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High performance foams for specialist markets worldwide



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Zotefoams plc is the world's leading manufacturer of cross-linked block foams. Its products are used in a wide range of markets including sports and leisure, packaging, transport, healthcare, toys, building, marine and the military.

Through a unique production process, the Company produces foams which have controllable properties and are of a strength, consistency, quality and purity superior to foams produced by other methods.

Products

Zotefoams uses a high-pressure nitrogen gas solution manufacturing process whereby extruded, cross-linked polymer sheets are impregnated with pure nitrogen and subsequently expanded in a pressure chamber without the use of moulds.

This unique process produces foams with exceptional cell size uniformity, low odour/high purity and outstanding physical attributes. The AZOTE range of foams is produced from a wide range of polymers, including LDPE, HDPE and PP, as well as EVA co-polymers.

Products are available in special grades with flame retardant additives (for the construction and aerospace industries) and conductive or static dissipative properties (for electronics manufacturing and packaging). Foams are produced in a wide density range from 15kg/m³ up to 120kg/m³.

AZOTE

AZOTE is the new Group brand name for Zotefoams' polyolefin foams... high quality foams from differing base polymers but all manufactured using the same unique nitrogen expansion process route.

AZOTE was used formerly as a name for nitrogen and is still used by French chemists to refer to the element. Azote foams derive many of their exceptional properties directly from the use of this inert, tasteless, odorless gas in the manufacturing process.

Zotefoams' well known product brands names; PLASTAZOTE®, EVAZOTE®, SUPAZOTE® and PROPOZOTE® will continue to stand for individual product types within the overall AZOTE product range.

ZOTEK®

ZOTEK® foams are a range of high performance foams manufactured, using Zotefoams' unique high-pressure nitrogen gas solution manufacturing process, from fluoropolymers, engineering polymers and speciality elastomers.

ZOTEK® F is a range of lightweight, closed cell, foams based on the fluoropolymer Kynar® PVDF (polyvinylidene fluoride). It is a remarkable material that offers a unique balance of properties including temperature, UV and chemical resistance combined with excellent flammability performance.

ZOTEK® N is a range of lightweight, closed cell, foams, currently in development and based on the engineering thermoplastic polyamide. The main benefits of polyamide are its thermal and chemical resistance. Polyamide is particularly resistant to swelling by hydrocarbons such as oils, which combined with its thermoplastic nature allow complex shapes to be fabricated economically.

	2005	2004
Turnover (£m)	28.0	25.2
Profit before tax excluding exceptional items (£m)	1.8	1.3
Profit before tax including exceptional items (£m)	3.3	1.3
Earnings per ordinary share excluding exceptional items (p)	3.5	3.2
Earnings per ordinary share including exceptional items (p)	6.7	3.2
Net cash inflow from operating activities (£m)	3.2	4.5
Net dividend per share (p)	4.5	4.5

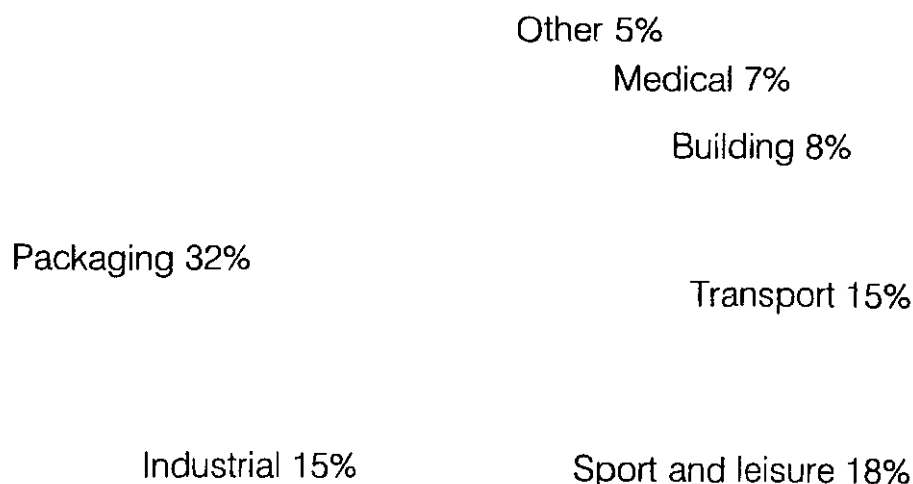
Applications

The uses of Zotefoams' foams are too numerous to list. Applications vary from personal protection to packaging, conservation to construction, and automotive to aerospace.

Because they are expanded in a free environment they have little in-built stress making them easy to fabricate by common conversion methods.

Wherever there is a need for light weight cushioning, impact absorption, sealing properties, buoyancy, or water resistance, Zotefoams could well offer the functional, pure, low odour, colourful, aesthetically pleasing solution.

Breakdown of turnover by market sector



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CHAIRMAN'S STATEMENT

Bill Fairservice

Sales		28.0
23.5	25.2	
2003	2004	2005

Our strategy

Zotefoams' strategy is to create sustained profit growth by expanding its sales internationally and by broadening its potential market with new unique products. This strategy is supported by our commitment to quality, innovation and customer service through investment in the training and development of our employees. We aim to remain at the forefront of foam technology by concentrating our resources in key areas, exploiting our unique capability. We also seek to develop and maintain relationships with others where our combination of expertise and resources will be beneficial.

Our objectives

We intend to grow sales in our core polyolefin foams business in excess of the rate of inflation in Europe and achieve significant growth in North America and Asia. Our sales growth in America is supported by our factory in Kentucky which opened in mid-2001 while in Asia we will consider a similar operation, either as a license or joint venture, as sales increase to a level where this is sensible. We are also committed to developing a portfolio of unique foam products from high-performance materials which will enjoy significant advantages over competitive materials, allow higher margins for Zotefoams and confirm our position as the pre-eminent foam technology company. We intend to achieve these while continuing to improve our return on capital employed through a more efficient use of assets and working capital.

Our board

After ten years with Zotefoams, John Marley retired from the Board as a non-executive Director in December. On behalf of the Board I would like to thank John for his service and contribution over the years. Effective 1 January 2006 Nigel Howard joined the Board as a non-executive Director and Chairman of the Remuneration Committee. I am delighted to welcome Nigel who is currently a non-executive Director of Alliance One International Inc. based in North Carolina, USA and previously worked for Morgan Crucible in a number of roles including Interim Chief Executive.

Our achievements

During 2005 we grew sales by 11%. Profit before tax and exceptional items increased by 40% to £1.8 million. Profit before tax including exceptional items was £3.3 million. Sales in Europe grew 7% which was approximately twice the level of inflation, while sales in North America and Asia grew 24% and 46% respectively. During 2005 we made the first meaningful sales of ZOTEK® high performance foams and continued to invest for the future with technological development in a number of exciting projects including polyamide (nylon) foams. Our return on capital employed, measured as profit before tax and exceptional items as a percentage of average equity, was 7.4%, up from 5.4% in 2004. We ended the year with a strong balance sheet and, despite the exceptional cash costs relating to pensions restructuring and the bid approach, we reduced net debt (borrowings less cash) to £1.1 million (2004:£1.7 million) at 31 December.

Zotefoams at a glance

a unique process

The first stage in production for all our products is to extrude a solid slab. The key to a successful extrusion is good mixing and sheet profile. We currently extrude a number of different polyolefins and our ZOTEK® F high performance foams with similar technology. Future developments, such as polyamide and silicone, while also starting as an extruded slab, will require different extrusion equipment and Zotefoams plans to invest and further develop our competence in these areas.

Zotefoams proprietary technology uses high pressure autoclaves to dissolve nitrogen gas in solid polymer slabs. Our vessels are capable of achieving temperatures up to 250 degrees Celsius and pressures of 670 atmospheres. Under these extreme conditions we are able to dissolve gas into many different polymers which is the key to development of high performance foams. The vessels are then cooled and depressurised before removing the solid slab (at this stage saturated with pressurised nitrogen gas).

Gassed slabs may be expanded immediately in the UK or may be shipped to our plant in Kentucky, USA for final processing. This final (expansion) stage is also controlled in a heated and pressurised autoclave which is necessary to ensure product quality and consistency. The plant in Kentucky allows us to access the large and demanding North American market in a cost effective manner by shipping solid material from our capital intensive UK plant before final expansion to foam close to the customer.

The Directors are recommending a final dividend of 3.0p net per share payable on 26 May 2006 to shareholders on the Company register at the close of business on 28 April 2006. This would bring the total declared dividend to 4.5p for 2005 and is unchanged from the dividend declared for 2004.

W H Fairservice
Chairman
13 March 2006

Zotefoams' strategy is to create sustained profit growth by expanding its sales internationally and by broadening its potential market with new unique products.

Watersports footwear depends on Azote foam

Mion, a division of Timberland, has launched a range of watersports footwear for the serious amphibious athlete. A key component of the line is an 'ergomorphic[®]' footbed that takes an impression of the contours of the foot after the first twelve hours of wear and is then able to provide ultimate individualised support and comfort.

The concept derives from the orthotic insoles developed by the medical industry to combat such conditions as 'diabetic foot', and depends on the unique thermoforming properties of Azote foams.

The fact that they are expanded without the use of chemical blowing agents also fits with Mion's and Timberland's environmentally conscious approach to business.

MANAGING DIRECTOR'S REVIEW

David Stirling

Profit before tax
excluding exceptional items

1.839

1.309

0.955

2003	2004	2005
£m	£m	£m

2003 under UK GAAP, 2004-5 under IAS. See appendix on page 50 for explanation of principal differences.

Our year

I am pleased to report improved results for 2005 as sales increased 11% to £28.0 million and profit before tax excluding exceptional items increased 40% to £1.8 million. Profit before tax including exceptional items was £3.3 million. Importantly, in a year where our raw material and energy prices rose sharply, we were able to recover these increases through price rises and a surcharge linked to polymer prices and therefore gross margins for the year were satisfactory at 22.6% (2004: 22.1%). Overall sales volume increased 3%. Unusually, sales in the second half of the year were stronger than in the first half as volumes rose by 7% and sales value increased by 17%. Sales of our ZOTEK® high performance foams grew to US\$1 million (£555,000) which accounted for 2% of turnover.

Before exceptional items our effective tax rate is 31% (2004: 11%) giving profit for the year of £1.3 million (an increase of 9% over 2004) and earnings per share of 3.5p (2004: 3.2p). After exceptional items profit for the year was £2.4 million with earnings per share of 6.7p.

On 14 January 2005 Zotefoams received a preliminary approach from a third party looking to buy the company. Discussions continued with a number of parties through most of 2005, absorbing a significant amount of management time and resource, until 2 November 2005 when the Zotefoams' Board terminated discussions. The costs of this unsolicited approach were £413,000 and these are classified as an exceptional item.

Effective 31 December 2005 Zotefoams closed its UK defined benefit scheme to future service accrual for existing members. The defined benefit scheme had been closed to new entrants from October 2001. All employees who were active members of the defined benefit scheme as at 31 December 2005 were offered membership of an alternative defined contribution scheme. This restructuring resulted in an exceptional profit of £2.0 million due to the actuarial impact of the reduction in future obligations on the defined benefit scheme. Net of associated costs, including explanatory presentations to employees, an exceptional gain of £1.9 million is shown in the accounts for the period. Further detail is given in the Finance Director's review.

Our business

Foams produced and sold by Zotefoams fall into two main business segments which are best characterised by their constituent raw materials: polyolefins and high performance polymers. Development of materials for sale in the high performance polymer foams market is a key element in our business strategy. Zotefoams' proprietary technology allows the foaming of materials which we believe cannot currently be achieved by other means or, alternatively, our process gives either an economic or material performance advantage. We are seeking to exploit this technical advantage by foaming materials other than polyolefin to meet the needs of markets outside traditional polyolefin foams. However, we believe polyolefin foam will continue to be our largest product group for the foreseeable future and the combination of growth in this product and the development of new materials will make a real and sustainable positive difference to our business.

Zotefoams at a glance

developing products

Development of new products begins with market knowledge. Zotefoams approach product development on two levels. Most short-term development is focussed specifically at the immediate need of a customer and involves modification of an existing product. Long-term development can take many years and is more fundamental, examining industry trends, market requirements and matching this with our strategy and process capability. We do not currently undertake longer term developments for specific customer applications.

There is no guarantee of success in product development. Zotefoams approach to managing this risk is to maintain a balanced portfolio and review developments frequently. Current focus is on three main long-term projects: foams from fluoropolymer (PVDF), polyamide and silicone. PVDF was first launched in 2004 with a range extension in January 2006. We believe this PVDF "family" will continue to grow as new opportunities emerge and these "core" products are modified to customer requirements.

Longer term developments require continual review and integration with sales and marketing resource. Technical feasibility, fit with our operational capability, market testing and economic assessment all need to be considered as products progress to launch. Our business development team therefore blend technical and commercial backgrounds and typically have experience elsewhere in Zotefoams. Significant technical support is often required after product launch to support customer evaluations which are often very demanding and undertaken over long timescales.

Polyolefin foams

Overall volumes in polyolefin foams grew 3% compared to 2004. Increased selling prices, product mix and a temporary surcharge to customers in relation to raw materials costs combined with the volume increase to give an overall increase in sales of polyolefin foams of 9% compared to 2004.

In a climate of increasing material costs 2005 was always likely to be a year of subdued volume growth. Germany, which grew 9% in volumes, was the only major market where sales volumes increased significantly. In other areas we saw a mixed picture with quite dramatic swings in timing of sales and product mix over the business as a whole and in France and North America in particular. The second six months saw a more encouraging picture with volumes up 7% and sales value, including the impact of raw material surcharges, up 14% on the previous year.

Sales in the UK and Eire grew 5% as Zotefoams continues to work on end-user market development and support of customers in specific market segments. UK manufacturing overall continues to be a difficult market but new applications in construction together with some recovery in the marine segment, offset a slower than expected year in specialist packaging.

In Germany sales grew by 15% as a result of strong performances in the packaging and transport segments both through our main distributor and through direct accounts. In France, as our prices increased, some business was lost in the industrial and construction segments although this was partly compensated for by growth in marine applications. Italy and Spain remain difficult

**Sales increased 11% to
£28.0 million and profit before
tax excluding exceptional items
increased 40% to £1.8 million.**

Waste-free packaging environment

A zero waste packaging environment is a key objective for the major car manufacturers. Honda, Rolls Royce and BMW, and many tier one and two suppliers to the industry, have turned to reusable packaging solutions devised by IMP Ltd a specialist UK converter; solutions that incorporate Azote foams.

Azote cross-linked closed cell foams are easily tailored to fit individual components, providing sufficient 'hold' for optimum scratch-free protection while offering easy access for improved ergonomic efficiency.

MANAGING DIRECTOR'S REVIEW

David Stirling

North American sales		Total
		13,344
		HPP: 1,005
	10,779	
9,135		
		Polyolefins:
		12,339
2003	2004	2005
\$000	\$000	\$000

markets for Zotefoams with sales performing below our expectations for the second successive year and our approach in both countries is currently under review. Our performance in Scandinavia, with a volume increase of 7%, was particularly pleasing with strong contributions from the industrial segment and growth of newly developed accounts in packaging.

In North America sales to the automotive and general construction segment were at similar levels to 2004. Growth in this region came predominantly from the military, specialty construction and health and beauty segments. Although overall volumes increased by only 3% in North America the more favourable product mix led to an overall increase in revenues from polyolefin foam of 15%.

The Rest of the World sales volume grew by 21% during the year with strong contributions in specific regions from the construction, sports and leisure and packaging segments.

During 2000 and 2001 Zotefoams entered into a worldwide sales and marketing alliance for polyolefin foams with the Sekisui Chemical Company Ltd ('Sekisui'), who act as exclusive agent and distributor for Zotefoams in Continental Europe and Asia respectively. Sekisui also act as agent for certain customers in North America.

As announced in December the Board has, for some time, been in discussions with Sekisui in relation to certain of their obligations under two of these contracts. While still open to the prospect of resolution through other means, the Board has decided to pursue its rights through the prescribed dispute resolution processes and Zotefoams has

therefore instigated arbitration proceedings which are scheduled to be heard at the end of March 2006 and in June 2006. Commercial arrangements with Sekisui continue as normal.

Our major raw materials are commodity polymers and therefore are subject to rapid and sometimes large price movements. Low density polyethylene, by far our largest raw material cost, averaged €1,056 per tonne in 2005, up 24% on 2004. In 2005 significant price increases were experienced in both gas and electricity and Group energy costs were 5.8% of sales. While efforts are underway to minimise the impact of energy price rises in our business we anticipate further increases in our energy costs in 2006.

High Performance Foams

Our high performance foams are marketed under the ZOTEK® brand. The first ZOTEK® product, a fluoropolymer foam known as ZOTEK® F30, was launched in January 2004 with the key attributes of excellent fire, chemical and UV-light resistance. This is a radical departure from existing materials both for Zotefoams and for our customers and therefore requires a significant market development effort. However, ZOTEK® F30 has now gained acceptance in demanding aviation applications and the majority of the US\$1 million of sales during 2005 were in aviation in North America.

Our materials partner, Arkema Inc., offers a wide range of fluoropolymers under the Kynar® trademark and we anticipate developing a range of the ZOTEK® F foams exploiting the various properties of these polymers. We have already secured initial orders for our second major product, ZOTEK® F HT,

Zotefoams at a glance

wide applications

Azote foam used for expansion joints in the construction industry... wide elastic working range and excellent resistance to contaminants.

Azote foam helps protect pallet racking from forklift damage... impact absorbing and durable.

Azote foam used in specialised 3D gaskets and light-weight void fillers in automotive manufacture ... lightweight, consistent and mouldable.

Development of materials for sale in the high performance polymer foams market is a key element in our business strategy.

offering higher temperature and improved chemical resistance, which was launched in January 2006.

Zotefoams are currently working on additional exciting projects in aviation, military and in the chemical industry with ZOTEK® grades. These projects are often for much larger values than offered by a typical polyolefin foam application. However, the performance requirements and test conditions are very demanding and evaluation can take many months or sometimes years. Therefore the inherent uncertainty of such projects, particularly their timing and the unique requirements of specific applications which will vary from project to project, makes projecting revenues and success rates extremely difficult, especially at this early stage in their development.

Operational Capability

Zotefoams operates a unique and proprietary manufacturing process which has been used for production of polyolefin foams for many years. Our strategy is to apply this process to higher value polymers which cannot be foamed by conventional means or where our process would give significant advantages. Therefore all products we make share significant common elements of equipment and processes.

In April 2005 we commissioned a new high pressure autoclave to increase our production capacity and flexibility. This capacity addition was required to allow older machinery to be removed from production as part of a rolling refurbishment and upgrade programme planned to continue into 2015. In August one of our older high pressure vessels was removed from service as part of this process.

The largest hoses in the world

Dunlop Oil & Marine has been supplying flexible rubber hoses for the offshore dredging industry since the early 1970's. Principal applications for the hoses include estuary clearance, beach replenishment or large land reclamation and other civil engineering projects.

The buoyancy properties provided by incorporating Plastazote® foam material in the construction, allow these hoses to be manufactured in bore diameters from 150mm up to 1100mm, or larger on request. They are available in lengths up to 11.8m and are suitable for working pressures up to 30 bar.

MANAGING DIRECTOR'S REVIEW

David Stirling

Zotefoams are currently working on additional exciting projects in aviation, military and in the chemical industry with ZOTEK® foams.

Research and development spending

	734	776
635		

2003	2004	2005
£000	£000	£000

Zotefoams at a glance

wide applications

Azote lightweight foam in composite construction paddle rackets... lightweight and durable.

Azote foam used in medical device manufacture... soft touch, durable and MRI / X-ray lucent.

Azote foam used in point of sale packaging... aesthetically pleasing and protective.

As this work progressed it became apparent there was some unanticipated corrosion being caused by the water-cooling mechanism which Zotefoams have used on this site since the 1940s. Further investigations uncovered the same issue, to varying degrees, on all high pressure vessels operating using water cooling. To minimise the extent of this corrosion (which ultimately would impair both the useful life and operating pressure of these vessels as well as increase the risk of a health and safety incident) the Board has decided to accelerate the refurbishment and upgrade programme.

Our target, which is based on the most prudent course from a safety perspective while continuing to operate, is for a serial refurbishment of all water-cooled vessels on the shortest practical timescale. Approximately 60% of our high pressure capacity remains to be refurbished on an accelerated timescale which will result in capital expenditure of approximately £9 million being phased over 6 years rather than 10 years as originally planned.

Expenditure on research and development, all of which has been charged to profits in the year of expenditure, increased by 6% to £0.8 million in 2005. The majority of this was spent on fluoropolymer, polyamide and silicone foams, although there are other projects being evaluated. Developments with fluoropolymer are aimed at extending the grade range and are strongly influenced by feedback from market evaluations of the ZOTEK® F30 foams which were sold during the year. Our polyamide foam development is at an advanced stage and market launch is expected around mid-2006. The technical development of low-density silicone foam is well advanced and we are at the stage of addressing specific engineering and handling aspects of this material. The production and certain uses of PVDF, polyamide and silicone foams are covered by patents.

Employees

Customers, employees and technology define our business. 2005 brought significant challenges of rising input costs against a backdrop of uncertainty caused by the bid approach. In these challenging circumstances I am delighted at the response from Zotefoams' employees and I would like to express my thanks to each and every one for their effort during the year.

The future

The key challenges for Zotefoams in the coming year are to manage the impact of changes in commodity prices (primarily energy and materials costs) and competitive environment while pursuing our stated objectives to:

1. grow sales in our polyolefin business in excess of the rate of inflation in Europe and achieve significant growth in North America and Asia;
2. develop a high performance foams portfolio to deliver enhanced margins;
3. improve our return on capital employed.

During 2004 and 2005 we met all these objectives and they continue to offer a valid benchmark of our performance into 2006. We continue to generate cash, to return cash to shareholders through dividends and to invest for the future. I firmly believe the balance is appropriate for Zotefoams at this stage in our development and that our business will evolve and prosper while managing the risks outlined above. The combination of a solid foundation in polyolefin foams and opportunities in development of high performance materials offers exciting prospects for the future.



David Stirling
Managing Director
13 March 2006

New materials find favour

The ZOTEK® F range of fluoropolymer foams has been extended with the addition of new variants that offer a substantially higher operational temperature performance with an upper limit of 160°C, an improvement of 50°C over the initial grades. These new products also offer enhanced chemical and solvent resistance combined with higher levels of structural rigidity.

The new ZOTEK® F grades are expected to find uses in chemical engineering and pharmaceutical insulation and sealing applications and are also targeted at commercial and military aircraft and aerospace industries. Evaluation trials have led to initial orders being received and official NATO codification has already been achieved for one of these new grades for a confidential military application.

FINANCE DIRECTOR'S REVIEW

Clifford Hurst

Finance Director's review

Group turnover was £28.0 million, 11% higher than 2004. Roughly half of this increase was due to price rises and a material surcharge as high input prices on polymer and energy were passed on. The average price of low density polyethylene, our major raw material, rose 24% while our energy prices increased by £0.3 million. It is therefore pleasing that through a combination of price increases and efficiency improvements we were able to maintain gross margins at around 22%.

Underlying distribution and administrative expenses, pre-exceptional items, increased by £0.3 million with an additional investment of £0.1 million in technical support. Sales of our new materials in the year exceeded £0.5 million compared to practically nil in 2004 and we have an exciting pipeline of new products.

Profit before tax and exceptional items was £1.8million, a 40% increase compared to 2004. Profit before tax after exceptional items was £3.3 million.

There are two exceptional items shown within administrative expenses. In January 2005 the Board announced that it had received a preliminary approach that might lead to an offer for the share capital of the Company. Discussions continued with a number of parties until the Board announced in November 2005 that these talks were terminated. The advisory and other costs associated with this approach were £0.4 million.

In December 2005 the Company closed its defined benefit pension scheme to future accrual of benefit. The actuarial gain from

this curtailment, less associated costs, was £1.9 million.

The tax charge for the year was £0.9 million, an effective tax charge of 26%. This is after an exceptional £0.3 million release of a deferred tax provision. The provision related to insurance proceeds received after a fire in 2000 which were recorded as an exceptional profit and now that the tax computations have been agreed with Her Majesty's Revenue and Customs the surplus provision has been released as an exceptional item.

Profit after tax was therefore £2.4 million with earnings per share of 6.7 pence. Excluding exceptional items earnings per share are 3.5p compared to 3.2p in 2004.

Cash flow and funding

EBITDA excluding exceptional items was £5.3 million (2004: £5.0 million). Working capital increased by £0.7 million due to higher sales in the second half of the year. Depreciation was £3.3 million, significantly above capital expenditure of £1.1 million. After a period of major capital expenditure in 2000 to 2002 (£8 million was spent on opening a North American manufacturing facility and £6 million on rebuilding the Croydon site following a fire) depreciation has been substantially above capital expenditure. Nevertheless, the capital expenditure in 2005 was abnormally low due to phasing of projects and we expect capital expenditure to rise in 2006.

With cash generated from operating activities of £3.2 million the Group produced strong cash flow, reducing net debt (borrowings less cash) in the year from £1.7 million to £1.1 million. Gearing (measured as net debt

EBITDA excluding exceptionals

4.973 5.345

4.252

(3.578) (1.659) (1.068)

2003 under UK GAAP, 2004-5 under IAS. See appendix on page 50 for explanation of principal differences. Net debt is borrowings less cash.

divided by shareholder's equity) has fallen to 4% from 7% in 2004.

A final dividend of 3.0p net per share is proposed which brings the total declared for the year to 4.5p, the same level as 2004.

Pensions

The Company operates a defined benefit pension scheme in the UK which has been closed to new entrants since October 2001. Following the tri-annual actuarial valuation in April 2005 the deficit on an ongoing valuation basis increased from £0.6 million to £3.8 million. In view of the risks involved in running defined benefit pension schemes, the Board, after a period of consultation, closed the scheme to future accrual of benefit on 31 December 2005.

Employees who were members of the scheme have been offered membership of an alternative defined contribution scheme. The contribution level to this scheme has been set by an actuary to provide a similar level of benefit to that which the member could have expected, as at 31 December 2005, when they retired from the defined benefit scheme. The cash cost of doing this for the Company is similar to that which it contributed to the defined benefit scheme for ongoing benefits. However, by fixing the contribution level at 31 December 2005 the Company now has a predictable cost for future service without bearing investment or mortality risk.

The Company retains the risk on employee service in the defined benefit scheme prior to 31 December 2005. By closing the scheme to future accrual the deficit on an ongoing valuation basis was reduced to a net present value of £2.5 million as at 5 April 2005. The Company has agreed with the trustees to pay

off this deficit in equal monthly instalments of £50,000 over the next five years. However, in the future there is a risk that investment performance and mortality may differ, either favourably or unfavourably, from current assumptions. The Company has therefore not eliminated all the risks associated with the scheme, but it has reduced them compared to leaving the scheme open to future benefit accrual.

Treasury

In 2005 average exchange rates did not change significantly compared to 2004. However, with most of the costs of the business being in sterling and the majority of sales being in euros and US dollars the Group has a significant foreign exchange exposure. The Board therefore has defined policies and procedures relating to treasury management. These are designed to provide appropriate business support, consistency of reporting and to mitigate risk. Foreign currency hedges are used to reduce the foreign currency exposure based on a proportion of the next six month's anticipated sales. Translation exposure is not hedged. Interest rates on borrowings are all based on variable rates plus a bank margin

and are unhedged as the interest rate risk is not, at present, considered material.

Accounting policies

During the year the Group adopted International Financial Reporting Standards for the first time. Full details of the adjustments on transition and of the principal differences can be found in the Appendix: Explanation of Transition to IFRS on page 50. The accounting policies now adopted are set out in detail in note 1 to the financial statements on page 34.

Going concern statement

After making enquiries, the Directors have a reasonable expectation that the Group has 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.



C G Hurst
Finance Director
13 March 2006

Earnings per share excluding exceptional items

3.2 3.5

2.0

Exchange rates

	2005		2004	
	Average	Year end	Average	Year end
US Dollar/Sterling	1.82	1.72	1.83	1.92
Euro/Sterling	1.46	1.46	1.47	1.41

2003 under UK GAAP, 2004-5 under IAS. See appendix on page 50 for explanation of principal differences.

DIRECTORS AND ADVISERS

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1. Bill Fairservice PhD BSc#

Non-executive Chairman and Chairman of the Nominations Committee, age 65
Led the MBO of Zotefoams from BP Chemicals in 1992, when he became Managing Director of Zotefoams Limited and later Zotefoams plc. Appointed Chairman in January 1999. Relinquished his executive role and became part-time Chairman in July 2001. Previously spent most of his working career with BP Chemicals in a number of technical, production and business management roles.

2. David Stirling BSc CA MBA MSc Managing Director, age 39

Joined Zotefoams plc in September 1997 as Finance Director. Appointed Managing Director in May 2000. Previously with BICC plc, Price Waterhouse in USA and Poland and KPMG. A graduate of Warwick and London Business Schools.

5. Nigel Howard BSc ARCS*†#

Non-executive Director and Chairman of the Remuneration Committee, age 60
Joined the Board in January 2006. Previously a Director of Morgan Crucible Plc where he worked for over 36 years in a number of roles including Interim Chief Executive. He is a non-executive Director of Alliance One International Inc. which is listed on the New York Stock Exchange. He is a graduate of Harvard Business School ISMP program.

6. Anthony Eldrett MBA

Operations and Projects Director, age 61
A Director since the MBO in September 1992. Previously employed by BP Chemicals for a number of years, holding wide ranging positions in human resources, health and safety, engineering projects and operations management.

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London EC3A 6HA

Auditors

KPMG Audit Plc
1 Forest Gate
Brighton Road
Crawley RH11 9PT

Bankers

Barclays Bank PLC
1 Churchill Place
London E14 5HP

Solicitors

Lawrence Graham LLP
190 Strand
London WC2R 1JN

Collyer-Bristow

4 Bedford Row
London WC1R 4DF

Registrars

Computershare Investor Services PLC
PO Box 82
The Pavilions
Bridgwater Road
Bristol BS99 7NH
www.computershare.com

Corporate brokers

Evolution Securities Ltd
100 Wood Street
London EC2V 7AN

3. Clifford Hurst BA FCA MCT

Finance Director and
Company Secretary, age 43

Joined Zotefoams plc in October 2000 from
Thermos Limited where he was Commercial
Director and prior to that Finance Director.
Previously with Caradon plc (now Novar plc),
ICI plc and Ernst & Young.

He is a governor of Harrow College of
Further Education.

4. Chris Ryan BSc FiChemE CEng*†#

Non-executive Director, age 59

Appointed to the Board in December 1999.
Formerly Managing Director of Air Products PLC
and Senior Vice President of Air Products
and Chemicals Inc. with responsibility for
Air Products' European Gases businesses.

He is a graduate of the Harvard Business
School ISMP Program and was previously
based in the USA for five years, with global
accountability for Air Products' Electronics
Business, as well as Corporate Planning
and Strategy.

7. Roger Lawson FCA*†#

Senior independent non-executive
Director and Chairman of the Audit
Committee, age 60

Appointed to the Board in December 2002.
Previously a Director of 3i plc and a former
President of the Institute of Chartered
Accountants in England and Wales.

He is a non-executive Director of a number
of unlisted companies and a trustee of the
Thalidomide Trust.

* Member of the Remuneration Committee

† Member of the Audit Committee

Member of the Nominations Committee

DIRECTORS' REPORT

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

Principal activity

The Group's principal activity is the manufacture and distribution of cross-linked block foams. A review of activities during the financial year and future developments is presented on pages 2 to 11 of the annual report.

Results and dividends

Profit attributable to shareholders for the year amounted to £2.4 million (2004: £1.2 million). An interim dividend of 1.5p (2004: 1.5p) net per share was paid on 30 September 2005. The Directors recommend that a final dividend of 3.0p (2005: 3.0p) net per share be paid on 26 May 2006 to shareholders who are on the Company's register at the close of business on 28 April 2006.

Directors

All the current Directors named on pages 12 to 13 served throughout the year, except for N G Howard, who was appointed on 1 January 2006. In addition J C Marley was a Director throughout the year retiring on 31 December 2005. The Directors retiring by rotation at the Annual General Meeting are A Eldrett, R H Lawson and C J Ryan who, being eligible, offer themselves for re-election. N G Howard, who was appointed a Director since the last Annual General Meeting, being eligible, also offers himself for re-appointment at the Annual General Meeting. A Eldrett has a service contract which is terminable on twelve months' written notice, and R H Lawson C J Ryan and N G Howard have service contracts terminable on six months' written notice. Biographical details of A Eldrett, R H Lawson, C J Ryan and N G Howard can be found in the section on Directors and Advisers on pages 12 to 13.

Employees

To ensure employee welfare, the Group has documented and well-publicised policies on occupational health and safety, the environment and training. It operates an equal opportunities, single status employment policy, together with an open management style. The Company operates to a number of recognised industry standards including Quality (ISO 9001), Environmental (ISO 14001) and Occupational Health and Safety (OHSAS 18001) approvals.

Substantial shareholdings

As at 10 March 2006, the Company had received notice of the following material interests of 3% or more in the issued ordinary share capital.

	Ordinary share of 5p	Percentage of issued share capital
Schroder Investment Management	4,417,325	12.16%
Liontrust Asset Management Ltd	4,029,608	11.09%
Alveo AG (a subsidiary of Sekisui Chemical Co Ltd)	3,465,762	9.54%
Third Advance Value Realisation Company Limited	1,854,192	5.11%
H T Troplast AG	1,429,992	3.94%

The holding held by Schroder Investment Management includes beneficial and non-beneficial interests. The non-beneficial interests include holdings held on behalf of the Mineworkers Pension Scheme (2,625,000 shares, 7.23%) and British Coal Staff Superannuation Scheme (2,041,612 shares, 5.62%).

Directors' shareholdings are shown in the Report of the Board of Directors on Directors' Remuneration.

Research and development

The amount spent by the Group on R&D in the year was £776,000 (2004: £734,000). This included work on PVDF, nylon and silicone as well as potential longer-term products in the development pipeline. In the opinion of the Directors none of this expenditure met the requirements for capitalisation in IAS 38 and it was consequently expensed in the Consolidated Income Statement.

Creditor payment policy

It is not Group policy to follow any standard or code of payment practice. Payment terms are agreed with suppliers when negotiating contracts or transactions. The Group aims to ensure that subject to any necessary variations which may result from supplier-related problems, the agreed payment terms are adhered to. At 31 December 2005, trade creditors of the Company represented 28 days of purchases (2004: 33 days).

Share capital and reserves

Changes to the issued share capital during the year are due to exercised employee share options. Movements in reserves are shown in note 19 to the financial statements.

Treasury and financial instruments

Information in respect of the Group's policies on financial risk management objectives, including policies for hedging, as well as an indication of exposure to financial risk is given on page 11 and in note 20 to the financial statements.

Pension scheme

Zotefoams plc closed its defined benefit pension scheme to new entrants in October 2001 and offers new joiners membership of a defined contribution pension scheme instead. Following the tri-annual actuarial valuation of the defined benefit scheme in April 2005 the Company, after a period of consultation, took the decision to close the defined benefit scheme to future accrual of benefit effective from 31 December 2005. Employees who were members of the defined benefit pension scheme were offered an alternative defined contribution scheme.

Charitable and political donations

The Group made US \$2,000 of charitable contributions and no political contributions in the year.

Auditors

A resolution to re-appoint KPMG Audit Plc as the Company's auditor will be proposed at the forthcoming Annual General Meeting.

By order of the Board


C G Hurst
Secretary
13 March 2006

REPORT OF THE BOARD OF DIRECTORS ON DIRECTORS' REMUNERATION

This report has been prepared in accordance with Schedule 7A of the Companies Act 1985. The report also meets the relevant requirements of the Listing Rules of the Financial Services Authority and describes how the Board has applied the principles relating to Directors' remuneration. As required by the Act, a resolution to approve the report will be proposed at the Annual General Meeting of the Company at which the financial statements will be approved.

The Act requires the auditor to report to the Company's members on certain parts of the Directors' Remuneration Report and to state whether in their opinion those parts of the report have been properly prepared in accordance with the Companies Act 1985. The report has therefore been divided into separate sections for audited and unaudited information.

INFORMATION NOT SUBJECT TO AUDIT

Remuneration Committee

The Company has established a Remuneration Committee which is constituted in accordance with the recommendations of the Combined Code except that its Chairman J C Marley completed 10 years' service with the Company in August 2005 and may not be considered independent under the guidelines of the Code. However, as explained in the Corporate Governance Statement, the Board believes that J C Marley was independent in the period before his retirement on 31 December 2005. He has been replaced on the Committee and as chair of the Committee by N G Howard from 1 January 2006. N G Howard attended a meeting of the Committee in December 2005 as an observer in order to facilitate this handover. The other members of the Committee during 2005, apart from J C Marley, were R H Lawson and C J Ryan who are independent non-executive Directors.

None of the Committee has any personal financial interest (other than as shareholders), conflicts of interest from cross-directorships or day-to-day involvement in running the business. The Committee makes recommendations to the Board. No Director plays a part in any discussion about his remuneration.

In determining aspects of the Directors' remuneration for the year, the Committee consulted W H Fairservice (Chairman) and D B Stirling (Managing Director) about its proposals. The Committee made reference to independent surveys of Directors' remuneration although the scope of the Committee was limited by the rules of the Takeover Panel as the Company was in discussions regarding a potential takeover approach for most of the year.

Remuneration policy for the executive Directors

Executive remuneration packages are prudently designed to attract, motivate and retain Directors of the high calibre needed to maintain the Group's position as a market leader and to reward them for enhancing value to shareholders. The performance measurement of the executive Directors and key members of senior management and the determination of their annual remuneration package are undertaken by the Committee.

There are five main elements of the remuneration package for executive Directors and senior management:

- basic salary;
- benefits;
- annual bonus plan;
- long-term incentive schemes; and
- pension arrangements.

The Company's policy is that a substantial proportion of the remuneration of the executive Directors should be performance related. As described below, executive Directors may earn annual incentive payments which are capped as a percentage of basic salary together with the benefits of participation in share option schemes.

Basic salary

An executive Director's basic salary is reviewed by the Committee at the beginning of each year and when an individual changes position or responsibility. In deciding appropriate levels the Committee considers the Group as a whole, individual performance and independent surveys of Directors' remuneration. The scope of the Committee to make salary awards in 2005 was restricted by the rules of the Takeover Panel as the Company was in discussions regarding a potential takeover approach for most of the year. Basic salaries were increased on 1 March 2005.

Benefits

The executive Directors receive certain benefits, principally a car allowance and private medical insurance.

Annual bonus payments

The Committee establishes the objectives that must be met for each financial year if a cash bonus is to be paid. In setting appropriate bonus levels the Committee refers to independent surveys of Directors' remuneration. The Committee believes that any incentive compensation awarded should be tied to the interests of the Company's shareholders and that the principal measure of those interests is growth in profit before taxation. Executive Directors, other than the Managing Director, are also set personal objectives the non-achievement of which can restrict the bonus award made. The bonus award is capped at 100% of basic salary. Incentive payments under the scheme for the year ended 31 December 2005 varied between 28% and 30% of basic salary for the executive Directors. Profit before taxation, excluding exceptional items increased by 40%.

The Company was in discussions regarding a potential takeover approach for most of the year. This resulted in an exceptional workload for the Managing Director and Finance Director. The Committee therefore decided at the end of the year to award an exceptional bonus of £10,000 each to these two individuals in recognition of the additional effort required in relation to this approach whilst continuing successfully to improve the business performance.

REPORT OF THE BOARD OF DIRECTORS ON DIRECTORS' REMUNERATION

Share options

The Committee has responsibility for supervising the operation of the Executive Share Option Scheme and the grant of options under its terms. The performance condition that the Committee has selected is growth in normalised earnings per share excluding exceptional items. This performance criterion, which applies to all executive Directors to whom options have been granted under the scheme, was chosen because the Committee believes it best aligns this incentive with shareholder interests. The Company's policy is to phase the granting of share options by annual awards of up to a maximum of 1.5 times salary rather than to award them in a single large block to any individual. Options granted under the scheme are normally exercisable no earlier than three years from the date of grant and no later than ten years from the date of the grant. The scheme incorporates a clause so that it is agreed with the individual, before they are granted an option, that the Company will transfer its National Insurance Contributions (NICs) liability to the individual, or it will recover any NICs paid in this regard upon the exercise of an option from the individual.

UK based executive Directors and senior management have been granted share options under a Her Majesty's Revenue and Customs Approved Share Option Scheme. These options are not exercisable unless the Group's normalised earnings per share, excluding exceptional items, increases by at least six percentage points in excess of the increase in the Retail Price Index over the same period.

The exercise price of the options granted under the above schemes is equal to the market value of the Company's share price at the time when the options are granted. The Company also operates a SAYE Share Option Scheme for eligible employees under which options may be granted at a discount of up to 20% of market value. The executive Directors are entitled to participate provided they meet the eligibility requirements of the scheme.

The Company does not operate any long-term incentive schemes other than the share option schemes described above. No significant amendments are proposed to be made to the terms and conditions of any entitlement of a Director to share options. However, if in the future other performance criteria prove to be more appropriate, these may be imposed instead, provided they satisfy the guidelines of institutional shareholders.

Pension arrangements

The executive Directors were active members of the Company's defined benefit pension scheme. These pension arrangements provided for a pension on retirement of two-thirds of basic salary (subject to HMRC limits) after 40 years' eligible service. Their dependants are eligible for dependants' pensions and the payment of a lump sum in the event of death in service. No other payments to Directors are pensionable.

This pension scheme closed to future accrual of benefits on 31 December 2005. The executive Directors became deferred members of the scheme as at that date and joined the Zotefoams Defined Contribution Alternative Pension Scheme on 1 January 2006.

The Zotefoams Defined Contribution Alternative Pension Scheme is a stakeholder pension plan. Contributions to the plan have been calculated by an actuary to give a similar benefit to that which the member might have expected when they retired under the previous Defined Benefit Scheme as at 31 December 2005. However, the contributions made by the Company will not change in the future other than an increase of 3% every five years until the member reaches his 65th birthday. Individual contributions are set at 5% of pensionable salary while the Company contribution reflects age, sex, salary level at 31 December 2005 and other actuarial factors. The calculation made by the actuary was the same for the executive Directors as that made for other employees of the Company. The Company contributions are 6.75% of pensionable salary for D B Stirling, 20.00% of salary for A Eldrett and 10.75% for C G Hurst.

Performance Graph

The following graph charts the total cumulative shareholder return (share price movements plus dividends reinvested) of the Company since January 2000. It is compared to the FTSE All-Share Index which the Board believes is the most relevant comparison for a company of Zotefoams' size.

Zotefoams plc and FTSE All-Share Total Return Index ("TRI") re-based to 100 (January 2000 to December 2005)

Service contracts

The executive Directors have service contracts with the Company which are terminable on twelve months' written notice from the Company or the respective Director.

The non-executive Directors have three year contracts which can be terminated by the Director or the Company on six months' written notice.

The service agreements between each of the Directors and the Company do not entitle the respective Director to payment of compensation on termination other than statutory compensation.

Non-executive Directors

All independent non-executive Directors have specific terms of engagement and their remuneration is determined by the Board within the limits set by the Articles of Association and based on independent surveys of fees paid to non-executive Directors of similar companies. Independent non-executive Directors cannot participate in any of the Company's share options schemes and are not eligible to join the Company's pension scheme. In 2005 the discussions regarding a potential takeover approach which went on for most of the year imposed an abnormal burden on the independent non-executive Directors and the Board approved an exceptional bonus of £5,000 each for the three independent non-executive Directors in recognition of this additional workload.

The Chairman, although now a non-executive Director, was a former executive Director of the Company and therefore continued his involvement in the Company Defined Benefit Pension Scheme up to 2 November 2005 when he reached 65 and became a deferred member of the scheme. Company contributions to his pension arrangements ceased when he reached 65. He remains eligible for private medical insurance which was continued as a benefit when he took a non-executive role. His remuneration is set by the Remuneration Committee with reference to independent surveys of chairman positions in other similar companies and approved by the full Board excluding the Chairman.

INFORMATION SUBJECT TO AUDIT Directors' emoluments

Remuneration in £	Basic salary /fees	Operational bonus	Bonus/fees in relation to bid approach	Car allowance	Other benefits	Total 2005	Total 2004
W H Fairservice	52,350	—	—	—	2,169	54,519	52,591
D B Stirling	122,756	37,300	10,000	11,584	813	182,453	134,276
A Eldrett	93,939	27,390	—	10,510	1,953	133,792	104,669
C G Hurst	88,786	25,600	10,000	10,510	1,136	136,032	98,652
N G Howard	—	—	—	—	—	—	—
R H Lawson	20,600	—	5,000	—	—	25,600	20,600
J C Marley	23,227	—	5,000	—	—	28,227	23,227
C J Ryan	20,059	—	5,000	—	—	25,059	20,059
	421,717	90,290	35,000	32,604	6,071	585,682	454,074

Note:

- 1) Other benefits are calculated in terms of taxable values in the UK.
- 2) J C Marley retired from the board on 31 December 2005.
- 3) N G Howard was appointed to the Board on 1 January 2006.

Directors' shareholdings

The beneficial and non-beneficial interests of the Directors (including persons connected with them within the meaning of Section 346 of the Companies Act 1985) in the ordinary shares of the Company are set out below:

Number of ordinary 5p shares	31 December 2005	31 December 2004
W H Fairservice	1,087,752	1,087,250
D B Stirling	40,962	28,625
A Eldrett	904,000	938,358
C G Hurst	37,366	25,029
N G Howard	Nil	Nil
R H Lawson	5,000	5,000
J C Marley	40,208	40,208
C J Ryan	20,000	20,000
	2,135,288	2,144,470

There have been no changes to Directors' interests between the end of the financial year and the date of this report.

REPORT OF THE BOARD OF DIRECTORS ON DIRECTORS' REMUNERATION

Share options

Options over ordinary shares granted:

		As at 31 December 2004	Granted	Exercised	Lapsed	As at 31 December 2005	Exercise price	Exercisable	Expiry date
D B Stirling	Savings related SOS	12,337	—	12,337	—	—	77.0p	1.6.2005	1.12.2005
C G Hurst	Savings related SOS	12,337	—	12,337	—	—	77.0p	1.6.2005	1.12.2005
D B Stirling	HMRC SOS	37,500	—	—	—	37,500	80.0p	18.3.2006	17.3.2013
A Eldrett	HMRC SOS	37,500	—	—	—	37,500	80.0p	18.3.2006	17.3.2013
C G Hurst	HMRC SOS	41,379	—	—	—	41,379	72.5p	7.4.2007	6.4.2014
D B Stirling	Executive SOS	210,093	—	—	210,093	—	80.5p	20.8.2005	19.8.2012
A Eldrett	Executive SOS	161,731	—	—	161,731	—	80.5p	20.8.2005	19.8.2012
C G Hurst	Executive SOS	148,975	—	—	148,975	—	80.5p	20.8.2005	19.8.2012
D B Stirling	Executive SOS	217,748	—	—	—	217,748	80.0p	18.3.2006	17.3.2013
A Eldrett	Executive SOS	167,624	—	—	—	167,624	80.0p	18.3.2006	17.3.2013
C G Hurst	Executive SOS	154,403	—	—	—	154,403	80.0p	18.3.2006	17.3.2013
D B Stirling	Executive SOS	246,280	—	—	—	246,280	72.5p	7.4.2007	6.4.2014
C G Hurst	Executive SOS	178,895	—	—	—	178,895	72.5p	7.4.2007	6.4.2014
A Eldrett	Executive SOS	189,589	—	—	—	189,589	72.5p	7.4.2007	6.4.2014
D B Stirling	Executive SOS	—	240,584	—	—	240,584	77.0p	22.12.2008	21.12.2015
A Eldrett	Executive SOS	—	183,896	—	—	183,896	77.0p	22.12.2008	21.12.2015
C G Hurst	Executive SOS	—	173,863	—	—	173,863	77.0p	22.12.2008	21.12.2015

Savings Related (SAYE) Share Option Scheme

UK resident Directors and UK based employees of the Company with a contractual working week of at least 20 hours and at least one year's service are eligible to participate in Zotefoams' Savings Related (SAYE) Share Option Scheme.

HMRC Approved Share Option Scheme (HMRC SOS)

These options have been granted under a HMRC Approved Share Option Scheme. These options are not exercisable unless the Group's earnings per share, before exceptional items, increases over a three year period by at least six percentage points in excess of the increase in the Retail Price Index over the same period.

Executive Share Option Scheme

These options have been granted under the Zotefoams Executive Share Option Scheme. These options are not exercisable unless the Group earnings per share, before exceptional items, increase by a percentage in excess of the increase in the Retail Price Index over a three year period. Further conditions control the amount of shares available under these options. The option awards are reduced by one-third or two-thirds if certain thresholds are not reached. The thresholds are as follows:

Executive share options exercisable in	Percentage increase above RPI needed for:		
	Full award	Two-third award	One-third award
2005	40%	30%	20%
2006	40%	30%	20%
2007	300%	200%	100%
2008	200%	150%	100%

So, for example, if the Retail Price Index increased by 9% from 2002 to 2005 a 49% increase in earnings per share over the three year period 2002 to 2005 would be required for the 2005 options to become capable of being exercised in full.

There have been no changes in options granted between the end of the year and the date of this report.

The middle market quoted share price at 30 December 2005 was 75.5p and the high and low prices during the year were 95p and 68.5p respectively.

Directors' pension entitlements

The following Directors have accrued final salary benefits in the Zotefoams Defined Benefit Pension Scheme over the last Company year:

	Accrued pension in scheme at year end ⁽¹⁾ £	Gross increase in pension £	Increase in accrued pension net of inflation £	Value of accrued pension at year end ⁽²⁾ £	Value of accrued pension at start of year £	Total change in value over period less Directors' contributions ⁽³⁾ £
W H Fairservice*	21,253	2,080	1,562	386,800	318,063	62,208
D B Stirling	14,538	2,065	1,728	84,727	58,639	19,559
A Eldrett	55,672	2,992	1,570	816,965	682,677	128,473
C G Hurst	7,375	1,617	1,462	49,443	31,645	12,318

* non-executive Director

Notes

- 1) The pension entitlement shown is that which would be paid annually on retirement at normal retirement age (or immediately upon late retirement), based on service to the end of the year and excluding any future increases under the rules of the Scheme.
- 2) Transfer values have been calculated in accordance with version 9.2 of guidance note GN11 issued by the Institute and Faculty of Actuaries, on the basis agreed with the Trustees of the Pension Scheme.
- 3) The change in the transfer value over the year includes the effect of fluctuations in the transfer value due to factors beyond the control of the Company and Directors, such as changes in financial conditions. It is calculated after deducting the Directors' contributions.

The following is additional information relating to Directors' pensions:

- a) Members of the Scheme have the option of paying Additional Voluntary Contributions (AVCs). The value of these AVCs has been excluded from the above figures.
- b) Normal retirement age is 65.
- c) A spouse's pension is payable on death in service equal to one-third of the member's annual salary at death.

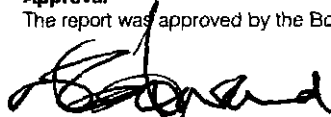
On death after leaving service and before retirement, a spouse's pension is payable of one-half of the member's preserved pension at leaving, revalued from leaving to the date of death, in line with statutory revaluation increases.

On death in retirement, a spouse's pension is payable of one-half of the member's pension at death, without reduction for any part of the member's pension surrendered for cash at retirement.

- d) Members' guaranteed minimum pension increase at statutory rates. Other pensions increase at the lesser of 5% per annum or the increase in the Retail Price Index.

Approval

The report was approved by the Board of Directors on 13 March 2006 and signed on its behalf by:



N G Howard
Non-executive Director and Chairman of the Remuneration Committee
13 March 2006

AUDIT COMMITTEE REPORT

Summary of the role of the Audit Committee

The Audit Committee is appointed by the Board and includes the independent non-executive Directors of the Company. J C Marley completed ten years' service with the Company in 2005 and may not be considered, under the guidelines of the Code, independent. However, as explained in the Corporate Governance Statement, the Board believes that J C Marley was independent in this period before his retirement on 31 December 2005. He has been replaced on the Committee by N G Howard from 1 January 2006. The Audit Committee's terms of reference include all matters indicated by the Combined Code. The terms of reference are considered annually by the Audit Committee and are then referred to the Board for approval.

The Audit Committee is responsible for:

- monitoring the integrity of the financial statements of the Group and any formal announcements relating to the Group's financial performance and reviewing significant financial reporting judgements contained therein;
- reviewing the external auditor's management letter and management responses;
- reviewing the Group's internal controls and risk management systems;
- reviewing the arrangements by which staff may, in confidence, raise concerns about possible improprieties ('the whistleblowing policy');
- assessing the need for an internal audit function;
- making recommendations to the Board, for a resolution to be put to the shareholders for their approval in general meeting, in relation to the appointment of the external auditor and the approval of the remuneration and terms of engagement of the external auditor;
- reviewing and monitoring the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements; and
- developing and implementing a policy on the engagement of the external auditor to supply non-audit services, taking into account relevant guidance regarding the provision of non-audit services by the external audit firm.

The Audit Committee is required to report its findings to the Board, identifying any matters in respect of which it considers that action or improvement is needed, and make recommendations as to the steps to be taken.

Composition of the Audit Committee

The members of the Audit Committee in 2005 were R H Lawson, J C Marley and C J Ryan. J C Marley retired from the Committee on 31 December 2005 and was replaced by N G Howard. R H Lawson, C J Ryan and N G Howard are independent non-executive Directors. R H Lawson is Chairman of the Committee and is a Fellow of the Institute of Chartered Accountants in England and Wales. The Committee is normally comprised of three members, with a minimum of two members at any time. Two members constitute a quorum.

The Audit Committee structure requires the inclusion of one financially qualified member with relevant financial experience. Currently the Audit Committee Chairman fulfils this requirement. All Audit Committee members are expected to be financially literate. The Company provides training if required.

Meetings

The Audit Committee is required to meet at least twice per year and has an agenda linked to events in the Company's financial calendar. The agenda is predominantly cyclical and is therefore approved by the Audit Committee Chairman on behalf of his fellow members. Each Audit Committee member has the right to require reports on matters of interest in addition to cyclical items.

The Audit Committee invites the Company Chairman, Managing Director, Finance Director, Financial Controller and senior representatives of the external auditor to attend relevant meetings, although it reserves the right to request any of these individuals to withdraw. For part of a meeting each year it meets with senior representatives of the external auditor without anyone else being present. Other senior management may be invited to present such reports as are required for the Committee to discharge its duties.

Overview of the actions taken by the Audit Committee to discharge its duties

Since the beginning of 2005 the Audit Committee has:

- reviewed the financial statements in the 2004 and 2005 reports and accounts and the interim report issued in August 2005. As part of this review the Committee received reports from the external auditor on the audit of the annual reports and accounts and the review of the interim report;
- considered the output from the Group-wide process used to identify, evaluate and mitigate high level business risks;
- reviewed the effectiveness of the Group's internal controls (including, but not limited to, financial controls) and disclosures made in the annual report on this matter;
- reviewed and agreed the scope of the audit work to be undertaken by the external auditor;
- monitored the work being undertaken by the Group in preparation for the introduction of International Financial Reporting Standards;
- considered the views of the external auditor on the effectiveness of the Group's internal financial controls;
- agreed the fees to be paid to the external auditor for their audit and work on the accounts, interim report and conversion of the Group accounts to International Financial Reporting Standards;
- reviewed its own effectiveness;
- undertaken an assessment of the need for an Internal Audit function; and
- undertaken an evaluation of the independence of the external auditor.

External auditor

The Audit Committee is responsible for the development, implementation and monitoring of the Group's policy on external audit. Although the external auditor is allowed to provide non-audit services the Committee monitors the extent of these services to ensure that they do not compromise the auditor's objectivity. It also assesses the effectiveness of the external auditor in relation to their fulfilment of the agreed audit plan, the robustness and perceptiveness of the auditor in handling key accounting and audit judgements and the thoroughness of the auditor's review of internal financial controls. As a consequence of its satisfaction with the results of these activities the Audit Committee has recommended to the Board that the external auditor should be re-appointed.

Internal audit function

The Audit Committee has reviewed the need for an internal audit function and concluded that given the size of the Group and the proximity of the executive Board members to Group operations an internal audit function covering financial controls is not considered necessary at this time. However, an internal audit function does exist to ensure compliance with procedures for environmental, quality and health and safety procedures. The Audit Committee also maintains an oversight over the Company's whistleblowing policy.

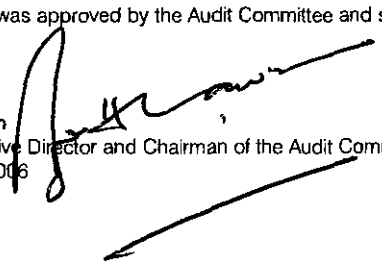
Overview

As a result of its work during the year, the Audit Committee has concluded that it has acted in accordance with its terms of reference and has ensured the independence and objectivity of the external auditor. The Chairman of the Audit Committee will be available at the Annual General Meeting to answer any questions about the work of the Committee.

Approval

This report was approved by the Audit Committee and signed on its behalf by:

R H Lawson
Non-executive Director and Chairman of the Audit Committee
13 March 2006



SAFETY, HEALTH AND ENVIRONMENT ("SHE") REPORT

The Board has separate policies in place relating to Health, Safety and Environment. In line with best practice, the Company is certified to accredited standards OHSAS 18001 on Health and Safety and ISO 14001:2004 the updated International Standard for Environmental Management Systems.

The Board has ultimate responsibility for SHE policy and performance and receives reports on SHE issues on a quarterly basis. Annual performance objectives are agreed by the Board and performance against these objectives is monitored as part of our quarterly reporting programme.

The Operations and Projects Director is directly responsible to the Board for Health, Safety and Environmental performance. Site committees meet quarterly to consider all SHE matters and Steering Committees, chaired by the Managing Director, also meet quarterly to consider overall performance and the impact of current and impending legislation. A Health and Safety Adviser and an Environmental Adviser support these groups.

Senior managers are responsible for ensuring that SHE policies are implemented in their departments, all employees are informed of the departmental requirements and departmental training on environmental issues and safe working practices is up to date. Regular audits are conducted to ensure policy and procedure implementation is appropriate. All employees are aware that primary responsibility for safety lies with the employee.

Health and safety performance

The operational environment at Zotefoams contains few controlled substances and our manufacturing plant involves mainly manual handling and materials processing. The risks to our process are assessed whenever new or altered equipment or materials are introduced and at regular periods thereafter. The most strictly controlled parts of our sites are where pressure is used.

Operating vessels at high pressures, Zotefoams is subject to the Pressure Systems Safety Regulations 2000 in the UK and OSHA in the US. Tightly defined procedures and operational controls are in place to manage the safety of our pressure systems. Fail-safe mechanisms known as Pressure Relief Valves (PRV's) and bursting disks, which are the equivalent of fuses in an electrical system, are designed and installed into our pressure systems. Failure of a PRV or bursting disk leads to depressurisation of sections of our system releasing nitrogen gas into the atmosphere and mitigating any further risks.

During the year reportable injuries reduced from 5 to 3.

However as a result of an internal campaign encouraging employees to report all injuries, no matter how small, the number of minor injuries rose from the low level of 2004 to historically typical levels in 2005.

We take reporting of all incidents very seriously, including "near misses" and plant or equipment damage not resulting in personal injury. All events are investigated by appropriate levels of management to establish root cause and to eliminate re-occurrence wherever possible. The Company also operates an internal audit system to supplement the annual audit by accreditation bodies.

Environmental performance

The Board considers the processes used by Zotefoams to be among the most, if not the most, environmentally friendly way to manufacture polymer foams. Our process uses pure nitrogen gas to expand the foams. The common peroxide cross-linking agent, which enhances foam properties, is completely utilised during processing and, importantly, no other chemical additives are present in our basic foam products. The result is that our basic foam products have no toxic or volatile chemicals (such as solid chemical residues, CFC, HCFC or volatile hydrocarbons) remaining in the material structure. Such substances are present in competitive products.

During 2005 the overall environmental performance of the Group remained at the improved level achieved in 2004. The most frequently reported incident remained the releases of nitrogen gas into the air from bursting disks. While Zotefoams record this as an environmental incident principally on the grounds of utility loss and noise, we consider that the safety of our plant is of primary importance and regard these incidents as evidence that our safety processes are functioning as designed.

CORPORATE GOVERNANCE

The Company is committed to the principles of corporate governance contained in the Combined Code on Corporate Governance (the 'Code') for which the Board is accountable to shareholders.

Statement of compliance with the Combined Code

Throughout the year ended 31 December 2005 the Company has been in compliance with the Code provisions set out in Section 1 of the Code except for the following matter:

- J C Marley, the Company's senior independent non-executive Director, completed over ten years' service with the Company in 2005 and therefore under the Code guidelines may no longer be regarded as independent. The Board considered this matter and asked J C Marley to stay longer than envisaged in the Code, as it believed that non-executive Director continuity was in shareholders' interest given that the Board was in discussions regarding potential takeover approaches for most of 2005. These discussions terminated in November 2005 and J C Marley retired from the Board at the end of December 2005. The Board believes that J C Marley functioned as an independent Director though the Code indicates that he may not be considered independent for this time.

Statement about applying the principles of the Code

The Company has applied the principles set out in Section 1 of the Code, including both the main principles and the supporting principles, by complying with the Code as reported above. Further explanation of how the principles and supporting principles have been applied is set out below and in the Report of the Board of Directors on Directors' Remuneration and the Audit Committee Report.

Board effectiveness

The Board's role is to provide the entrepreneurial leadership of the Company within a framework of prudent and effective controls which enable risk to be assessed and managed. The Board sets the strategic aims of the Company, ensures that the necessary resources are in place to achieve the Company's objectives and reviews management performance. The Board's role is to act as representative of the shareholders, who are the Company's owners and focuses on the governance of the Company. Management is delegated to the executive Directors and the senior executive management of the Group.

The Board has three major committees which report into it and function within defined terms of reference. These are the Audit Committee, the Remuneration Committee and the Nominations Committee. Attendance details for 2005 by the Directors for meetings of the Board and these Committees are shown below:

Attendance at meetings	Full Board meetings	Audit Committee meetings	Remuneration Committee meetings	Nomination Committee meetings
Total number of meetings	8	3	3	2
W H Fairservice	8	n/a	n/a	2
D B Stirling	8	n/a	n/a	n/a
A Eldrett	7	n/a	n/a	n/a
C G Hurst	8	n/a	n/a	n/a
R H Lawson	8	3	3	2
J C Marley	8	3	3	2
C J Ryan	7	2	3	2

Chairman and Managing Director

The Chairman is responsible for leadership of the Board, ensuring its effectiveness on all aspects of its role and setting its agenda. The Chairman is also responsible for ensuring that the Directors receive accurate, timely and clear information. The Chairman facilitates the effective contribution of the non-executive Directors in particular and ensures constructive relations between executive and non-executive Directors.

The Managing Director is responsible for the running of the Company's business. He is supported by the other executive Directors and senior management team members in the Group.

Board balance and independence

The Board structure comprises three executive Directors, three independent non-executive Directors and a non-executive Chairman. J C Marley completed ten years' service as a non-executive Director in August 2005. Given his length of service he may not be considered as being truly independent according to the Code guidelines. He retired from the Board in December 2005.

The Chairman, W H Fairservice, is a former Managing Director of the Company. He works in a non-executive capacity and is not a member of the two major Board committees – Remuneration and Audit.

No one other than the Committee Chairman and members is entitled to be present at a meeting of the Remuneration, Audit and Nomination Committees, but others may attend at the invitation of the Committees. During the year the Chairman met with the non-executive Directors without the executive Directors present.

Appointments to the Board

Appointments to the Board are proposed by the Nominations Committee which is comprised of the Chairman and the independent non-executive Directors. J C Marley was Chairman of the Committee in 2005. He was replaced on 1 January 2006 as a Committee member by N G Howard and as Chairman of the Committee by W H Fairservice.

The Nominations Committee operates within a defined set of terms of reference from the Board and is responsible for managing the recruitment of new Board members within a specification set by the Board. Appointments to the Board are made on merit and against objective criteria. Care is taken to ensure that appointees have enough time to devote to the job.

Following the retirement of J C Marley, the Nominations Committee received some nominations from the Company's Financial Advisors on potential replacements. Given that one of these candidates, N G Howard, met the specification precisely the Committee decided not to proceed with the use of an external search consultancy or open advertising.

CORPORATE GOVERNANCE

Information and professional development

Each month all Directors receive management reports and briefing papers in relation to Board matters. New appointments to the Board receive an induction and, if appropriate, training. Training is available subsequently in order to fulfil the requirements of being a Director of a listed company. All the Directors have access to the Company Secretary and independent professional advice at the Company's expense if required for the furtherance of their duties.

Board evaluation

A formal review of Board and Committee performance is carried out annually. The Chairman's performance is reviewed by the other non-executive Directors in consultation with the executive Directors. The other non-executive Directors performance is evaluated by the Chairman in consultation with the executive Directors. Executive Directors performance is evaluated by the Remuneration Committee in conjunction with the Chairman and the Managing Director (except in the case of the Managing Director, when the Managing Director is not present).

Re-election

Re-election of Board members is required at the first Annual General Meeting following appointment and at least every three years thereafter. At the Annual General Meeting in 2006 four Directors will stand for re-election:

- A Eldrett, having completed a three year term;
- R H Lawson, having completed a three year term;
- C J Ryan, having completed a three year term; and
- N G Howard, following his appointment in January 2006.

As required under the Code in the case of a non-executive Director standing for re-election the Board confirms, that following a formal performance evaluation R H Lawson's and C J Ryan's performance continues to be effective and they continue to demonstrate a commitment to the role. This would be R H Lawson's second and C J Ryan's third term as a non-executive Director following their initial appointments to the Board in 2002 and 1999 respectively.

Remuneration

The principles and details of remuneration policy are set out in the Report of the Board of Directors on Directors' Remuneration.

Financial reporting

The Directors' responsibilities for preparing the financial statements are set out in the Statement of Directors' Responsibilities.

Audit Committee and auditors

A separate Audit Committee Report provides details of the role and activities of the Committee and its relationship with the external auditor.

Relations with shareholders

Meetings with institutional shareholders are held twice a year following announcement of the Group's interim and final results. Other meetings may be held at institutional shareholder request. To ensure that the Board, particularly the non-executive Directors, understand the views of major shareholders, the Company's brokers provided a summary of feedback from the meetings following the interim and final results announcements. The Chairman, Senior Independent Director (R H Lawson) and the other non-executive Directors will attend meetings with major shareholders if requested.

The Board considers the annual report and financial statements and Annual General Meeting to be the primary vehicles for communication with private investors. The members of the Audit and Remuneration Committee will normally be present to speak at the Annual General Meeting. The corporate website www.zotefoams.com contains information on the Company.

Internal control

The Board is ultimately responsible for the Group's system of internal control and for reviewing its effectiveness. However, such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can provide only reasonable and not absolute assurance against material misstatement or loss.

The Combined Code requires that the Directors review the effectiveness of the Group's system of internal controls. This review should cover all controls including financial, operational, environmental, health and safety, compliance and risk management.

The Board confirms there is an ongoing process for identifying, evaluating and managing significant risks faced by the Company, that it has been in place for the year under review and up to the date of approval of the annual report and accounts, that it is regularly reviewed by the Board and accords with the guidance of the Combined Code.

Key elements of the Group's system of internal controls are as follows:

Control environment

The Group is committed to the highest standards of business conduct and seeks to maintain these standards across all of its operations throughout the world. The Group has adopted a Code of Business Conduct, approved by the main Board, which provides practical guidance for all staff. This guidance is included in the employee handbook and incorporated into an induction process which all employees must complete.

The Group has an appropriate organisational structure for planning, executing, controlling and monitoring business operations in order to achieve Group objectives. Overall business objectives are set by the Board and communicated through the organisation. Lines of responsibility and delegations of authority are documented.

Risk identification

Group management are responsible for the identification and evaluation of key risks applicable to their areas of business. These risks are assessed on a continual basis and may be associated with a variety of internal or external sources including control breakdowns, disruption in information systems, competition, natural catastrophe and regulatory requirements.

Information and communication

Annual budgets are a key part of the planning process and performance against plan is actively monitored at Board level supported by quarterly forecasts. Statistics and commentary on actual operating performance are made available to all Directors monthly, and forecasts are presented to the Board quarterly.

Through these mechanisms, Group performance is continually monitored, risks identified in a timely manner, their financial implications assessed, control procedures re-evaluated and corrective actions agreed and implemented.

Control procedures

The Group has implemented control procedures designed to ensure complete and accurate accounting for financial transactions and to limit the potential exposure to loss of assets or fraud. Measures taken include physical controls, segregation of duties, reviews by management, and external audit to the extent necessary to arrive at their audit opinion.

A process of control self-assessment and hierarchical reporting has been established which provides for a documented and auditable trail of accountability. These procedures are relevant across Group operations and provide for successive assurances to be given at increasingly higher levels of management and, finally, to the Board. Planned corrective actions are independently monitored for timely completion.

Monitoring and corrective action

There are clear and consistent procedures in place for monitoring the system of internal financial and non-financial controls. The Audit Committee meets at least twice a year and, within its remit, reviews the effectiveness of the Group's system of internal financial controls. The Committee receives reports from external auditors and management.

Non-financial controls are reviewed regularly by executive management who report any issues and corrective actions taken directly to the Board.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Statement of Directors' responsibilities in respect of the annual report and the financial statements

The Directors are responsible for preparing the annual report and the Group and Parent Company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with IFRSs as adopted by the EU and have elected to prepare the Parent Company financial statements on the same basis.

The Group and Parent Company financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position of the Group and the Parent Company and the performance for that period; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

In preparing each of the Group and Parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' Report, Directors' Remuneration Report and the Corporate Governance Statement that comply with that law and those regulations.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

REPORT OF THE INDEPENDENT AUDITOR

to the members of Zotefoams plc

We have audited the Group and Parent Company financial statements (the "financial statements") of Zotefoams plc for the year ended 31 December 2005 which comprise the Group Income Statement, the Group and Parent Company Balance Sheets, the Group and Parent Cash Flow Statements, the Group and Company Statement of Recognised Income and Expense and the related notes. 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 Auditor's 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 auditor

The Directors' responsibilities for preparing the annual report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU are set out in the Statement of Directors' Responsibilities on page 26.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant 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 and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985 and, as regards the financial statements, Article 4 of the IAS Regulation. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, 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 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 other information contained in the annual report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

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 to be audited. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's and 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 to be 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 to be audited.

Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the Group's affairs as at 31 December 2005 and of its profit for the year then ended;
- the Parent Company financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU as applied in accordance with the provisions of the Companies Act 1985, of the state of the Parent Company's affairs as at 31 December 2005; and
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985 and, as regards the financial statements, Article 4 of the IAS Regulation.

KPMG Audit Plc
Chartered Accountants
Registered auditor
13 March 2006

CONSOLIDATED INCOME STATEMENT

for the year ended 31 December 2005

	Note	2005			2004 £000
		Pre- exceptional Items £000	Exceptional items (see note 4) £000	Post- exceptional Items £000	
Revenue	2	27,975	—	27,975	25,176
Cost of sales		(21,640)	—	(21,640)	(19,607)
Gross profit		6,335	—	6,335	5,569
Distribution costs		(1,905)	—	(1,905)	(1,863)
Administrative expenses		(2,407)	1,449	(958)	(2,104)
Operating profit		2,023	1,449	3,472	1,602
Financial income	6	813	—	813	750
Finance costs	6	(997)	—	(997)	(1,043)
Profit before tax		1,839	1,449	3,288	1,309
Taxation	7	(569)	(292)	(861)	(139)
Profit for the year	3, 9	1,270	1,157	2,427	1,170
Attributable to:					
Equity holders of the parent		1,270	1,157	2,427	1,170
Earnings per share					
Basic (p)	8			6.7	3.2
Diluted (p)	8			6.7	3.2

CONSOLIDATED STATEMENT OF RECOGNISED INCOME AND EXPENSE for the year ended 31 December 2005

	2005 £000	2004 £000
Foreign exchange translation differences on investment in foreign subsidiary	846	(576)
Effective portion of changes in fair value of cash flow hedges net of recycling	(79)	—
Actuarial (losses)/gains on defined benefit schemes	(42)	264
Tax on items taken directly to equity	13	(79)
Net income/(expense) recognised directly in equity	738	(391)
Profit for the year	2,427	1,170
Total recognised income and expense for the year	3,165	779
Attributable to equity holders of the Parent	3,165	779

COMPANY STATEMENT OF RECOGNISED INCOME AND EXPENSE for the year ended 31 December 2005

	2005 £000	2004 £000
Effective portion of changes in fair value of cash flow hedges net of recycling	(79)	—
Actuarial (losses)/gains on defined benefit schemes	(42)	264
Tax on items taken directly to equity	13	(79)
Net (expense)/income recognised directly in equity	(108)	185
Profit for the year	2,985	481
Total recognised income and expense for the year	2,877	666
Attributable to equity holders of the Company	2,877	666

CONSOLIDATED BALANCE SHEET

as at 31 December 2005

	Note	2005 £000	2004 £000
Non-current assets			
Property, plant and equipment	10	28,364	29,795
Deferred tax assets	17	132	—
Total non-current assets		28,496	29,795
Current assets			
Inventories	12	3,933	3,126
Trade and other receivables	13	6,182	5,675
Cash and cash equivalents	14	432	298
Total current assets		10,547	9,099
Total assets		39,043	38,894
Equity			
Issued share capital	18	(1,816)	(1,813)
Share premium	19	(13,753)	(13,707)
Capital redemption reserve	19	(5)	(5)
Translation reserve	19	(270)	576
Hedging reserve	19	79	—
Retained earnings	19	(9,857)	(9,104)
Total equity	19	(25,622)	(24,053)
Liabilities			
Interest-bearing loans and borrowings	16	(1,100)	(1,500)
Employee benefits	22	(5,220)	(7,192)
Deferred tax liabilities	17	(2,730)	(2,585)
Total non-current liabilities		(9,050)	(11,277)
Interest-bearing loans and borrowings	16	(400)	(457)
Tax payable		(698)	(577)
Trade and other payables	15	(3,273)	(2,530)
Total current liabilities		(4,371)	(3,564)
Total liabilities		(13,421)	(14,841)
Total equity and liabilities		(39,043)	(38,894)

These financial statements were approved by the Board of Directors on 13 March 2006 and signed on its behalf by:



W H Fairservice
Chairman



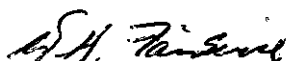
C G Hurst
Finance Director

COMPANY BALANCE SHEET

as at 31 December 2005

	Note	2005 £000	2004 £000
Non-current assets			
Property, plant and equipment	10	22,063	23,787
Investment in subsidiaries	11	7,035	6,416
Total non-current assets		29,098	30,203
Current assets			
Inventories	12	3,101	2,274
Trade and other receivables	13	5,537	5,373
Cash and cash equivalents	14	209	65
Total current assets		8,847	7,712
Total assets		37,945	37,915
Equity			
Issued share capital	18	(1,816)	(1,813)
Share premium	19	(13,753)	(13,707)
Capital redemption reserve	19	(5)	(5)
Hedging reserve	19	79	—
Retained earnings	19	(9,218)	(7,907)
Total equity	19	(24,713)	(23,432)
Liabilities			
Interest-bearing loans and borrowings	16	(1,100)	(1,500)
Employee benefits	22	(5,220)	(7,192)
Deferred tax liabilities	17	(2,730)	(2,563)
Total non-current liabilities		(9,050)	(11,255)
Interest-bearing loans and borrowings	16	(400)	(457)
Tax payable		(718)	(380)
Trade and other payables	15	(3,064)	(2,391)
Total current liabilities		(4,182)	(3,228)
Total liabilities		(13,232)	(14,483)
Total equity and liabilities		(37,945)	(37,915)

These financial statements were approved by the Board of Directors on 13 March 2006 and signed on its behalf by:



W H Fairservice
Chairman



C G Hurst
Finance Director

CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 December 2005

	Note	2005 £000	2004 £000
Cash flows from operating activities			
Profit for the year		2,427	1,170
Adjustments for:			
Depreciation, amortisation and impairment		3,322	3,371
Loss on sale of property, plant and equipment		—	23
Financial income		(813)	(750)
Financial expense		997	1,043
Equity-settled share-based payments		(14)	46
Taxation		861	139
Operating profit before changes in working capital and provisions		6,780	5,042
(Increase)/decrease in trade and other receivables		(346)	136
Increase in stock		(704)	(13)
Increase in trade and other payables		334	188
Decrease in provisions and employee benefits		(2,003)	(92)
Cash generated from the operations		4,061	5,261
Interest paid		(151)	(254)
Tax paid		(713)	(520)
Net cash from operating activities		3,197	4,487
Proceeds on disposal of property, plant and equipment		—	1
Interest received		26	—
Acquisition of property, plant and equipment		(1,070)	(1,331)
Net cash used in investing activities		(1,044)	(1,330)
Proceeds from the issue of share capital		49	—
Repayment of borrowings		(400)	(851)
Proceeds from new loan		—	2,000
Payment of finance lease liabilities		(57)	(119)
Dividends paid		(1,631)	(1,269)
Net cash used in financing activities		(2,039)	(239)
Net increase in cash and cash equivalents		114	2,918
Cash and cash equivalents at 1 January		298	(2,616)
Effect of exchange rate fluctuations on cash held		20	(4)
Cash and cash equivalents at 31 December	14	432	298

Cash and cash equivalents comprise cash at bank and short-term highly liquid investments with a maturity date of less than three months.

COMPANY CASH FLOW STATEMENT

for the year ended 31 December 2005

	Note	2005 £000	2004 £000
Cash flows from operating activities			
Profit for the year		2,985	481
Adjustments for:			
Depreciation, amortisation and impairment		2,899	2,940
Foreign exchange (gains)/losses		(623)	424
Loss on sale of property, plant and equipment		—	23
Financial income		(1,126)	(949)
Financial expense		1,026	1,041
Equity-settled share-based payments		(14)	46
Taxation		1,219	144
Operating profit before changes in working capital and provisions		6,366	4,150
(Increase)/decrease in trade and other receivables		(151)	264
(Increase)/decrease in stock		(827)	91
Increase in trade and other payables		389	193
Decrease in provisions and employee benefits		(2,003)	(92)
Cash generated from the operations		3,774	4,606
Interest paid		(156)	(252)
Tax paid		(599)	(506)
Net cash flow from operating activities		2,919	3,848
Proceeds on disposal of property, plant and equipment		—	1
Interest received		313	199
Acquisition of property, plant and equipment		(1,046)	(934)
Net cash used in investing activities		(733)	(734)
Proceeds from issue of share capital		49	—
Repayment of borrowings		(400)	(851)
Proceeds from new loan		—	2,000
Payment of finance lease liabilities		(57)	(119)
Dividends paid		(1,631)	(1,269)
Net cash used in financing activities		(2,039)	(239)
Net increase in cash and cash equivalents		147	2,875
Cash and cash equivalents at 1 January		65	(2,828)
Effect of exchange fluctuations on cash held		(3)	18
Cash and cash equivalents at 31 December	14	209	65

NOTES TO THE FINANCIAL STATEMENTS

1. Accounting policies

Zotefoams plc (the 'Company') is a Company incorporated in the UK.

The Group financial statements consolidate those of the Company and its subsidiaries (together referred to as the 'Group'). The Parent Company financial statements present information about the Company as a separate entity and not about its Group.

Both Parent Company financial statements and the Group financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs"). On publishing the Parent Company financial statements here together with the Group financial statements the Company is taking advantage of the exemption in Section 230 of the Companies Act 1985 not to present its individual Income Statement and related notes that form part of these approved financial statements.

The accounting policies set out below have, unless otherwise stated, been applied consistently for both the Group and the Company to all periods presented in these consolidated and Company financial statements and in preparing an opening IFRS Balance Sheet at 1 January 2004 for the purposes of the transition to Adopted IFRSs. The principal exception is that, as more fully explained below, financial instruments accounting is determined on different bases in current year and comparative year due to transitional provisions of IAS 32 and IAS 39.

Judgments made by the Directors, in the application of these accounting policies that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 25.

a) Transition to Adopted IFRS

Both the Group and the Company's financial statements are presented in accordance with Adopted IFRS for the first time and consequently both have applied IFRS 1. An explanation of how the transition to Adopted IFRS has affected the reported financial position, financial performance and cash flows of the Group is provided in the Appendix: Explanation of Transition to IFRS on page 50.

In addition to exempting companies from the requirement to restate comparatives for IAS 32 and IAS 39, IFRS 1 grants certain exemptions from the full requirements of IFRSs in the transition period. The following exemptions have been taken in these financial statements:

- Employee benefits – all cumulative actuarial gains and losses on defined benefit plans have been recognised in equity on 1 January 2004;
- Cumulative translation differences – cumulative translation differences for all foreign operations have been set to zero at 1 January 2004; and
- Share-based payments – the recognition and measurement requirements of IFRS 2 were not applied to share options awarded before 7 November 2002.

b) Measurement convention

The financial statements are prepared on the historical cost basis except that derivative financial instruments are stated at their fair value.

c) Basis of consolidation

i) SUBSIDIARIES

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

ii) TRANSACTIONS ELIMINATED ON CONSOLIDATION

Intra-Group balances and transactions, including any unrealised gains and losses or income and expenses arising from such transactions are eliminated in preparing the financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

d) Foreign currency

i) FOREIGN CURRENCY TRANSACTIONS

Transactions in foreign currencies are translated at the foreign exchange rate prevailing at the time of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to sterling at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in profit and loss. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

ii) FINANCIAL STATEMENTS OF FOREIGN OPERATIONS

The assets and liabilities of foreign operations, including fair value adjustments arising on consolidation, are translated to sterling at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated to sterling at the average rate of exchange ruling during the year where this rate approximates to the foreign exchange rates ruling at the dates of the transactions.

Exchange differences arising from this translation of foreign operations, and of related qualifying hedges, are taken directly to translation reserve. They are released into the Income Statement upon disposal.

e) Derivative financial instruments

The Group uses derivative financial instruments to hedge its exposure to foreign exchange risks arising from operational, financing and investment activities. In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, derivative financial instruments are stated at fair value. The gain or loss on re-measurement is recognised immediately in the Income Statement. Where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged (see accounting policy f).

The fair value of forward exchange contracts is their quoted market price at the balance sheet date, being the present value of the quoted forward price.

f) Cash flow hedging

When a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or of a highly probable forecasted transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in equity. If a hedge of a forecasted transaction subsequently results in the recognition of a financial asset or a financial liability, then the associated gains or losses that were recognised directly in equity are reclassified into the Income Statement in the same period or periods during which the asset acquired or liability assumed affects the Income Statement (i.e., when interest income or expense is recognised).

The ineffective part of any gain or loss is recognised immediately in the Income Statement.

When a hedging instrument expires or is sold, terminated or exercised, or the entity revokes designation of the hedge relationship but the hedged forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, then the cumulative unrealised gain or loss recognised in equity is recognised immediately in the Income Statement.

The Group has taken advantage of the transitional arrangements of IFRS 1 not to restate corresponding amounts in accordance with IAS 32 and IAS 39.

CASH FLOW HEDGING – COMPARATIVE PERIOD

In 2004, hedging instruments were not recognised and hedged items were held at cost (amortised as appropriate) without any adjustment in respect of the hedged risk.

No adjustments have been made to bring the hedged items and hedging instruments in place at 1 January 2005 on to the Balance Sheet in accordance with the 2005 policy, as the accounting impact is not material. Furthermore, disclosure about the impact of IAS 32/39 onto the 2004 Balance Sheet has not been given as again the impact is not material.

g) Property, plant and equipment

i) OWNED ASSETS

Items of property, plant and equipment are stated at cost or deemed cost less accumulated depreciation and impairment losses (see accounting policy l).

When parts of an item of property, plant and equipment have different useful lives, those components are accounted for as separate items of property, plant and equipment.

ii) LEASED ASSETS

Leases in terms of which the Group assumes substantially all of the risks and rewards of ownership are classified as finance leases. Lease payments are accounted for as described in accounting policy r.

iii) DEPRECIATION

Depreciation is charged to the Income Statement on a straight line basis over the estimated useful lives of each part of the item of property, plant and equipment. Land is not depreciated. The estimated useful lives are as follows:

Buildings	20 years
Plant and equipment	5–15 years
Computer equipment and vehicles	3–5 years

h) Intangible assets – research and development

Expenditure on research activities undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognised in the Income Statement as an expense incurred. Expenditure on development activities, whereby research findings are applied to a plan or design for the production of new or substantially improved products and processes, is capitalised if the product or process is technically and commercially feasible and the Group has sufficient resources to complete development.

i) Trade and other receivables

Trade and other receivables are stated at their nominal amounts less impairment losses (see accounting policy l).

j) Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completing and selling expenses.

In determining the cost of raw materials, consumables and goods purchased for resale, the weighted average purchase price is used. For work in progress and finished goods manufactured by the Group, cost is taken as production cost, which includes an appropriate proportion of attributable overheads.

k) Cash and cash equivalents

Cash and cash equivalents comprises cash balances and call deposits with an original maturity of three months or less. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purposes of the statement of cash flows.

l) Impairment

The carrying amounts of the Group's assets, other than inventories (see accounting policy j), employee benefits (see accounting policy o) and deferred tax assets (see accounting policy s), are reviewed at each balance sheet date where there is an indication that the asset may be impaired. If any such indication exists, the asset's recoverable amount is estimated (see below).

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the Income Statement.

NOTES TO THE FINANCIAL STATEMENTS

1. Accounting policies (continued)

l) Impairment (continued)

l) CALCULATION OF RECOVERABLE AMOUNT

The recoverable amount of assets is the greater of their net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

ll) REVERSALS OF IMPAIRMENT

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

m) Dividends

Dividends are recognised as a liability in the period in which they are approved.

n) Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any differences between cost and redemption values being recognised in the Income Statement over the period of the borrowings on an effective interest basis where material. In 2004, interest-bearing loans were shown at cost, although there was no impact of transition to the new policy.

o) Employee benefits

l) DEFINED CONTRIBUTION PLANS

Obligations for contributions to defined contribution pension plans are recognised as an expense in the Income Statement as incurred.

ll) DEFINED BENEFITS PLANS

The Group's net obligation in respect of defined benefit post employment plans, including pension plans, is calculated separately for each plan by estimating the amount of future benefit that the employees have earned in return for their service in the current and prior periods. That benefit is discounted to determine its present value, and the fair value of any plan assets is deducted. The discount rate is the yield at the balance sheet date on AA credit rated bonds that have maturity dates approximating the terms of the Group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method.

All actuarial gains and losses at 1 January 2004, the date of transition to IFRS, were recognised. The Group recognises the actuarial gains and losses that arise subsequent to 1 January 2004 through the Statement of Recognised Income and Expense.

lll) SHARE-BASED PAYMENT TRANSACTIONS

The share option programme allows Group employees to acquire shares of the Company. The fair value of options granted is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employee becomes unconditionally entitled to the options. The fair value of the options granted is measured using a Monte Carlo simulation method taking into account the terms and conditions upon which the options were granted.

p) Trade and other payables

Trade and other payables are stated at cost.

q) Revenue

Revenue from the sale of goods is recognised in the Income Statement at the point of despatch when significant risks and rewards of ownership is deemed to have been transferred to the buyer.

r) Expenses

l) OPERATING LEASE PAYMENTS

Payments made under operating leases are recognised in the Income Statement on a straight line basis over the term of the lease. Lease incentives received are recognised in the Income Statement as an integral part of the total lease expenses.

ll) FINANCE LEASE PAYMENTS

The finance charge, where material, is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

s) Taxation

Tax on the Income Statement for the periods presented comprises current and deferred tax. Tax is recognised in the Income Statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustments to the tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Additional tax that arises from the distribution of dividends is recognised at the same time as the liability to pay the related dividend.

Information as to the calculation of tax on the Income Statement is included in note 7.

t) Segmental reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

u) Investments in equity securities

Investments in subsidiaries are stated at cost less impairment.

v) Adopted IFRSs not yet applied

The following adopted IFRSs were available for early application but have not been applied by the Group in these financial statements:

- IAS 39 amendments: 'Financial instruments: recognition and measurement.'
- IFRS 7 'Financial instruments: disclosure applicable for years commencing on or after 1 January 2007'.

The application of the IAS 39 amendments and IFRS 7 in 2005 would not have affected the Balance Sheet or Income Statement. The Group plans to adopt the IAS 39 amendments on 1 January 2006 and IFRS 7 on 1 January 2007.

2. Business segments

The Group manufactures and sells high-performance foams for specialist markets worldwide. These fall into two main business segments best categorised by their constituent raw materials.

- Polyolefins: these foams are made from olefinic homopolymer and copolymer resin. The most common resin used is polyethylene.
- High performance polymers (HPP): these foams exhibit high performance on certain key properties, such as improved chemical, flammability or temperature performance, due to the resins on which they are based. Turnover in the segment is currently derived from our ZOTEK® F foams made from PVDF fluoropolymer. Other polymers being assessed in development include polyamide (nylon) and silicone.

Due to our unique manufacturing technology Zotefoams can produce polyolefin foams with superior performance to other manufacturers. However, our strategy is to use the capabilities of our technology to produce foams from other materials as well as polyolefins. The development of foams from high-performance polymers business is currently in its early stages with costs (including the technical and marketing costs to develop these materials) exceeding revenues.

	Note	Polyolefins		HPP		Consolidated	
		2005 £000	2004 £000	2005 £000	2004 £000	2005 £000	2004 £000
Revenue		27,420	25,173	555	3	27,975	25,176
Segment result		2,219	1,997	(196)	(395)	2,023	1,602
Exceptional items	4	—	—	—	—	1,449	—
Net financing costs		—	—	—	—	(184)	(293)
Taxation		—	—	—	—	(861)	(139)
Profit for the period		—	—	—	—	2,427	1,170
Segment assets		38,026	38,203	885	691	38,911	38,894
Unallocated assets		—	—	—	—	132	—
Total assets						39,043	38,894
Segment liabilities		(9,752)	(11,677)	(241)	(2)	(9,993)	(11,679)
Unallocated liabilities		—	—	—	—	(3,428)	(3,162)
Total liabilities						(13,421)	(14,841)
Depreciation		3,272	3,314	50	57	3,322	3,371
Capital expenditure		1,053	1,297	17	34	1,070	1,331

Geographical segments

	UK and Eire £000	Europe £000	North America £000	Rest of the World £000	Total
For the year ending 31 December 2005					
Revenue from external customers	7,332	12,604	7,336	703	27,975
Segment assets	29,744	—	9,167	—	38,911
Capital expenditure	1,046	—	24	—	1,070
For the year ending 31 December 2004					
Revenue from external customers	6,985	11,764	5,909	518	25,176
Segment assets	30,841	—	8,053	—	38,894
Capital expenditure	1,040	—	291	—	1,331

NOTES TO THE FINANCIAL STATEMENTS

3. Expenses and auditor's remuneration

	2005 £000	2004 £000
Included in profit for the year are:		
Research and development costs expensed	776	734
Net exchange gains	(111)	(108)
Auditor's remuneration:		
Group – audit	69	66
– fees receivable by the auditor and their associates in respect of other services:		
– other services pursuant with legislation	53	12
– other services relating to taxation	11	37
– services relating to corporate finance transactions	8	—
	141	115
Company – audit	63	61

Amounts paid to the Company's auditor in respect of services to the Company, other than the audit of the Company's financial statements, have not been disclosed as the information is required instead to be disclosed on a consolidated basis.

4. Exceptional items

The Company has classified the following items as exceptional:

Bid costs

Relating to legal, advisory and other costs incurred in respect of a preliminary approach for the share capital of the Company which was announced in January 2005 and terminated in November 2005.

Pension curtailment costs

On 31 December 2005, the Zotefoams Defined Benefit Pension Scheme for UK employees was closed to future accrual of benefits. The actuarial gain on closing the scheme to future accrual of benefits and the associated costs have been classified as an exceptional item.

Tax adjustment to exceptional items in prior year

In 2001 and 2002, the Group recorded an exceptional profit on insurance proceeds following a fire in 2000 at the Group's Croydon site. The tax computations relating to 2001 and 2002 have now been agreed with the Revenue resulting in a £267,000 release on the deferred tax provided in relation to these proceeds. This is released as an exceptional item because it relates to a previous exceptional item.

	2005 £000	2004 £000
Bid costs	(413)	—
Pension curtailment:		
Actuarial gain	1,972	—
Associated costs borne by the Company	(110)	—
Net curtailment gain	1,862	—
Exceptional items before taxation	1,449	—
Tax on above	(559)	—
Adjustment to tax on prior year exceptional item	267	—
Exceptional items after taxation	1,157	—

5. Staff numbers and expenses

The average number of people employed by the Group and Company (including Directors) during the year, analysed by category, was as follows:

	Number of employees			
	Group		Company	
	2005	2004	2005	2004
Production	130	128	120	117
Maintenance	20	19	16	17
Distribution and marketing	32	33	22	22
Administration and technical	60	60	52	52
	242	240	210	208

The aggregate payroll costs of these persons were as follows:

	Group		Company	
	2005 £000	2004 £000	2005 £000	2004 £000
Wages and salaries	6,937	6,415	5,984	5,520
Social security costs	622	589	528	495
Share based payments	(14)	46	(14)	46
Other pension costs	574	560	468	476
	8,119	7,610	6,966	6,537

Details of individual Directors' emoluments, pension costs and share options are dealt with on pages 15 to 19 in the Report of the Board of Directors on Directors' Remuneration.

6. Finance income and costs

Financial income

	2005 £000	2004 £000
Interest on bank deposits	26	—
Expected return on assets of defined benefit pension fund	787	750
	813	750

Finance costs

	2005 £000	2004 £000
On bank loans and overdrafts	120	201
On finance leases	16	24
Interest on defined benefit pension obligation	861	818
	997	1,043

7. Taxation

	Note	2005 £000	2004 £000
UK corporation tax at 30% (2004: 30%)		917	871
Overseas taxation		2	24
Adjustment to prior year UK tax charge		(84)	(176)
Current taxation		835	719
Deferred taxation	17	26	(580)
Total tax charge		861	139

Factors affecting the tax charge

The tax charge for the period is lower (2004: lower) than the standard rate of corporation tax in the UK of 30% (2004: 30%). The differences are explained below:

	2005 £000	2004 £000
Tax reconciliation		
Profit on ordinary activities before tax	3,288	1,309
Tax at 30% (2004: 30%)	986	393
Effects of:		
Research and development tax credits less expenses not deductible for tax purposes	115	(8)
Partial recognition of US tax losses	(54)	—
Higher/(lower) tax rates on overseas earnings	15	(17)
Intra-Group stock movements	—	35
Adjustments to tax charge in respect of previous periods	66	(264)
Adjustment to tax charge on prior year exceptional items	(267)	—
Total tax charge	861	139

8. Dividends and earnings per share

	2005 £000	2004 £000
Final dividend prior year of 3.0p (2004: 2.0p) net per 5p ordinary share	1,087	725
Interim dividend of 1.5p (2004: 1.5p) net per 5p ordinary share	544	544
Dividends paid during the year	1,631	1,269

The proposed final dividend for the year ended 31 December 2005 of 3.0p per share (2004: 3.0p) is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements.

Earnings per ordinary share

Earnings per ordinary share is calculated by dividing profit after tax of £2,427,000 (2004: £1,170,000) by the weighted average number of shares in issue during the year. Diluted earnings per ordinary share adjusts for the potential dilutive effect of share option schemes in accordance with IAS 33.

	2005	2004
Average number of ordinary shares issued	36,276,976	36,255,772
Deemed issued for no consideration	—	30,973
Diluted	36,276,976	36,286,745

NOTES TO THE FINANCIAL STATEMENTS

8. Dividends and earnings per share (continued)

Shares deemed issued for no consideration have been calculated based on the potential dilutive effect of the Executive Share Option Scheme and options granted under the HMRC Approved Share Option Scheme:

Date from which exercisable	Exercise price	Number of shares under option	
		2005	2004
1 June 2005	77.0p	—	177,475
20 August 2005	80.5p	—	654,494
18 March 2006	80.0p	872,865	872,865
7 April 2007	72.5p	1,130,034	1,130,034
22 December 2008	77.0p	1,026,320	—
		3,029,219	2,834,868

The average fair value of one ordinary share during the year was considered to be 72.0p (2004: 75.3p).

9. Profit for the financial year

The Group accounts do not include a separate Income Statement for Zotefoams plc (the parent undertaking) as permitted by Section 230 of the Companies Act 1985. The Parent Company profit after tax for the financial year is £2,985,000 (2004: £481,000).

10. Property, plant and equipment

a) Group

	Land and buildings £000	Plant and equipment £000	Fixtures and fittings £000	Under construction £000	Total £000
Cost					
Balance at 1 January 2004	14,275	34,069	2,088	2,267	52,699
Other acquisitions	256	175	72	792	1,295
Disposals	—	(54)	—	—	(54)
Reclassifications	—	367	—	(367)	—
Effect of movement in foreign exchange	(284)	(277)	(8)	—	(569)
Balance at 31 December 2004	14,247	34,280	2,152	2,692	53,371
Balance at 1 January 2005	14,247	34,280	2,152	2,692	53,371
Other acquisitions	14	627	44	514	1,199
Disposals	—	—	(61)	—	(61)
Reclassifications	—	2,080	3	(2,083)	—
Effect of movement in foreign exchange	432	423	13	—	868
Balance at 31 December 2005	14,693	37,410	2,151	1,123	55,377
Depreciation and impairment					
Balance at 1 January 2004	2,478	16,367	1,472	7	20,324
Depreciation charge for the year	563	2,335	366	107	3,371
Disposals	—	(30)	—	—	(30)
Effect of movement in foreign exchange	(32)	(51)	(6)	—	(89)
Balance at 31 December 2004	3,009	18,621	1,832	114	23,576
Balance at 1 January 2005	3,009	18,621	1,832	114	23,576
Depreciation charge for the year	574	2,440	255	53	3,322
Disposals	—	—	(61)	—	(61)
Reclassifications	—	93	—	(93)	—
Effect of movement in foreign exchange	64	97	15	—	176
Balance at 31 December 2005	3,647	21,251	2,041	74	27,013
Net book value					
At 1 January 2004	11,797	17,702	616	2,260	32,375
At 31 December 2004 and 1 January 2005	11,238	15,659	320	2,578	29,795
At 31 December 2005	11,046	16,159	110	1,049	28,364

Included in fixtures and fittings for both the Company and the Group are assets of nil (2004: £79,000) in respect of the net book value of assets held under finance leases.

Included in plant and machinery for both the Company and the Group are assets of £1,500,000 (2004: £1,900,000) pledged as security for a bank loan.

During the year both the Company and the Group commenced a number of programs to construct and refurbish plant and equipment and fixtures and fittings. Costs incurred up to the balance sheet date totalled £1,123,000 (2004: £2,692,000).

b) Company

	Land and buildings £000	Plant and equipment £000	Fixtures and fittings £000	Under construction £000	Total £000
Cost					
Balance at 1 January 2004	10,462	29,934	1,995	2,267	44,658
Other acquisitions	125	37	50	792	1,004
Disposals	—	(10)	—	—	(10)
Reclassifications	—	367	—	(367)	—
Balance at 31 December 2004	10,587	30,328	2,045	2,692	45,652
Balance at 1 January 2005	10,587	30,328	2,045	2,692	45,652
Other acquisitions	3	614	44	514	1,175
Disposals	—	—	(61)	—	(61)
Reclassifications	—	2,080	3	(2,083)	—
Balance at 31 December 2005	10,590	33,022	2,031	1,123	46,766
Depreciation and impairment					
Balance at 1 January 2004	2,114	15,394	1,415	7	18,930
Depreciation charge for the year	416	2,079	338	107	2,940
Disposals	—	(5)	—	—	(5)
Balance at 31 December 2004	2,530	17,468	1,753	114	21,865
Balance at 1 January 2005	2,530	17,468	1,753	114	21,865
Depreciation charge for the year	421	2,173	252	53	2,899
Disposals	—	—	(61)	—	(61)
Reclassifications	—	93	—	(93)	—
Balance at 31 December 2005	2,951	19,734	1,944	74	24,703
Net book value					
At 1 January 2004	8,348	14,540	580	2,260	25,728
At 31 December 2004 and 1 January 2005	8,057	12,860	292	2,578	23,787
At 31 December 2005	7,639	13,288	87	1,049	22,063

11. Investments in subsidiaries

	Company	
	2005 £000	2004 £000
Shares in Group undertakings – at cost	4,505	4,505
Provision against the value of investment in subsidiary to reflect the value of the underlying net assets	(3,294)	(3,294)
Loan to Zotefoams Inc.	5,824	5,205
	7,035	6,416

The investments consist of the entire ordinary share capital of Zotefoams International Limited and a \$10,000,000 loan to Zotefoams Inc.

The following is a complete list of the subsidiary undertakings of the Company, in all of which the Company owns either directly or indirectly 100% of the ordinary share capital:

Zotefoams International Limited
Zotefoams Inc.
Zotefoams Fabrications Limited – in voluntary liquidation

All the limited companies are incorporated in the United Kingdom, with the exception of Zotefoams Inc. which is incorporated in the USA.

The principal activities of the subsidiary undertakings are as follows: Zotefoams Inc. purchases and distributes cross-linked block foams and Zotefoams International Limited is a holding Company. Zotefoams Fabrications Limited used to manufacture cross-linked block foams but these activities have been transferred to other Group companies and Zotefoams Fabrications Limited is now in members' voluntary liquidation.

In the opinion of the Directors the investments in the Company's subsidiary undertakings are worth at least the amount at which they are stated in the Balance Sheet.

12. Inventories

	Group		Company	
	2005 £000	2004 £000	2005 £000	2004 £000
Raw materials and consumables	1,593	1,171	1,571	1,156
Work in progress	1,085	845	945	661
Finished goods	1,255	1,110	585	457
	3,933	3,126	3,101	2,274

The carrying amount of inventories subject to retention of title clauses is £335,000 (2004: £123,000).

NOTES TO THE FINANCIAL STATEMENTS

13. Trade and other receivables

	Note	Group		Company	
		2005 £000	2004 £000	2005 £000	2004 £000
Amounts falling due within one year:					
Trade receivables		5,893	5,331	4,339	4,310
Fair value derivatives	20	17	—	17	—
Amounts owed by Group undertakings		—	—	940	728
Other receivables		31	54	31	54
Prepayments and accrued income		241	290	210	281
		6,182	5,675	5,537	5,373
Trade receivables are shown net of: impairment losses		50	52	43	40

14. Cash and cash equivalents/bank overdrafts

	Group		Company	
	2005 £000	2004 £000	2005 £000	2004 £000
Cash and cash equivalents per balance sheet	432	298	209	65
Cash and equivalents per cash flow statements	432	298	209	65

15. Trade and other payables

	Note	Group		Company	
		2005 £000	2004 £000	2005 £000	2004 £000
Trade payables		831	942	831	940
Other creditors including taxation and social security:					
Other taxation and social security		170	152	164	146
Fair value derivatives	20	96	—	96	—
Other payables		205	72	86	23
Accruals and deferred income		1,971	1,364	1,887	1,282
		3,273	2,530	3,064	2,391

16. Interest-bearing loans and borrowings

	Group and Company	
	2005 £000	2004 £000
Obligations under finance leases	—	57
Bank loans (see note 20)		
Amounts falling due within one year	400	400
	400	457
Amounts falling due in more than one year	1,100	1,500
	1,100	1,500

17. Deferred tax assets and liabilities

Recognised deferred tax assets and liabilities – Group

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2005 £000	2004 £000	2005 £000	2004 £000	2005 £000	2004 £000
Property, plant and equipment	—	—	3,327	3,891	3,327	3,891
Rolled-over gain	—	—	967	830	967	830
Inventories	(78)	—	—	22	(78)	22
Employee benefits	(1,564)	(2,158)	—	—	(1,564)	(2,158)
Tax value of loss carry-forwards recognised	(54)	—	—	—	(54)	—
Tax (assets)/liabilities	(1,696)	(2,158)	4,294	4,743	2,598	2,585
Set off tax	1,564	2,158	(1,564)	(2,158)	—	—
Net tax (assets)/liabilities	(132)	—	2,730	2,585	2,598	2,585

At 31 December 2005, a deductible temporary difference of £882,000 (2004: £667,000) relating to undistributed reserves in a subsidiary has not been recognised because the Group controls whether the liability will be incurred and is satisfied that it will not be incurred in the foreseeable future.

Unrecognised deferred tax assets

The Group has \$6.2 million of tax losses carried forward in the USA. These tax losses at a 35% tax rate and year end exchange rates have a value of £1.3 million. The Group has only recognised £54,000 of these tax losses as a deferred tax asset representing what the Board believe is a reasonable estimate of the expected US tax utilisation in the near future.

Movement in deferred tax during the year

	Balance 1 January 2005 £000	Recognised in income £000	Recognised in equity £000	Balance 31 December 2005 £000
Property, plant and equipment	3,891	(564)	—	3,327
Rolled-over gain	830	137	—	967
Inventories	22	(100)	—	(78)
Employee benefits	(2,158)	607	(13)	(1,564)
Tax value of loss carry-forwards	—	(54)	—	(54)
	2,585	26	(13)	2,598

Movement in deferred tax during the prior year

	Balance 1 January 2004 £000	Recognised in income £000	Recognised in equity £000	Balance 31 December 2004 £000
Property, plant and equipment	4,462	(571)	—	3,891
Rolled-over gain	830	—	—	830
Inventories	40	(18)	—	22
Employee benefits	(2,246)	9	79	(2,158)
	3,086	(580)	79	2,585

Deferred tax assets and liabilities – Company

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2005 £000	2004 £000	2005 £000	2004 £000	2005 £000	2004 £000
Property, plant and equipment	—	—	3,327	3,891	3,327	3,891
Rolled-over gain	—	—	967	830	967	830
Employee benefits	(1,564)	(2,158)	—	—	(1,564)	(2,158)
Tax (assets)/liabilities	(1,564)	(2,158)	4,294	4,721	2,730	2,563
Set off tax	1,564	2,158	(1,564)	(2,158)	—	—
Net tax liabilities	—	—	2,730	2,563	2,730	2,563

Movement in deferred tax during the year

	Balance 1 January 2005 £000	Recognised in income £000	Recognised in equity £000	Balance 31 December 2005 £000
Property, plant and equipment	3,891	(564)	—	3,327
Rolled-over gain	830	137	—	967
Employee benefits	(2,158)	607	(13)	(1,564)
	2,563	180	(13)	2,730

Movement in deferred tax during the prior year

	Balance 1 January 2004 £000	Recognised in income £000	Recognised in equity £000	Balance 31 December 2004 £000
Property, plant and equipment	4,174	(283)	—	3,891
Rolled-over gain	830	—	—	830
Employee benefits	(2,246)	9	79	(2,158)
	2,758	(274)	79	2,563

18. Share capital

	2005 £	2004 £
Authorised		
At 31 December		
Equity: 56,000,000 ordinary shares of 5.0p each	2,800,000	2,800,000
Allotted, called-up and fully paid		
At 31 December		
Equity: 36,319,924 (2004: 36,255,772) ordinary shares of 5.0p each	1,815,996	1,812,789

Details of share options are provided in note 8 to the accounts on page 39.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

NOTES TO THE FINANCIAL STATEMENTS

19. Capital and reserves

Reconciliation of movement in capital and reserves – Group

	Share capital £000	Share premium £000	Capital redemption reserve £000	Translation reserve £000	Hedging reserve £000	Retained earnings £000	Total equity £000
Balance at 1 January 2004	1,813	13,707	5	—	—	8,972	24,497
Total recognised income and expense	—	—	—	(576)	—	1,355	779
Equity-settled share-based payment transactions net of tax	—	—	—	—	—	46	46
Dividends	—	—	—	—	—	(1,269)	(1,269)
Balance at 31 December 2004	1,813	13,707	5	(576)	—	9,104	24,053
Balance at 1 January 2005	1,813	13,707	5	(576)	—	9,104	24,053
Total recognised income and expense	—	—	—	846	—	2,398	3,244
Own shares sold	3	46	—	—	—	—	49
Financial instruments	—	—	—	—	(79)	—	(79)
Equity-settled share-based payment transactions net of tax	—	—	—	—	—	(14)	(14)
Dividends	—	—	—	—	—	(1,631)	(1,631)
Balance at 31 December 2005	1,816	13,753	5	270	(79)	9,857	25,622

The aggregate current and deferred tax relating to items that is credited to equity is £13,000 (2004: charge of £79,000).

Reconciliation of movement in capital and reserves – Company

	Share capital £000	Share premium £000	Capital redemption reserve £000	Hedging reserve £000	Retained earnings £000	Total equity £000
Balance at 1 January 2004	1,813	13,707	5	—	8,464	23,989
Total recognised income and expense	—	—	—	—	666	666
Equity-settled share-based payment transactions net of tax	—	—	—	—	46	46
Dividends	—	—	—	—	(1,269)	(1,269)
Balance at 31 December 2004	1,813	13,707	5	—	7,907	23,432
Balance at 1 January 2005	1,813	13,707	5	—	7,907	23,432
Total recognised income and expense	—	—	—	—	2,956	2,956
Own shares sold	3	46	—	—	—	49
Financial instruments	—	—	—	(79)	—	(79)
Equity-settled share-based payment transactions net of tax	—	—	—	—	(14)	(14)
Dividends	—	—	—	—	(1,631)	(1,631)
Balance at 31 December 2005	1,816	13,753	5	(79)	9,218	24,713

The aggregate current and deferred tax relating to items that is credited to equity is £13,000 (2004: charge of £79,000).

Translation reserve

Translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations, as well as the translation of liabilities that hedge the Company's net investment in a foreign subsidiary.

Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedging transactions that have not yet occurred.

20. Financial instruments

Policy

The Group does not enter into significant derivative transactions. The Group's principal financial instruments comprise bank loans, cash and short-term deposits. 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 from the Group's financial instruments are credit risk, interest rate risk, liquidity risk and foreign exchange risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below. These policies have remained fundamentally unchanged throughout the year.

Credit risk

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. The Group does not require collateral in respect of financial assets.

In 2005 and 2004, the Group had credit insurance to mitigate this risk. However, cover is not comprehensive so elements of risk remain.

At the balance sheet date there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the Balance Sheet.

Interest rate risk

The Group finances its operations through a mixture of retained profits and bank borrowings. The Group borrows in the desired currency generally at a variable rate of interest.

The interest rate profile of the Group at 31 December was:

	2005			2004		
	Fixed rates £000	Variable rates £000	Total £000	Fixed rates £000	Variable rates £000	Total £000
Sterling	—	1,500	1,500	57	1,900	1,957
	—	1,500	1,500	57	1,900	1,957

The interest rate payable on the sterling overdraft is determined by LIBOR (or similar) plus a bank margin.

Liquidity risk

The Group's objective is to maintain a balance of continuity of funding and flexibility through the use of overdrafts, loans and finance leases as applicable. The maturity profile of the Group's borrowings is shown in note 16 on page 42.

The Group has a short-term facility of £5.0 million which is freely transferable and convertible into sterling.

This facility expires in April 2006 and is utilised by Zotefoams plc and its subsidiary undertakings under a cross-guarantee structure.

On 25 August 2004, Zotefoams plc borrowed £2.0 million under a five year mortgage, repayable in equal quarterly instalments. This facility is secured over specific plant assets.

Foreign currency risk

The Group is exposed to foreign currency risk on sales, purchases, assets and liabilities which are denominated in a currency other than sterling. The currencies giving rise to this risk are primarily the euro and the US dollar.

The Group hedges a proportion of its estimated cash exposure in respect of trade and other receivables, trade and other payables and forecast sales receipts and purchase payments for the next nine months. The Group uses forward exchange contracts to hedge its foreign currency risk. As at 31 December 2005, these forward currency contracts covered approximately two-thirds of the estimated net cash foreign exchange exposure for the next nine months.

In respect of other monetary assets and liabilities held in currencies other than the euro and the US dollar, the Group ensures that the net exposure is kept to a manageable level, by buying or selling foreign currencies at spot rates where necessary to address short-term imbalances.

Forecasted transactions

The Group classifies its forward exchange contracts hedging forecasted transactions as cash flow hedges and states them at fair value. The net fair value of forward exchange contracts used as hedges of forecasted transactions at 31 December 2005 was a net liability of £79,000 (2004: net asset of £43,000) comprising assets of £17,000 (2004: £120,000) and liabilities of £96,000 (2004: £77,000) that were recognised in fair value derivatives in 2005. In 2004 the accounting treatment followed UK GAAP as explained in note 1 Accounting policies (f) on page 35.

Recognised assets and liabilities

Changes in the fair value of forward exchange contracts that economically hedge monetary assets and liabilities in foreign currencies and for which no hedge accounting is applied are recognised in the Income Statement. Both the changes in fair value of the forward contracts and the foreign exchange gains and losses relating to the monetary items are recognised as part of administrative expenses (see note 3).

Sensitivity analysis

In managing currency risks the Group aims to reduce impact of short-term fluctuations on the Group's earnings. Over the longer-term, however, permanent changes in foreign exchange and interest rates would have an impact on consolidated earnings.

Short-term fluctuations in interest rates are not hedged as the Group, at present, does not consider them material. At 31 December 2005 it is estimated that a general increase of one percentage point in interest rates would decrease the Group's profit before tax by approximately £15,000 (2004: £20,000).

At 31 December 2005, it is estimated that an increase of one percentage point in the value of sterling against the euro and the dollar and would decrease the Group's profit before tax by approximately £43,000 (2004: £62,000) and £45,000 (2004: £26,000) respectively. The forward exchange contracts have been included in this calculation.

The Group has significant undertakings in the USA whose revenue and expenses are denominated in US dollars. Zotefoams plc makes a significant proportion of its sales to European customers and these revenues are predominantly in euros. It was the Group's policy in 2005 to hedge the foreign currency cash flows of invoiced sales net of expected foreign expenditure. Hedging is achieved by the use of foreign currency contracts expiring in the month of expected cash flow.

NOTES TO THE FINANCIAL STATEMENTS

20. Financial instruments (continued)

Fair values

The fair values together with the carrying amounts shown in the Balance Sheet are as follows:

	2005		2004	
	Carrying amount £000	Fair value £000	Carrying amount £000	Fair value £000
Trade and other receivables	6,165	6,165	5,675	5,675
Cash and cash equivalents	432	432	298	298
Forward exchange risks				
– assets	17	17	—	—
– liabilities	(96)	(96)	—	—
Secured bank loans	(1,500)	(1,500)	(1,900)	(1,900)
Finance lease liabilities	—	—	(57)	(57)
Trade and other payables	(3,177)	(3,177)	(2,530)	(2,530)

Estimation of fair values

The following summarises the major methods and assumptions used in estimating fair values of financial instruments reflected in the table.

Derivatives

Forward exchange contracts are marked to market using listed market prices.

Interest-bearing loans and borrowings, finance lease liabilities and trade and other receivables/payables

Carrying amounts equals the fair value.

21. Commitments

	2005 £000	2004 £000
(i) Capital contracts at the end of the financial year for which no provision has been made	1,088	115
(ii) The Group has annual commitments under non-cancellable operating leases which expire		
– within one year	74	93
– between two and five years	37	62

The above amounts apply to the Company as well as the Group apart from capital commitments which includes nothing (2004: £5,000) in respect of subsidiary undertakings.

22. Employee benefits

The Group and Company operate one defined benefit scheme in the UK which offers both pensions in retirement and death benefits to members. Pension benefits are related to the members' final salary at retirement and their length of service. Since 1 October 2001, the scheme has been closed to new members.

From 31 December 2005, future accrual of benefits for existing members of the scheme ceased and the Company has recognised this curtailment immediately.

Contributions to the plan will be £50,000 per month for five years finishing in December 2011 plus an initial lump sum of £100,000, which was paid following the agreement with the trustees to close the fund to future accrual.

The Company has opted to recognise all actuarial gains and losses immediately via the Statement of Recognised Income and Expenditure (SORIE). An actuarial valuation of the scheme was carried out as at 5 April 2005 and the preliminary results have been updated to 31 December 2005 by a qualified independent actuary. The major assumptions used by the actuary were (in nominal terms) as follows:

	As at 31 December 2005	As at 31 December 2004
Discount rate	4.80%	5.30%
Expected return on plan assets	6.13%	6.75%
Rate of salary increase	4.40%	4.40%
Rate of increase to pensions in payment	2.80%	2.50%
Rate of inflation	2.90%	2.90%
Mortality assumption	90% of PA92	90% of PA92

The assumptions used in determining the overall expected return of the scheme have been set with reference to yields available on government bonds and appropriate risk margins.

The assets in the scheme and the expected rates of return were:

	Long-term rate of return expected at 31 December 2005	Value at 31 December 2005 £000	Long-term rate of return expected at 31 December 2004	Value at 31 December 2004 £000
Equities	6.6	11,387	7.2	9,350
Bonds	4.1	1,915	4.9	1,603
Other	4.5	957	4.5	576
		14,259		11,529
The actual return on assets over the period was:		2,366		1,109
Present value of defined obligation:				
Funded plans		(19,479)		(18,721)
Total		(19,479)		(18,721)
Deficit in the scheme		(5,220)		(7,192)
Related deferred tax asset		1,566		2,158
Net pension liability		(3,654)		(5,034)

Reconciliation of opening and closing balances of the present value of the defined benefit obligation:

Benefit obligation at beginning of year	18,721	17,488
Service cost	440	376
Interest cost	861	818
Contributions by plan participants	209	216
Actuarial loss	1,621	93
Benefits paid	(401)	(270)
Curtailments and settlements	(1,972)	—
Benefit obligation at end of year	19,479	18,721

Reconciliation of opening and closing balances of the fair value of plan assets:

Fair value of plan assets at beginning of year	11,529	10,066
Expected return on plan assets	787	750
Actuarial gain	1,579	299
Contributions by employers	556	468
Contributions by plan participants	209	216
Benefits paid	(401)	(270)
Fair value of plan assets at end of year	14,259	11,529

The amounts recognised in the Income Statement are:

Current service cost	440	376
Interest on obligation	861	818
Expected return on plan assets	(787)	(750)
Gains on settlements and curtailment	(1,972)	—
Total (gain)/expense	(1,458)	444

The (gain)/expense is recognised in the following line items in the Income Statement:

	Group and Company	
	2005 £000	2004 £000
Cost of sales	242	261
Distribution costs	38	35
Administrative expenses	160	80
Financial income	(787)	(750)
Finance costs	861	818
Exceptional gain in administrative expenses	(1,972)	—
	(1,458)	444

Actuarial (losses)/gains to be shown in SORIE:

Actuarial (losses)/gains	(42)	264
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NOTES TO THE FINANCIAL STATEMENTS

22. Employee benefits (continued)

History of scheme assets, obligations and experience adjustments

	As at 31 December 2005	As at 31 December 2004
Present value of defined benefit obligation	19,479	18,721
Fair value of scheme assets	14,259	11,529
Deficit in the scheme	(5,220)	(7,192)
Experience adjustments arising on scheme liabilities	1,621	93
Experience item as a percentage of scheme liabilities	8%	0%
Experience adjustments arising on scheme assets	1,579	299
Experience item as a percentage of scheme assets	11%	3%

Other pension schemes

In addition to the defined benefit pension scheme, Zotefoams plc operated in 2005 a stakeholder scheme for employees who joined after 1 October 2001. The contributions paid by the Company in 2005 were £12,000 (2004: £11,000).

For US based employees Zotefoams Inc. operates a 401(k) plan and a defined contribution pension plan into which Zotefoams Inc. contributes 6.2% of pensionable salary.

23. Share-based payments

The Company has a share option scheme that entitles senior management personnel to purchase shares in the Company. Options are exercisable at a price equal to the average quoted closing market price of the Company's shares on the previous day. The vesting period is three years. If the options remain unexercised after a period of ten years from the date of grant, the options expire. Options are forfeited if the employee leaves the Group before the options vest.

Additionally, one share award and one SAYE share option scheme expired in 2005. These options were granted before 7 November 2002 and therefore the recognition and measurement principles in IFRS 2 have not been applied to these grants in accordance with the transitional provisions in IFRS 1 and IFRS 2.

Details of the vesting conditions for the share option awards is given in the Report of the Board of Directors on Directors' Remuneration on page 15.

Details of the options outstanding during the year are as follows:

	2005		2004	
	Number of share options	Weighted average exercise price (p)	Number of share options	Weighted average exercise price (p)
Outstanding at beginning of the period	2,834,868	76.9	2,231,946	83.6
Forfeited during the period	(767,817)	80.0	(527,112)	95.6
Exercised during the period	(64,152)	77.0	—	—
Granted during the period	1,026,320	77.0	1,130,034	72.5
Outstanding at the end of the period	3,029,219	76.2	2,834,868	76.9
Exercisable at the end of the period	3,029,219	76.2	2,834,868	76.9

The options outstanding at 31 December 2005 have an exercise price of between 72.5p and 80.0p and a weighted contractual life of 8.5 years.

The fair value received in return for share options granted are measured by reference to the fair value of share options granted. The estimate of fair value of the services received is measured based on a Monte Carlo model. The contractual life of the option (ten years) is used as an input into this model. No allowance is made for early leavers.

Fair value of share options and assumptions

The expected volatility is based on historic volatility since 1995.

	18 March 2003	7 April 2004	22 December 2005
Share price (p)	80.3	72.0	75.5
Exercise price (p)	80.0	72.5	77.0
Expected volatility (expressed as weighted average volatility used in modelling under Monte Carlo model)	30%	30%	28%
Option life (expressed as weighted average life used in the modelling under Monte Carlo model)	five years	five years	five years
Expected dividends (assumed to be increasing at 2.5%pa)	7.5	4.5	4.5
Risk-free interest rate (based on national government bonds)	4.2%	4.8%	4.2%

The share option awards are granted under a service condition and a performance condition. There are no market conditions associated with the share options.

The amounts recognised in the Income Statement for share-based payments are as follows:

	Group and Company	
	2005	2004
	£000	£000
Within administrative expenses	(14)	46
Element of the above relating to Directors of Zotefoams plc	(10)	27

24. Related parties

Directors

Directors of the Company and their immediate relatives control 5.9% of the voting shares of the Company. Details of Directors' pay and remuneration are given in the Report of the Board of Directors on Directors' Remuneration on page 15.

Subsidiaries

Zotefoams plc owns 100% of the shares of Zotefoams Inc., which is incorporated in the USA and Zotefoams Fabrications Limited which is incorporated in the UK but is now in members' voluntary liquidation. Transactions between Zotefoams plc and these companies are as follows:

Income Statement	Sales to		Service fees to		Interest from	
	2005	2004	2005	2004	2005	2004
	£000	£000	£000	£000	£000	£000
Zotefoams Inc.	4,143	2,704	47	49	287	179
Zotefoams Fabrications Limited	—	740	—	—	—	22

Balance Sheet

	Interest-bearing loan owed by		Receivables owed by	
	2005	2004	2005	2004
	£000	£000	£000	£000
Zotefoams Inc.	5,824	5,205	940	728
Zotefoams Fabrications Limited	—	—	—	—

25. Accounting estimates and judgements

Management discussed with the Audit Committee the development, selection and disclosure of the Group's critical accounting policies and estimates and the application of these policies and estimates.

Key sources of estimation uncertainty

In note 20 detailed analysis is given of the foreign exchange exposure of the Group and risks in relation to foreign exchange movements.

Under IAS 38 development costs must be capitalised when specified criteria have been met. Following a review of the Company's research and development expenditure, because of the uncertainties which still exist on the development of new products, it was concluded that no material development costs met the IAS 38 criteria require for capitalisation and therefore all development costs have been expensed.

Pensions assumptions

The assumptions made on rate of return and inflation are disclosed in note 22. These have a major effect on the pension fund valuation. The pension scheme liability as at 31 December 2005 has been calculated using 90% of the mortality rates as set out in the standard PA92 mortality tables, published by the Institute and Faculty of Actuaries, projected to year 2020 to allow for continuing improvements in member longevity/deterioration. These adjusted rates suggest that a man aged 65 retiring at 31 December 2005 could expect to live, on average, until age 86. A 5% change in life expectancy would increase/decrease the pension scheme liability by approximately £0.7 million (£0.5 million after deferred tax), all other things being equal.

APPENDIX: EXPLANATION OF TRANSITION TO IFRS

Principal differences

Group

The reconciliations of equity as at 1 January 2004 (date of transition to IFRS) and at 31 December 2004 (date of last UK GAAP financial statements) and the reconciliation of profit for 2004, as required by IFRS 1, have been included below.

Reconciliation of equity at 1 January 2004

	Previous GAAP 1 January 2004 £000	Remove proposed dividend £000	Provide deferred tax on rolled over gains £000	Recognise pension deficit £000	Recognise share options £000	IFRS 1 January 2004 £000
Non-current assets						
Property, plant and equipment	32,375	—	—	—	—	32,375
Total non-current assets	32,375	—	—	—	—	32,375
Current assets						
Inventories	3,178	—	—	—	—	3,178
Trade and other receivables	5,893	—	—	—	—	5,893
Cash and cash equivalents	212	—	—	—	—	212
Total current assets	9,283	—	—	—	—	9,283
Total assets	41,658	—	—	—	—	41,658
Equity						
Issued capital	(1,813)	—	—	—	—	(1,813)
Share premium	(13,707)	—	—	—	—	(13,707)
Capital redemption reserve	(5)	—	—	—	—	(5)
Retained earnings	(14,311)	(725)	830	5,236	(2)	(8,972)
Total equity	(29,836)	(725)	830	5,236	(2)	(24,497)
Liabilities						
Interest-bearing loans and borrowings	(57)	—	—	—	—	(57)
Employee benefits	—	—	—	(7,480)	—	(7,480)
Deferred tax (liabilities)/assets	(4,502)	—	(830)	2,244	2	(3,086)
Total non-current liabilities	(4,559)	—	(830)	(5,236)	2	(10,623)
Bank overdraft	(2,828)	—	—	—	—	(2,828)
Interest-bearing loans and borrowings	(905)	—	—	—	—	(905)
Tax payable	(385)	—	—	—	—	(385)
Trade and other payables	(3,145)	725	—	—	—	(2,420)
Total current liabilities	(7,263)	725	—	—	—	(6,538)
Total liabilities	(11,822)	725	(830)	(5,236)	2	(17,161)
Total equity and liabilities	(41,658)	—	—	—	—	(41,658)

Reconciliation of equity as at 31 December 2004

	Previous GAAP 31 December 2004 £000	Remove proposed dividend £000	Provide deferred tax on rolled over gains £000	Reclassify translation differences to translation reserve £000	Recognise pension deficit £000	IFRS 31 December 2004 £000
Non-current assets						
Property, plant and equipment	29,795	—	—	—	—	29,795
Total non-current assets	29,795	—	—	—	—	29,795
Current assets						
Inventories	3,126	—	—	—	—	3,126
Trade and other receivables	5,675	—	—	—	—	5,675
Cash and cash equivalents	298	—	—	—	—	298
Total current assets	9,099	—	—	—	—	9,099
Total assets	38,894	—	—	—	—	38,894
Equity						
Issued capital	(1,813)	—	—	—	—	(1,813)
Share premium	(13,707)	—	—	—	—	(13,707)
Capital redemption reserve	(5)	—	—	—	—	(5)
Translation reserve	—	—	—	576	—	576
Retained earnings	(13,305)	(1,087)	830	(576)	5,034	(9,104)
Total equity	(28,830)	(1,087)	830	—	5,034	(24,053)
Liabilities						
Interest-bearing loans and borrowings	(1,500)	—	—	—	—	(1,500)
Employee benefits	—	—	—	—	(7,192)	(7,192)
Deferred tax (liabilities)/assets	(3,913)	—	(830)	—	2,158	(2,585)
Total non-current liabilities	(5,413)	—	(830)	—	(5,034)	(11,277)
Interest-bearing loans and borrowings	(457)	—	—	—	—	(457)
Tax payable	(577)	—	—	—	—	(577)
Trade and other payables	(3,617)	1,087	—	—	—	(2,530)
Total current liabilities	(4,651)	1,087	—	—	—	(3,564)
Total liabilities	(10,064)	1,087	(830)	—	(5,034)	(14,841)
Total equity and liabilities	(38,894)	—	—	—	—	(38,894)

Reconciliation of profit for the year ended 31 December 2004

	Previous GAAP £000	Pensions £000	Recognise share options £000	IFRS £000
Revenue	25,176	—	—	25,176
Cost of sales	(19,669)	62	—	(19,607)
Gross profit	5,507	62	—	5,569
Distribution costs	(1,871)	8	—	(1,863)
Administrative expenses	(2,080)	22	(46)	(2,104)
Operating profits	1,556	92	(46)	1,602
Finance costs	(225)	(68)	—	(293)
Profit before tax	1,331	24	(46)	1,309
Taxation	(130)	(7)	(2)	(139)
Profit for the year	1,201	17	(48)	1,170

APPENDIX: EXPLANATION OF TRANSITION TO IFRS

Principal differences

Company

The reconciliations of equity as at 1 January 2004 (date of transition to IFRS) and at 31 December 2004 (date of last published UK GAAP statements) as required by IFRS 1 has been included below:

Reconciliation of equity as at 1 January 2004

	Previous GAAP 1 January 2004 £000	Remove proposed dividend £000	Provide deferred tax on rolled over gains £000	Recognise pension deficit £000	Recognise share options £000	IFRS 1 January 2004 £000
Non-current assets						
Property, plant and equipment	25,728	—	—	—	—	25,728
Investments	7,581	—	—	—	—	7,581
Total non-current assets	33,309	—	—	—	—	33,309
Current assets						
Inventories	2,365	—	—	—	—	2,365
Trade and other receivables	5,041	—	—	—	—	5,041
Total current assets	7,406	—	—	—	—	7,406
Total assets	40,715	—	—	—	—	40,715
Equity						
Issued capital	(1,813)	—	—	—	—	(1,813)
Share premium	(13,707)	—	—	—	—	(13,707)
Capital redemption reserve	(5)	—	—	—	—	(5)
Retained earnings	(13,803)	(725)	830	5,236	(2)	(8,464)
Total equity	(29,328)	(725)	830	5,236	(2)	(23,989)
Liabilities						
Interest-bearing loans and borrowings	(57)	—	—	—	—	(57)
Employee benefits	—	—	—	(7,480)	—	(7,480)
Deferred tax (liabilities)/assets	(4,174)	—	(830)	2,244	2	(2,758)
Total non-current liabilities	(4,231)	—	(830)	(5,236)	2	(10,295)
Bank overdraft	(2,828)	—	—	—	—	(2,828)
Interest-bearing loans and borrowings	(905)	—	—	—	—	(905)
Tax payable	(396)	—	—	—	—	(396)
Trade and other payables	(3,027)	725	—	—	—	(2,302)
Total current liabilities	(7,156)	725	—	—	—	(6,431)
Total liabilities	(11,387)	725	(830)	(5,236)	2	(16,726)
Total equity and liabilities	(40,715)	—	—	—	—	(40,715)

Reconciliation of equity as at 31 December 2004

	Previous GAAP 31 December 2004 £000	Remove proposed dividend £000	Provide deferred tax on rolled over gains £000	Recognise pension deficit £000	IFRS 31 December 2004 £000
Non-current assets					
Property, plant and equipment	23,787	—	—	—	23,787
Investments	6,416	—	—	—	6,416
Total non-current assets	30,203	—	—	—	30,203
Current assets					
Inventories	2,274	—	—	—	2,274
Trade and other receivables	5,373	—	—	—	5,373
Cash and cash equivalents	65	—	—	—	65
Total current assets	7,712	—	—	—	7,712
Total assets	37,915	—	—	—	37,915
Equity					
Issued capital	(1,813)	—	—	—	(1,813)
Share premium	(13,707)	—	—	—	(13,707)
Capital redemption reserve	(5)	—	—	—	(5)
Retained earnings	(12,684)	(1,087)	830	5,034	(7,907)
Total equity	(28,209)	(1,087)	830	5,034	(23,432)
Liabilities					
Interest-bearing loans and borrowings	(1,500)	—	—	—	(1,500)
Employee benefits	—	—	—	(7,192)	(7,192)
Deferred tax (liabilities)/assets	(3,891)	—	(830)	2,158	(2,563)
Total non-current liabilities	(5,391)	—	(830)	(5,034)	(11,255)
Interest-bearing loans and borrowings	(457)	—	—	—	(457)
Tax payable	(380)	—	—	—	(380)
Trade and other payables	(3,478)	1,087	—	—	(2,391)
Total current liabilities	(4,315)	1,087	—	—	(3,228)
Total liabilities	(9,706)	1,087	(830)	(5,034)	(14,483)
Total equity and liabilities	(37,915)	—	—	—	(37,915)

The Company profit for 2004 after applying IFRS is £481,000.

APPENDIX: EXPLANATION OF TRANSITION TO IFRS

Principal differences

1. Dividend recognition

Previously under UK GAAP, dividends were recognised in the financial results for the period to which they relate. However, under IFRS, a dividend can only be recognised if it has been formally declared during the accounting period being reported.

The Zotefoams' Board declares interim and final dividends after the end of each accounting period at the same time as approving the interim and annual reports. Hence, we will no longer accrue proposed dividends in the financial period to which they relate.

Consequently the final dividend for 2003 and 2004 are not recognised as a liability in the Balance Sheet as at 1 January 2004 and 31 December 2004.

2. Deferred tax

Under IAS 12 deferred tax is recognised on deferred capital gains. Under FRS 19 deferred tax was only recognised on deferred capital gains when the assets into which the gain has been rolled over were sold.

3. Accounting for foreign currency transactions and financial instruments

Zotefoams has a policy of taking out forward foreign currency contracts to cover forecast foreign currency income streams to provide an element of short-term predictability in its results.

Under IAS 39 the fair value of forward foreign currency contracts have to be recognised in the Balance Sheet when effective. Ineffective hedges are immediately recognised in the Income Statement. Zotefoams has adopted cash flow hedge accounting with effect from 1 January 2005 and therefore the movement in fair value can be deferred in a hedging reserve until the associated transaction occurs at which point the cumulative movement is released to the Income Statement. The Company has taken the exemption in IFRS 1 not to restate comparative information for 2004.

Translation differences on the exchange conversion of a foreign subsidiary are now posted to a translation reserve rather than the profit and loss account reserve.

4. Pensions

Under UK GAAP, Zotefoams has accounted for pensions in accordance with SSAP 24, which spreads the costs of the defined benefit scheme over the employees' working lives within the Group. Zotefoams has also made additional disclosures giving details of the pension fund deficit, liabilities and operating charges on the valuation methodologies in accordance with FRS 17.

IAS 19 'Employee benefits' requires the actuarial deficit arising under the defined benefit scheme to be recognised in the Balance Sheet based on fair valuations of the assets and liabilities at the balance sheet date. The movement in the deficit as a result of the current service cost, and other finance income has to be recognised in the Income Statement and Zotefoams has taken the option under IAS 19 to recognise actuarial gains and losses through the Statement of Recognised Income and Expense as opposed to the Income Statement.

Note that similar adjustments would have been required under FRS 17 in 2005.

5. Share-based payments

The Company has adopted IFRS 2 'Share-based payments' only in respect of awards granted after 7 November 2002 which had not vested at 1 January 2005. A charge is made to operating profit representing the fair value of share options granted to employees with the opposing entry taken to equity. The fair value has been calculated using a Monte Carlo simulation model and is charged to the Income Statement over the relevant vesting period. The charge is adjusted to reflect actual and expected levels of vesting, and for the expected achievement of any non-market performance conditions attached to each option.

6. Segmental reporting

Both UK GAAP and IFRS require statutory segmental reporting to match the internal reporting structure. Under UK GAAP there is an exemption if the disclosure of a particular segment is considered by the Directors to be prejudicial to the interests of the Company. Under IFRS there is no exemption and Zotefoams will disclose its high performance polymers business separately from its polyolefins business.

7. Intangible assets

Under IAS 38 Zotefoams is required to capitalise intangible assets subject to certain specified criteria. Zotefoams' policy under UK GAAP in respect of research and development expenditure was to expense such costs. Under IAS 38, research expenditure is expensed whereas development costs must be capitalised when specified criteria have been met. Following a review of the Company's research and development expenditure, no material development costs met the IAS 38 criteria required for capitalisation and therefore no adjustment has been made under IFRS.

NOTICE OF 2006 ANNUAL GENERAL MEETING

Notice is hereby given that the Annual General Meeting of Zotefoams plc (the "Company") will be held at the offices of Zotefoams plc, 675 Mitcham Road, Croydon CR9 3AL on 16 May 2006 at 10.00am for the following purposes:

Ordinary business

To consider and, if thought fit, pass the following resolutions as ordinary resolutions:

1. To receive and adopt the audited accounts and the Directors' and Auditor's Report for the year ended 31 December 2005.
2. To receive and approve the Report of the Board of Directors on Directors' Remuneration for the year ended 31 December 2005.
3. To declare a final dividend for the year ended 31 December 2005 of 3.0p net per ordinary share, such dividend to be payable on 26 May 2006 to shareholders on the register at the close of business on 28 April 2006.
4. To re-elect R H Lawson as a Director who retires by rotation.
5. To re-elect C J Ryan as a Director who retires by rotation.
6. To re-elect N G Howard as a Director having been appointed since the last Annual General Meeting.
7. That KPMG Audit Plc be and are hereby re-appointed as auditor of the Company to hold office from the conclusion of this meeting until the conclusion of the next Annual General Meeting at which accounts are laid before the Company at a remuneration to be fixed by the Directors.
8. That the Board be and is hereby generally and unconditionally authorised to exercise all powers of the Company to allot relevant securities (within the meaning of Section 80(2) of the Companies Act 1985) of the Company up to an aggregate nominal amount of £604,726 to such persons and on such terms as it thinks fit provided that this authority shall expire on the date of the next Annual General Meeting after the passing of this resolution or 15 months after the passing of this resolution (whichever shall be earlier) save that the Company may before such expiry make such an offer or agreement which would or might require relevant securities to be allotted after such expiry and the Board may allot relevant securities in pursuance of such an offer or agreement as if the authority conferred hereby had not expired, such authority to be in substitution for any existing authorities conferred on the Board pursuant to Section 80 of the Companies Act 1985.

Special business

To consider and, if thought fit, to pass the following resolutions which will be proposed as special resolutions:

9. That subject to the passing of resolution 8 the Board be and is hereby empowered pursuant to Section 95 of the Companies Act 1985 to allot equity securities (within the meaning of Section 94(2) to Section 94 (3A) of the said Act) for cash pursuant to the authority conferred by the previous resolution as if Section 89(1) of the said Act did not apply to any such allotment provided that this power shall be limited:
 - (a) to the allotment of equity securities in connection with an issue in favour of ordinary shareholders where the equity securities respectively attributable to the interests of all ordinary shareholders are proportionate (as nearly as maybe) to the respective numbers of ordinary shares held by them subject only to such exclusions or other arrangements as the Directors may consider appropriate to deal with fractional entitlements or legal or practical difficulties under the laws, rules or regulations of any jurisdiction, stock exchange or other regulatory body whatsoever; and
 - (b) to the allotment (otherwise than pursuant to sub-paragraph (a) above) for cash of equity securities up to an aggregate nominal value of £90,799, and shall expire on the date of the next Annual General Meeting of the Company after the passing of this resolution or 15 months after the passing of this resolution (whichever shall be earlier) save that the Company may before expiry make an offer or agreement which would or might require equity securities to be allotted after such expiry and the Board may allot equity securities in pursuance of such an offer or agreement as if the authority conferred hereby had not expired, such authority to be in substitution for any existing authorities conferred on the Board pursuant to Section 95 of the Companies Act 1985. This power applies in relation to a sale of shares which is an allotment of equity securities by virtue of Section 94 (3A) of the said Act as if the words "pursuant to the authority conferred by the previous resolution" were omitted.

NOTICE OF 2006 ANNUAL GENERAL MEETING

10. That the Company be and is hereby generally and unconditionally authorised for the purposes of Section 166 of the Companies Act 1985 to make one or more market purchases (within the meaning of Section 163(3) of the said Act) on the London Stock Exchange plc of ordinary shares of 5p each in the capital of the Company provided that:

- (a) the maximum aggregate number of ordinary shares hereby authorised to be purchased is 3,631,992 (representing 10% of the Company's issued ordinary share capital);
- (b) the minimum price which may be paid for such shares is 5p per share (exclusive of any applicable taxes and expenses);
- (c) the maximum price (exclusive of any applicable taxes and expenses) which may be paid for an ordinary share shall not be more than 5% above the average of the market values for an ordinary share as derived from the London Stock Exchange Daily Official List for the five business days immediately preceding the date on which the ordinary share is purchased;
- (d) unless previously renewed, varied or revoked, the authority hereby conferred shall expire at the conclusion of the Company's next Annual General Meeting or 15 months from the date of passing this resolution, if earlier; and
- (e) the Company may make a contract or contracts to purchase ordinary shares under the authority hereby conferred prior to the expiry of such authority which will or may be executed wholly or partly after the expiry of such authority and may make a purchase of ordinary shares in pursuance of any such contract or contracts.

11. Amendments to the Memorandum and Articles of Association:

THAT:

- (a) the Company's Memorandum of Association be and is amended by the insertion of a new sub-clause 4(36) as follows:

To provide any current or former Director, secretary or other officer of the Company with funds to meet expenditure incurred or to be incurred by him in defending any criminal or civil proceedings or in connection with any application under those provisions of the Companies Act 1985 referred to in Section 337A(2) of the said act and to do anything to enable such persons to avoid incurring such expenditure.

- (b) the Company's Articles of Association be and are amended as detailed in the appendix marked A accompanying the notice of Annual General Meeting dated 7 April 2006 (a copy of which is presented to the meeting and signed by the Chairman for the purpose of identification).

By order of the Board



C G Hurst
Company Secretary
Zotefoams plc

Registered office
675 Mitcham Road
Croydon CR9 3AL

7 April 2006

Notes

- (i) Shareholders are entitled to attend and vote at this meeting and may appoint one or more proxies to attend and on a poll, vote instead of him. A proxy need not be a member of the Company. A form of proxy is enclosed for the use of members and must reach the office of the Registrars of the Company not less than 48 hours prior to the start of the meeting.
- (ii) The appointment of a proxy will not prevent the member from subsequently attending and voting at the meeting in person.
- (iii) Copies of the following will be available for inspection at the registered office of the Company, 675 Mitcham Road, Croydon CR9 3AL during normal business hours from the date of the above notice until the date of the Annual General Meeting and at the place of the meeting for 15 minutes prior to and until the termination of the Meeting:
 - (a) the register of Directors' share interests; and
 - (b) copies of executive Directors' service contracts.
- (iv) Only those members registered in the register of members of the Company as at 10.00am on 14 May 2006 will be entitled to attend or vote at the meeting in respect of the number of ordinary shares of 5p registered in their respective names at that time. Changes to entries on the register after 10.00am on 14 May 2006 will be disregarded in determining the rights of any person to attend or vote at the meeting.

FIVE YEAR TRADING SUMMARY

	IFRS 2005 £m	IFRS 2004 £m	UK GAAP 2003 £m	UK GAAP 2002 £m	UK GAAP Restated 2001 £m
Turnover	28.0	25.2	23.5	23.5	23.0
Operating profit (excluding exceptional items)	2.0	1.6	1.1	2.2	2.9
Profit before tax (excluding exceptional items)	1.8	1.3	1.0	2.0	2.8
Profit before tax (including exceptional items)	3.3	1.3	1.0	8.6	3.5
Profit after tax	2.4	1.2	0.7	6.0	3.3
Capital expenditure	1.1	1.3	1.6	5.2	6.1
Cash generated from the operations	4.1	5.3	3.5	11.0	0.8
Dividends per ordinary share (p)	4.5	4.5	4.5	7.5	7.5
Earnings per share excluding exceptional items (p)	3.5	3.2	2.0	4.0	5.6
Earnings per share including exceptional items (p)	6.7	3.2	2.0	16.6	9.0

The amounts disclosed for 2003 and earlier periods is stated on the basis of UK GAAP because it is not practicable to restate amounts prior to the date of transition to IFRSs. The principal differences between UK GAAP and IFRSs are explained in the Appendix: Explanation of Transition to IFRS on page 50.

FINANCIAL CALENDAR

Annual General Meeting	16 May 2006
Payment of final dividend	26 May 2006 to shareholders on the register at the close of business on 28 April 2006
Announcement of 2006 interim results	August 2006
Payment of interim dividend	October 2006
Announcement of 2006 results	March 2007

Registrars

Enquiries concerning the holding of ordinary shares in the Company should be addressed to the registrars who should also be notified of any changes in a holder's address.

The registrars are: Computershare Investor Services Plc, PO Box 82, The Pavilions, Bridgwater Road, Bristol BS99 7NH.

Website

The Company has a website (www.zotefoams.com) which provides information on the business and products.

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