a Group objective that it should attract and retain executives of high calibre and that the executives should be rewarded in a manner, which encourages value creation for shareholders. The Committee is consulted on board appointments and measures the performance of the executive directors and key members of senior management, as a basis for determining their annual remuneration packages. The non-executive directors comprising the Remuneration Committee determine executive remuneration and bonus scheme targets together with performance conditions under which executive share option schemes operate. The Board of Directors, having regard to the time commitment required and the level of fees in similar companies, determines remuneration for non-executive directors. No director plays a part in any discussion about his own remuneration.

The Company's policy is that the main elements in executive directors' remuneration packages are a basic annual salary (with benefits comprising a company car or company car allowance and private medical insurance), an annual performance related bonus and long-term incentives currently in the form of share options and pension rights. The Committee takes a balanced view of remuneration policy considering each element relative to the market. The position was established by research and analysis against a comparator group of public companies of similar size and complexity to the Company. The Board and Remuneration Committee have completed a review of the remuneration of senior management assisted by New Bridge Street Consultants LLP. The conclusion was that the current policy was appropriate with the exception that a new long-term incentive plan should be proposed for approval at the AGM.

The recommended plan is a Performance Share Plan ('PSP') based on the following principles:

- A normal maximum award of 100% of salary each year;
- A fixed 3 year performance period (with no retesting); and
- A performance condition based on total shareholder return ('TSR') and on earnings per share ('EPS').

The intention would be for the PSP to replace the Company's existing Share Option Plans. Further details will be set out in the documentation accompanying the notice of the Annual General Meeting.

Main components of Executive Directors' remuneration packages

(i) Basic salary and benefits

The intention is to ensure that the remuneration package is set at a competitive rate for comparable posts and that the achievement of clearly defined objectives will provide the opportunity to achieve attractive remuneration levels. Levels of basic salaries are reviewed annually or when an individual has a change of responsibility.

(ii) Performance related bonus

Executive directors can earn incentive payments based on Group performance targets and individual performance targets. In setting the Group performance targets, the Committee takes account of the Board's expectation for the year and how these relate to external expectations. The maximum payment achievable was 50% of basic salary for 2005 or in the case of the Chief Executive 100%, with 40% or 90% respectively based on financial objectives and 10% based on non-financial objectives. The financial objectives were not met and so this part of the bonus was not payable. A bonus of £41,000 was payable to P.D. Atkinson for the year including a discretionary bonus (2004 – £20,000) for achieving certain personal objectives.

The same scheme has been adopted for 2006 except that the potential maximum bonus for the Chief Executive has increased to 150% for one year only and is based on achieving more stretching financial targets. It also reflects the compulsory deferral of one third of any bonus award exceeding 100% of salary to be invested in shares of the Company for a three-year period under the terms of The Macfarlane Group PLC Bonus Deferral Plan.

(iii) Long-term incentives

The Remuneration Committee has responsibility for the share option schemes in force and approved the grant of options in September 2005. The Remuneration Committee proposed that the performance conditions attached to these grants would be based on TSR growth in the three years from the time the options were granted.

It is the Company's policy to phase the granting of share options rather than award them in a single large block to any individual. As detailed previously the introduction of a new long-term incentive scheme will be proposed at the AGM in 2006.

(iv) Pension rights

The Group operates four types of pension scheme, one based on final pensionable salary, two based on defined contributions and a stakeholder pension plan. The final salary scheme was closed to new entrants during 2002. New employees of the Group are eligible to join one of the defined contribution schemes after a suitable qualifying period.

G.H. Casey and J. Love are members of the final salary scheme with retirement benefits based on pensionable earnings in the years prior to retirement, which is consistent for all members of the pension scheme. Bonuses for directors do not form part of pensionable earnings. Where the Group's pension schemes are restricted in respect of any executive director by reason of the statutory capping limit of pension (the Earnings Cap), the Company may contribute to a Funded Unapproved Retirement Benefit Scheme ("FURBS") for the executive director and the Remuneration Committee keeps this under review.

During 2005 contributions to self-standing pension arrangements were provided for P.D. Atkinson in accordance with the terms of his service contract.

There have been no changes to any of the executive directors' pension entitlements during the year. There are no unfunded pension commitments or similar arrangements for current or previous executive directors.

Performance graph

The following graph shows the Company's performance, measured by Total Shareholder Return, compared with the performance of the FTSE Index for Support Services, also measured by Total Shareholder Return. The Index for Support Services has been selected for this comparison because it includes a range of companies, which the directors consider to be the best available comparison for Macfarlane Group PLC for this purpose.

Directors' service contracts

P.D. Atkinson has a service contract dated 6 October 2003 with a standard notice period of one year. A provision in this contract to extend the notice period to two years in the event of a takeover of the Company was voluntarily reduced to one year on 11 May 2004. G.H. Casey and J. Love have service contracts dated 19 April 2002 and 11 October 1999 respectively, each with a standard notice period of one year. All three service contracts terminate on the individual attaining the age of 65.

Details of the directors retiring by rotation at the forthcoming Annual General Meeting are set out in the Report of the Directors on page 11 and directors' contracts of service will be available for inspection prior to the AGM in May 2006.

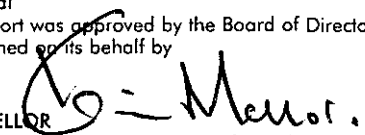
Where terms and conditions agreed by the Nominations Committee provide for an initial notice period in excess of one year, the Remuneration Committee recommends that there should be a reduction to one year as soon as practicable. The Committee considers the length of the notice periods to be in the best interests of the Company in maintaining the services of its key directors. Nevertheless the Committee also supports the principle of mitigation and phased payments relative to any compensation settlement on the departure of an executive director and is authorised to take legal advice in respect of any settlements to be proposed.

Executive directors are entitled to accept appointments outside the Company provided the Board's permission is obtained, thus ensuring that the commitment does not conflict with his duties to the Company. The Board may require the fees from such appointments to be accounted for to the Company. During 2005, P.D. Atkinson was appointed a director of Speedy Hire plc. He is allowed to retain the emoluments from this position, which is based on a time commitment of 18 days per annum.

Neither the Chairman nor the two non-executive directors have service contracts. Their appointments are for an initial period not exceeding three years, subject to review and re-election at the Annual General Meeting. Letters of appointment for Messrs A.S. Hunter, G. Bissett and K.D. Mellor are dated 13th January 2004, 11th May 2004 and 11th May 2004 respectively and they are each due to be proposed for re-election, at the Annual General Meetings in 2007, 2008 and 2008 respectively.

Approval

This report was approved by the Board of Directors on 28 March 2006 and signed on its behalf by


K.D. MELLOR
Chairman of the Remuneration Committee

CORPORATE GOVERNANCE

INTRODUCTION

The Company is committed to the principles of corporate governance contained in the Combined Code on Corporate Governance ("the Combined Code"), which is appended to the Listing Rules of the Financial Services Authority ("the Listing Rules"). The Company's compliance is set out in the narrative statement on pages 18 to 20 and for directors' remuneration in the Board Report on Directors' Remuneration on pages 14 to 17.

COMPLIANCE

Throughout the year ended 31 December 2005, the Company has been in compliance with the Code provisions set out in Section 1 of the 2003 Combined Code.

The Company's auditors, Deloitte & Touche LLP, are required to review whether the above statement reflects the Company's compliance with the nine provisions of the 2003 FRC Combined Code specified for its review by the Listing Rules and to report if it does not reflect such compliance.

THE BOARD

The Board currently comprises the Chairman, two independent non-executive directors and three executive directors. The names of the directors together with their biographical details, which illustrate their range of experience, are set out on page 10. Details of executive directors' service contracts are given in the Board Report on Directors' Remuneration and since 11 May 2004 all notice periods are for one year.

The Board structure is in compliance with the 2003 FRC Combined Code, which requires companies outside the FTSE 350 to have at least two independent non-executive directors. The Board includes sufficient independent non-executive directors who have recent and relevant experience and can bring strong, independent judgement to the Board's deliberations. Non-executive directors are given access to independent professional advice at the Group's expense, subject to certain limits and procedures, when it is deemed necessary in order for them to carry out their responsibilities. No such advice was sought during the year.

The Company has maintained directors' and officers' liability insurance cover throughout the financial year.

Details of the Chairman's other commitments are included in his biography on page 10. The Board is satisfied that these do not interfere with the performance of his duties for the Group, which is based on a commitment of approximately 50 days per annum.

The Board considers its non-executive directors to be independent both in character and judgement. No non-executive director:

- Has been an employee of the Group within the last five years;
- Has, or has had within the last three years, a material business relationship with the Group;
- Receives remuneration other than a director's fee;
- Has close family ties with any of the Group's advisers, directors or senior employees;
- Holds cross-directorships or has significant links with other directors through involvement in other companies or bodies;
- Represents a significant shareholder;
- Has served on the Board for more than nine years.

At this time the Board does not intend to appoint any further directors but the balance of the Board's skills and experience will be kept under review.

THE ROLES OF THE CHAIRMAN AND CHIEF EXECUTIVE

The division of responsibilities between the Chairman of the Board, Archie Hunter, and the Chief Executive, Peter Atkinson, is clearly defined and has been approved by the Board. The Chairman is responsible for the running of the Board, ensuring that all directors receive sufficient and relevant information on financial, business and corporate issues prior to meetings to allow all directors to bring independent judgement to bear on all issues. As Chief Executive, Peter Atkinson's responsibilities focus on managing the business and implementing strategy.

SENIOR INDEPENDENT DIRECTOR

The Board appointed Kevin Mellor as Senior Independent Director on 11 May 2004. Kevin is the director whom shareholders may contact if they feel their concerns are not being addressed and resolved through the existing mechanisms for investor communication.

RE-ELECTION OF DIRECTORS

All directors will submit themselves for re-election by shareholders at least once in every three-year period. At the 2006 Annual General Meeting, John Love and Peter Atkinson fall due to retire by rotation and being eligible offers themselves for re-election.

Subject to the Company's Articles of Association, the Companies Acts and satisfactory performance evaluation, non-executive directors are appointed for an initial period of three years. Before the third and sixth anniversary of the non-executive directors' first appointment, the Chairman will discuss with the director whether it is appropriate for a further three-year term to be served.

COMPANY SECRETARY

Andrew Cotton, the Company Secretary, is responsible for advising the Board through the Chairman on all matters relating to corporate governance. All directors have access to the advice and services of the Company Secretary. The Company's Articles of Association and the schedule of matters reserved for the Board provide that the appointment and removal of the Company Secretary is a matter for the Board as a whole.

BOARD PROCEDURES

The Group is controlled through its Board of Directors. The Board's main roles are to set the Group's strategic objectives, guide and support management in achieving these objectives, create value and safeguard the interests of shareholders within the appropriate legal and regulatory framework. The Board meets at least ten times a year and individual attendance at those and the Board Committee meetings is set out in the table on page 19. In 2005 four Board meetings were held at operational locations to allow the Board to meet management and further develop their understanding of the Group. The statement of Directors' Responsibilities is set out on page 21.

The Board has a formal schedule of matters reserved for its approval. The specific matters reserved to the Board include setting the overall Group's strategy and approving an annual budget, reviewing management performance, approving acquisitions, divestments and major capital expenditure, monitoring returns on investment, reviewing the Group's systems of financial control and risk management and consideration of significant financing matters in order to ensure that the Company's obligations to shareholders are understood and met.

The Board has delegated to the Executive responsibility for the development and recommendation of strategic plans for consideration by the Board, the implementation of the strategies and policies of the Group as determined by the Board, the delivery of the operating and financial plan, the approval of capital expenditure below Board authorities and the development and implementation of risk management systems.

Regular reports and papers are circulated to the directors in a timely manner in preparation for Board and Committee meetings. These papers are supplemented by information specifically requested by the directors from time to time.

All directors receive monthly management accounts and a monthly report from the Chief Executive, which together with other papers enables them to scrutinise the Group's and management's performance against agreed objectives. At each meeting, the Board considers reports from the Chief Executive, Peter Atkinson, and the Finance Director, John Love.

BOARD AND COMMITTEE MEETINGS

The number of regular Board meetings and Committee meetings attended by each director during 2005 was as follows:

	Board	Audit Committee	Remuneration Committee	Nominations Committee
Archie Hunter (Chairman)	11 (11)	2 (2)*	3 (3)*	1 (1)
Peter Atkinson (Chief Executive)	9 (11)	n/a	n/a	1 (1)*
Graeme Bissett (Non-Executive Director)	8 (11)	4 (4)	5 (5)	1 (1)
Graham Casey (Executive Director)	10 (11)	n/a	n/a	n/a
John Love (Finance Director)	11 (11)	n/a	n/a	n/a
Kevin Mellor (Senior Independent Director)	11 (11)	4 (4)	5 (5)	1 (1)
Guy Stenhouse (Non-Executive Director)	4 (4)	2 (2)	2 (2)	0 (1)

Figures in brackets indicate the maximum number of meetings in the period in which the individual was a Board or Committee member.

* indicates that a director is attending but is not a member of the relevant Committee.

Where a director cannot attend a Board or Committee meeting, his comments on the papers to be considered at that meeting are relayed in advance to the relevant Chairman.

PROFESSIONAL DEVELOPMENT

On appointment, directors complete an induction programme designed to give them a thorough understanding of the Group and its activities. They receive information about the Group, the matters reserved for the Board, the terms of reference and membership of the Board committees, and the latest financial information. This is supplemented with visits to key locations and meetings with and presentations from senior management.

BOARD PERFORMANCE EVALUATION

The Board has established a formal process, led by the Chairman, for the annual performance evaluation of the Board, its Committees and individual directors. All directors are made aware on appointment that their performance will be subject to regular evaluation.

The Board has completed a self-assessment questionnaire based on the Higgs guidance contained within the Combined Code. This includes specific reference to the objectives and performance of the Board and the performance and processes for all Board Committees. The results have been collated by the Company Secretary and reviewed by the Board to identify any areas for improvement and to confirm objectives for the year ahead. The Chairman has held individual meetings with directors to review performance and set individual objectives.

The Chairman meets periodically with the non-executive directors without the executive directors present. Led by the Senior Independent Director, the non-executive directors meet annually without the presence of the Chairman to conduct a performance evaluation of the Chairman.

RELATIONS WITH SHAREHOLDERS

The Group maintains a corporate website (www.macfarlanegroup.net) containing a wide range of information of interest to institutional and private investors. Detailed reviews of the performance and financial position are included in the Operations Review and Financial Review on pages 4 to 9 of this report. The Board uses this together with the Chairman's Statement on pages 2 and 3 and the Directors' Report on pages 11 to 13 to present its assessment of the Company's position and prospects.

The Chairman maintains a regular dialogue with shareholders and gives feedback to the Board on issues raised. The Group has frequent discussions with institutional shareholders including meetings following the preliminary announcement in March and the announcement of interim results in August. In addition the Group responds to individual requests for discussions from shareholders.

The Board receives feedback on meetings with shareholders including broker feedback on meetings scheduled at the time of the preliminary announcement and the interim results. The Senior Independent Director is available to meet with shareholders if they have concerns with contact through the normal channels of Chairman, Chief Executive or Finance Director.

The Annual General Meeting is attended by all directors and shareholders are invited to ask questions during the meeting and to meet directors after the formal proceedings have ended. All shareholders have an opportunity to put questions to members of the Board on matters relating to the Group's operations and performance at the meeting. Details of the resolutions to be proposed at the Annual General Meeting can be found in the proxy card accompanying the Annual Report and Accounts. In line with the requirements of the Combined Code, the results of proxy votes are disclosed at the Annual General Meeting and made available on the Group website and the Notice of Meeting is sent out more than 20 days in advance of the Meeting.

NOMINATIONS COMMITTEE

The Nominations Committee currently comprises Archie Hunter (Chairman), Kevin Mellor, and Graeme Bissett. The Chief Executive, Peter Atkinson, attends meetings by invitation. The Nominations Committee's terms of reference can be found on the Group website.

The Committee's responsibilities include reviewing the structure, size and composition of the Board and giving full consideration to succession planning for directors and other senior executives. The Nominations Committee will continue to consider the mix of skills and experience that the Board requires and seek the appointment of directors to meet its assessment of what is required to ensure that the Board is effective in discharging its responsibilities.

The Committee met once during 2005 to consider proposing Graham Casey for re-election at the 2005 Annual General Meeting. Graham was recommended for re-election and this was approved at the AGM. The Nominations Committee has considered and recommended the re-election of John Love and Peter Atkinson as directors of the Company at the Annual General Meeting on 9 May 2006.

REMUNERATION COMMITTEE

The Remuneration Committee currently comprises Kevin Mellor (Chairman) and Graeme Bissett, both independent non-executive directors. The Company Chairman attends meetings by invitation and the Remuneration Committee met 5 times during the year. The Remuneration Committee's terms of reference are available on the Group website. The Board Report on Directors' Remuneration is set out on pages 14 to 17.

CORPORATE GOVERNANCE

AUDIT COMMITTEE

The Audit Committee comprises Graeme Bissett (Chairman) and Kevin Mellor, both of whom are independent non-executive directors. The Audit Committee Chairman, Graeme Bissett, has recent and relevant financial experience being a chartered accountant, with substantial experience in the accountancy profession and senior financial roles in industry. Kevin Mellor has a wide range of commercial experience, as evidenced in the biographical details on page 10. The Company Chairman is not a member of the Committee but is regularly asked by the Committee Chairman to join meetings to give the Committee the benefit of his relevant experience. The Audit Committee met 4 times during 2005 and its agenda is linked to events in the Group's financial calendar.

The Committee meets privately with the external and internal auditors and executive directors are invited to attend meetings as required. The Committee's terms of reference are displayed on the Group website and its principal oversight responsibilities cover:

- Internal control and risk management;
- Internal audit;
- External audit (including auditor independence); and
- Financial reporting.

Under its terms of reference, the Audit Committee monitors the integrity of the Group's financial statements and any formal announcements relating to the Group's performance. The Committee is responsible for monitoring the effectiveness of the external audit process and making recommendations to the Board in relation to the appointment, re-appointment and remuneration of the external auditors. It is responsible for ensuring that an appropriate relationship between the Group and the external auditors is maintained, including reviewing non-audit services and fees.

The Committee reviews annually the Group's system of internal control and processes for evaluating and monitoring the risks facing the Group. The Committee reviews the effectiveness of the internal audit function and its terms of reference on an annual basis and recommends to the Board any changes required as a result of the review.

In 2005 the Audit Committee discharged its responsibilities by:

- Reviewing the Group's draft financial statements and interim results statement prior to Board approval and reviewing the external auditors' reports thereon;
- Reviewing the impact of International Financial Reporting Standards;
- Reviewing the external auditors' plan for the audit of the Group accounts which included confirmations of auditor independence and approval of the engagement letter;
- Reviewing and approving the audit fee and keeping non-audit fees paid to the Group's auditors under review;
- Recommending the re-appointment of the external auditors; and
- Reviewing an annual report on the Group's systems of internal control and its effectiveness, reporting to the Board on the results of the review and receiving regular updates from the internal auditors.

The Audit Committee also monitors the Group's arrangements by which staff may in confidence raise concerns about possible improprieties in matters of financial reporting and other areas. These arrangements, commonly referred to as "whistleblowing" procedures, incorporate telephone helpline numbers for independent advice and were reconfirmed with all staff during 2005. Brief details are included on the Group website. All concerns will continue to be investigated at the earliest opportunity and the employee's anonymity is preserved.

The Audit Committee monitors regularly the non-audit services provided to the Group by its external auditors. It decided not to implement a formal policy but keeps all services provided by the external auditors under review so as to ensure the independence and objectivity of the external auditors, taking account of relevant professional and regulatory requirements. Details of the amounts paid to the external auditors during the year for audit and other services are set out in note 3 to the financial statements on page 33.

The Audit Committee Chairman will be available to answer questions on any aspect of the work of the Committee at the Annual General Meeting.

RISK MANAGEMENT AND INTERNAL CONTROL

The Board is responsible for the Group's system of internal control and for reviewing its effectiveness. It is the role of management to implement the Board's policies on risk and control through the design and operation of appropriate internal control systems. Such systems are designed to manage rather than eliminate the risk of failure to achieve business objectives and by its nature can only provide reasonable and not absolute assurance against material misstatement or loss.

The Board confirms that an ongoing process for identifying, evaluating and managing the significant risks faced by the Group was in place in compliance with the guidance of the Turnbull Committee. The process has been in place throughout the year under review and has continued up to the date of approval of the annual report and financial statements. This includes a regular programme of risk assessment within each business unit and at Board level to ensure that the Board and senior management review the overall risk profile and identify controls to manage these risks and through regular review meetings with each business unit these risk profiles are updated.

The directors have continued to review the effectiveness of the Group's system of financial and non-financial controls including: reviews of the internal financial controls by the internal auditors; structured meetings between each business unit and executive directors; management assurance of the maintenance of controls and reports from the external auditors on matters identified in the course of its statutory audit work. A key part of the process is a six monthly assurance process by which responsible financial managers confirm the adequacy of financial controls within their business, their compliance with approved levels of authority and report any control weaknesses, which are identified, together with appropriate corrective action.

GOING CONCERN

After making enquiries, the directors have formed a judgement at the time of approving the financial statements that there is a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the financial statements.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Annual Report and the financial statements. The directors have chosen to prepare accounts for the Group in accordance with International Financial Reporting Standards (IFRSs) and for the Company in accordance with United Kingdom Generally Accepted Accounting Practice (UK GAAP).

In the case of UK GAAP accounts, the directors are required to prepare financial statements for each financial year, which give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the directors are required to:

- (a) select suitable accounting policies and then apply them consistently;
- (b) make judgements and estimates that are reasonable and prudent;
- (c) state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- (d) prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

In the case of the Group's IFRS accounts, IAS1 requires that financial statements present fairly for each financial year the Company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the preparation and Presentation of Financial Statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable IFRSs. Directors are also required to:

- (a) properly select and apply accounting policies;
- (b) present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- (c) provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- (d) prepare the accounts on a going concern basis unless, having assessed the ability of the Company to continue as a going concern, management either intends to liquidate the entity or to cease trading, or have no realistic alternative but to do so.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company, for the system of internal control, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a Directors' Report and Directors' Remuneration Report which comply with the requirements of the Companies Act 1985. The directors are responsible for the maintenance and integrity of the Company website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements differs from legislation in other jurisdictions.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF MACFARLANE GROUP PLC

We have audited the group and individual company financial statements (the "financial statements") of Macfarlane Group PLC for the year ended 31 December 2005 which comprise the consolidated income statement, the consolidated and individual company balance sheets, the consolidated cash flow statement, the consolidated statement of recognised income and expense, the statement of accounting policies and the related notes 1 to 52 together with the consolidated reconciliation of movements in shareholders' equity. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the directors' remuneration report that is described as having been audited.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted for use in the European Union and for preparing the individual company financial statements and the directors' remuneration report in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements and the part of the directors' remuneration report described as having been audited in accordance with relevant United Kingdom legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view in accordance with the relevant financial reporting framework and whether the financial statements and the part of the directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985 and whether, in addition, the group financial statements have been properly prepared in accordance with Article 4 of the IAS Regulation. We report to you if, in our opinion, the directors' report is not consistent with the financial statements. We also report to you if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We also report to you if, in our opinion, the company has not complied with any of the four directors' remuneration disclosure requirements specified for our review by the Listing Rules of the Financial Services Authority. These comprise the amount of each element in the remuneration package and information on share options, details of long term incentive schemes, and money purchase and defined benefit schemes. We give a statement, to the extent possible, of details of any non-compliance.

We review whether the corporate governance statement reflects the company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the group's corporate governance procedures or its risk and control procedures.

We read the directors' report and the other information contained in the annual report including the unaudited part of the directors' remuneration report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

BASIS OF AUDIT OPINION

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the directors' remuneration report described as having been audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the directors' remuneration report described as having been audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the directors' remuneration report described as having been audited.

OPINION

In our opinion:

- the group financial statements give a true and fair view, in accordance with IFRSs as adopted for use in the European Union, of the state of the group's affairs as at 31 December 2005 and of its profit for the year then ended;
- the group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation;
- the individual company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the individual company's affairs as at 31 December 2005; and
- the individual company financial statements and the part of the directors' remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985.



DELOITTE & TOUCHE LLP
Chartered Accountants and Registered Auditors

Glasgow
United Kingdom
28 March 2006

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2005

	Note	2005 £000	2004 £000
Continuing operations			
Revenue	1	127,247	122,705
Cost of sales		(85,122)	(82,200)
Gross profit		42,125	40,505
Distribution costs		(6,521)	(6,829)
Administrative expenses		(32,676)	(33,581)
Operating profit before property transactions		2,928	95
Gain on disposal of properties	2	1,048	3,566
Operating profit	3	3,976	3,661
Investment income		103	94
Finance costs	5	(1,189)	(1,772)
Profit before tax		2,890	1,983
Tax	6	(161)	26
Profit for the year from continuing operations		2,729	2,009
Discontinued operations			
Profit/(loss) for the year from discontinued operations after tax	7	656	(845)
Loss on disposal of discontinued operations		-	(1,400)
Total profit/(loss) for the year from discontinued operations after tax		656	(2,245)
Profit/(loss) for the year		3,385	(236)
Earnings/(loss) per share	10		
From continuing operations			
Basic		2.43p	1.79p
Diluted		2.41p	1.78p
From continuing and discontinued operations			
Basic		3.01p	(0.21p)
Diluted		2.99p	(0.21p)

CONSOLIDATED STATEMENT OF RECOGNISED INCOME AND EXPENSE

For the year ended 31 December 2005

	Note	2005 £000	2004 £000
Exchange difference on translation of foreign operations	27	144	(180)
Actuarial (losses)/gains on defined benefit pension schemes	34	(5,553)	222
Tax on items taken directly to equity		1,666	(67)
Net expense recognised directly in equity		(3,743)	(25)
Profit/(loss) for the year		3,385	(236)
Total recognised income and expense for the year		(358)	(261)

CONSOLIDATED RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' EQUITY

For the year ended 31 December 2005

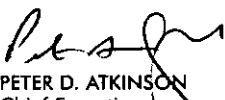
	Note	2005 £000	2004 £000
Profit/(loss) for the year		3,385	(236)
Dividends to equity holders in the year	9	(844)	(844)
Net expense recognised directly in equity		(3,743)	(25)
Movements in equity in the year		(1,202)	(1,105)
Opening equity		26,641	27,746
Closing equity		25,439	26,641

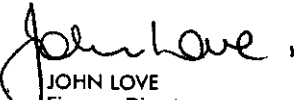
CONSOLIDATED BALANCE SHEET

At 31 December 2005

	Note	2005 £000	2004 £000
Non-current assets			
Goodwill	11	17,182	17,054
Property, plant and equipment	12	14,608	17,601
Investment property	13	1,701	1,701
Other receivables	16	863	2,242
Deferred tax asset	21	6,651	5,013
Total non-current assets		41,005	43,611
Current assets			
Inventories	15	8,803	8,689
Trade and other receivables	16	29,639	28,611
Cash and cash equivalents	20	1,203	2,018
Total current assets		39,645	39,318
Non-current assets classified as held for sale	17	1,925	3,580
		41,570	42,898
Total assets		82,575	86,509
Current liabilities			
Trade and other payables	18	24,681	26,777
Current tax liabilities		796	595
Obligations under finance leases	19	272	479
Bank overdrafts and loans	20	7,830	14,226
Liabilities directly associated with assets classified as held for sale	17	485	-
Total current liabilities		34,064	42,077
Net current assets/(liabilities)		5,581	(2,759)
Non-current liabilities			
Retirement benefit obligations	34	22,977	17,424
Obligations under finance leases	19	95	367
Total non-current liabilities		23,072	17,791
Total liabilities		57,136	59,868
Net assets		25,439	26,641
Equity			
Share capital	22	28,755	28,755
Capital redemption reserve	23	-	2,952
Share premium account	24	-	7,547
Revaluation reserves	25	167	274
Own shares	26	(1,406)	(1,406)
Translation reserves	27	(36)	(180)
Retained earnings	28	(2,041)	(11,301)
Total equity		25,439	26,641

These financial statements were approved by the Board of Directors on 28 March 2006 and signed on its behalf by


PETER D. ATKINSON
 Chief Executive


JOHN LOVE
 Finance Director

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2005

	Note	2005 £000	2004 £000
Net cash from operating activities	30	1,990	2,170
Investing activities			
Interest received		119	93
Proceeds on disposal of property, plant and equipment		6,255	6,563
Purchases of property, plant and equipment		(869)	(3,925)
Net cash from investing activities		5,505	2,731
Financing activities			
Dividends paid		(844)	(844)
Repayments of obligations under finance leases	30	(479)	(469)
Decrease in bank overdrafts	30	(6,396)	(3,596)
Net cash used in financing activities		(7,719)	(4,909)
Net decrease in cash and cash equivalents	30	(224)	(8)
Cash and cash equivalents at beginning of year		2,018	2,026
Cash and cash equivalents at end of year	20	1,794	2,018

ACCOUNTING POLICIES

For the year ended 31 December 2005

SUMMARY OF ACCOUNTING POLICIES

The following accounting policies have been applied consistently for items which are considered to be material in relation to the financial statements.

(a) Basis of accounting

The financial statements for the year ended 31 December 2005 have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union for the first time. The disclosures required by IFRS1, "First-time Adoption of IFRS" concerning the transition from UK GAAP to IFRSs are given in note 37 to the financial statements.

The financial statements have been prepared on the historical cost basis as modified by the revaluation of certain group properties. The principal accounting policies adopted are set out below.

(b) Basis of consolidation

The consolidated income statement and the consolidated balance sheet include the financial statements of the parent company and all its subsidiaries (all of which are wholly owned) made up to the end of the financial year. Transactions between group companies are eliminated on consolidation.

On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the fair values of the identifiable net assets is recognised as goodwill.

The results of subsidiaries acquired or disposed of during the period are included in the consolidated income statement from the effective date of acquisition or disposal, as appropriate.

The consolidated profit or loss on disposal of a subsidiary is the difference between the net proceeds of sale and the Group's share of the subsidiary's net assets together with the carrying value of any goodwill at the date of disposal.

(c) Non-current assets held for sale

Non-current assets classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell.

Non-current assets and disposal groups are classified as held for sale if their carrying value will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset or disposal group is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

(d) Goodwill

Goodwill arising on consolidation, represents the excess of the cost of acquisition over the net fair values of the identifiable assets and liabilities of the acquired subsidiary at the date of acquisition.

Goodwill is allocated to cash generating units for the purpose of impairment testing. The carrying value of goodwill is considered annually and also reviewed where management have reason to believe that a change in circumstances may have given rise to an impairment.

On disposal of a subsidiary, the attributable amount of goodwill is included in the determination of the gain or loss on disposal. Goodwill written off to reserves in respect of acquisitions up to 31 December 1997 has not been reinstated and therefore will not be included in determining any subsequent gain or loss on disposal. From 1 January 1998, goodwill is initially recognised as a non-current asset at amortised carrying value under UK GAAP at the transition date.

(e) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided to third parties in the normal course of business, net of discounts, VAT and other sales related taxes. Sales of goods are recognised when goods are delivered and title has passed.

(f) Leasing

Leases are classed as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are recognised as tangible assets of the Group at their fair value as determined at the inception of the lease. Depreciation is provided in accordance with the Group's accounting policy for the class of tangible asset concerned or over the term of the lease if shorter. Interest costs are charged over the lease term and future obligations included in the balance sheet as finance lease obligations. Rentals payable under operating leases are charged to the income statement on a straight-line basis over the term of the relevant lease.

(g) Foreign currencies

The financial statements of each subsidiary are presented in the currency of the primary economic environment in which the business operates (its functional currency). For the purpose of the Group financial statements, the results and the financial position of each business are expressed in sterling, being the Group's functional and presentation currency. Exchange differences arising on the settlement and retranslation of monetary items on an ongoing basis are included in the profit or loss for the period.

For the purposes of preparing the Group's financial statements, the assets and liabilities denominated in foreign currencies and financial statements of foreign subsidiaries are translated into sterling at the rates of exchange prevailing on the balance sheet date. Exchange differences arising in the consolidated accounts on the retranslation at closing rates of the Group's net investments in foreign subsidiary companies and on foreign currency borrowings to the extent that they hedge the Group's investment in such operations are recorded as movements on the Group's translation reserve and reported in the statement of recognised income and expense. Such translation differences are recognised in the profit or loss in the period in which the foreign business is disposed of.

(h) Retirement benefit costs

For defined benefit retirement benefit schemes, the cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out triennially and updated at each balance sheet date. Actuarial gains and losses are recognised in full in the period in which they occur in the statement of recognised income and expense.

Past service cost is recognised immediately to the extent that benefits are already vested and otherwise is amortised on a straight-line basis over the average period until the benefits become vested.

The retirement benefit obligation recognised in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognised past service cost, and as reduced by the fair value of the scheme assets. The obligations are measured on an actuarial basis and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term to the scheme's liabilities.

Payments made to defined contribution retirement benefit schemes are charged as an expense as they fall due.

(i) Taxation

The tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on the taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

The carrying value of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity. Deferred tax assets and liabilities are not discounted.

(j) Property, plant and equipment

Property, plant and equipment are stated at cost to the Group except in the case of certain properties, where previous revaluations in 1987 or the fair value of the property on acquisition by the Group have been treated as the deemed cost on transition to IFRS. On transition to IFRS, the Group elected to retain the existing base cost of its other properties, plant and equipment as its deemed cost and not to revalue to fair value.

No depreciation is provided on land. Depreciation is charged so as to write off the cost or valuation of the assets, less estimated residual values, by equal annual instalments over their estimated useful lives. The rates of depreciation vary between 2% – 5% per annum on buildings and 7% – 33% per annum on plant, vehicles and fittings.

(k) Investment properties

Investment properties, which are properties held to earn rentals and/or capital appreciation, are stated at cost at the balance sheet date. Gains or losses arising from changes in the fair value of investment properties are included in the income statement for the period to which they relate.

(l) Inventories

Inventories are consistently valued at the lower of cost and net realisable value. Such cost is determined by average cost and is stated less any provisions required for obsolescence. In the case of work in progress and finished goods, cost comprises direct materials, direct labour costs and attributable overheads. Net realisable value is based on estimated selling price, less further costs expected to be incurred to completion and disposal.

(m) Financial instruments

(i) Trade receivables do not carry interest and are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts.

(ii) Interest-bearing bank overdrafts are recorded at the proceeds received, net of direct issue costs.

(iii) Trade payables are not interest bearing and are stated at their nominal value.

(n) Share-based payments

The Group has applied the requirements of IFRS2 "Share-Based Payments" and in accordance with the transitional provisions IFRS2 has been applied to all grants of equity instruments after 7 November 2002 that were unvested as of 1 January 2005.

The Group issues equity-settled share-based payments to certain employees. Equity settled share based payments are measured at fair value at the date of the grant. The fair value determined at the grant date of the equity-settled share based payments is expensed as an employee benefits expense on a straight-line basis over the vesting period, based on the Group's estimate of shares that will eventually vest.

The fair value is determined by the use of a binomial model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferrability, exercise restrictions and behavioural considerations.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

1. BUSINESS AND GEOGRAPHICAL SEGMENTS

	Continuing £000	Discontinued £000	2005 £000	Continuing £000	Discontinued £000	2004 £000
Turnover	127,247	3,618	130,865	122,705	4,634	127,339
Cost of sales	(85,122)	(2,082)	(87,204)	(82,200)	(2,540)	(84,740)
Gross profit	42,125	1,536	43,661	40,505	2,094	42,599
Distribution costs	(6,521)	(104)	(6,625)	(6,829)	(427)	(7,256)
Administration costs	(32,676)	(682)	(33,358)	(33,581)	(2,512)	(36,093)
Profit/(loss) before property transactions	2,928	750	3,678	95	(845)	(750)
Gain on property disposals	1,048	–	1,048	3,566	–	3,566
Operating profit/(loss)	3,976	750	4,726	3,661	(845)	2,816
Investment income	103	32	135	94	–	94
Finance costs	(1,189)	–	(1,189)	(1,772)	–	(1,772)
Profit/(loss) before tax	2,890	782	3,672	1,983	(845)	1,138
Tax	(161)	(126)	(287)	26	–	26
Loss on disposal of business	–	–	–	–	(1,400)	(1,400)
Profit/(loss) after tax	2,729	656	3,385	2,009	(2,245)	(236)

Business Segments

The Group's activities are centred around two principal activities, with those manufacturing operations discontinued in the current and prior years disclosed separately.

(i) Packaging Distribution

The Distribution of packaging materials and supply of storage and warehousing services in the UK.

(ii) Manufacturing Operations

The manufacture and supply of self-adhesive and resealable labels and plastic-injection moulded products to a variety of FMCG customers in the UK and Europe and the manufacture, assembly and supply of timber, corrugated and foam based packaging materials in the UK and US/Mexico.

(iii) Discontinued Operations

The operations in Hungary were sold at the start of 2006 and are classified as discontinued in the above table. The 2004 figures include the results of Tom Brands Electrical Services Limited.

2005

Group Segment	External Sales £000	Inter-segment Sales £000	Total Revenue £000	Segment Result £000
Packaging Distribution	73,915	–	73,915	661
Manufacturing Operations	53,332	2,776	56,108	2,267
Continuing activities	127,247	2,776	130,023	2,928
Discontinued Operations	3,618	–	3,618	750
	130,865	2,776	133,641	3,678
Profit from discontinued operations				(750)
Profit before property transactions				2,928
Gain on disposal of properties				1,048
Operating profit				3,976
Investment income				103
Finance costs				(1,189)
Profit before tax				2,890
Tax				(161)
Profit from discontinued operations after tax				656
Profit after tax and discontinued operations				3,385

1. BUSINESS AND GEOGRAPHICAL SEGMENTS (continued)

2005

Group Segment	Capital Additions £000	Depreciation & Amortisation £000	Segment Assets £000	Segment Liabilities £000	Net Assets £000
Packaging Distribution	241	1,252	47,301	37,465	9,836
Manufacturing Operations	664	2,029	33,349	19,186	14,163
Continuing activities	905	3,281	80,650	56,651	23,999
Discontinued operations	25	68	1,925	485	1,440
	930	3,349	82,575	57,136	25,439

2004

Group Segment	External Sales £000	Inter-segment Sales £000	Total Revenue £000	Segment Result £000
Packaging Distribution	74,095	—	74,095	(769)
Manufacturing Operations	48,610	2,615	51,225	864
Continuing activities	122,705	2,615	125,320	95
Discontinued operations	4,634	30	4,664	(845)
	127,339	2,645	129,984	(750)
Loss from discontinued operations				845
Profit before property transactions				95
Gain on disposal of properties				3,566
Operating profit				3,661
Investment income				94
Finance costs				(1,772)
Profit before tax				1,983
Tax				26
Profit from discontinued operations				(845)
Loss on disposal of discontinued operations				(1,400)
Loss after tax and discontinued operations				(236)

2004

Group Segment	Capital Additions £000	Depreciation & Amortisation £000	Segment Assets £000	Segment Liabilities £000	Net Assets £000
Packaging Distribution	816	1,313	45,138	39,315	5,823
Manufacturing Operations	2,690	2,094	41,371	20,553	20,818
Continuing activities	3,506	3,407	86,509	59,868	26,641
Discontinued operations	—	—	—	—	—
	3,506	3,407	86,509	59,868	26,641

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

1. BUSINESS AND GEOGRAPHICAL SEGMENTS (continued)

Geographical Segments

The Group's operations are primarily located in the UK, Europe and US/Mexico. Packaging Distribution's activities are solely in the UK. Within the Manufacturing operations, the Labels & Plastics Division operates in the UK and Europe and the Packaging Manufacturing Division operates in the UK and US/Mexico.

The discontinued activities were based in Europe in 2005 and in the UK and Europe in 2004.

	UK £000	Europe £000	US/Mexico £000	Discontinued Activities £000	2005 £000
2005					
Revenue					
Total revenue	95,819	11,124	20,304	3,618	130,865
Result					
Segment result	1,798	528	602	750	3,678
Carrying value of assets	13,583	6,312	4,104	1,440	25,439
Capital additions in year	506	34	365	25	930
	UK £000	Europe £000	US/Mexico £000	Discontinued Activities £000	2004 £000
2004					
Revenue					
Total revenue	98,229	9,409	15,067	4,634	127,339
Result					
Segment result	259	(93)	(71)	(845)	(750)
Carrying value of assets	14,932	9,028	2,681	–	26,641
Capital additions in year	2,694	366	446	–	3,506

2. GAIN ON DISPOSAL OF PROPERTIES

Three properties were sold during 2005 for a combined consideration of £4,880,000. On 4 February 2005, the Group sold its vacant premises at Govan near Glasgow for a consideration after attributable expenses of £2,715,000. The disposal gave rise to a gain of £1,300,000 in the financial statements for 2005. On 4 February 2005 the Group also announced the disposal of a six-bay distribution site in Grantham, with the Company, as part of the disposal, taking a lease at market rent for the two bays from which its Grantham Packaging Distribution business operates. Sale proceeds from the Grantham site of £1,935,000 after expenses equated to book value. In April 2005 the Group sold its vacant site at Glenrothes for a consideration of £230,000 after expenses, which also equated to book value.

In 2004, the Group sold its premises at Braehead near Glasgow for a consideration of £8,625,000. The disposal gave rise to a gain of £3,845,000 in the financial statements for 2004.

The costs to operate vacant properties in the year amounted to £252,000 (2004 – £279,000) and were offset against the gains arising on disposal.

3. OPERATING PROFIT

	2005 £000	2004 £000
Operating profit has been arrived at after charging/(crediting):		
Depreciation of property, plant and equipment	3,349	3,407
Gain on disposal of property, plant and equipment	(27)	(66)
Auditors' remuneration Audit services	159	166
Non-audit services	84	56
Staff costs (see note 4)	24,919	26,014
Cost of inventories recognised as an expense	80,021	77,186
Write-down of inventories recognised as an expense	201	619

Auditors' remuneration

A more detailed analysis of auditors' remuneration on a worldwide basis is provided below:

Audit services	Statutory audit	159	166
Further assurance services		42	—
Tax services	Compliance services	36	23
	Advisory services	6	—
Other services	Internal audit	—	33
		243	222

Fees for further assurance services principally comprise reviews of group information following the transition to International Financial Reporting Standards in 2005. In addition to the amounts shown above, the auditors received fees of £6,000 (2004 – £6,000) for the audit of the Group's pension schemes.

4. STAFF COSTS

	2005 No.	2004 No.
The average monthly number of employees was:		
Production	473	542
Sales and distribution	377	390
Administration	224	214
	1,074	1,146

	2005 £000	2004 £000
The costs incurred in respect of these employees were:		
Wages and salaries	22,634	23,370
Social security costs	1,571	1,760
Other pension costs	714	884
	24,919	26,014

5. FINANCE COSTS

	2005 £000	2004 £000
Interest on bank loans and overdrafts	(698)	(1,183)
Interest on obligations under finance leases	(43)	(72)
Interest cost of pension scheme liabilities	(2,728)	(2,734)
Total interest expense	(3,469)	(3,989)
Expected return on pension scheme assets	2,280	2,217
Total finance costs	(1,189)	(1,772)

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

6. TAX

	2005 £000	2004 £000
Current tax		
United Kingdom corporation tax at 30% (2004: 30%)	(40)	–
Foreign tax	(121)	(99)
Prior year adjustment	–	24
Current tax charge	(161)	(75)
Deferred taxation	–	101
Total	(161)	26

The standard rate of current tax for the year, based on the UK rate of corporation tax is 30% (2004 – 30%). Taxation for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions.

The actual tax charge for current and previous year is less than 30% of the results as set out in the income statement for the reasons set out in the following reconciliation:

	2005 £000	2004 £000
Profit before taxation	2,890	1,893
Tax on profit at 30%	(867)	(568)
Factors affecting tax credit for the year:		
Depreciation in excess of capital allowances	107	1,300
Non taxable gain	390	1,153
Other differences	(1,000)	(573)
Tax losses utilised/(unutilised)	1,281	(1,471)
Difference on overseas tax rates	(72)	60
Prior year adjustment	–	24
Current tax charge for the year	(161)	(75)

7. DISCONTINUED ACTIVITIES

	Total 2005 £000	Total 2004 £000	Hungary 2004 £000	Brands 2004 £000
Revenue	3,618	4,634	3,370	1,264
Cost of sales	(2,082)	(2,540)	(2,037)	(503)
Gross profit	1,536	2,094	1,333	761
Net overheads	(786)	(2,939)	(923)	(2,016)
Operating profit/(loss)	750	(845)	410	(1,255)
Investment income	32	–	–	–
Profit/(loss) before tax	782	(845)	410	(1,255)
Tax	(126)	–	–	–
Loss on disposal of discontinued operations	–	(1,400)	–	(1,400)
Profit/(loss) after tax from discontinued operations	656	(2,245)	410	(2,655)
Basic and diluted earnings/(loss) per share	0.58p	(2.00p)		

In January 2006, the Company's Hungarian subsidiary was sold. As the decision to sell the business was taken before 31 December 2005, the results for 2005 and 2004 are classified as discontinued operations. The assets and liabilities sold in January 2006 are classified as non-current assets and current liabilities held for sale at 31 December 2005 in note 17. The results from the former subsidiary Tom Brands Electrical Services Limited are also classified as discontinued operations in 2004.

8. PROFIT/(LOSS) FOR THE YEAR

	2005 £000	2004 £000
Loss of parent company	(1,402)	(1,336)
Profit of subsidiary companies	4,787	1,100
	3,385	(236)

The Company has taken advantage of Section 230 of the Companies Act 1985 and consequently a separate profit and loss account for the parent company is not presented as part of these financial statements.

9. DIVIDENDS

	2005 £000	2004 £000
Amounts recognised as distributions to equity holders in the year:		
Special interim dividend for the year ended 31 December 2005 of 0.75p per share (2004 – Special interim dividend of 0.75p per share)	844	844

Dividends are not payable on own shares held in the employee share trust.

10. EARNINGS/(LOSS) PER SHARE

From continuing and discontinued operations

The calculation of the basic and diluted earnings/(loss) per share is based on the following data:

	2005 £000	2004 £000
Earnings/(loss) from continuing and discontinued operations for the purposes of earnings per share being net profit attributable to equity holders of the parent	3,385	(236)
Adjustments to exclude (profit)/loss for the year from discontinued operations		
(Profit)/loss for the year from discontinued operations	(656)	845
Loss on disposal of discontinued operations	-	1,400
Earnings from continuing operations for the purposes of earnings per share being net profit attributable to equity holders of the parent	2,729	2,009

Number of shares in issue for the purposes of calculating basic and diluted earnings/(loss) per share

	2005 Number of shares '000	2004 Number of shares '000
Weighted average number of ordinary shares in issue	115,019	115,019
Own shares in Employee Share Ownership Trusts	(2,491)	(2,491)
Weighted average number of shares in issue for the purposes of basic earnings/(loss) per share	112,528	112,528
Effect of dilutive potential ordinary shares due to share options	602	69
Weighted average number of shares in issue for the purposes of diluted earnings/(loss) per share	113,130	112,597

As the diluted loss per share reduces the loss per share in 2004, the basic loss per share has been reflected as the diluted figure in the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

11. GOODWILL

	Packaging Distribution £000	Manufacturing Operations £000	2005 £000
Cost			
At 1 January 2005	15,533	1,521	17,054
Exchange movements	–	128	128
At 31 December 2005	15,533	1,649	17,182
Carrying amount			
At 31 December 2005	15,533	1,649	17,182
At 31 December 2004	15,533	1,521	17,054

The Group tests goodwill annually for impairment, or more frequently if there are indications that goodwill might be impaired. Packaging Distribution is treated as one cash generating unit ("CGU") for the purposes of impairment testing. There are three separate CGUs within Manufacturing Operations. The recoverable amount of each CGU is determined using value in use calculations with key assumptions relating to discount rates, growth rates and expected changes to selling prices and costs during the period. Discount rates are used which reflect current market assessments of the time value of money and the risks specific to the businesses in question. Growth rates and changes in selling prices and costs are based on our expectations of future performance in the markets in which we operate.

12. PROPERTY, PLANT & EQUIPMENT

	Land & buildings £000	Plant, vehicles & fittings £000	2005 Total £000
Cost			
At 1 January 2005	6,553	43,860	50,413
Additions	176	754	930
Assets of businesses classified as held for sale	–	(455)	(455)
Disposals	–	(6,894)	(6,894)
At 31 December 2005	6,729	37,265	43,994
Accumulated depreciation and impairment			
At 1 January 2005	1,847	30,965	32,812
Charge for year	25	3,324	3,349
Assets of businesses classified as held for sale	–	(288)	(288)
Disposals	–	(6,487)	(6,487)
At 31 December 2005	1,872	27,514	29,386
Carrying amount			
At 31 December 2005	4,857	9,751	14,608
At 31 December 2004	4,706	12,895	17,601

The carrying amount of tangible fixed assets of £14,608,000 (2004 – £17,601,000) includes an amount of £762,000 (2004 – £1,130,000) in respect of assets held under finance leases. The depreciation charge in respect of these assets is £368,000 (2004 – £385,000).

Contractual commitments for capital expenditure for which no provision has been made in the accounts amounted to £196,000 (2004 – £120,000).

Land & buildings at net book value comprise:

	2005 £000	2004 £000
Freeholds	1,969	1,844
Long leaseholds	2,788	2,756
Short leaseholds	100	106
	4,857	4,706

13. INVESTMENT PROPERTY

	2005 £000	2004 £000
Cost		
At 1 January and 31 December	1,701	1,701

The investment property has been stated at depreciated original cost. The property rental income earned by the Group from its investment property, all of which is received under an operating lease is £180,000 (2004 – £180,000). This lease expires in December 2007.

14. SUBSIDIARY COMPANIES

Details of the principal operating subsidiaries, including the names and countries of incorporation are set out on page 61.

15. INVENTORIES

	2005 £000	2004 £000
Raw materials and consumables	2,009	1,697
Work in progress	138	215
Finished goods and goods for resale	6,656	6,777
	8,803	8,689

Allowances are made for obsolescence estimated by the Group's management based on prior experience and their assessment of the current economic environment.

16. TRADE AND OTHER RECEIVABLES

	2005 £000	2004 £000
Due within one year		
Trade receivables	23,315	22,916
Other receivables	3,145	4,020
Prepayments and accrued income	3,179	1,675
	29,639	28,611
Due after more than one year		
Other receivables	–	1,375
Prepayments and accrued income	863	867
	863	2,242

The Group's credit risk is primarily attributable to its trade receivables. The amounts presented in the balance sheet are net of allowances for doubtful receivables of £395,000 (2004 – £458,000), estimated by the Group's management based on prior experience and their assessment of the current economic environment.

Included in other receivables is a loan made to one executive under the group house purchase scheme. The total balance outstanding at 31 December 2005 amounted to £3,000 (2004 – £4,000). The amount outstanding at 1 January 2005 represented the maximum balance during the year.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

17. NON-CURRENT ASSETS AND CURRENT LIABILITIES CLASSIFIED AS HELD FOR SALE

2005

In January 2006, the Group's Hungarian subsidiary was sold. As the decision to sell the business was taken before 31 December 2005, consequently the results of the subsidiary for 2005 and 2004 are classified as discontinued operations in the consolidated income statement. The component parts of the balance sheet sold in January 2006 are classified as non-current assets and current liabilities held for sale at 31 December 2005 as shown below:

	2005 £000
Property, plant and equipment	167
Inventories	265
Trade and other receivables	902
Cash and cash equivalents	591
Non-current assets held for sale	1,925
Trade and other payables	484
Tax liabilities	1
Total liabilities associated with assets classified as held for sale	485
Net Assets of Disposal Group	1,440

2004

As set out in note 2, the Group disposed of certain property assets during 2005 for a combined consideration of £4,880,000, realising gains of £1,300,000. These assets had previously been classified as held for resale at the end of 2004 at a carrying value of £3,580,000.

18. TRADE AND OTHER PAYABLES

	2005 £000	2004 £000
Due within one year		
Trade creditors	19,365	19,129
Other taxation and social security	748	1,129
Other creditors	947	2,196
Accruals and deferred income	3,621	4,323
	24,681	26,777

Trade and other payables principally comprise amounts outstanding for trade purchases and ongoing costs.

19. OBLIGATIONS UNDER FINANCE LEASES

	2005 £000	2004 £000
Amounts payable under finance leases		
Due within one year	272	479
Due between one and two years	95	272
Due between two and five years	—	95
	367	846
Due for settlement within 12 months (shown under current liabilities)	(272)	(479)
Obligations under finance leases	95	367

All lease obligations are denominated in sterling. The finance leases are secured over the assets to which the leases relate.

20. CASH AND CASH EQUIVALENTS AND BANK OVERDRAFTS

A summary of the Group's policies for financial instruments is included in the Financial Review on page 8. The numerical disclosures in this note deal with financial assets and financial liabilities.

	2005 £000	2004 £000
Cash and cash equivalents		
Currency		
Sterling	89	120
Euros	691	1,353
Swedish krone	81	2
Hungarian forints	591	52
US Dollars	342	491
	1,794	2,018
Less: Amounts in non-current assets classified as held for sale		
Hungarian forints	(591)	–
Cash and cash equivalents	1,203	2,018
Bank overdrafts		
Currency		
Sterling	7,830	14,197
US Dollars	–	29
Bank overdrafts and loans	7,830	14,226

Cash and cash equivalents as set out above comprise cash at bank and other short-term highly liquid investments with a maturity of three months or less.

All bank overdrafts shown above are repayable on demand. The Group had no bank loans in either 2005 or 2004.

The Company and certain UK subsidiaries have given inter-company guarantees to secure their respective overdrafts. The overall credit lines for these borrowing facilities total £13,750,000 (2004 – £17,500,000).

Interest rates

All Group deposits and borrowings are held at floating rates of interest. The average effective interest rate on bank overdrafts approximates to 6.50 per cent (2004 – 6.35 per cent) per annum.

Currency analysis of monetary assets and liabilities

At 31 December 2005 the Group had no significant currency exposure generating gains or losses within the consolidated income statement. All monetary assets and liabilities are denominated in the functional currency of the Group business to which they belong.

Fair value of financial instruments

Current assets and liabilities are all held at floating rates. The fair values of cash and cash equivalents and bank overdrafts at December 2005 all materially equate to book values.

Borrowing facilities

The Group has various committed undrawn overdraft facilities. The facilities available at 31 December 2005 in respect of which all conditions precedent had been met were as follows:

	Expiring within one year 2005 £000	Expiring within one year 2004 £000
Drawn down	7,830	14,226
Undrawn	5,920	3,274
	13,750	17,500

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

21. DEFERRED TAX ASSET

	Accelerated tax depreciation £000	Retirement benefit obligations £000	Total £000
At 1 January 2004	(180)	5,193	5,013
Credited in income statement	–	101	101
Charge to equity – deferred tax on actuarial gain	–	(67)	(67)
Exchange differences	(34)	–	(34)
At 1 January 2005	(214)	5,227	5,013
Charge to equity – deferred tax on actuarial loss	–	1,666	1,666
Exchange differences	(28)	–	(28)
At 31 December 2005	(242)	6,893	6,651

Deferred taxation has not been provided in respect of gains realised that have been rolled over into the acquisition cost of replacement assets. This tax will become payable if the replacement assets are sold and further rollover relief is not obtained. The estimated amount of tax that would become payable in these circumstances is £1.3m (2004 – £1.8m).

Deferred taxation has not been provided on revaluations of fixed assets. This tax will only become payable if the assets are sold and rollover relief not obtained. The estimated amount of tax that would become payable in these circumstances is £52,000 (2004 – £84,000).

Deferred taxation has not been provided in respect of earnings, which are retained overseas as there is no intention to repatriate these profits in the foreseeable future. The estimated amount of tax that would become payable in these circumstances is £760,000 (2004 – £1,457,000).

The balance of UK tax losses totalling approximately £10.0m have been carried forward and are available for offset against future trading profits. As in previous years, Macfarlane Group will derive benefit from these losses against future trading profits and accordingly, no deferred tax has been recognised in respect of these losses.

22. SHARE CAPITAL

	Number of shares	2005 £000	2004 £000
Ordinary shares of 25p each			
Authorised	200,000,000	50,000	50,000
Allotted, issued and fully paid:			
At 1 January and 31 December	115,019,000	28,755	28,755

There have been no movements in share capital during the year.

23. CAPITAL REDEMPTION RESERVE

	2005 £000	2004 £000
At 1 January	2,952	2,952
Cancellation of reserve (see note 28)	(2,952)	–
At 31 December	–	2,952

Following shareholder approval at the Annual General Meeting on 10 May 2005, the Company petitioned the Court to have its Capital Redemption Reserve and Share Premium Account cancelled. The petition was approved on 1 September 2005 and the reserves were cancelled and reinstated as distributable reserves.

24. SHARE PREMIUM ACCOUNT

	2005 £000	2004 £000
At 1 January	7,547	7,547
Cancellation of reserve (see note 28)	(7,547)	–
At 31 December	–	7,547

Following shareholder approval at the Annual General Meeting on 10 May 2005, the Company petitioned the Court to have its Capital Redemption Reserve and Share Premium Account cancelled. The petition was approved on 1 September 2005 and the reserves were cancelled and reinstated as distributable reserves.

25. REVALUATION RESERVES

	2005 £000	2004 £000
At 1 January	274	279
Released to retained earnings on disposal of properties (see note 28)	(107)	(5)
At 31 December	167	274

The movements relate to the disposal of the Govan site in 2005 and the disposal of Braehead site in 2004.

26. OWN SHARES

	2005 £000	2004 £000
At 1 January and 31 December	(1,406)	(1,406)

At 31 December 2005, the Company's Employee Share Ownership Trust ("ESOT") held 2,491,325 (2004 – 2,491,325) ordinary shares in Macfarlane Group PLC with a market value of £828,000 (2004 – £747,000) against the future exercise of share options. The ESOT has waived its right to receive dividends on these shares.

27. TRANSLATION RESERVES

	2005 £000	2004 £000
At 1 January	(180)	–
Exchange differences on translation of overseas operations at year end	144	(180)
At 31 December	(36)	(180)

Exchange differences arising in the consolidated accounts on the retranslation at closing rates of the Group's net investments in foreign subsidiary companies are recorded as movements on the Group's translation reserve above. Such translation differences are recognised in the consolidated income statement when any foreign business is disposed of.

28. RETAINED EARNINGS

	2005 £000	2004 £000
At 1 January	(11,301)	(10,381)
Net profit/(loss) for the year	3,385	(236)
Dividends paid	(844)	(844)
Released from revaluation reserve on disposal of properties	107	5
Post-tax actuarial (loss)/gain in pension scheme taken direct to equity	(3,887)	155
Cancellation of capital redemption reserve	2,952	–
Cancellation of share premium account	7,547	–
At 31 December	(2,041)	(11,301)

29. DISPOSAL OF SUBSIDIARY UNDERTAKINGS

	2004 £000
Net assets disposed:	
Property, plant and equipment	551
Inventories	25
Trade receivables	1,149
Trade payables	(325)
Net assets disposed of	1,400
Loss on disposal	(1,400)
Consideration (net of attributable expenses)	–

The directors of the Company's subsidiary, Tom Brands Electrical Services Limited petitioned for the appointment of a provisional liquidator on 26 October 2004 to realise the assets of the business. An exceptional cost of £1.4 million was incurred in the second half of 2004 as a result of this exit. The trading activities of the Brands business have been disclosed as discontinued activities in 2004 comparative figures.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

30. NOTES TO THE CASH FLOW STATEMENT

		2005 £000	2004 £000
Operating profit	Continuing operations	3,976	3,661
	Discontinued operations	750	(845)
Operating profit		4,726	2,816
Adjustments for:			
Depreciation of property, plant and equipment		3,349	3,407
Gain on disposal of property, plant and equipment		(1,075)	(3,911)
Operating cash flows before movements in working capital		7,000	2,312
(Increase)/decrease in inventories		(379)	1,205
(Increase) in receivables		(1,981)	(437)
(Decrease)/increase in payables		(1,233)	36
Cash generated by operations		3,407	3,116
Income taxes (paid)/received		(212)	744
Interest paid		(1,205)	(1,690)
Net cash from operating activities		1,990	2,170

Cash inflows in respect of the discontinued operations for operating activities amounted to £531,000 for 2005, (2004 Outflow of £370,000) cash inflows in respect of investing activities totalled £32,000 (2004 – £7,000) and cash outflows from financing activities amounted to £268,000 (2004 – £1,003,000).

	2005 £000	2004 £000
Decrease in cash and cash equivalents in the year	(224)	(8)
Decrease in bank overdrafts	6,396	3,596
Cash flows from debt and lease financing	479	469
Loan notes issued in the year	–	(200)
Movement in net debt in the year	6,651	3,857
Opening net debt	(13,054)	(16,911)
Closing net debt	(6,403)	(13,054)
Net debt comprises:		
Cash and cash equivalents	1,203	2,018
Cash and cash equivalents in business held for resale	591	–
Bank overdrafts and loans	(7,830)	(14,226)
Obligations under finance leases	(367)	(846)
Closing net debt	(6,403)	(13,054)

Cash and cash equivalents, which are presented as a single class of assets on the face of the balance sheet, comprise cash at bank and other short-term highly liquid investments with a maturity of three months or less.

31. FINANCIAL COMMITMENTS

During the year the Group made minimum lease payments under non-cancellable operating leases as follows:

	Land & buildings 2005 £000	Other 2005 £000	Land & buildings 2004 £000	Other 2004 £000
Charge for the year	4,798	2,092	4,769	2,101

At the balance sheet date the Group had total commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	Land & buildings 2005 £000	Other 2005 £000	Land & buildings 2004 £000	Other 2004 £000
Leases which expire				
Within one year	147	779	47	690
Within two to five years	4,607	2,749	3,195	4,613
After five years	50,200	–	52,252	–
	54,954	3,528	55,494	5,303

The majority of the 31 leases of land and buildings summarised above are subject to rent reviews. 12 of these leases are subject to sub-let arrangements or assignments with third parties to reduce the property cost to the Group.

32. SHARE-BASED PAYMENTS

Equity-settled share option plans

The Group share option plans provide for a grant price, which approximates to the average quoted market price of the Group shares on the date of grant. The vesting period is generally three years. If the options remain unexercised after a period of ten years from the date of grant, the options expire. Furthermore options are forfeited if the employee leaves the Group before the options vest. The Group recognised an expense of £75,000 (2004 – £32,000) relating to equity-settled share-based payment transactions.

	Number of shares 2005	Number of shares 2004
A summary of the movements on share options during the year is as follows:		
Outstanding at 1 January	5,383,757	4,433,481
Granted during the year	1,355,000	1,861,538
Forfeited during the year	(203,898)	(911,262)
Outstanding at 31 December	6,534,859	5,383,757
Exercisable at 31 December	Nil	Nil

The inputs to the binomial model for these options giving rise to a charge are as follows:

	2005	2004
Weighted average share price	43p	43p
Weighted average exercise price	43p	43p
Expected volatility	41%	41%
Expected life	6.5 years	6.5 years
Risk free rate	4.5%	4.5%
Expected annual dividend yield	0.0%	0.0%

The options in existence have an average exercise price of 30p (2004 – 28p)

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

32. SHARE-BASED PAYMENTS (continued)

The share options granted to employees, including executive directors, and outstanding at 31 December under existing share option schemes together with exercise prices and dates of exercise are set out below:

	Exercise price per share	Exercise date	Number of shares 2005	Number of shares 2004
The Macfarlane Group (Clansman) PLC. 1995 Executive Share Option Scheme	220p	January 2004	140,000	185,000
		– January 2006		
The Macfarlane Group (Clansman) PLC. 1995 Executive Share Option Scheme	59p	March 2004	532,498	591,396
		– March 2010		
The Macfarlane Group Company Share Option Plan 2000	68½p	March 2005	315,644	315,644
		– March 2011		
The Macfarlane Group PLC Executive Share Option Scheme 2000	68½p	March 2005	211,679	211,679
		– March 2011		
The Macfarlane Group Company Share Option Plan 2000	78½p	September 2005	143,932	143,932
		– September 2011		
The Macfarlane Group PLC Executive Share Option Scheme 2000	78½p	September 2005	13,568	13,568
		– September 2011		
The Macfarlane Group Company Share Option Plan 2000	88p	April 2005	92,783	92,783
		– April 2012		
The Macfarlane Group PLC Executive Share Option Scheme 2000	88p	April 2005	518,217	518,217
		– April 2012		
The Macfarlane Group Company Share Option Plan 2000	28½p	April 2006	636,779	661,779
		– April 2013		
The Macfarlane Group PLC Executive Share Option Scheme 2000	28½p	April 2006	713,221	788,221
		– April 2013		
The Macfarlane Group Company Share Option Plan 2000	30p	January 2007	100,000	100,000
		– January 2014		
The Macfarlane Group PLC Executive Share Option Scheme 2000	30p	January 2007	800,000	800,000
		– January 2014		
The Macfarlane Group PLC Executive Share Option Scheme 2000	26p	October 2007	961,538	961,538
		– October 2014		
The Macfarlane Group Company Share Option Plan 2000	35p	September 2008	478,134	–
		– September 2015		
The Macfarlane Group PLC Executive Share Option Scheme 2000	35p	September 2008	876,866	–
		– September 2015		
Total share options outstanding 31 December			6,534,859	5,383,757

33. MACFARLANE GROUP ALL EMPLOYEE SHARE OWNERSHIP PLAN

No monies were paid in 2004 or 2005 to the Trustees of the Macfarlane Group All Employee Share Ownership Plan, which was established in 2002. The shares held by the trustees of the All Employee Share Ownership Plan vest unconditionally in the employees on normal maturity date and the dividends on the shares are paid to the employees. At 31 December 2005 the Scheme held 380,923 ordinary shares of 25p each, which had a market value of £127,000 on behalf of the employees. Transfers of ordinary shares to eligible employees out of the Plan take place each year on request following the completion of the five-year tax efficient period.

34. PENSIONS

The Group operates a pension scheme based on final pensionable salary for its UK operations. The assets of the scheme are held separately from those of the Group in managed funds under the overall supervision of the scheme trustees.

The contributions are determined by the scheme's qualified actuary on the basis of triennial valuations using the projected unit method. The most recent triennial valuation was as at 1 May 2005. The principal assumptions adopted were that investment returns would average 7.75% per annum and that salary increases would average 3.5% per annum. The valuation showed that the market value of the relevant assets of the scheme was £35,259,000 and the actuarial value of these assets represented 76% of the value of benefits that had accrued to members.

The final salary scheme was closed to new entrants during 2002 and the rate of contributions from both employees and the employer was increased. The employer contribution rate increased from 13.5% to 15.5% of pensionable salary, and the employee contribution rate increased from 5% to 7% of pensionable salary from 1 July 2002 following actuarial advice.

Following the actuarial valuation, the Board has agreed to make additional payments to the scheme of £0.7 million per annum for three years commencing 2006 to reduce the net pension deficit. These additional payments will increase the pension scheme assets; they are not a charge against profits.

Balance sheet disclosures

The figures below have been based on the actuarial valuation as at 1 May 2005, updated to the current year-end. The assets in the scheme, the net liability position for the scheme at 31 December 2005 and the expected rates of return were:

Asset class	Fair value 2005 £000	Long-term expected rate of return	Fair value 2004 £000	Long-term expected rate of return	Fair value 2003 £000	Long-term expected rate of return
Equities	24,077	7.50%	19,911	7.75%	18,500	8.25%
Bonds	16,678	4.50%	15,173	5.00%	14,300	5.00%
Other (cash)	21	4.50%	37	5.00%	100	4.50%
Fair value of assets	40,776	6.27%	35,121	6.56%	32,900	6.82%
Present value of scheme liabilities	(63,753)		(52,545)		(50,212)	
Deficit in the scheme	(22,977)		(17,424)		(17,312)	
Related deferred tax asset (see note 21)	6,893		5,227		5,193	
Net pension liability	(16,084)		(12,197)		(12,119)	

The long-term expected rate of return is based on equity returns, bond yields and cash balance returns at each balance sheet date. The overall expected rate of return on the scheme assets is a blended rate of the individual investment categories.

The scheme's liabilities at 31 December 2005 were calculated on the following bases as required under IAS 19:

Assumptions	2005	2004	2003
Discount rate	4.75%	5.25%	5.50%
Rate of increase in salaries	2.75%	2.75%	4.00%
Rate of increase in pensions in payment	3% or 5% for fixed increases or 2.75% for LPI	3% or 5% for fixed increases or 2.75% for LPI	3% or 5% for fixed increases or 2.75% for LPI
Inflation assumption	2.50% post 5 April 2005 2.75%	2.75%	2.75%

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

34. PENSIONS (continued)

	2005 £000	2004 £000
Movement in the present value of defined benefit obligations		
At 1 January	52,545	50,212
Service costs	298	438
Interest costs	2,728	2,734
Contribution from scheme members	231	263
Changes in assumptions underlying the defined benefit obligations	9,646	592
Benefits paid	(1,695)	(1,694)
At 31 December	63,753	52,545
Movement in the fair value of scheme assets		
At 1 January	35,121	32,900
Expected return on scheme assets	2,280	2,217
Actual return less expected return on scheme assets	4,093	814
Contributions from sponsoring companies	746	621
Contribution from scheme members	231	263
Benefits paid	(1,695)	(1,694)
At 31 December	40,776	35,121
Analysis of amounts charged to operating profit		
Current service costs	(298)	(438)
Expected return on pension scheme assets	2,280	2,217
Interest cost of pension scheme liabilities	(2,728)	(2,734)
Amounts charged to operating profit	(746)	(955)
Analysis of the actuarial (loss)/gain as included in the statement of recognised income and expense		
Actual return less expected return on scheme assets	4,093	814
Experience gains & losses arising on scheme liabilities	(490)	338
Changes in assumptions underlying the present value of the scheme's liabilities	(9,156)	(930)
Actuarial (loss)/gain	(5,553)	222
Movement in scheme deficit in the year		
At 1 January	(17,424)	(17,312)
Current service cost	(298)	(438)
Contributions	746	621
Other financial charges	(448)	(517)
Actuarial (loss)/gain in the year	(5,553)	222
At 31 December	(22,977)	(17,424)

The history of experience adjustments is as follows:

	2005 £000	2004 £000	2003 £000	2002 £000
Present value of defined benefit obligations	(63,753)	(52,545)	(50,212)	(46,100)
Fair value of scheme assets	40,776	35,121	32,900	29,500
Deficit in the scheme	(22,977)	(17,424)	(17,312)	(16,600)
Experience adjustment on scheme liabilities				
Amount	(9,646)	592	167	(4,565)
Percentage of scheme liabilities	(15.1%)	1.1%	0.3%	(9.90%)
Experience adjustment on scheme assets				
Amount	4,093	814	1,761	5,786
Percentage of scheme liabilities	10.0%	2.3%	5.4%	19.6%

Defined contribution schemes

The Group also operates a number of defined contribution pension schemes. The assets of these schemes are held separately from those of the Group in independently administered funds. The pension cost charge represents contributions paid by the Group to the funds and amounted to £416,000 (2004 – £446,000). During 2002 Macfarlane Group also introduced a stakeholder pension arrangement for those employees not eligible for membership of any of the Group's contributory pension schemes.

35. RELATED PARTY TRANSACTIONS

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed.

During the year the Group incurred fees for corporate advice amounting to £20,000 (2004 – £5,000) to Noble Grossart Limited, of which R.G.T. Stenhouse, a non-executive director of the Company until 10 May 2005, is a director. The directors have considered the implications of IAS 24 "Related Party Disclosures" and are satisfied that there are no other related party transactions occurring during the year, which require disclosure.

36. POST BALANCE SHEET EVENT

On 12 January 2006, the Group announced the disposal of its Hungarian packaging manufacture and assembly operation, Macfarlane Packaging Kft to Nefab AB, a Swedish based company, for a total cash consideration of £2.3 million after attributable expenses. £2.1 million of the consideration was paid immediately, with the retained consideration becoming payable in March 2008.

The gross assets disposed of were £1.9 million at 31 December 2005 and the net assets being sold totalled £1.4 million at the same date. The business made an operating profit of £0.7 million on turnover of £3.6 million in the year to 31 December 2005. The directors estimate that the disposal will produce a realised gain of £0.9 million in the financial year to 31 December 2006.

37. EXPLANATION OF TRANSITION TO IFRSs

This is the first year that the Group has presented its financial statements under IFRS. The following disclosures are required in the year of transition. The last financial statements under UK GAAP were for the year ended 31 December 2004 and the date of transition to IFRSs was therefore 1 January 2004. The major policy choices with an impact on results are noted below.

Goodwill

Under UK GAAP, goodwill was amortised over its useful economic life. Under IFRS3 "Business Combinations" goodwill is no longer amortised but held at carrying value with impairment reviews being undertaken annually or when there is an indication that the carrying value has been reduced. Under IFRS1 the Group has applied the change from the date of transition as opposed to full application to all business combinations prior to that date. As a result, goodwill arising from previous acquisitions was recorded initially in the opening balance sheet at the amortised carrying value under UK GAAP on that date. The goodwill on the balance sheet at the date of transition was £17.1 million.

The impact on the 31 December 2004 income statement was a reversal of the amortisation previously charged under UK GAAP of £890,000. Goodwill was tested for impairment at 1 January 2004 and 31 December 2004 in accordance with IFRS and no adjustment deemed necessary.

Employee Benefits

Under UK GAAP, the transitional provisions of FRS17 "Retirement Benefits" required the pension deficit to be shown as a memorandum disclosure in the notes to the accounts for periods up to 31 December 2004 rather than accounted for on the balance sheet. IAS19 "Employee Benefits" requires the operating and financing costs of the defined benefit pension schemes to be shown separately in the consolidated income statement and that the pension deficit to be shown on the face of the balance sheet. IAS19 also allows a number of options for the recognition of actuarial gains and losses.

The Group has adopted the approach of recognising the full pension deficit at the date of transition. The overall impact of recognising the pension deficit, net of incorporating the related deferred tax asset, was a reduction in net assets of £12.1 million at 31 December 2003, and £12.2 million at 31 December 2004. Actuarial gains and losses have been recognised in full in the consolidated statement of recognised income and expense on the assumption that the EU will endorse the revised version of IAS19.

IAS 19 requires the recording of a holiday pay accrual. The holiday year of the Group is the calendar year and no holidays can be carried forward. Consequently no accrual was required at 31 December 2003 or 31 December 2004.

Share-based Payments

Under UK GAAP, no charge was made to the profit and loss account for the value of options granted to employees as options were granted at their intrinsic value. Under IFRS2 "Share-Based Payments" a charge is made reflecting the fair value of options granted since 7 November 2002, adjusted to reflect the actual and expected levels of vesting, which is applying the exemption permitted under IFRS1. The impact was a charge of £32,000 in the year to 31 December 2004 and accumulated accruals of £5,000 and £37,000 at 31 December 2003 and 31 December 2004 respectively.

Foreign Exchange

Under IFRS, translation differences arising from the date of transition to IFRS, permitted to be taken to reserves must be tracked in a separate foreign exchange translation reserve. The Group has elected to take the exemption, permitted under the transitional rules of not applying IAS 21 "The Effect of Changes in Foreign Exchange Rates" retrospectively; this has permitted the Group to absorb its foreign exchange gains and losses for the period to 31 December 2003 in retained earnings. The translation losses incurred during 2004 and accumulated in the translation reserve at 31 December 2004 amounted to £180,000.

Non-current Assets Held for Sale

Under IFRS5 "Non-current Assets Held for Sale and Discontinued Operations" the Group reclassified the values of surplus properties from "Property, plant and equipment" to "Non-current assets classified as held for sale" on the balance sheet. The reclassifications totalled £5,985,000 at 31 December 2003 and £3,580,000 at 31 December 2004. These related to Group's properties at Braehead, Govan, Grantham and Glenrothes, which were sold in March 2004, February 2005, February 2005 and April 2005 respectively.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

37. EXPLANATION OF TRANSITION TO IFRSs (continued)

(i) Reconciliation of equity at 1 January 2004 (date of transition to IFRSs)

	UK GAAP £000	IAS 19 Employee benefits £000	IFRS 2 Share based payments £000	Reclassify £000	IFRSs £000
Non-current assets					
Goodwill	17,054				17,054
Property, plant and equipment	28,613			(7,686)	20,927
Investment property	0			1,701	1,701
Other receivables	0			838	838
Deferred tax asset	0	5,013			5,013
Total non-current assets	45,667	5,013	0	(5,147)	45,533
Current assets					
Inventories	9,919				9,919
Trade and other receivables	28,901			(838)	28,063
Cash and cash equivalents	2,026				2,026
Total current assets	40,846			(838)	40,008
Non-current assets held for sale	0			5,985	5,985
	40,846	0	0	5,147	45,993
Total assets	86,513	5,013	0	0	91,526
Current liabilities					
Trade and other payables	27,526		(5)		27,531
Current tax liabilities	0				0
Obligations under finance leases	432				432
Bank overdrafts and loans	17,822				17,822
Total current liabilities	45,780	0	(5)	0	45,785
Non current liabilities					
Retirement benefit obligations	0	(17,312)			17,312
Deferred tax liabilities	180	180			0
Obligations under finance leases	683				683
Total non-current liabilities	863	(17,132)	0	0	17,995
Total liabilities	46,643	(17,132)	(5)		63,780
Net assets	39,870	(12,119)	(5)	0	27,746
Equity					
Share capital	28,755				28,755
Capital redemption reserve	2,952				2,952
Share premium account	7,547				7,547
Revaluation reserve	279				279
Own shares	(1,406)				(1,406)
Retained earnings	1,743	(12,119)	(5)		(10,381)
Total equity	39,870	(12,119)	(5)	0	27,746

37. EXPLANATION OF TRANSITION TO IFRSs (continued)

(ii) Reconciliation of income statement reconciliation for the year to 31 December 2004

	UK GAAP £000	IAS 19 Employee benefits £000	IFRS 2 Share based payments £000	IFRS 3 Business combination £000	IFRSs £000
Continuing operations					
Revenue	122,705				122,705
Cost of sales	(82,200)				(82,200)
Gross profit	40,505				40,505
Distribution expenses	(6,829)				(6,829)
Administrative expenses	(34,622)	183	(32)	890	(33,581)
Profit/(loss) before property transactions	(946)	183	(32)	890	95
Gain on disposal of properties	3,566				3,566
Profit from operations	2,620	183	(32)	890	3,661
Investment income	94				94
Finance costs	(1,255)	(517)			(1,772)
Profit before tax	1,459	(334)	(32)	890	1,983
Tax	(75)	101			26
Profit for the year from continuing operations	1,384	(233)	(32)	890	2,009
Discontinued operations					
Loss for the year from discontinued operations	(845)				(845)
Loss on disposal of discontinued operations	(1,400)				(1,400)
Loss for the year	(861)	(233)	(32)	890	(236)

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2005

37. EXPLANATION OF TRANSITION TO IFRSs (continued)

(iii) Reconciliation of equity at 31 December 2004

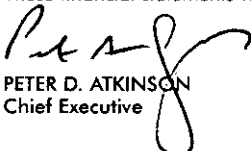
	UK GAAP £000	IAS 19 Employee benefits £000	IFRS 2 Share based payments £000	IFRS 3 Business combination £000	Reclassify £000	IFRS £000
Non-current assets						
Goodwill	15,994			1,060		17,054
Property, plant and equipment	22,882				(5,281)	17,601
Investment property	0				1,701	1,701
Other receivables	0				2,242	2,242
Deferred tax assets	0	5,013				5,013
Total non-current assets	38,876	5,013	0	1,060	(1,338)	43,611
Current assets						
Inventories	8,689					8,689
Trade and other receivables	30,853				(2,242)	28,611
Cash and cash equivalents	2,018					2,018
Total current assets	41,560				(2,242)	39,318
Non-current assets held for sale	0				3,580	3,580
	41,560	0	0	0	1,338	42,898
Total assets	80,436	5,013	0	1,060	0	86,509
Current liabilities						
Trade and other payables	26,570		(37)	(170)		26,777
Current tax liabilities	595					595
Obligations under finance leases	479					479
Bank overdrafts and loans	14,226					14,226
Total current liabilities	41,870	0	(37)	(170)	0	42,077
Non current liabilities						
Retirement benefit obligations	0	(17,424)				17,424
Deferred tax liabilities	214	214				0
Obligations under finance leases	367					367
Total non-current liabilities	581	(17,210)	0	0	0	17,791
Total liabilities	42,451	(17,210)	(37)	(170)	0	59,868
Net assets	37,985	(12,197)	(37)	890	0	26,641
Equity						
Share capital	28,755					28,755
Capital redemption reserve	2,952					2,952
Share premium account	7,547					7,547
Revaluation reserve	274					274
Own shares	(1,406)					(1,406)
Translation reserve	0				(180)	(180)
Retained earnings	(137)	(12,197)	(37)	890	180	(11,301)
Total equity	37,985	(12,197)	(37)	890	0	26,641

COMPANY BALANCE SHEET

At 31 December 2005

	Note	2005 £000	2004 £000 As restated
Fixed assets			
Tangible assets	39	103	131
Investments	40	20,702	21,576
		<u>20,805</u>	<u>21,707</u>
Current assets			
Debtors	41	36,850	44,172
Cash at bank and in hand		39	4
Total current assets		<u>36,889</u>	<u>44,176</u>
Creditors – amounts falling due within one year	42	(10,801)	(19,124)
Net current assets		<u>26,088</u>	<u>25,052</u>
Total assets less current liabilities		<u>46,893</u>	<u>46,759</u>
Creditors – amounts falling due after more than one year	43	(1,785)	(285)
NET ASSETS EXCLUDING NET PENSION LIABILITY		<u>45,108</u>	<u>46,474</u>
Net pension liability	44	(13,365)	(10,435)
NET ASSETS INCLUDING NET PENSION LIABILITY		<u>31,743</u>	<u>36,039</u>
Equity			
Share capital	45	28,755	28,755
Capital redemption reserve	46	–	2,952
Share premium account	47	–	7,547
Own shares	48	(1,406)	(1,406)
Profit and loss account	49	4,394	(1,809)
Total equity	51	<u>31,743</u>	<u>36,039</u>

These financial statements were approved by the Board of Directors on 28 March 2006 and signed on its behalf by


PETER D. ATKINSON
 Chief Executive


JOHN LOVE
 Finance Director

NOTES TO THE COMPANY FINANCIAL STATEMENTS

For the year ended 31 December 2005

38. SIGNIFICANT ACCOUNTING POLICIES

The Company financial statements have been prepared on the historical cost basis and in accordance with United Kingdom Accounting Standards. The principal accounting policies adopted are as noted below:

Restatement

This is the first year that the Company is required to adopt the full provisions of FRS 17 "Retirement Benefits" and include the pension scheme deficit and related deferred tax asset in the balance sheet. The amounts to be included are set out in note 44 to these financial statements. Accordingly the results for the year ended 31 December 2004 have been restated to take account of FRS 17 and a prior period adjustment has been reflected in these financial statements as set out in note 49.

This is the first year that the Company is required to adopt the full provisions of FRS 20 "Share Based Payments" and include a charge reflecting the fair value of options granted since 7 November 2002, adjusted to reflect the actual and expected levels of vesting. The amounts to be included are set out in note 49 to these financial statements. Accordingly the results for the year ended 31 December 2004 have been restated to take account of FRS 20 and a prior period adjustment has been reflected in these financial statements as set out in note 49.

Investments

Investments held as fixed assets are stated in note 40 at cost less provision for impairment.

Tangible fixed assets

Tangible fixed assets are stated at cost. No depreciation is provided on land. Depreciation is calculated at fixed rates on a straight-line basis to write off the cost of the assets over the period of their expected useful lives. The rates of depreciation vary between 2% – 5% per annum on buildings and 7% – 33% per annum on plant, vehicles and fittings.

Retirement benefit costs

For defined benefit retirement benefit schemes, the cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out triennially and updated at each balance sheet date. Actuarial gains and losses are recognised in full in the period in which they occur directly in reserves.

Past service cost is recognised immediately to the extent that benefits are already vested and otherwise is amortised on a straight-line basis over the average period until the benefits become vested.

The retirement benefit obligation recognised in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognised past service cost, and as reduced by the fair value of the scheme assets. The obligations are measured on an actuarial basis and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term to the scheme's liabilities.

Payments made to defined contribution retirement benefit schemes are charged as an expense as they fall due.

Financial instruments

- (i) Trade receivables do not carry interest and are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts.
- (ii) Interest-bearing bank overdrafts are recorded at the proceeds received, net of direct issue costs.
- (iii) Trade payables are not interest bearing and are stated at their nominal value.

Taxation

Provision is made for corporation tax on all profits and realised gains up to the balance sheet date, at the latest known corporation tax rates.

Deferred taxation

In accordance with FRS 19, deferred tax is provided in full on timing differences which result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

Cash flow statement

The Company has not presented a cash flow statement. It has taken advantage of the exemption contained in FRS1 (revised 1996) "Cash Flow Statements" as Macfarlane Group PLC has included a consolidated cash flow statement within its group accounts.

Share-based payments

The Company issues equity-settled share-based payments to certain employees. Equity settled share based payments are measured at fair value at the date of the grant. The fair value determined at the grant date of the equity-settled share based payments is expensed as an employee benefits expense on a straight-line basis over the vesting period, based on the Company's estimate of shares that will eventually vest.

The fair value is determined by the use of a binomial model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferrability, exercise restrictions and behavioural considerations.

39. TANGIBLE ASSETS

	Land & buildings £000	Plant, vehicles & fittings £000	Total £000
Cost			
At 1 January 2005 and 31 December 2005	15	386	401
Depreciation			
At 1 January 2005	7	263	270
Charge for year	1	27	28
At 31 December 2005	8	290	298
Net book value			
At 31 December 2005	7	96	103
At 31 December 2004	8	123	131

The parent company had no assets held under finance leases in 2005 or in 2004.

40. INVESTMENTS

	2005 £000	2004 £000
Investment in subsidiaries at cost		
At 1 January	21,576	22,448
Struck off during the year	(874)	(872)
At 31 December	20,702	21,576

Details of the principal operating subsidiaries are set out on page 61.

41. DEBTORS

	2005 £000	2004 £000 As restated
Due within one year		
Amounts owed by subsidiaries	31,720	39,841
Other receivables	626	665
Prepayments and accrued income	494	536
Deferred tax asset	4,010	3,130
	36,850	44,172

Included in amounts owed by subsidiaries are amounts due after more than one year totalling £25,220,000 (2004 – £32,641,000).

	2005 £000	2004 £000 As restated
Deferred tax asset		
At 1 January	3,130	3,108
Increase in deferred tax asset on pension scheme deficit	880	22
At 31 December	4,010	3,130

The deferred tax asset relates to the pension scheme deficit. Recovery of the deferred tax asset is anticipated against future group profits from trading.

NOTES TO THE COMPANY FINANCIAL STATEMENTS

For the year ended 31 December 2005

42. CREDITORS – AMOUNTS FALLING DUE WITHIN ONE YEAR

	2005 £000	2004 £000 As restated
Bank overdrafts	8,794	16,348
Trade creditors	308	468
Amounts owed to group companies	–	34
Corporation tax	478	478
Other taxation and social security	66	32
Other creditors	450	887
Accruals and deferred income	705	877
	<u>10,801</u>	<u>19,124</u>

All bank overdrafts are repayable on demand. The Company had no bank loans in either 2005 or 2004.

The Company and certain subsidiaries have given inter-company guarantees to secure their respective overdrafts. The overall credit lines for these borrowing facilities total £13,750,000. (2004 – £17,500,000).

43. CREDITORS – AMOUNTS FALLING DUE OUTWITH ONE YEAR

	2005 £000	2004 £000
Amounts owed to group companies	<u>1,785</u>	<u>285</u>

44. PENSIONS

The parent company, Macfarlane Group PLC, operates a pension scheme based on final pensionable salary for its UK operations. The assets of the scheme are held separately from those of the Group in managed funds under the overall supervision of the scheme trustees. The underlying share of the scheme's assets and liabilities relating to the parent company are detailed in this note.

Contributions are determined on the basis of triennial valuations using the projected unit method by the scheme's qualified actuary. The most recent triennial valuation was as at 1 May 2005. The principal assumptions adopted were that investment returns would average 7.75% per annum and that salary increases would average 3.5% per annum. The valuation showed that the market value of the relevant assets of the Group scheme was £35,259,000 and the actuarial value of these assets represented 76% of the value of benefits that had accrued to members.

The final salary scheme was closed to new entrants during 2002 and the rate of contributions from both employees and the employer was increased. The employer contribution rate increased from 13.5% to 15.5% of pensionable salary, and the employee contribution rate increased from 5% to 7% of pensionable salary from 1 July 2002 following actuarial advice.

Following the actuarial valuation, the Board has agreed to make additional payments to the scheme of £0.7 million per annum for three years commencing 2006 to reduce the net pension deficit. These additional payments will increase the pension scheme assets; they are not a charge against profits.

44. PENSIONS (continued)

Balance sheet disclosures

The figures below have been based on the actuarial valuation as at 1 May 2005, updated to the current year-end. The share of the assets in the scheme and the share of the present value of the liabilities in the scheme relating to the parent company at 31 December 2005 and the expected rates of return were:

Asset class

	Fair value 2005 £000	Long-term expected rate of return	Fair value 2004 £000	Long-term expected rate of return	Fair value 2003 £000	Long-term expected rate of return
Equities	14,004	7.50%	11,581	7.75%	10,760	8.25%
Bonds	9,700	4.50%	8,825	5.00%	8,317	5.00%
Other (cash)	12	4.50%	21	5.00%	56	4.50%
Fair value of assets	23,716		20,427		19,133	
Present value of scheme liabilities	(37,081)		(30,862)		(29,492)	
Deficit in the scheme	(13,365)		(10,435)		(10,359)	
Related deferred tax asset (note 41)	4,010		3,130		3,108	
Net pension liability	(9,355)		(7,305)		(7,251)	

The scheme's liabilities at 31 December 2005 were calculated on the following bases as required under FRS17:

Assumptions

	2005	2004	2003
Discount rate	4.75%	5.25%	5.50%
Rate of increase in salaries	2.75%	2.75%	4.00%
Rate of increase in pensions in payment	3% or 5% for fixed increases or 2.75% for LPI. 2.50% post 5 April 2005	3% or 5% for fixed increases or 2.75% for LPI	3% or 5% for fixed increases or 2.75% for LPI
Inflation assumption	2.75%	2.75%	2.75%

Analysis of amounts charged to operating profit

	2005 £000	2004 £000
Current service costs	(28)	(69)

Analysis of amounts charged to net finance charges

	2005 £000	2004 £000
Expected return on pension scheme assets	1,310	1,289
Interest cost of pension scheme liabilities	(1,354)	(1,605)
	(44)	(316)

Analysis of the actuarial loss included in the statement of total recognised gains and losses

	2005 £000	2004 £000
Actual return less expected return on scheme assets	2,381	473
Experience gains & losses arising on scheme liabilities	(287)	198
Changes in assumptions underlying the present value of the scheme's liabilities	(5,023)	(413)
Actuarial loss	(2,929)	258

NOTES TO THE COMPANY FINANCIAL STATEMENTS

For the year ended 31 December 2005

44. PENSIONS (continued)

	2005 £000	2004 £000
Movement in scheme deficit in the year		
At 1 January	(10,435)	(10,359)
Current service cost	(28)	(69)
Contributions	71	51
Other financial charges	(44)	(316)
Actuarial (loss)/gain in the year	(2,929)	258
At 31 December	(13,365)	(10,435)

	2005 £000	2004 £000	2003 £000
History of experience gains and losses			
Difference between expected and actual return on scheme assets	2,381	473	1,024
Percentage of scheme assets	10.0%	2.3%	5.4%
Experience gains and losses on scheme liabilities	(287)	198	475
Percentage of the present value of the scheme's liabilities	(0.8%)	0.6%	1.6%
Total amount recognised directly in equity	(2,929)	258	(416)
Percentage of the present value of the scheme's liabilities	(7.9%)	0.8%	(1.4%)

Defined contribution schemes

The Company also participated in a defined contribution scheme, the Macfarlane Group Personal Pension Scheme. Contributions to the scheme for the year were £3,000 (2004 – £3,000).

45. SHARE CAPITAL

	Number of shares	2005 £000	2004 £000
Ordinary shares of 25p each			
Authorised	200,000,000	50,000	50,000
Allotted, issued and fully paid: At 1 January and 31 December	115,019,000	28,755	28,755

There have been no movements in share capital during the year.

46. CAPITAL REDEMPTION RESERVE

	2005 £000	2004 £000
At 1 January	2,952	2,952
Cancellation of reserve	(2,952)	–
At 31 December	–	2,952

Following shareholder approval at the Annual General Meeting on 10 May 2005, the Company petitioned the Court to have its Capital Redemption Reserve and Share Premium Account cancelled. The petition was approved on 1 September 2005 and the reserves were cancelled and reinstated as distributable reserves.

47. SHARE PREMIUM ACCOUNT

	2005 £000	2004 £000
At 1 January	7,547	7,547
Cancellation of reserve	(7,547)	–
At 31 December	–	7,547

Following shareholder approval at the Annual General Meeting on 10 May 2005, the Company petitioned the Court to have its Capital Redemption Reserve and Share Premium Account cancelled. The petition was approved on 1 September 2005 and the reserves were cancelled and reinstated as distributable reserves.

48. OWN SHARES

	2005 £000	2004 £000
At 1 January and 31 December	(1,406)	(1,406)

At 31 December 2005, the Company's Employee Share Ownership Trust ("ESOT") held 2,491,325 (2004 – 2,491,325) ordinary shares in Macfarlane Group PLC with a market value of £828,000 (2004 – £747,000) against the future exercise of share options. The ESOT has waived its right to receive dividends on these shares.

49. PROFIT AND LOSS ACCOUNT

	2005 £000	2004 £000 As restated
At 1 January as previously stated	5,533	7,447
Prior period adjustments (see below) (see below)	(7,305) (37)	(7,251) (5)
At 1 January 2005 as restated	(1,809)	191
Net loss for the year	(1,402)	(1,336)
Dividends paid	(844)	(844)
Post-tax actuarial (loss)/gain in pension scheme taken direct to equity	(2,050)	180
Cancellation of capital redemption reserve and share premium accounts	10,499	–
	4,394	(1,809)

Prior period adjustments

Under UK GAAP, the transitional provisions of FRS17 "Retirement Benefits" required the pension deficit to be shown as a memorandum disclosure in the notes to the accounts for periods up to 31 December 2004 rather than accounted for on the balance sheet. For accounts for periods after this date, FRS17 requires the operating and financing costs of the defined benefit pension schemes to be shown separately in the profit and loss account and requires the pension deficit be shown on the face of the balance sheet. Actuarial gains and losses are to be recognised in full directly in reserves.

The Company has adopted the approach of recognising the full pension deficit at the date of transition, 1 January 2004. The overall impact of recognising the pension deficit of £10,435,000 (2003 – £10,359,000), net of incorporating the related deferred tax asset of £3,130,000 (2003 – £3,108,000), is a reduction in net assets of £7,305,000 at 31 December 2004 and £7,251,000 at 1 January 2004. In adopting the requirements of FRS17 "Retirement Benefits", these amounts have been disclosed as a prior period adjustment and opening reserves adjusted accordingly. For the accounting years 2004 and 2005, the movement in actuarial gains or losses and the related deferred tax thereon, have been reflected in full directly in reserves.

Previously, no charge was made to the profit and loss account for the value of options granted to employees as options were granted at their intrinsic value. A charge has now been made reflecting the fair value of options granted since 7 November 2002, adjusted to reflect the actual and expected levels of vesting. The impact was a charge of £32,000 in the year to 31 December 2004 and reductions in net assets of £37,000 at 31 December 2004 and £5,000 at 1 January 2004. Accordingly these amounts have also been disclosed as a prior period adjustment with opening reserves adjusted accordingly.

NOTES TO THE COMPANY FINANCIAL STATEMENTS

For the year ended 31 December 2005

50. OPERATING PROFIT

	2005 £000	2004 £000
Operating profit for the parent company has been arrived at after charging:		
Auditors' remuneration Audit services	25	18
Non-audit services	69	32
Staff costs (see below)	1,066	1,081
The average monthly number of employees was:		
Administration	15	15
The costs incurred in respect of these employees were:		
Wages and salaries	928	913
Social security costs	107	96
Other pension costs	31	72
	1,066	1,081

51. RECONCILIATION OF MOVEMENTS IN EQUITY

	2005 £000	2004 £000 As restated
Loss for the year	(1,402)	(1,336)
Dividends to equity holders in the year	(844)	(844)
Post actuarial (loss)/gain in pension scheme taken direct to equity	(2,050)	180
Movements in equity in the year	(4,296)	(2,000)
Opening equity shareholders' funds as previously stated	43,381	45,295
Prior period adjustments (see note 49)	(7,342)	(7,256)
Opening equity shareholders' funds as restated	36,039	38,039
Closing equity shareholders' funds	31,743	36,039

52. RELATED PARTY TRANSACTIONS

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed.

During the year the Company incurred fees for corporate advice amounting to £20,000 (2004 – £5,000) to Noble Grossart Limited, of which R.G.T. Stenhouse, a non-executive director of the Company until 10 May 2005, is a director. The directors have considered the implications of FRS 8 "Related Party Transactions" and are satisfied that there are no other related party transactions occurring during the year, which require disclosure.

FIVE YEAR RECORD

	2001 £000	2002 £000	2003 £000	2004 £000	2005 £000
Turnover	198,200	149,618	130,971	122,705	127,247
Profit/(loss) before interest, discontinued operations, exceptional items and tax	11,001	(1,951)	(9,379)	95	2,928
Contribution from discontinued activities	-	-	-	(845)	750
Net interest payable	(418)	(398)	(1,051)	(1,678)	(1,054)
	10,583	(2,349)	(10,430)	(2,428)	2,624
Profit/(loss) on disposal of assets	822	2,145	(239)	3,566	1,048
Restructuring costs	(4,880)	(2,324)	(4,680)	-	-
Goodwill impairment	(5,178)	(2,720)	-	-	-
Loss on disposal of operations	(2,770)	(410)	(3,235)	(1,400)	-
Profit/(loss) before tax	(1,423)	(5,658)	(18,584)	(262)	3,672
Taxation	(3,071)	1,836	1,354	26	(287)
Profit/(loss) for the financial year	(4,494)	(3,822)	(17,230)	(236)	3,385
Earnings/(loss) per ordinary share	(3.63p)	(3.25p)	(15.31p)	(0.21p)	3.01p
Dividends	(6,050)	(5,745)	-	(844)	(844)
Dividends per ordinary share	5.00p	5.00p	Nil p	0.75p	0.75p
Dividend cover	N/A	N/A	N/A	N/A	4.0

The amounts disclosed for 2003 and earlier periods are stated on the basis of UK GAAP because it is not practicable to restate amounts for periods prior to the date of transition to IFRSs. The principal differences between UK GAAP and IFRSs are explained in note 37 to the financial statements, which provides an explanation of the transition to IFRSs.

FINANCIAL DIARY

FINANCIAL RESULTS

Interim	Announced – August
Final	Announced – March

ACCOUNTS AND ANNUAL GENERAL MEETING

Report and financial statements	Posted to shareholders in April.
Annual General Meeting	Held in Glasgow in May.

SHAREHOLDER ENQUIRIES

Enquiries regarding shareholdings, dividend payments, dividend mandate instructions, lost share certificates, tax vouchers, changes of address, transfers of shares to another person and other administrative matters should be addressed to the Company's registrars, Lloyds TSB Registrars Scotland, PO Box 28448, Finance House, Orchard Brae, Edinburgh EH4 1WQ.

Telephone: 0870 6015366
Fax: 0870 900 0030
Website: www.shareview.co.uk

PRINCIPAL OPERATING SUBSIDIARIES

COMPANY NAME	PRINCIPAL ACTIVITIES	Country of registration
MACFARLANE GROUP UK LIMITED Coventry Telephone 02476 511511	Supply and distribution of all forms of packaging materials and equipment.	England
Grantham Telephone 01476 574747 Westbury Telephone 01373 858555	Design, manufacture, assembly, storage and supply chain management of specialist packaging.	England
MACFARLANE LABELS LIMITED Kilmarnock Telephone 01563 525151	Manufacture of high quality printed self-adhesive labels and resealable labelling solutions.	Scotland
MACFARLANE LABELS (IRELAND) LIMITED Dublin Telephone 00 353 1832 0220	Manufacture of high quality printed self-adhesive labels and resealable labelling solutions.	Ireland
MACFARLANE GROUP SWEDEN AB Helsingborg Telephone 00 46 42 13 75 55	Manufacture of high quality printed self-adhesive labels and resealable labelling solutions.	Sweden
MACFARLANE PLASTICS LIMITED Newtownmountkennedy Telephone 00 353 1281 0234	Manufacture of injection mouldings for nutraceutical, pharmaceutical, medical, toy, retail and petrochemical industries.	Ireland
MACFARLANE WESTERN FOAM INC Union City Telephone 001 510 324 3626 Ontario Telephone 001 909 390 4422	Design, manufacture, assembly, storage and supply chain management of specialist packaging.	USA
MACFARLANE DE MEXICO S.A. De C.V. Tijuana Telephone 00 52 66 49 03 3985 Guadalajara Telephone 00 52 33 33 65 8765	Design, manufacture, assembly, storage and supply chain management of specialist packaging.	Mexico

Note: All the above subsidiaries are wholly owned either by Macfarlane Group PLC or one of its subsidiary companies and operate within their country of registration. A full list of trading and non-trading subsidiaries is available from the registered office, 21 Newton Place, Glasgow G3 7PY.

Disposal on 11 January 2006

COMPANY NAME	PRINCIPAL ACTIVITIES	Country of registration
MACFARLANE PACKAGING KH Budapest Telephone 00 36 1305 3080	Design, manufacture, assembly, storage and supply chain management of specialist packaging.	Hungary

MACFARLANE GROUP PLC

21 Newton Place
Glasgow G3 7PY
Telephone: 0141 333 9666
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E-mail: investorinfo@macfarlanegroup.net
Website: <http://www.macfarlanegroup.net>