Spirax-Sarco Engineering plc

The Business of Solutions 2012

Spirax-Sarco Engineering plc
Annual Report and Accounts 2012

Introduction

Spirax-Sarco Engineering plc is a multi-national industrial engineering group specialising in steam and pump technology.

What is our investment proposition?

- We seek to deliver consistent annual organic sales growth and have a long history of steady growth and high trading margins.
- We have excellent prospects for future growth – organic sales revenues over the past 30 years have increased by more than 8% per annum.
- We have a resilient business model. We benefit from the diversity of our end user industries and customers, our geographic spread and significant presence in emerging markets, high replacement product content and a large base of industrial steam systems installed around the world that require continual upkeep and improvement.
- We operate with a strong balance sheet to protect the business and facilitate future growth. We manage capital employed to turn profit into cash, which we will reinvest to sustain and improve future returns or, where cash generated exceeds expected future requirements, will seek to return to shareholders.
- We provide value to shareholders through consistent growth in earnings and dividends, and are proud to have extended our dividend record to 45 years.

We are creating value…

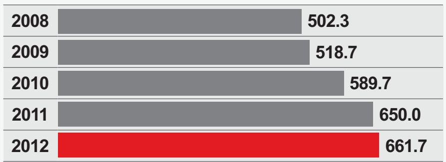
- In 2012, revenue grew 5% at constant currency to £662m
- Pre-tax profit grew £7m at constant currency to £139m
- Free cash flow £92m

In this report we explain how the business can generate more value for investors and what we are doing to make it happen.

Front cover image: Stainless steel chimneys in Munich, Germany.

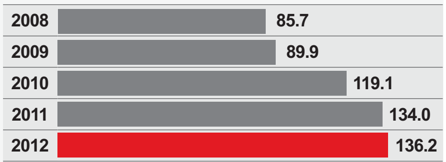
Performance highlights

Revenue £m



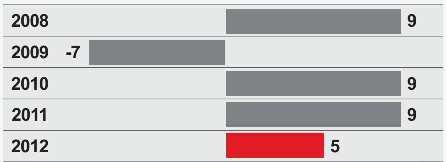
£661.7m **+2%**

Operating profit* £m



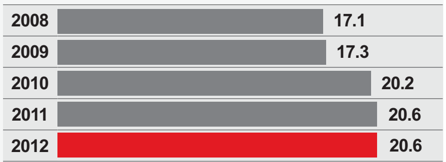
£136.2m **+2%**

Sales growth (organic) %



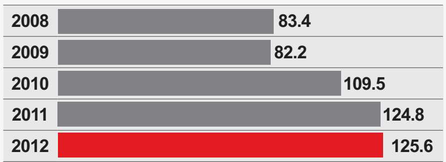
5%

Operating profit margin* %



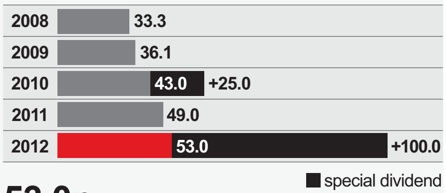
20.6%

Earnings per share* p



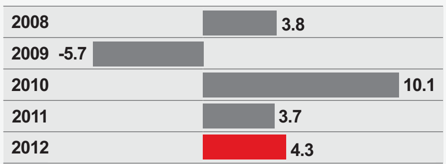
125.6p

Dividends per share p



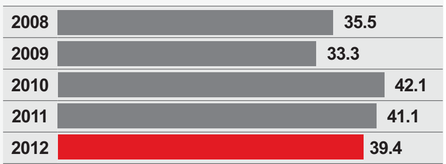
53.0p

Operational efficiency – change in sales per person** %



4.3%

Return on capital employed %



39.4%

- **Another year of record sales and profit**
- **Group organic sales increased 5%**
- **Operating profit up 6% at constant currency**
- **Cash generation at record levels – ending net cash £52m**
- **Core dividend up 8%**
- **Special dividend recommended of 100p (£78m)**

* based on adjusted operating profit
** at constant currency.

Contents

"The Group has developed a robust, global business model that has proved resilient through the business cycles."

Mark Vernon
Group Chief Executive

"The Group's prime financial objective remains to provide enhanced value to shareholders through consistent growth in earnings per share and dividends per share."

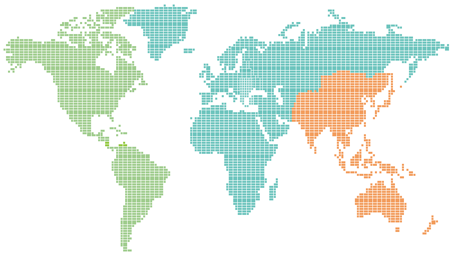
David Meredith
Finance Director

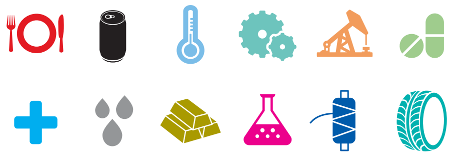
Overview

Understanding our global business

A welcome from our Chairman, an overview of what we do, the markets we work in and the size, scale and performance of our global operations.

John Pickering (National Contracts Manager) and Kevin Fox (Senior Sales Engineer) consulting plans for a turnkey steam system, Polestar Printworks, Sheffield, UK.





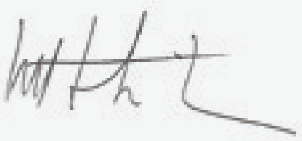
Chairman's statement
page 4

Global operations
page 8

Our markets
page 10

Chairman's statement

I am pleased to report further progress in 2012 and another year of record sales, profit and cash generation.



Bill Whiteley
Chairman

Sales increased by 2% from £650.0 million to £661.7 million. Organic sales growth was 5%, which continued through the second half year despite the slowing in global economic growth. Sales growth was strongest in Asia Pacific and Watson-Marlow Pumps, followed by more modest growth in the Americas and flat organic sales in Europe, Middle East and Africa (EMEA). Unfavourable currency movements reduced sales by 3%.

Operating profit increased by 2% from £134.0 million to £136.2 million with a constant currency increase of 6%. The operating profit margin was unchanged at last year's record level of 20.6% with, as anticipated, a significant improvement in the second half year. At constant currency the margin was slightly ahead of last year. Margins were higher for the year in Asia Pacific and Watson-Marlow Pumps.

Net finance income reduced from £1.1 million to £0.4 million due to lower finance income in respect of the Group's defined benefit pension schemes. The Group's share of the after tax profits of our Associate in India reduced from £2.1 million to £1.9 million due to unfavourable currency movements.

Pre-tax profit rose 1% to £138.5 million (2011 : £137.2 million) and at constant currency, pre-tax profit rose 5%. Adjusted earnings per share were 1% higher at 125.6p (2011 : 124.8p).

The statutory pre-tax profit was £127.7 million (2011 : £132.3 million), which was after charging the usual amortisation of acquisition-related intangible assets and acquisition and disposal costs, but also, in 2012, after recognising exceptional restructuring costs of £7.2 million (2011 : nil).

Cash generation was at record levels in 2012 and we continue to operate with a strong balance sheet, finishing the year with net cash of £51.7 million.

The interim dividend was increased by 8% to 16.0p per share, which was paid in November 2012. The Board is recommending an increase in the final dividend of 8% to 37.0p per share payable on 17th May 2013 to shareholders on the register at the close of business on 19th April 2013. The total Ordinary dividend is therefore 53.0p per share (2011 : 49.0p), an increase of 8%. The cost of the interim and final dividend is £41.4 million, which is covered 2.4 times by earnings. In addition, following a review of the Company's capital requirements, the Board is recommending a return of cash to shareholders of £78 million in the form of a special dividend of 100.0p per share in respect of 2012 (2011 : nil) payable on 3rd July 2013 to shareholders on the register at the close of business on 31st May 2013. This is equivalent to approximately 4% of the market capitalisation of the Company and, as is common with a significant return of capital, the Board recommends that this is combined with a share consolidation to maintain, as far as possible, the comparability of the share price before and after the special dividend.

Economic conditions have remained challenging and the Board expresses its thanks to all our employees for their resilience, hard work and dedication in contributing to the outstanding results in 2012.

In 2012 we were pleased to welcome three new Board members, Dr Trudy Schoolenberg as an independent Non-Executive Director, Nick Anderson as Executive Director for the steam specialties business in EMEA and Jay Whalen as Executive Director for Watson-Marlow Pumps. These Directors bring considerable knowledge, experience and diversity to the Board, and we look forward to their valuable contribution.

Corporate governance

The Board is ultimately responsible for ensuring that the Group achieves its strategic objectives, which leads to sustainable growth in shareholder value. In doing so, the Board and its Committees operate to the highest ethical standards and corporate governance practices, setting the tone for the entire organisation and for our other business stakeholders. We believe that good governance is about managing the business effectively and in a way that is honest, transparent and accountable. Corporate governance reporting and disclosure best practice have been developing rapidly. We have taken a further significant step in our 2012 Annual Report to improve the explanation of our strategy, objectives and business model, and to enhance the disclosures relating to the work of Board Committees, risk management, Board remuneration and how we comply with the provisions of the UK Corporate Governance Code, all of which I hope you find interesting and helpful.

Prospects

Global economic growth progressively slowed throughout 2012 and many European economies are back in recession. We anticipate that low rates of industrial production growth will persist in most of our mature markets in 2013, with higher rates of growth in our emerging markets, particularly in Asia.

2013 has started in line with our expectations and we look to generate our own sales growth by capitalising on our investments in market development and in new products, and by further penetrating our mature markets.

We have developed a robust and resilient business model, with excellent revenue diversification across geographic regions, industries, end-user customers and products, and with a high proportion of sales coming from replacement products and from our customers' maintenance budgets. These fundamental strengths, combined with our growth strategies and the full-year benefits of the cost reductions in 2012, give the Board confidence that the Group will make further progress in 2013.

Bill Whiteley
Chairman

Our businesses

We comprise two world-leading niche businesses:

- Spirax Sarco for steam specialties
- Watson-Marlow for peristaltic and niche pumps

Our Spirax Sarco steam specialties business is the global leader in the supply of engineered solutions for the design, maintenance and operation of efficient industrial and commercial steam systems.

As a heat source, steam is the natural choice in most industrial processes due to its high heat-carrying capacity, controllability, sterility and efficiency as a heat transfer fluid. With our specialist knowledge, technical expertise and wide range of products and services, as well as our extensive global presence, Spirax Sarco is uniquely positioned to provide a broad range of environmentally-friendly engineered solutions to the many industries using steam.

Our customers face a variety of challenges including high energy costs, pressure to improve the operating efficiency and capacity of existing processes, and the need to comply with increasingly stringent health, safety and environmental legislation. Our direct sales force is highly trained in product application, system performance and the troubleshooting of steam systems.

The Spirax Sarco offering is very wide, from single products through to complete turnkey bespoke packages that can include design, fabrication, installation, commissioning and maintenance.

Watson-Marlow is the global leader in peristaltic and selective niche pumps and systems, specialising not only in the design and manufacture of the most advanced pumps and tubing, but also in the application of those pumps to our customers' processes.

Our peristaltic pumps are ideal for difficult pumping applications. They are highly accurate and controllable and virtually maintenance -free, making them a very reliable and cost-effective solution.

Operating a make-to-order manufacturing system and uniquely extruding our own pump tubing, we have the leading position in the supply of peristaltic pumps and tubing to the biotechnology, pharmaceutical, wastewater treatment, mining and food industries.

The peristaltic pumping market is a small part of the global pump market but it is one of the fastest growing segments.

Group revenue

Spirax Sarco	£537.2m
Watson-Marlow	£124.5m
Total	**£661.7m**

Group operating profit

Spirax Sarco	£106.9m
Watson-Marlow	£36.8m
Total	**£143.7m**
Corporate expenses	(£7.4m)
Total	**£136.2m**

* Unless stated otherwise, all references are to adjusted profit, which excludes certain non-operational items as set out in note 2 on page 94.

Group at a glance

The Group comprises the Spirax Sarco steam specialties business and Watson-Marlow peristaltic and niche pumps.

The Spirax Sarco steam specialties business is split into three regional divisions:

- Europe, Middle East and Africa (EMEA)
- Asia Pacific
- Americas.

Spirax Sarco EMEA

	Change
Revenue £232.8m	-7%
Operating profit £36.7m	-14%
Operating margin 15.8%	-120bps

Highlights

- Organic sales flat (reported sales down 7% due mainly to weak euro)
- Economic conditions deteriorated throughout 2012
- Flat sales in combined large mature markets of France, Germany, Italy, Spain and the UK
- Eastern Europe impacted by Eurozone uncertainty but higher second half demand
- Restructuring actions taken to reduce cost base in Europe
- Operating profit down 4% at constant currency
- Uncertainty clouds outlook

page 18

Revenue £m

2008	226.1
2009	225.5
2010	230.0
2011	250.1
2012	232.8

Operating profit £m

2008	39.2
2009	35.6
2010	36.8
2011	42.5
2012	36.7

Spirax Sarco Asia Pacific

	Change
Revenue £166.9m	+13%
Operating profit £43.9m	+16%
Operating margin 26.3%	+60bps

Highlights

- Sales up 12% at constant currency – good growth across product groups
- Market conditions broadly positive
- Another outstanding year in China – good exposure to domestic consumption
- Good year in Korea from a strong project-driven second half
- Continued to add sales resource in emerging markets
- Operating profit up 11% at constant currency and margin at 26.3%

page 20

Revenue £m

2008	98.9
2009	104.7
2010	131.5
2011	147.1
2012	166.9

Operating profit £m

2008	21.1
2009	23.1
2010	34.3
2011	37.8
2012	43.9

Group structure

Spirax-Sarco Engineering plc

- **Spirax Sarco steam specialties**
  - EMEA
  - Asia Pacific
  - Americas
- **Watson-Marlow Pumps**

Revenue by business

Steam specialties EMEA	£232.8m
Steam specialties Asia Pacific	£166.9m
Steam specialties Americas	£137.5m
Watson-Marlow Pumps	£124.5m
Total	**£661.7m**

Operating profit by business

Steam specialties EMEA	£36.7m
Steam specialties Asia Pacific	£43.9m
Steam specialties Americas	£26.2m
Watson-Marlow Pumps	£36.8m
Total	**£143.7m**
Corporate expenses	(£7.4m)
Total	**£136.2m**

Spirax Sarco Americas

		Change
Revenue	£137.5m	+2%
Operating profit	£26.2m	-4%
Operating margin	19.1%	-130bps

Highlights

- Sales up 6% at constant currency (reported sales up 2% from unfavourable currency)
- North American market conditions broadly positive but slowing large project activity
- Softness in US with overall lower demand in Q4
- Latin America market conditions mixed
- Sales and profits down in Brazil – exceptional project benefited Argentina
- Operating profit up 3% at constant currency versus record prior year
- Margin lower at 19.1%

page 22

Revenue £m

2008	101.9
2009	104.6
2010	125.2
2011	134.4
2012	137.5

Operating profit £m

2008	12.1
2009	13.9
2010	24.3
2011	27.4
2012	26.2

Watson-Marlow

		Change
Revenue	£124.5m	+5%
Operating profit	£36.8m	+7%
Operating margin	29.6%	+50bps

Highlights

- Sales up 8% at constant currency – growth across all product lines
- Difficult trading conditions in EMEA but sales growth in most operations
- Trading conditions positive in bio-pharmaceuticals, precious metals processing and OEM
- Strong sales growth in the Americas and particularly Latin America
- Sales ahead in all operations in Asia Pacific – new operations in India and Singapore
- Operating profit up 10% at constant currency and margin increased to 29.6%

page 24

Revenue £m

2008	75.4
2009	83.8
2010	103.0
2011	118.4
2012	124.5

Operating profit £m

2008	18.4
2009	22.3
2010	30.8
2011	34.4
2012	36.8

Global operations

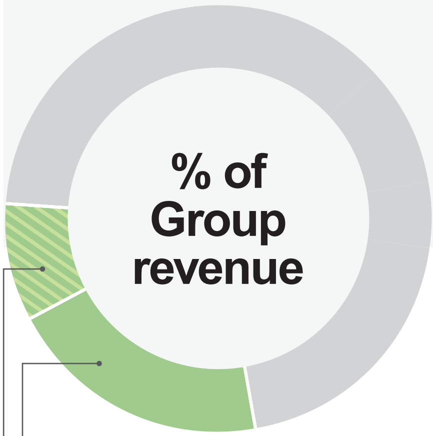
Operating in more than 100 countries worldwide, we are a company with a global reach. Our strong presence around the world makes us the first choice provider of steam specialties solutions and niche pumps. Our investment in emerging markets is delivering good organic sales growth and adding shareholder value.

Operating Company
Sales Offices
Distributors

Our **operating companies** are subsidiaries of Spirax-Sarco Engineering plc. They support and advise customers, supplying from local stocks. They include regionally based manufacturing operations supplying products largely to meet local or regional demand.

Our **sales offices** sell our products and services in specific geographical areas, ensuring comprehensive market coverage.

Our **distributors** are authorised to sell and deliver our products to customers in defined geographical areas.



Americas
29%
2011: 28%

Emerging markets
9%
2011: 9%

Argentina
Bolivia
Brazil
Canada
Chile
Colombia
Costa Rica
Dominican Republic
Ecuador
El Salvador
Guatemala
Honduras
Jamaica
Mexico
Netherlands Antilles
Nicaragua
Panama
Paraguay
Peru
Trinidad and Tobago
Uruguay
USA
Venezuela

EMEA

44%
2011: 48%

Emerging markets
8%
2011: 9%

Europe

Austria
Belgium
Bulgaria
Croatia
Czech Republic
Cyprus
Denmark
Estonia
Finland
France
Germany
Greece
Hungary
Iceland
Ireland
Italy
Latvia
Lithuania
Malta
Netherlands
Norway
Poland
Portugal
Romania
Russia
Slovak Republic
Slovenia
Spain
Sweden
Switzerland
Ukraine
UK

Middle East

Bahrain
Israel
Jordan
Kuwait
Lebanon
Oman
Qatar
Saudi Arabia
Syria
Turkey
UAE

Africa

Algeria
Cameroon
Egypt
Ethiopia
Ghana
Ivory Coast
Kenya
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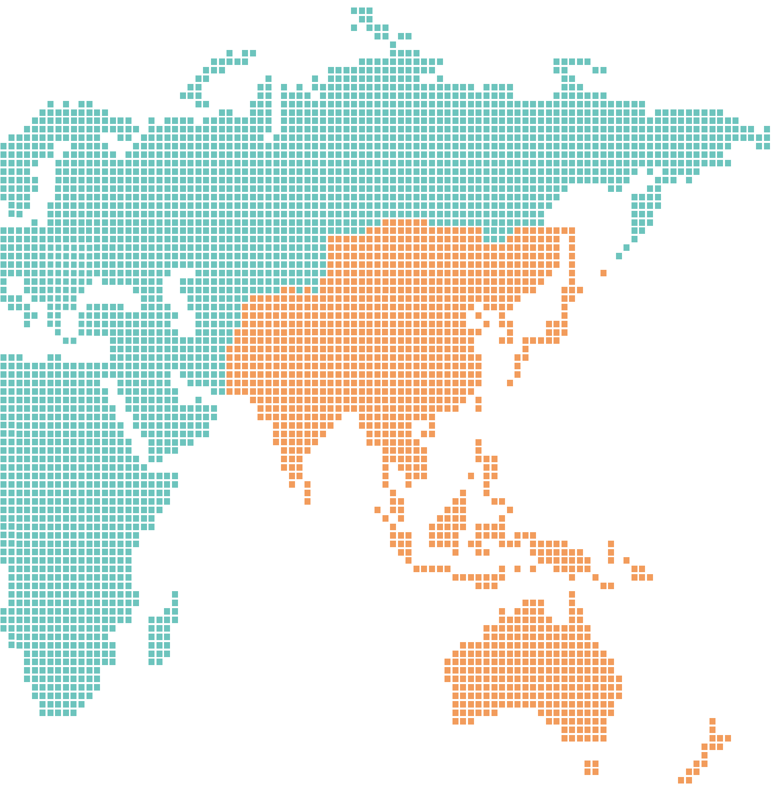
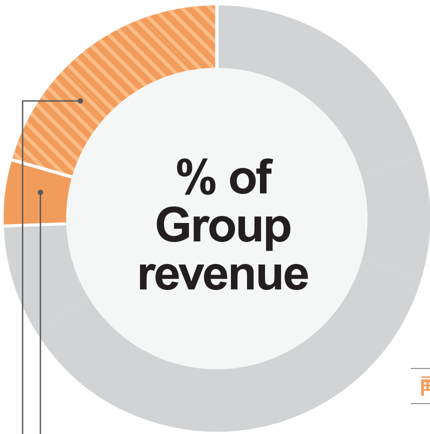
Namibia
Nigeria
South Africa
Sudan
Tanzania
Uganda
Zambia
Zimbabwe





Asia Pacific

27%
2011: 24%

Emerging markets
22%
2011: 20%

Australia
Bangladesh
China
Cambodia
India
Fiji
Hong Kong
Indonesia
Japan
Malaysia
Myanmar
New Zealand
Philippines
Singapore
South Korea
Taiwan
Thailand
Vietnam

Our markets

We serve a wide range of industries and this diversity insulates the Company from seasonal and cyclical demand. This section shows the specific applications in which we apply our tailored solutions to reduce energy costs and improve plant efficiency.

One of the great strengths of the Group is our diverse range of customers and end markets. We have an excellent balance between cyclic higher-growth end markets and those that are more 'defensive' that tend to be more recession-proof. More than 50% of the Group's revenues are derived from these defensive end markets including: foods, beverages, HVAC, pharmaceuticals, healthcare, water treatment, chemicals, textiles and power generation. More than 85% of our revenues are derived from our customers' annual maintenance or operations' budgets.

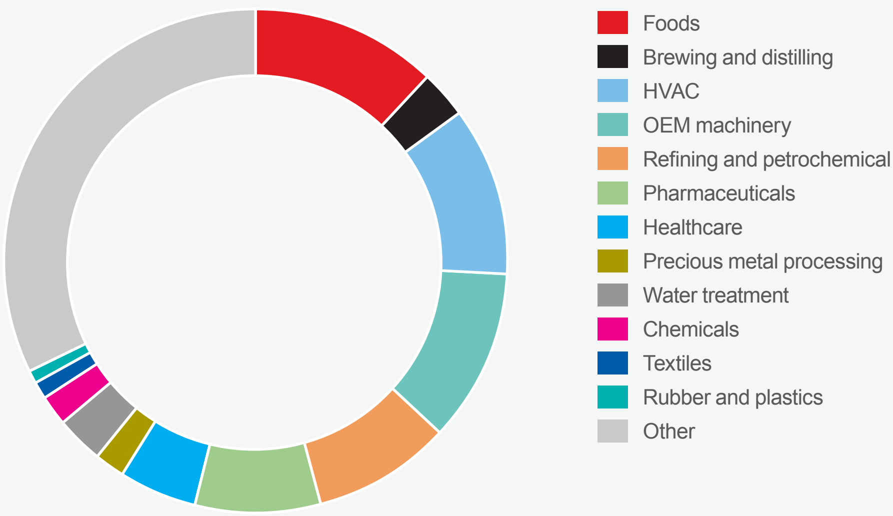
Foods processing is our largest single end market and represents approximately 12% of total Group sales. This end market has manysub-sectors such as rendering plants, slaughterhouses, packaged foods, dairies, raw foods processing, sugar processing and palm oil processing, which are important markets for both our steam specialties business and Watson-Marlow Pumps. We have a very high exposure to food processing throughout Asia, and this represents 40% or more of total Asia sales.

HVAC is our second largest end market (11% of sales) served by our steam specialties business, with applications in humidification (including during the production of semi-conductors, electronics and LCD and plasma screens), space heating (for large public buildings and university complexes) and instantaneous hot water (for hospitals, resort hotels and commercial buildings).

Our third largest end market is refining and petrochemicals (9% of sales). Steam is extensively used in catalytic and thermal cracking of crude oil, distillation columns, power generation and in heat tracing.

Pharmaceuticals, including biotechnology, is our fourth largest end market (8% of sales) and represents the single largest end market for our Watson-Marlow pumps business, comprising about 30% of total Watson-Marlow sales.

Revenue by sector



Foods

- Steam is widely used in the production of packaged foods, for blanching, cooking, baking, packaging and sterilising.

Brewing and distilling

- Steam is essential for brewing and distilling processes. It is used to protect product quality and flavour, and ensure compliance with industry standards.

HVAC

- Our products are used to provide space heating, humidification and hot water to create comfortable working conditions for employees and visitors in public and private buildings.

OEM machinery

- We work with manufacturers to optimise the performance of a diverse range of equipment, including mixers, reactors, paper and packaging machines, dryers, sterilisers and clinical diagnostic equipment.

Refining and petrochemical

- Our steam system services and products enable optimum performance in steam and condensate systems, and reduce energy use during refining and petrochemical production.

Pharmaceuticals

- Clean steam reduces the risk of product and process contamination, and our peristaltic pumps enable precise flow control and fluid isolation in the pharmaceutical industry.

Healthcare

- Our products have a wide range of applications in hospitals and clinics for space heating, hot water production, humidification and sterilisation.

Precious metal processing

- Peristaltic pumps reduce water, energy and chemical use and increase reliability and productivity while moving and processing highly abrasive ores and slurries.

Water treatment

- Peristaltic pumps are used to accurately dose chemicals during water treatment processes and efficiently transfer viscous and abrasive slurries.

Chemicals

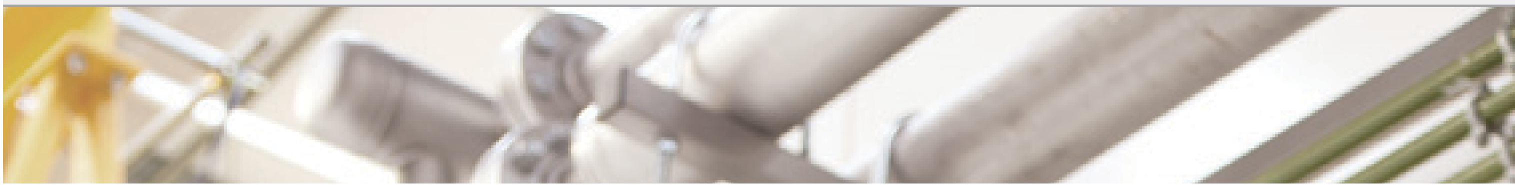
- Steam is widely used as an energy source in chemical production and product processing.

Textiles

- Fabric and carpet production use steam during the spinning, dyeing and finishing processes.

Rubber and plastics

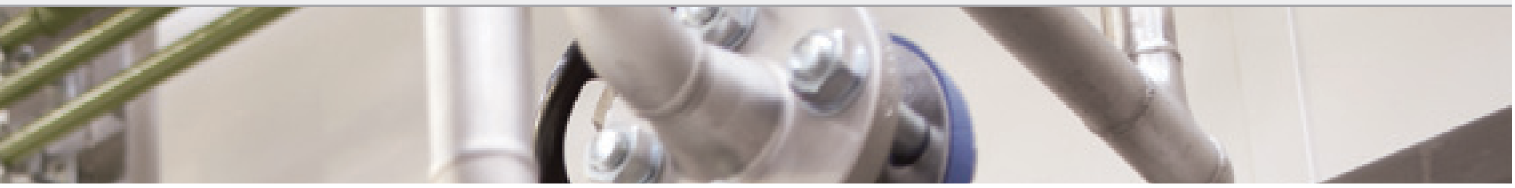
- Our products facilitate temperature control of exothermic process reactors, critical to the manufacture of modern composite materials.

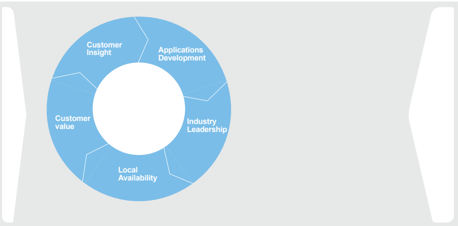


Generating value

An overview of our business model, our strategies for growth and business performance during 2012.

An engineer adjusting an installed bellows-sealed isolation valve, UK Technology Centre.





Business model

page 14

Strategies for growth

page 16

Business review

page 17

Business model

Our purpose

To assist our customers to achieve environmentally friendly solutions for energy savings, process efficiency, product quality and improvements in plant health, safety and regulatory compliance.

Our execution

Our business model is anchored by deep customer insight and strategy is delivered through innovation, market leadership, engineering, regional manufacturing and customer support.

Our vision

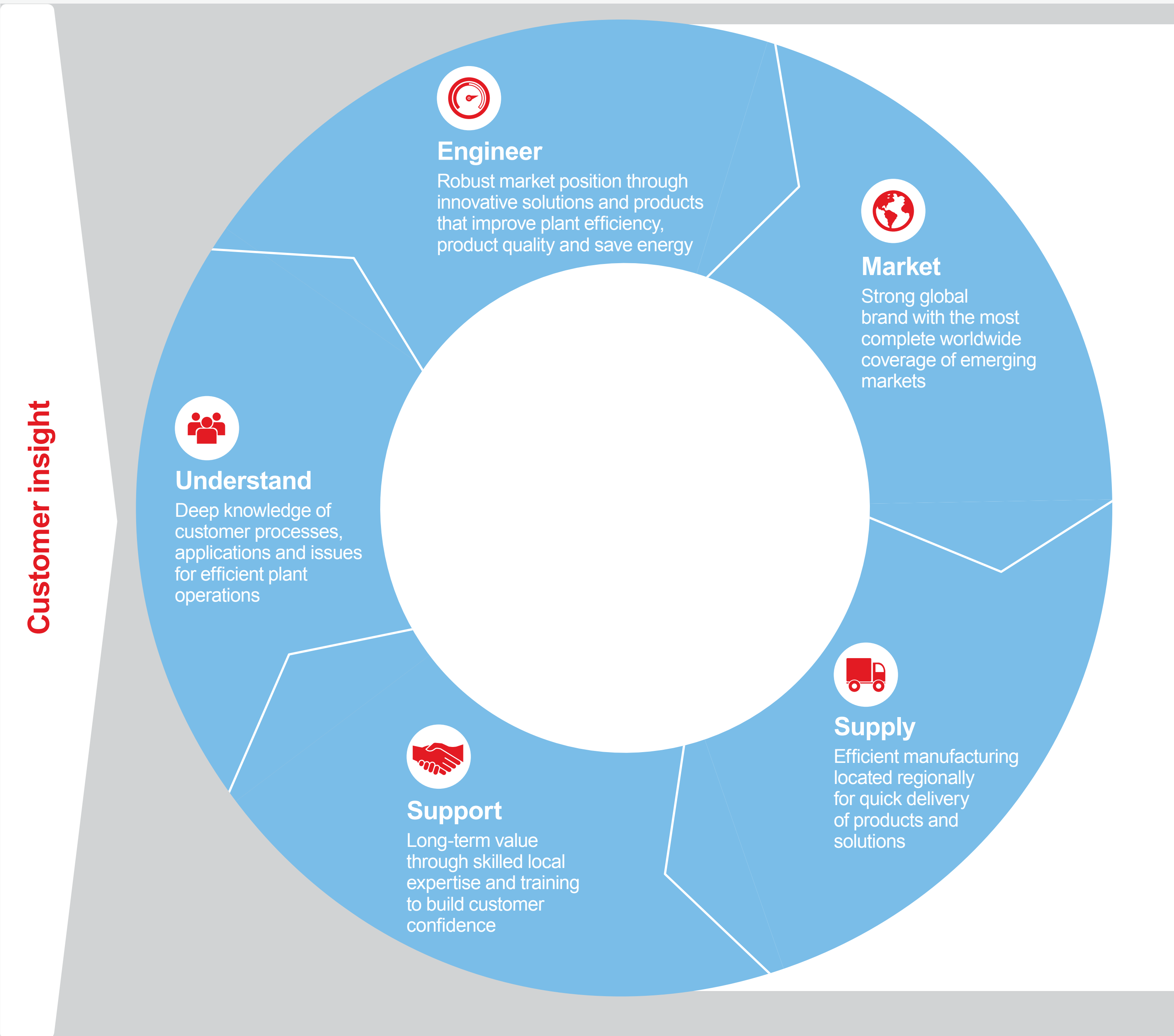
To deliver consistent, profitable and sustainable growth and shareholder value.

To be the customers' first choice provider of solutions for the effective use of steam and industrial fluids worldwide, as well as the global leader in the development and manufacture of peristaltic and niche pumps.

To act ethically at all times and embody our core values of respect, accountability, passion, integrity and delivery.

Business foundation

Strategic execution



Aligning results and reward

Remuneration policy

Our remuneration policy creates a strong alignment between the achievement of strategic objectives, the creation of long-term shareholder value and the remuneration received by Executive Directors.

In order to align results with rewards, a significant percentage of the remuneration package is dependent upon meeting challenging performance targets, including in respect of return on capital employed, profit and earnings per share.

We aim to reward employees fairly and provide performance-related remuneration to ensure that we recruit and retain the talented individuals required to meet the Group's strategic objectives in both the short and long-term.

For more details see the Remuneration report on page 60.

Underpinned by

Human capital
Building on a global team of professionals with process and application expertise that makes us a unique and valued customer partner.

Sustainability
Providing environmentally friendly solutions for energy savings, process efficiency, product quality and plant health, safety and regulatory compliance.

Operational excellence
Efficient, integrated operations that deliver market leading, high-quality products, services and solutions.

Risk management
Resilience through strengthening our robust business model with diverse revenue streams and emphasis on governance.

Financial discipline
Focus on growth, organisational efficiency and management of our balance sheet to generate higher profits, increase cash flows and maximise returns on capital.

Remuneration aligned to four key performance metrics

Operating profit (adjusted) £m

2011	134.0
2012	136.2

Return on capital employed (ROCE) %

2011	41.1
2012	39.4

Total shareholder return over a three year period %

2011	132.5
2012	104.7

Earnings per share growth p

2011	124.8
2012	125.6

Aligned to remuneration policy
See page 62

Strategies for growth

We have developed a robust global business model and seek to build upon this foundation with five primary strategies to develop our future growth prospects.

Mark Vernon
Group Chief Executive

Key strategies

Create strong market positions through local expertise and customer insight.

Deliver solutions to reduce energy usage through innovative engineering and comprehensive energy audits.

Broaden our global presence through first-to-market leadership in emerging markets.

Grow market share through increased market penetration and one-stop shop customer approach.

Generate consistent organic growth by providing greater customer value.

What are the strategies for developing the business over the longer term?

The Group has developed a robust, global business model that has proved resilient through the business cycles. We are seeking to build upon this foundation with five primary strategies to develop the future growth prospects of the business.

- We seek to further **strengthen our strong global market positions** in steam systems and niche pumping through strong customer relationships in which our highly-trained local sales engineers and technical support staff provide expertise in applications and in steam system design, operations and maintenance.
- We **supply effective solutions** in response to difficult customer plant productivity issues and we help our customers reduce their energy and water usage, and save money.
- We are **broadening our global presence** by being first to enter new markets with a direct presence that enables us to deliver to our customers the full range of engineering solutions, products and services.
- We seek to **grow our market share** by widening the range of products, services and pre-fabricated engineered packages that we supply, and to make it even easier for our customers to source all their requirements from us.
- We strive to **generate consistent organic sales growth** by providing greater customer value through skilled local expertise, close customer relationships and local availability of a wide range of products and engineering solutions.

How do the strategies align with the changing business environment?

High energy costs and reducing energy and water usage are areas of increasing concern to our customers. Changing legislative requirements that require substantial reductions in CO_2 emissions and other plant emissions, plus better hygienic operations in hospitals and in the production of foods, beverages and pharmaceuticals, are becoming increasingly burdensome to our customers. Additionally, many of our customers are reducing their plant staff and, as a result, are seeking fewer key suppliers to provide turnkey systems design, operations and maintenance consultation.

We have developed a large cadre of local sales and service engineers who are highly trained in efficient steam system design, maintenance and operations, and niche pumping. The skills of our sales and service engineers, coupled with our strategy of widening our range of engineered solutions, are making it easier for our customers to turn to Spirax Sarco to source all their requirements.

What are the short-term goals?

Over the short term, we will continue to add technical sales and support resources in emerging markets around the world. We see excellent growth opportunities in these markets and will continue an investment programme of sustained market development. For example, in the past three years we have added 100 sales and service engineers in our emerging markets in the Middle East, Asia, Africa, Latin America and Eastern Europe, and our sales growth is benefiting from these investments.

In addition to our market development objectives, our product development efforts are yielding exciting new products that are broadening our ability to effectively monitor, meter and control the use of steam and other process fluids. We are also expanding our range of pumps, controls and boilerhouse products to improve plant automation and are looking to introduce new heat exchange and heat recovery solutions to address more difficult heat transfer applications and to convert waste heat into usable energy or power.

Summary

I am confident that the Group is putting in place the longer term strategies that will build upon our already robust and resilient business model. The Group benefits from a very strong global market presence and brands, and we are looking to broaden our range of engineered solutions for our customers in more locations around the world in order to make it even easier for them to source all their steam system and niche pumping requirements from us.

Mark Vernon
Group Chief Executive

The Business of Solutions

We are a global team of professionals with applications and systems expertise that make us a unique and valued customer partner, able to address the key issues facing our customers.

Create strong market positions through local expertise and customer insight

Our understanding of customer processes and applications enables our local skilled engineers to deliver leading edge solutions for sustainable efficiencies in plant operations, ensuring a strong market position.

It is not our products alone that provide value to our customers – it is the application of our extensive knowledge in systems design, operations and maintenance. Our direct sales approach accounts for about 70% of total revenues and is fundamental to our growth. Working directly with our customers in close, long-term relationships, Spirax Sarco sales engineers around the world apply our deep applications and systems knowledge, breadth of products and expertise in offering the most extensive range of engineered solutions.

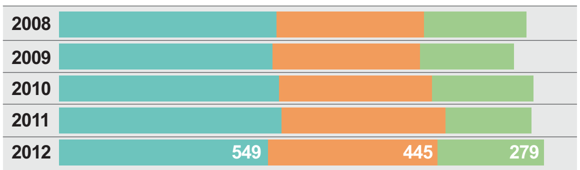
Our customers value the opportunity to source their steam system needs from a competent single source, and rely increasingly on Spirax Sarco. Today we employ nearly 1,300 local sales and service engineers who are focused on assisting steam and pump users to meet their challenges.

The heart of our business lies in our ability to improve the operating and energy efficiency of existing steam systems, increase the throughput of our customers' processes, improve their product quality and assist them in meeting more stringent environmental legislation. This demands that our sales and service people are intimate with the operating issues of individual customers' manufacturing plants and facilities.

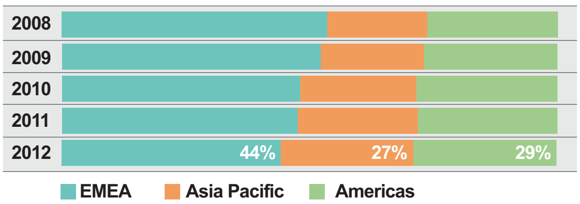
We train our sales engineers in our 42 training centres located around the world, most of which are equipped with live steam or pumping installations that facilitate hands-on training.

These centres are also used to train our customers' technical and maintenance staff. We have developed internet-based tools to improve the technical training of our sales engineers around the world and to speed their development. Additionally, we have installed information collection and sharing software to improve our ability to diffuse application knowledge and provide a common platform to share application knowledge amongst work groups across our global sales network.

Number of sales and service engineers by region



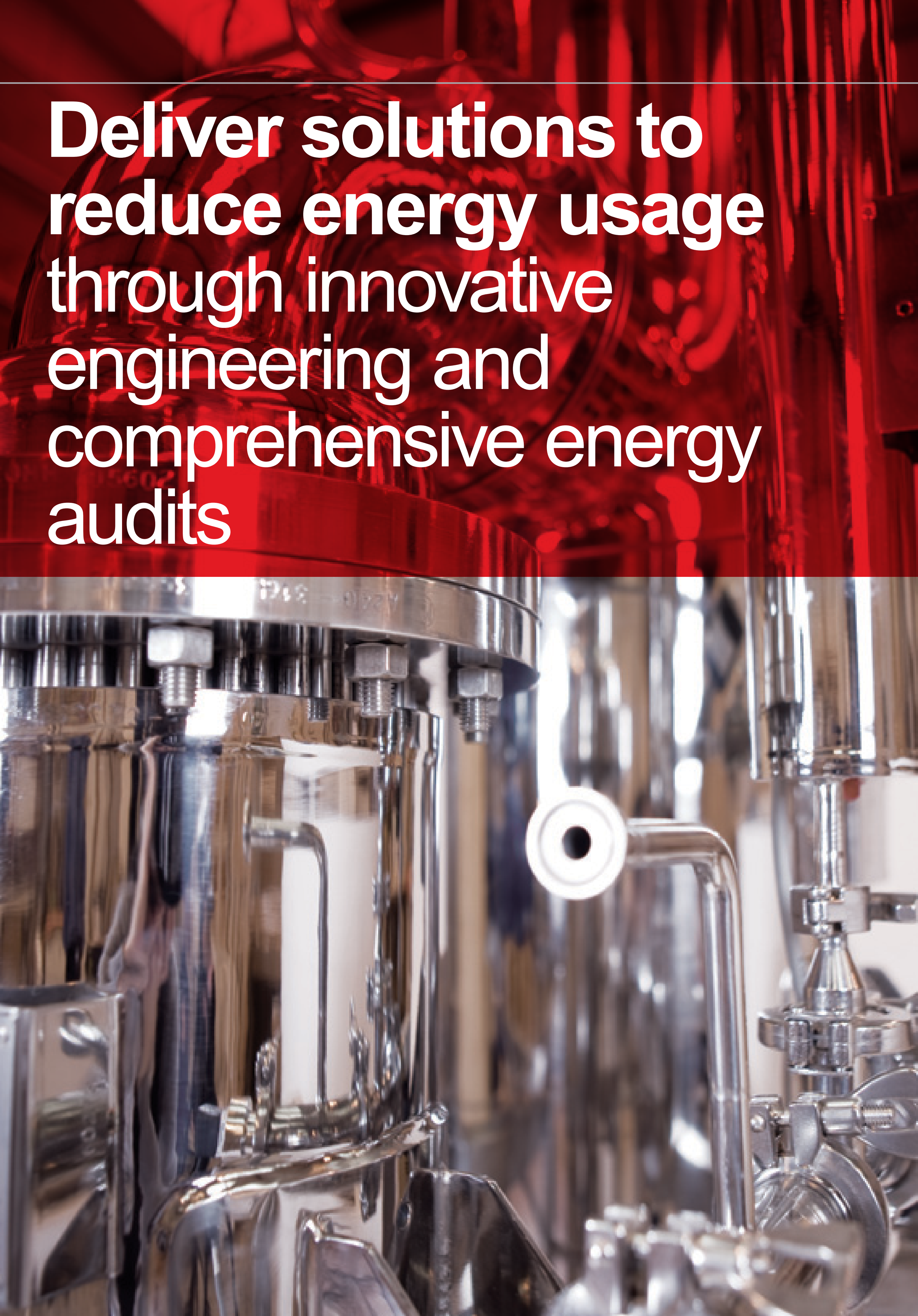
Percentage of sales by geographic region



Hungary for heat

An understanding of processes and applications at the Tiszai Vegyi Kombinat petrochemical plant in Hungary enabled Spirax Sarco engineers to design and implement a solution to solve the problem of a freezing water supply. The efficient and innovative solution, injecting steam directly into the supply pipe, has ensured a constant supply of water in the coldest months.

Deliver solutions to reduce energy usage through innovative engineering and comprehensive energy audits



We provide our customers with innovative engineering solutions and products that save energy, improve plant efficiencies and product quality, and achieve regulatory compliance.

The Group considers its commitment to new product development as critical to its long-term success. In the last four years, the Group has nearly doubled its R&D investments to accelerate the flow of new products, to extend our current range of products and applications, and open new markets.

In 2011, we completed construction of what we believe is the world's largest and most capable live steam testing facility, with the capacity to generate flows of up to 30,000 kg/hour of saturated steam and work at pressures of up to 110 bar (1,595 psig) – this facility enables us to accelerate product development and comprehensively test new product designs at elevated operating temperatures and pressures. Although we operate R&D development and test centres at several locations around the world, the bulk of our development activities for both steam system products and peristaltic pumps are centred in the UK.

This year we introduced our new range of EasiHeat™ pre-fabricated, hot water delivery systems incorporating our unique SIMS™ software technology for local and remote monitoring and configuration. The EasiHeat™ units deliver hot water instantaneously on demand and save significant energy by eliminating the need for our customers to supply continuous heating to maintain a high temperature of large volumes of stored hot water.

Our Watson-Marlow pump business launched the Qdos pump containing revolutionary new pumping technology. This new technology significantly extends the lifetime operation of our Qdos peristaltic pumps and improves plant efficiency by eliminating costly downtime and repair of other positive displacement pump types that are being replaced by the Qdos pump.

Our highly trained sales and service engineers are increasingly called upon to assist our customers in more comprehensive plant-wide energy audits to reduce their energy and water usage, lower plant emissions and improve overall energy efficiency. Although these audits typically cover the thermal aspects of plant energy usage, we also have capabilities to cover a broader range of energy consumption, including boiler efficiency, plant compressed air usage and HVAC efficiency. Investments made by our customers to improve their energy efficiency typically result in payback periods of less than two years.

R&D expenditure £m

2008	5.4
2009	6.7
2010	7.4
2011	9.9
2012	10.1

A reliable solution

Spirax Sarco recently supplied two further EasiHeat™ steam-to-hot-water systems to Doncaster Royal Infirmary, bringing its total to 12, underscoring the hospital's confidence in the technology's superior reliability and energy efficiency.

Broaden global presence through first-to-market leadership in emerging markets

We have strong global brands with the most complete worldwide coverage of emerging markets of any business in our sectors.

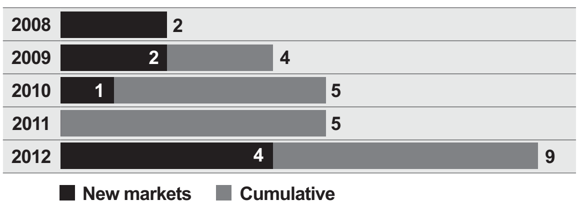
During the last five years, the overall contribution to total Group sales from our emerging markets has increased from 32% in 2008 to 39% in 2012. Perhaps even more importantly, these markets tend to carry higher profit margins and in 2012 represented 45% of Group operating profit.

Our strong global presence has resulted from decades of work and determination to build global brands that are easily recognisable and that symbolises expertise and reliability. We have a long-standing presence in many key developing markets. For example, in Latin America we established businesses in Argentina, Brazil and Mexico over 60 years ago and have built very strong, enviable businesses and brand positions in each of these countries. We entered the important Chinese and Russian markets with a direct presence in the mid-1990s and are reaping the benefits of our early market development initiatives – China today represents 10% of total Group sales and boasts our largest direct sales organisation anywhere in the world.

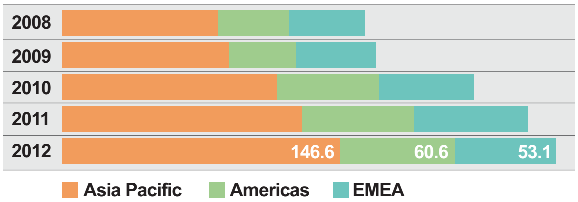
We are pioneering the introduction of peristaltic pumps in much of the developing world, demonstrating their superior technology and lower life cycle cost benefits for applications in bio-pharmaceuticals, precious metals processing, foods production and chemical dosing in water and wastewater treatment. In the past five years, we have commenced direct selling operations for Watson-Marlow in Argentina, India, Malaysia, Mexico, Poland and Singapore and are introducing customers to the benefits of our unique peristaltic and sinusoidal pumping technologies.

Our strong infrastructure around the world, quality people and local training capabilities in these markets, help us to more easily branch out into neighbouring markets that are, in most cases, at an earlier stage of development. Continued investment in market development in these important developing and emerging markets forms the basis of long-term growth opportunities for the Group.

Opening of new geographic territories



Emerging markets sales £m



Improving oil refining efficiency, GS Caltex, Korea

Spirax Sarco helped GS Caltex, a leading oil company in Korea, to improve efficiency, reduce waste and increase the quantity of 'light petroleum' products produced on their Heavy Oil line through re-modelling the steam system at their oil refinery in Yeosu, South Korea.

Grow market share through increased market penetration and one-stop shop customer approach

We see further opportunities for growth from our existing customers and markets by supplying a wider range of energy metering, controls, automation products, heat recovery solutions and pumps.

Our technically-expert direct sales force allows us to leverage our brands into new products and applications. As we have widened our range of products and extended our application reach, particularly in flow metering, boiler controls, automatic control valves, heat transfer systems and pumps, we are simplifying the buying process for our customers in offering an even wider range of choices and options for their steam system and pumping requirements. This increases the amount of plant spend that we can capture in small-scale capital projects and maintenance activities from our extensive customer base.

New products have contributed meaningfully to the organic sales growth. For the steam business, new products in areas such as automatic control valves, pre-fabricated heat transfer and heat recovery packages, on demand hot water generation systems, flow meters and steam system services, have resulted in these product families growing collectively at a significantly faster rate than overall sales growth over the past five years and contributing about 20% of the overall growth of steam business sales in the period.

For Watson-Marlow, the story is similar, as our pumps product range has been progressively widened and developed, making use of improved electronics, new pumping technologies and tubing materials to broaden the addressable markets. In the past five years, new products at Watson-Marlow also contributed about 20% of the overall organic growth of this business segment.

In our Watson-Marlow pumps business, we have been gradually transitioning our selling organisation in Europe to more direct sales, particularly for the Flexicon and MasoSine product ranges that have been acquired and that historically were sold through a distribution network. As a result, we are adding technical sales engineers and achieving faster rates of growth by better explaining to customers the technical and cost benefits of our pumps. This greater concentration of sales resources also enables Watson-Marlow to segment and focus selling activities into its core market areas of bio-pharmaceuticals, foods & beverages and water treatment.

Percentage of steam specialties sales %

Percentage of Watson-Marlow sales %

MasoSine pumps – solving a sticky problem

To produce toffee sauce at their Tenbury Wells plant, UK, Kerry Ingredients & Flavours needed a pump capable of handling the demanding viscosity and flow properties of condensed milk. Watson-Marlow's MasoSine SPS 2.5 pump provided the ideal solution.

Generate consistent organic growth
by providing greater customer value

We create consistent organic growth through our skilled local expertise, close customer relationships and the local availability of a wide range of products, services and engineered solutions.

Our knowledge of customer processes, applications and plant operation issues enables us to deliver unique engineering solutions that allow our customers to achieve enhanced and sustainable efficiencies. We form strong, long-term relationships with our customers who rely increasingly on our expertise to assist them in achieving energy and water savings, process and product quality improvements, and health, safety and environmental regulatory compliance. We do this through applying our extensive knowledge in proper steam system design and maintenance, temperature control, heat transfer, steam boiler efficiency and niche pumping of hygienic, corrosive or abrasive fluids.

As nearly one-third of our employees are engaged in customer-facing sales and service activities, effective time utilisation is of paramount importance. We continuously work to develop effective training programmes to improve the technical skills of our employees and to automate equipment sizing and selection and simplify paperwork – all of this in an effort to allow our sales and service people to spend more time directly with our customers.

Over the years, many customers have significantly reduced their maintenance and operations staff and have lost much of their steam systems expertise in plant operations and maintenance. As customers increase their outsourcing and look for simple, single-source transactions with competent full service suppliers to solve their local maintenance, operations and capacity expansion issues, our total solutions approach to problem solving is simply unmatched by any of our competitors.

We have located our major manufacturing plants strategically in all key market regions including our major factories in the United Kingdom, France, Italy, United States, Brazil, Argentina and China and we have invested over £50 million in the past four years including to expand our manufacturing footprint closer to the point of sale in emerging markets. We employ lean manufacturing systems built upon the concept of manufacturing today what was sold yesterday and centred on providing maximum flexibility and scalability of daily manufacture. We believe these manufacturing strategies help us compensate for our very short order books (typically five to six weeks) and that our top-line revenue growth is enhanced through local, off-the-shelf availability of our very wide range of steam system and pump products.

Total revenue by year £m

2008	502.3
2009	518.7
2010	589.7
2011	650.0
2012	661.7

Sales growth (organic) %

2008	9
2009	-7
2010	9
2011	9
2012	5

Perseverance pays off

Our technical expertise and understanding of customer requirements has enabled Spirax Sarco to deliver an added-value partnership with Linde Group while designing and supplying two compact and energy efficient condensate lift systems for an Acrylic Acid Complex in Saudi Arabia.

Turning strategy into sustainable value

We have a track record of revenue and profit growth. Combining the investments made in the last few years, together with our clear strategy, we look forward to continuing to create sustainable value for shareholders.

We have a resilient business model and continue to focus our efforts on creating our own growth opportunities. In 2012, Group operating profit was a record £136.2 million and Group organic sales increased by 5% to £661.7 million.

Current environment

Global economic growth and industrial output progressively slowed throughout 2012, characterised again by a sharp divergence in the rates of economic and industrial production growth between developed and emerging markets.

As anticipated, market conditions were weak across most of Europe, although our business performed better than might have been expected, as customer maintenance spending appeared to have bottomed early in the year and demand improved modestly in the second half of 2012. Our markets in North America were better than Europe, although we saw softness in the US in the last few months of the year.

Market conditions were generally positive in most of our emerging markets, particularly in China and in Southeast Asia. However, we experienced weakness in our emerging markets in Eastern Europe due to the continuing economic and financial turmoil in the Eurozone. Brazil was also challenging owing to a decline in industrial output and poor economic growth in 2012. Elsewhere in Latin America, our markets were generally robust.

Our customers are spread across a wide range of industries and institutions. Market conditions for our business tend to reflect general levels of local economic activity and, in particular, movements in industrial production. However, we have a resilient business model and we continue to focus our efforts on creating our own growth opportunities and in taking advantage of increasing customer preference to work with fewer, more capable suppliers that can provide a wider range of engineered solutions to help them improve plant productivity, reduce energy intensity and lower carbon emissions.

Trading

Group sales increased by 2% from £650.0 million to £661.7 million in 2012. Organic sales grew by 5% with higher sales in all segments except EMEA, which were flat year-on-year. The full-year effect of the two small business disposals in 2011 impacted sales by 0.5% and unfavourable currency movements reduced sales on translation by nearly 3%. Sales from emerging markets represented 39% of total Group sales in 2012, up from 38% in 2011.

In the steam specialties business, organic sales rose by nearly 5%. Traditional product sales of steam traps, valves and temperature/pressure controls increased in line with higher overall levels of basic customer maintenance spending, but metering sales were down due to the non-repeat of the exceptional flow metering project in 2011 related to the US Federal Government's energy management programme. Sales of pre-fabricated heat exchange packages, including clean steam generators, increased significantly in the year due to strong growth in Asia and in North America, where we are increasing our in-house fabrication capabilities to address greater customer demand for simpler energy saving solutions.

In the Watson-Marlow pumps business, organic sales grew 8%, in part due to backlog reduction in the US and good growth in our emerging markets. There were increases across the product range but we realised significantly higher sales from our Bredel hose pumps in precious metals processing and wastewater treatment applications, and from continued success with our Flexicon and MasoSine products. We also saw good initial sales of important new pump products launched during the year.

Group operating profit was a record £136.2 million, increasing by 2% from £134.0 million in the prior year. Using constant exchange rates, operating profit for the year was ahead 6% having been down 3% at the half year. Sales from our emerging markets generated 45% of total Group operating profit in 2012.

As expected, the second half year benefited from cost controls and European restructuring cost savings of £2 million. We continued to invest in research and development, and in market development, with further sales resource added in many emerging markets. As noted at the half year, the pace of R&D spending declined in the second half and in the future is expected to more closely reflect the rate of sales growth, having been raised to a much higher, and more appropriate, level over the last few years to support the business strategy requirements for new product development. The modest benefits of operational gearing from the 5% organic sales increase were offset by the impact of lower throughput in our main European steam specialties manufacturing plants, as we reduced stock levels and managed the volume reduction in European demand. The Group operating profit margin was unchanged at 20.6%, with unfavourable currency movements masking a small underlying advance in the margin for the year. Material cost increases and unfavourable product and market mix changes were broadly covered by our own price increases. In the second half year, which is seasonally our better trading period, we achieved a record operating profit margin of 22.4% (2011 H2 : 21.3%).

In August 2012, we announced that cost reduction actions were being taken in response to the persistently difficult economic conditions in Europe. These were implemented through the second half year, with overall headcount reductions of 9% across our steam specialties European sales operations and with additional actions taken in our European manufacturing plants. The associated one-off cost, which has been taken as an exceptional charge and excluded from adjusted operating profit, was £7.2 million; £1.7 million higher than provided for in the first half year. The annualised cost savings have therefore increased by £0.5 million to £5.5 million, of which £2.0 million was realised in 2012 with the full-year benefit accruing in 2013.

Europe, Middle East and Africa (EMEA)

Our markets remained relatively stable in 2012, despite the weak euro and deterioration in economic conditions in the Eurozone.

Nick Anderson
Executive Director

Sales in EMEA were down 7% to £232.8 million (2011 : £250.1 million) but were heavily impacted by the weak euro, where the average exchange rate for the year fell 7% versus sterling, and all other segment currencies were also lower against sterling. The impact of the two small business disposals in mid-2011 reduced sales by a further 1%, meaning organic sales were virtually flat for the year. Overall operating profit was down 14% to £36.7 million from £42.5 million in the prior year. Our sales operations in EMEA source their products from multiple locations and as the euro weakened, profits in Continental Europe were impacted by higher landed costs for products imported from the UK and from suppliers in Asia, and operating profit was down 4% at constant exchange rates. Operating profit margin was lower at 15.8% (2011 : 17.0%) due mostly to the unfavourable currency movements.

Economic conditions deteriorated in the Eurozone throughout the year and industrial output declined. Our markets remained weak but stable, with customer maintenance spending appearing to have bottomed in the first half of the year. We saw a modest improvement in underlying demand in the second half of the year despite deteriorating economic conditions – core maintenance expenditure by our customers reflected the need to keep their steam systems operating effectively, although increased market uncertainty led to delays in some local project work related to energy saving and operating efficiency.

In our large, mature markets in France, Germany, Italy, Spain and the UK, sales were comparatively resilient and were flat in constant currency overall, as exceptionally good sales growth in our French business and mid-single digit growth in our German operations was offset by lower sales in the UK and Spain. Total operating profit in these large markets was higher, particularly in France, due to good cost controls and some benefit from the restructuring cost savings. Southern Europe accounted for 8% of total Group sales in the year and declined just 1% at constant currency.

Elsewhere in EMEA, results were mixed with good performances in our smaller operations in Belgium and Switzerland. In Scandinavia, sales overall were lower amidst generally tough market conditions but profits were well ahead due to good cost controls and improved pricing.

Trading conditions in EMEA emerging markets in Russia and Eastern Europe were impacted by uncertainty spilling over from the Eurozone. Combined sales in these markets were down in the year, principally due to Russia where we saw a noticeable decline in refining and petrochemicals project activity and were therefore unable to repeat the outstanding sales and profit achieved in 2011. However, demand in our Eastern European markets improved sequentially versus the first half of the year. Our increased emphasis and investments in the Middle East and Africa resulted in robust order growth in the fourth quarter and we remain very encouraged by our longer term prospects in these increasingly important markets.

Our main manufacturing operations in the UK and France were impacted by a double-digit volume decline from destocking in our internal supply chain and reduced demand in our European sales companies. R&D spending was marginally higher for the year and we have now completed our objective of raising the overall level of investment in new product development. Construction of the new finished product distribution centre in Cheltenham was recently completed and will be brought fully into use through the second quarter of 2013, completing the final piece of investment to consolidate and modernise our manufacturing and R&D facilities in the UK.

As announced in August at our half year results, we have taken actions to reduce our cost base across many of our European companies in response to the decline in volumes in those markets since the start of the recession and to our expectation that the economic healing process in Europe will be slow and protracted. Overall the headcount in our sales operations was reduced by 9%, and there were additional reductions in our main manufacturing plants in Europe.

Revenue £m

Operating profit £m

Revenue
£232.8m
2011: £250.1m
-7%

Operating profit
£36.7m
2011: £42.5m
-14%

Operating margin
15.8%
2011: 17.0%
-120bps

Percentage of Group revenue
35%
2011: 38%

Market overview

The Group's legacy business operations are centred in Europe. Today, the contribution from Europe remains important to the Group but continues to proportionally reduce (EMEA Steam Business segment profit was 27% of total Group operating profit in 2012). We have 21 trading companies across EMEA, including Russia, the Czech Republic, Poland, Turkey and South Africa. We also have established direct sales operations in Hungary, Slovakia, Romania, Ukraine, Kenya and the United Arab Emirates. Our most important markets are foods, beverages, pharmaceuticals, institutions and OEM customers supporting these industries.

During 2012, our markets across Europe remained weak amid deteriorating economic conditions derived from the euro debt crisis. However, the low levels of customer maintenance spending seen in 2011 remained stable during the year and we saw no further deterioration in demand despite the economies of the Eurozone moving back into recession. We continued to enjoy good growth in several key markets such as Germany, France and Belgium, but most other Eurozone markets experienced varied degrees of weakness. The close trading relationship between the Eurozone and neighbouring countries resulted in weak demand across most non-euro markets in the UK, Scandinavia, Russia and Eastern Europe. The more distant markets in the Middle East and Africa were less affected and continued to show good growth.

Our core markets in foods & beverages remained mostly flat while progress was seen in the pharmaceuticals and healthcare sectors. Market conditions in refining & petrochemicals deteriorated across the region, with plant closures in Europe not being fully offset by progress in the Middle East.

Key markets

Foods

OEM Machinery

Pharmaceuticals

Healthcare

Market conditions
- Favourable
- Neutral
- Unfavourable

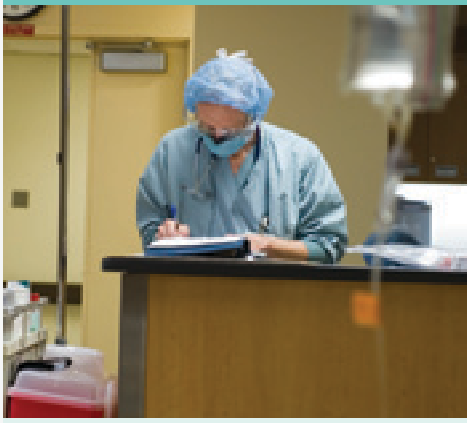
Strategy and outlook

Through our direct sales model we provide customers with a wide range of solutions for energy-saving and process productivity and we are therefore continuing to invest in strengthening the expertise of our sales force to identify and develop these growth opportunities.

Further, we see opportunities for growth through increased market penetration in pharmaceuticals and in the supply of pre-fabricated heat transfer packages for waste heat recovery and hot water delivery systems.

We remain fully committed to growing our presence in the emerging markets of Russia, Turkey, Eastern Europe, the Middle East and Africa, and look forward to making further progress in these markets during 2013 and beyond.

From survey to turnkey solution



Necker Hospital, in central Paris, has the objective of becoming the foremost centre for paediatric care in Europe. With this aim in mind, the hospital recently commenced a large-scale development project to construct a new building and comprehensively renovate an existing one. Having previously carried out steam trap surveys at the hospital, Spirax Sarco was asked to design and supply a complete turnkey heating solution.

Spirax Sarco worked closely with the hospital's technical teams to define and complete the specification and installation. The solution engineered by Spirax Sarco consisted of two heating packages of 2MW each, two heating packages of 4MW each, one platform and two feed tanks.

Before the installation of the new heating packages, steam consumption was approximately 2,000 kg/h at the site. The increased efficiency provided by Spirax Sarco's engineered solution has reduced steam consumption by 20% to 1,600 kg/h, resulting in substantial cost and energy savings. In addition, the straightforward control panels, with a single device controlling all the skids into each building, ensure that the heating packages are efficient and easy to operate.

The successful tendering for this project, worth €445,000, demonstrates Spirax Sarco's expert knowledge and understanding of customer needs and, as a result of this project, the Company has secured further contracts in this field.

Asia Pacific

Sales and operating profit increased as market conditions remained generally strong, particularly in China and Southeast Asia.

Neil Daws
Executive Director

Market conditions remained encouraging in Asia Pacific and our growth continued at a robust pace with sales increasing by 13% from £147.1 million to £166.9 million. Exchange rates have been reasonably stable and generally favourable, and at constant currency sales increased by 12%. We saw good sales growth from nearly all product groups and particularly strong growth in pre-fabricated heat exchange packages owing in part to increasing customer demand for simpler engineering solutions to reduce their energy intensity and carbon emissions. Operating profit increased by 16% from £37.8 million to £43.9 million, up 11% at constant currency, and the operating profit margin improved from 25.7% to 26.3% due to favourable currency movements.

Our business in China had another outstanding year and total sales in China, including our small Watson-Marlow pumps business, accounted for 10% of Group sales in the year. Our business in China is well spread across industry sectors but the domestic economy, including the important food & beverage market, underpins our sales. Our heavy exposure in China to domestic consumption means that our business is more resilient to the slowing economic growth from decreased country exports. Output at our manufacturing plant in Shanghai continued to grow rapidly across a widening range of products to meet domestic and regional demand in Southeast Asia, in line with our manufacturing strategy aimed at increasing flexibility and improving local customer service.

As anticipated, Korea had a much better second half year as the large projects were shipped, with a corresponding nice increase in sales and profits for the year. We achieved strong growth in Southeast Asia and continued to add sales resource into a number of newly emerging markets with meaningful future potential, including our first sales engineers in Myanmar and Cambodia. Elsewhere in the region, there were good performances by our smaller operations and another year of improvement in our Japanese business, despite the difficult local market conditions and protracted recovery.

Revenue £m

2008	98.9
2009	104.7
2010	131.5
2011	147.1
2012	166.9

Operating profit £m

2008	21.1
2009	23.1
2010	34.3
2011	37.8
2012	43.9

Revenue
£166.9m
2011: £147.1m
+13%

Operating profit
£43.9m
2011: £37.8m
+16%

Operating margin
26.3%
2011: 25.7%
+60bps

Percentage of Group revenue
25%
2011: 23%

Market overview

The Group has invested heavily in developing the important Asia Pacific region over the past 20 years. Today this region generates 31% of total Steam Business sales and the Group's business operations in China and Korea are now two of the largest in the Group. We have established 11 operating companies throughout the region and additionally have a strong, direct sales presence in newly emerging markets such as Indonesia, Vietnam, Myanmar and Cambodia. In the past three years, our headcount in the region has increased by more than 25% as we have added important sales and sales support people throughout the region and have increased our manufacturing footprint.

Market conditions were generally strong throughout the region in 2012 and demand in China was particularly robust as we benefited from our heavy exposure to domestic consumer industries and from our continued investment in geographic coverage, localised manufacture and sales of a broader range of engineering solutions. We see comparatively strong conditions throughout most of Southeast Asia and are taking additional steps to increase our direct selling presence in many of these small but important emerging markets. Elsewhere in the region, our Australian and New Zealand markets were benign but we benefited in New Zealand from a large hospital project.

Our most important industry sector in Asia Pacific is foods & beverages, which is easily our single largest sector and comprises a much higher percentage of sales in Asia Pacific than it does elsewhere for the Group. In this important market, we saw continued capital investments and higher levels of customer maintenance spending to address the needs of growing populations. We also saw good levels of customer spending at the refineries and petrochemical plants and higher levels of activity in pharmaceuticals.

Key markets

Foods

HVAC

Pharmaceuticals

Refining & petrochemical

Market conditions

Favourable

Neutral

Unfavourable

Strategy and outlook

We see very good mid-term growth opportunities throughout Asia Pacific due to the rapidly growing demand in local consumption. Our business model particularly benefits from our heavy exposure to foods & beverages, healthcare facilities, pharmaceuticals and textiles, and we therefore see continued strong organic growth opportunities.

We employ a direct sales model throughout the region and we see additional growth opportunities by increasing market share and geographic reach, as our people become more highly skilled in selling the broad range of engineering solutions already existing in our product portfolio.

We recognise the importance of accelerating the training of our sales people and technical support staff, so that they are better equipped to assist our customers in reducing their energy costs, improve plant efficiencies and reduce emissions.

We expect to maintain our strong investment approach and will continue to add more direct sales and service people in the growth markets. Additionally, we expect to expand our manufacturing footprint in the region to improve responsiveness, increase the number of products available from local stocks and reduce costs.

Providing mechanical and water treatment solutions, New Zealand

Carter Holt Harvey (CHH) Woodproducts business group, New Zealand, manufactures and markets a range of wood-based building products, which it supplies from nine manufacturing operations throughout New Zealand.

Spirax Sarco established a business relationship with CHH Woodproducts in 2007 and soon after earned 'New Zealand-wide preferred supplier status' for mechanical and water treatment programmes. Products and solutions supplied to CHH Woodproducts have included control valves, steam traps and polymer based boiler water treatments for boiler cleaning and protection.

The boiler at CHH Woodproduct's Futurebuild plant had a history of scale deposits, and intermittent problems with pre-treatment, prior to Spirax Sarco being engaged as their supplier. Spirax analysed the complete steam system to identify where the problems originated and deployed specialised polymer based chemicals. This reversed the condition, which resulted in improved boiler performance and efficiency, saving energy and eliminating scale build-up.

Evan Williams, Engineering Manager of CHH Woodproducts, commented: 'Spirax Sarco's diverse expertise, professionalism and ability to solve problems have been a great asset for us in increasing the reliability and longevity of our plant'.

Yeliz Azmak-Stevens (Senior Sales Engineer, Spirax Sarco NZ) discussing the benefits of Spirax Sarco's Water Treatment Technology with Evan Williams (Engineering Manager, CHH Woodproducts).

Americas

Organic sales increased by 6% to £137.5 million, with good progress in controls and pre-fabricated packages.

Alberto Grandi
Divisional Director

Sales in the Americas increased by 2% to £137.5 million (2011 : £134.4 million) but were impacted by unfavourable currency movements in Latin America, particularly Brazil, where the average exchange rate weakened by 14% against sterling. At constant currency, Americas sales were ahead 6%. Sales of controls were well ahead due to higher activity levels in Latin America. We also saw significantly higher sales of pre-fabricated packages in North America. Trading results were mixed and overall operating profit declined by 4% to £26.2 million (2011 : £27.4 million), although at constant currency operating profit was above the record result in the prior year. The operating profit margin was 19.1% (2011 : 20.4%), with the decrease due to product mix and volume respectively in our US and Brazilian operations.

In North America, market conditions were broadly positive, particularly in Canada where we achieved good project sales from oil sands developments in Western Canada booked early in the year and full year profits were well ahead of the prior year. In the US, we saw a meaningful rebound in underlying routine maintenance business, following a three-year period of restraint. We noted, however, softness in maintenance spending in the last two months of the year and a slowdown in large project activity in both the US and Canada in the second half of the year. In the US, sales in 2012 were lower, as expected, due to the non-repeat of the very large flow metering project in 2011 that was part of the energy management programme of the US Federal Government. This was reflected in lower profits in our US business, which was also impacted by an unfavourable product mix. Sales and profits were well ahead in Canada.

Market conditions in Latin America were mixed. Sales and profits were down in Brazil, where industrial production, a key underlying driver of our markets, contracted in each quarter of the year, although we noted easing in the rate of decline in the fourth quarter. The sharp fall in the Brazilian real is assisting in the economic turnaround but also contributed to lower profits reported in sterling. In Argentina, despite the fragile economy, we were successful in winning an exceptional project in the domestic OPC sector and profits were nicely ahead. Our Mexican business made strong progress in the year and we will shortly be breaking ground on the construction of a new £4 million manufacturing plant, which will be operational in 2014, as our Mexican business is fully integrated into our regional manufacturing strategy.

Revenue £m

2008	101.9
2009	104.6
2010	125.2
2011	134.4
2012	137.5

Operating profit £m

2008	12.1
2009	13.9
2010	24.3
2011	27.4
2012	26.2

Revenue
£137.5m
2011: £134.4m
+2%

Operating profit
£26.2m
2011: £27.4m
-4%

Operating margin
19.1%
2011: 20.4%
-130bps

Percentage of Group revenue
21%
2011: 21%

Market overview

The Group has a long history in the Americas, with ownership of our operations in Latin America, for example, dating back more than 60 years. We have strong businesses in the United States and in Canada, and have well-established trading companies in Mexico, Argentina, Brazil and, most recently, in Chile through the acquisition of our local distributor's steam business operations. In addition, we have also built direct sales operations in Colombia and Venezuela.

Due to our longstanding presence in Latin America, the Group benefits from a strong market position and relatively high market share. In Latin America, key markets include foods & beverages, refining & petrochemicals, and pharmaceuticals. In North America our largest end market industries are refining & petrochemicals, HVAC for district heating of large municipalities and university campuses, healthcare for sterilisation, laundry and hot water applications and chemicals.

Trading conditions were mixed across the Americas in 2012. In the United States, underlying customer maintenance spending on steam systems was comparatively robust following several years of depressed spending levels and overall market conditions were improved in Canada. In Latin America, several quarters of decline in overall industrial production output in Brazil weighed on our business operations but this was offset by favourable market conditions in Mexico and an outperformance in Argentina amidst a fragile economic landscape.

Key markets

Market	Market conditions
Foods	Favourable
Refining & petrochemical	Favourable
HVAC	Neutral
Brewing & distilling	Neutral

Market conditions
- Favourable
- Neutral
- Unfavourable

Strategy and outlook

We see good opportunities for growth across most of Latin America and are delighted to be in a position to more fully develop the fast-growing market in Chile, as we broaden the training of our sales people and introduce a wider range of energy saving solutions to our customers. We will continue to selectively add sales resources in our developing markets.

In the past year, we acquired additional fabrication capacity and capabilities in the United States to support the growth of pre-fabricated engineered packages for heat transfer applications, in addition to our standard and bespoke pump, valve and steam trap stations and manifolds. We are also continuing to develop the expertise of our direct sales people in North America to sell our wide range of energy saving and heat recovery solutions.

A US turnkey solution

Sanford, North Carolina is home to a manufacturing plant operated by Pfizer, one of the world's leading bio-pharmaceutical companies. Stringent regulations are applied to pharmaceutical companies seeking to export their products overseas, including strict compliance with the steam sterilization requirements under European directive EN 285.

The management at the Sanford plant turned to Spirax Sarco for help meeting the directive, requesting an evaluation and audit of their entire pure steam system.

A Pure Steam Audit identified where improvements could be made to the steam distribution system to remove moisture and non-condensables and, importantly, to increase steam dryness.

Several solutions were identified by Spirax Sarco to ensure that Pfizer's pure steam system met the standards required by EN 285. Pfizer agreed to all the recommendations presented and also asked the Spirax Sarco experts to design, install and validate the company's pure steam improvement project. A process that began as a steam system audit to ensure regulatory compliance, developed into a turnkey solution that successfully enabled the Pfizer facility to improve its pure steam system, exceed EN 285 requirements and export its products to Europe.

Watson-Marlow

Organic sales increased by 8% to £124.5 million, with all product lines experiencing growth.

Jay Whalen,
Executive Director

Sales increased by 5% to £124.5 million (2011 : £118.4 million). Overall currency movements were unfavourable, in particular due to the weakness of the euro, and at constant currency sales were up 8%. There were increases across all product lines, with the strongest contributions from our larger capacity Bredel hose pumps, our OEM-based Alitea microflow pumps and Watson-Marlow tubing products. Operating profit increased by 7% to £36.8 million (2011 : £34.4 million). Excluding the impact of unfavourable currency movements, operating profit was ahead 10%. The operating profit margin improved to 29.6% (2011 : 29.1%), having been lower at the half year due to significantly higher market penetration and product development expense in the period, which, as expected, moderated in the second half.

Trading conditions were broadly positive in the bio-pharmaceutical, precious metals processing and OEM markets, and we have made good gains in the food & beverage markets. Capital project spending in our water & wastewater treatment markets was lower due to continued restrictions on government finances in many countries, and the general industrial market has been weak, with continued significant price pressures.

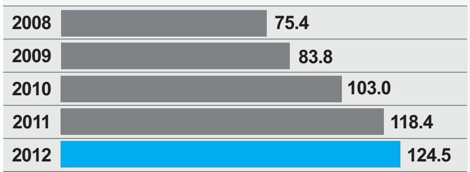
Sales growth was achieved in all geographic regions. Trading conditions were least favourable in EMEA, which accounts for just over 40% of Watson-Marlow Pumps sales, although most EMEA operations saw sales growth, with good progress in many of our small and emerging markets as direct sales expanded and further sector-focused sales resource was added.

Sales were ahead in all Watson-Marlow companies in Asia Pacific and the new operations in India and Singapore performed well. The emerging markets in Asia Pacific continue to be a focus for our direct sales approach as we seek to capitalise on the many opportunities in the region's under-developed peristaltic pumping market.

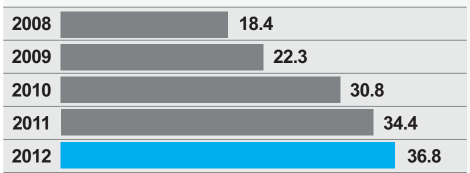
Sales growth was strongest for Watson-Marlow in the Americas and in Latin America in particular, where each of our companies performed well ahead of the prior year. North America, which accounts for nearly 40% of Watson-Marlow Pumps sales, performed well, due in part to a significant backlog reduction in the US in the fourth quarter, although there was softer underlying demand in part due to the timing of OEM orders.

Product development is an important contributor to the growth of Watson-Marlow Pumps as we expand the capability, functionality and performance of our pumps and tubing in order to open up new market areas and take market share from other pump types. 2012 was a good year for new products, including the successful launch of the important and innovative Qdos pump with its revolutionary pump head where initial sales have exceeded our expectations.

Revenue £m



Operating profit £m



Revenue
£124.5m
2011: £118.4m
+5%

Operating profit
£36.8m
2011: £34.4m
+7%

Operating margin
29.6%
2011: 29.1%
+50bps

Percentage of Group revenue
19%
2011: 18%

Market overview

The Watson-Marlow pump business was acquired in 1990 and since then has grown from contributing 4% of sales that year to 19% of Group sales in 2012. We have made several acquisitions in the last few years that have expanded our addressable markets and extended our applications capability in our important bio-pharmaceuticals and foods & beverage markets.

Our Watson-Marlow pump business is centred in Europe and in the United States, together comprising about 80% of total pump sales, about evenly split, but we are rapidly expanding into emerging markets in Asia, Eastern Europe and Latin America. Our core markets are in bio-pharmaceuticals and biotechnology (together which represent about one-third of total pump sales), foods & beverages, water & wastewater treatment and in the processing or extraction of precious metals. These applications are ideal for our pumps, which are unequalled in the pumping of hygienic fluids and, alternatively, abrasive, corrosive or erosive fluids and slurries.

The market conditions for our Watson-Marlow pumps in 2012 were largely similar to the steam business from a geographical perspective. Maintenance spending for bio-pharmaceuticals was relatively stable around the world but capital spending on wastewater treatment projects in the United States was subdued. Market conditions for our precious metals processing business in Brazil, South Africa and Africa were relatively robust.

Key markets

Pharmaceuticals

Foods

Water treatment

OEM machinery

Market conditions
- Favourable
- Neutral
- Unfavourable

Strategy and outlook

We are looking to strategically deliver growth through continued penetration of emerging markets, where we see excellent opportunities, and through further sectorisation of our field sales force in our foods & beverages, pharmaceuticals and wastewater treatment markets.

We will also continue to progress the transition from distributor sales to a value-added direct sales approach in more markets in Europe and in Asia.

Further, we have recently introduced several important new pumps, with revolutionary new pumping technology, which continues our strategy of increasing our addressable markets and aims to take market share from other positive displacement pump types that our customers may currently be using.

We selectively seek synergistic value-added niche pump and associated equipment acquisitions that will allow us to leverage sales of existing and new products through our direct sales market sector sales channel.

Bredel hose pumps, New Mexico

Sapphire Energy is a pioneer in algae-based green crude oil production. 'Green crude' has the potential to revolutionise the energy and petrochemical landscape for the better, through the production of renewable, 'green' biofuel.

Sapphire's products differ significantly from other forms of biofuel because they are made solely from photosynthetic microorganisms (algae and cyanobacteria), use sunlight and CO_2 as their feedstock, are not dependent on food crops or valuable farmland and do not use potable water. Additionally, they are compatible with existing infrastructure, are low carbon, renewable and scalable.

Sapphire Energy is using Watson-Marlow's Bredel hose pumps for the transfer of algae between growth ponds at their R&D facility in Las Cruces, New Mexico and at their new 300-acre Integrated Algal Bio-Refinery in Columbus, New Mexico.

The Bredel hose pump's versatility to handle variable flow, regardless of pressure changes, its gentle pumping action that protects the sheer sensitive algae, and its robust design that allows it to withstand the harsh desert environment, enabled Sapphire to expand from pilot plant into true farm pond commercial production.

Finance review

The Group's prime financial objective remains to provide enhanced value to shareholders through consistent growth in earnings per share and dividends per share.

David Meredith
Finance Director

Spirax Sarco uses adjusted figures as key performance measures in addition to those reported under International Financial Reporting Standards (IFRS), as the Board believes that these are more representative of the underlying performance. Adjusted figures are used unless otherwise stated and in 2012 they excluded the amortisation of acquisition-related intangible assets, acquisition and disposal costs, contingent consideration fair value adjustments, together with the tax effects on these items. Additionally in 2012, as announced at the half year, we have implemented cost reductions actions that have lowered headcount, predominantly in our European operations that has resulted in a one-off exceptional restructuring charge of £7.2 million for the year (2011 : nil). This is a small increase on the amount charged at the half year, reflecting a larger headcount reduction across our European sales operations of 9%. There were also reductions in Latin America and in our main manufacturing plants in the UK and France in response to the lower business volume in Europe.

Sales increased by 2% from £650.0 million to £661.7 million. Organic sales increased by 5%, which was partly offset by unfavourable currency movements, principally the euro and related currencies and those in Latin America, which reduced sales on translation by 3% and by two small business disposals in Spain and South Africa in 2011 that impacted sales growth by 0.5%. Sales in the US accounted for 17% of total Group sales and China accounted for 10%.

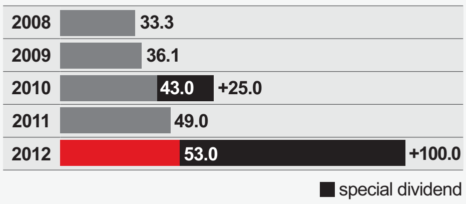
Operating profit increased by 2% from £134.0 million to £136.2 million. Unfavourable currency movements impacted operating profit by £5.1 million, with a significant negative in EMEA of £4.1 million and negatives of £1.8 million in the Americas and £1.1 million in Watson-Marlow Pumps, mitigated by an exchange gain in Asia Pacific of £1.9 million. At constant currency, Group operating profit was ahead 6%. There were a number of factors, both positive and negative, that contributed to the overall good performance in 2012:

- Operational gearing on the increased sales benefited profit, although these gains were modest on the 5% organic sales growth and were partially offset by the impact of our internal destocking on production volumes at our steam specialties plants in the UK and France. This will continue in 2013 albeit at a likely slower pace of destocking.
- The restructuring actions, primarily in Europe, generated annualised cost savings of £5.5 million, delivering an initial £2.0 million of benefit in the year, with the further savings to be realised in 2013.
- The prior year included a number of one-off factors that reduced profit by a net £1.2 million that were not repeated in 2012.
- Our main steam specialties manufacturing plants in Europe saw a double-digit decline in volume reflecting the successful actions to reduce stocks in our internal supply chain and the small fall in volume from their primarily European customer base.
- Investment in market development was again increased, with further sales resource added in emerging markets.
- Overall, material costs, including an unfavourable product mix effect, increased broadly in line with our own price increases. As expected, the material cost increases seen in the first half of the year, moderated in the second half.

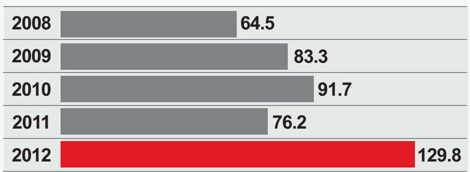
The Group operating profit margin was unchanged from the prior year record of 20.6% and at constant currency was slightly improved.

We continue to focus on our own CO_2e emissions, where the intensity reduced in the year expressed as a ratio to sales (inflation and currency adjusted). Our customers reduce their own emissions through the use of our products and our assessment, using an externally verified process, is that customer emissions savings increased again in the year.

Dividends per share p



Adjusted operating cash flow £m



Interest

Net finance income was lower at £0.4 million (2011 : £1.1 million) and reflects a small deterioration in respect of the Group's defined benefit pension schemes following a reduction in the return on asset assumption for the year, compared with the prior year. The position in respect of bank interest receivable/payable was little changed, with continuing very low interest returns on cash deposits.

With effect from 2013, the Group will adopt a new accounting standard, IAS19 Employee Benefits, which significantly changes the accounting for investment returns in respect of defined benefit pension schemes. In future, investment returns will be assessed based on assumed bond yields, rather than the current basis, which uses a blended return on the actual assets being held by the pension schemes. Had the new accounting standard applied in 2012, then our reported net finance income would be £3.6 million lower. This change is presentational and does not in any way impact the cash flows of the Group. When the new standard is adopted in 2013, the comparative prior year results for 2012 will be restated to reflect this new accounting policy.

Associates

The Group's 49.3% share of the after-tax profit of our Associate company in India was £1.9 million (2011 : £2.1 million). The Indian rupee weakened by 12% on average against sterling during the year and, at constant currency, sales were modestly ahead and profit broadly unchanged reflecting an unfavourable mix of business and increased investment.

Pre-tax profit

The profit before tax increased by 1% from £137.2 million to £138.5 million; at constant currency the increase was 5%. The statutory profit before tax declined by 4% to £127.7 million (2011 : £132.3 million) and is after taking into account certain non-operating items including:

- A charge of £4.1 million (2011 : £4.4 million) in respect of the amortisation of acquisition-related intangible assets, £0.3 million of which related to our Indian Associate (2011 : £0.4 million)
- Acquisition and disposal costs of £0.3 million (2011 : £0.4 million)
- One-off exceptional headcount reduction costs of £7.2 million (2011 : nil), predominantly in Europe
- Contingent consideration fair value credit adjustment of £0.6 million (2011 : nil) in respect of the acquisition of our distributor in Turkey in 2009.

Taxation

The tax charge on the adjusted pre-tax profit, excluding our Associate, was marginally lower at 29.6% (2011 : 29.8%). The Group's powerful direct sales business model means that we are structured with many, typically small, operating companies spread worldwide, addressing our customers directly with local sales resource and local stocks. Our tax rate essentially reflects the blended average of the many different tax jurisdictions in which we operate.

Earnings per share

The Group's prime financial objective remains to provide enhanced value to shareholders through consistent growth in earnings per share and dividends per share. Adjusted basic earnings per share increased by 1% to a record 125.6p (2011 : 124.8p). The statutory basic earnings per share were 115.6p (2011 : 120.0p). The fully diluted earnings per share were not materially different in either year.

Dividends

The Board has proposed a final dividend of 37.0p per share (2011 : 34.2p), an increase of 8%. Together with the interim dividend of 16.0p per share (2011 : 14.8p), this gives an increase of 8% in the total Ordinary dividend for the year to 53.0p per share (2011 : 49.0p), extending our dividend record to 45 years. The interim dividend was paid on 9th November 2012 and, if approved by the shareholders at the AGM on 9th May 2013, the final dividend will be paid on 17th May 2013 to shareholders on the register as at 19th April 2013.

In addition, having reviewed the capital requirements of the Company, the Board is proposing a return of capital to shareholders of £78 million in the form of a special dividend of 100.0p per share in respect of 2012. If approved at the AGM, the special dividend will be paid on 3rd July 2013 to shareholders on the register at 31st May 2013. This is equivalent to approximately 4% of the market capitalisation of the Company and, as is common with a significant return of capital to shareholders, the Board recommends that this is combined with a share consolidation. This is intended to maintain, as far as possible, the comparability of the share price, earnings per share and dividends per share before and after the special dividend, and to remove the impact of the special dividend on employee equity-based incentives. It is anticipated, therefore, that the market price of each Ordinary share should remain at a broadly similar level following the special dividend and share consolidation.

Acquisitions and disposals

We continue to devote considerable resource to finding and unlocking suitable acquisitions. Our focus is largely directed at adding new products and technologies to our existing businesses, and expanding direct market access, although we remain interested in complementary businesses that are adjacent to our main markets. Our strong balance sheet, even allowing for the special dividend, provides considerable scope to fund appropriate acquisitions.

On 7th November 2012 the Group announced the acquisition of the business and assets of the steam specialties business of our Chilean distributor for a total consideration of £3.1 million, of which an initial payment of £1.6 million was paid in the year with the remaining £1.5 million to be paid in 2013 against certain performance conditions being met. Chile is an expanding market with good future growth prospects that will be enhanced by our direct sales approach.

In January 2013, we announced the acquisition of a 30% stake in Econotherm (UK) Limited for £1.0 million, with an option to acquire the remaining equity. Econotherm specialises in the design and manufacture of heat pipes and associated heat exchanges for industrial waste heat recovery, utilising unique and patented technology.

The full-year effect of the disposal of two small businesses in mid-2011 reduced sales growth in 2012 by 0.5%.

Research & development

Investment in research and development increased in the first half year and was marginally up for the full year as several major projects were successfully completed. R&D spending has been significantly stepped up over the last four years, nearly doubling since 2008, to a level that will allow us to sustainably support the business strategy requirements for product development. Our steam specialties business made full use of the new Steam Technology Centre and released nearly 40 new or improved products during the year, compared with about 25 in the previous year, including the world's first self-powered wireless flow meter that harvests heat energy from the steam mains piping to power the meter through a Seebeck Effect power generator. Our Watson-Marlow pumps business had a very busy product development year with the release of two major new product platforms, including the Qdos pump that uses revolutionary pulseless pumping technology that will further expand our addressable markets. The products released by the Group during the year have a greater sales potential than those released in 2011.

Capital employed

Total capital employed at £339 million was down 1% at constant currency. The net book value of property, plant and equipment rose by £4 million or 3% at constant currency to £175 million with, as anticipated, capital investment at £25 million moderating from the exceptionally high level in 2011. In particular the manufacturing site consolidation and facilities improvement project in Cheltenham was completed, with the new finished goods distribution centre becoming operational in March 2013. Investment in production machinery and equipment in China continued as output was ramped up to meet local demand and, increasingly, for export to support Asian markets as part of our regional manufacturing strategy. We have outgrown our manufacturing plant in Mexico and have purchased a new site where construction of a much larger facility, at a total cost of £4 million, will shortly commence with relocation and production start-up expected early in 2014. Investment in software and IT systems was notably higher at £7 million. Total Group capital expenditure is expected to remain at around £30 million in 2013 as we expand output in China and progress the Mexican facility and a number of IT projects.

Total working capital, comprising inventory, debtors and creditors, fell by £8 million or 4% at constant currency to £164 million due to inventory levels falling by £9 million or 8% at constant currency with a reduction in stock weeks in all regions. Buffer stocks related to the site consolidation project in Cheltenham were unwound and total inventory shows an improvement when measured against the 16% increase in organic sales over the last two years. Trade receivables remain well controlled and rose by 5% at constant currency. Trade and other debtors and creditors were overall little changed, despite the sales growth, with trade creditors reflecting the inventory control actions and with generally lower bonus accruals. The ratio of working capital to sales improved from 27.4% to 24.8%.

Capital employed	2012 £000	2011 £000
Property, plant and equipment	174,836	174,648
Inventories	103,690	116,325
Trade receivables	145,686	142,484
Prepayments and other current assets/(liabilities)	(85,140)	(80,906)
Capital employed	**339,072**	**352,551**
Intangibles and investment in Associate	97,268	93,530
Post-retirement benefits	(72,663)	(71,925)
Deferred tax	23,696	19,476
Provisions and long-term payables	(2,500)	(5,781)
Net cash	51,676	12,269
Net assets	**436,549**	**400,120**
Adjusted operating profit	**136,245**	**133,960**
Average capital employed	**345,812**	**325,647**
Return on capital employed	**39.4%**	**41.1%**

Return on capital employed

During the year, capital employed was down 1% at constant currency due to the good control of working capital. However, average capital employed (using the average of opening and closing sterling balance sheets for 2012 and 2011) increased by 6%, reflecting the rising profile of capital employed in the prior year and the high level of capital investment as our manufacturing facilities have been improved. The adjusted operating profit for the year increased by 2% and at constant currency rose by 6% but this was more than offset by the impact of the rise in average capital employed, resulting in a small decline in ROCE from 41.1% to 39.4%.

Post-retirement benefits

The net post-retirement benefit liability shown on the balance sheet was little changed, rising from £71.9 million (£51.6 million net of deferred tax) to £72.7 million (£52.4 million net of deferred tax). Asset values were sharply higher, increasing by 12% as investment returns exceeded scheme assumptions and deficit reduction contributions of £8 million were made into the main UK schemes. However, further falls in bond yields again forced up reported liability values, which rose by 9%, causing the small overall increase in the reported deficit under IAS19. Distortions in bond markets, in part caused by large gilt purchases by the Bank of England under the programme of Quantitative Easing, have pushed up the reported value of liabilities. Most of the asset and liabilities relate to the main UK defined benefit pension schemes that were closed to new entrants in 2001, and are managed under a dynamic de-risking strategy under which asset and liability values are monitored on a daily basis by the asset manager and appropriate asset allocation decisions taken as the funding levels improve against pre-agreed trigger points.

The triennial valuations of the main UK defined benefit schemes as at 31st December 2010 resulted in a continuation of deficit reduction cash contributions of approximately £8 million per year that progressively reduce to nil by 2018.

Cash flow

We were very pleased with the cash flow performance in 2012. Adjusted operating cash flow increased from £76.2 million to £129.8 million with a substantial turnaround in working capital following the outflow in 2011 (caused by the disruption of the Cheltenham manufacturing site consolidation). There was just a small outflow from working capital of £0.5 million with the reduction in stocks generating a cash inflow of £8.6 million. This was partially offset by a reduction in creditors due to lower material purchases and lower bonus accruals. Trade debtors increased by 5% at constant currency in line with the 5% organic sales increase. As expected, capital expenditure, net of disposals, reduced to £29.7 million from the exceptionally high level in the prior year. Operating cash flow conversion was 95% of operating profit.

Adjusted cash flow	2012 £000	2011 £000
Operating profit	136,245	133,960
Depreciation and amortisation	21,241	16,784
Adjustments (including share plans)	2,559	1,764
Working capital changes	(546)	(32,942)
Net capital expenditure (including R&D)	(29,691)	(43,395)
Adjusted operating cash flow	**129,808**	**76,171**
Net interest paid	(206)	(333)
Tax paid	(37,941)	(33,433)
Free cash flow	**91,661**	**42,405**
Net dividends paid	(37,887)	(52,705)
Pension deficit reduction payments and provisions	(6,974)	(10,915)
Restructuring costs paid	(5,569)	–
Proceeds from issue of shares	4,028	4,363
Acquisitions	(4,501)	(3,387)
Cash flow for the year	**40,758**	**(20,239)**
Exchange movements	(1,351)	(1,884)
Opening net cash	12,269	34,392
Net cash at 31st December	**51,676**	**12,269**

Free cash flow more than doubled from £42.4 million to £91.7 million. Tax payments increased by 13% to £37.9 million. Dividends of £37.9 million were paid out of free cash flow. This was lower than the £52.7 million in the prior year, which included a special dividend of £19.4 million; the underlying Ordinary dividend payments increased by 14%. Special pension deficit reduction contributions of £7.5 million were paid in the year as were cash restructuring costs of £5.6 million, with further cash restructuring payments of £1.6 million in 2013. There was an outflow of £4.5 million for acquisitions, including an initial payment of £1.6 million in respect of the purchase of our distributor in Chile and a further instalment of £2.0 million in respect of our acquisition in Mexico in 2010. These outflows were partially offset by a £4.0 million inflow from the issue of shares under the Group's various employee share schemes.

The net cash inflow for the year was therefore £40.8 million, which, net of a £1.4 million reduction from unfavourable currency movements, meant that we finished the year with net cash balances of £51.7 million compared with £12.3 million at 31st December 2011.

Capital structure and treasury policy

Our policy is to operate with a strong balance sheet to protect the business and facilitate future growth, whether via capital investment, organic expansion or acquisitions. Where cash resources exceed expected future requirements, we will generally seek to return excess cash to shareholders. The Group has operating companies in 36 countries and the Group Treasury function in the UK centrally manages the various treasury and currency issues that arise from our geographically diverse business, and is responsible for ensuring that our Treasury Policy is rigorously applied and closely monitored. The Group's trading results and balance sheet can be affected by currency movements, the most significant of which are the euro, dollar, Chinese renminbi and Korean won. We do not undertake complex derivative transactions and typically use simple forward contracts to appropriately manage exposures to known cash flows. We do not hedge profit translation exposures.

Sustainability

We are committed to the sustainability of our business and recognise our responsibilities towards the environment, the communities in which we operate and the people in our workplaces.

Our environment

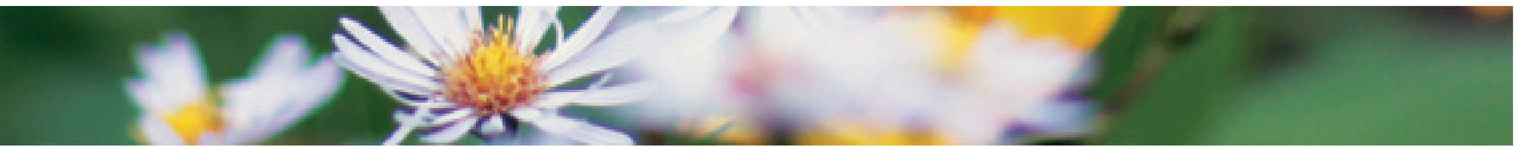
page 33

Our communities

page 36

Our workplaces

page 38



Sustainability review

With operations and offices in over 100 countries, and reaching customers in many more through our supply chain, the world is not just where we do business – it is where we live, play and raise our families.

We are committed to increasing the sustainability of our business and that of our customers, and recognise our responsibilities towards the environment, the communities in which we operate and the people in our workplaces.

Our sustainability objectives include:

- **Our business:** Using our expertise to provide innovative solutions to meet our customers' needs and to ensure increasing shareholder value.
- **Our environment:** Leading as an accountable corporation working with our customers and suppliers to minimise our impact on the environment.
- **Our communities:** Being a positive influence in the communities in which we work and live.
- **Our workplaces:** Maintaining a professionally challenging, respectful and safe workplace for all Spirax-Sarco Engineering associates and business partners.

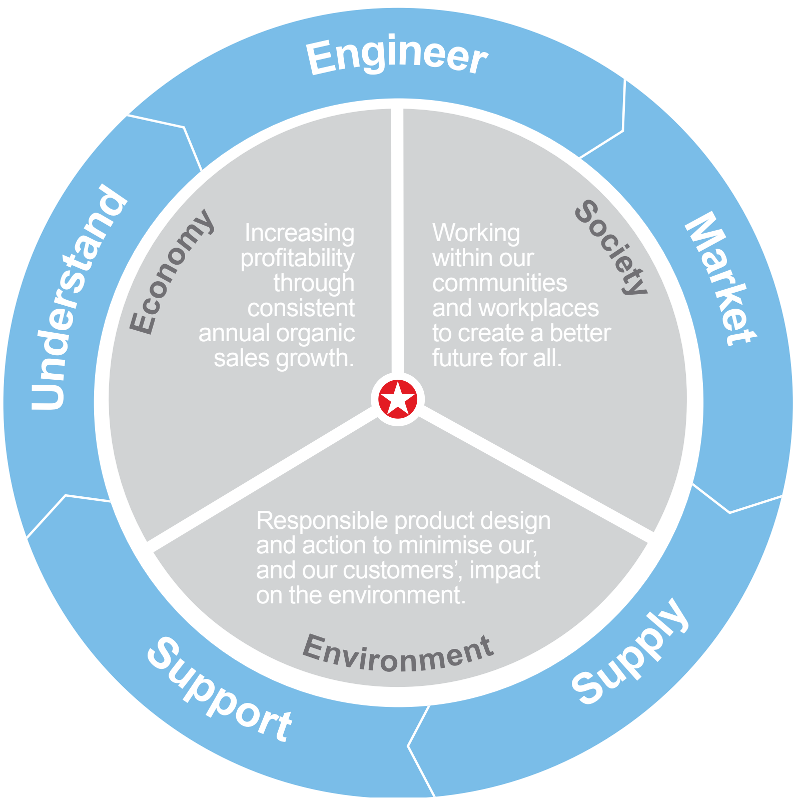
The Group comprises exceptional people who share our core values of respect, accountability, passion, integrity and delivery. These values give us a strong foundation on which we base our decisions, drive innovation and actively manage our operations across the globe.

We aim to do what is right, what is best and what is fair, while delivering value to our customers and maintaining a strong and viable business.

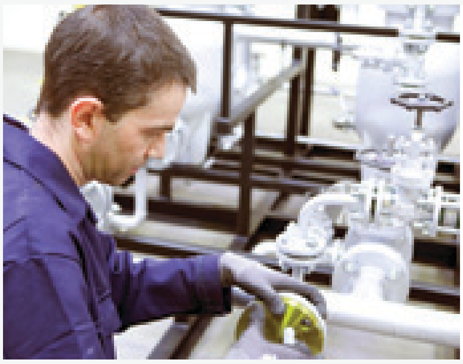
We recognise the importance of sustainability in our business operations and believe that a sustainable business is one that provides long-term shareholder value, while reducing environmental impact and improving the societies and communities in which it operates. Sustainability is an intrinsic part of our long-term strategy, which creates competitive advantage and helps to achieve profitable, sustainable growth.

Accountability is essential. While the Group is accountable to its shareholders, it also recognises that it has responsibilities to other stakeholders, including employees, customers, suppliers and the local communities in which it operates. The Board accepts its responsibility to be accountable to all stakeholders and is committed to sustainable and ethical business practices.

Economic, social and environmental sustainability are at the heart of our business model:



Creating sustainable, profitable growth



UK Supply factory reduces carbon emissions

Within Spirax Sarco's UK factory, insulating ancillary steam equipment has saved 376 tonnes of CO_2e emissions and reduced running costs by as much as £100,000 per annum. In addition, work recently completed to proactively manage the compressed air system is expected to achieve targeted savings in excess of 50 tonnes of CO_2e emissions per year, compared to 2011.

Our environment

Greenhouse gas emissions

Spirax Sarco is determined to be a leader in addressing the threat of climate change. Improved carbon management is, and will continue to be, a priority across our businesses. In accordance with national and international commitments on climate change, we endeavour to continuously reduce the carbon intensity of our business, implement initiatives to cut our carbon emissions and improve the sustainability of our operations, and help our customers to do the same. We are committed to reducing our carbon footprint worldwide.

We have reduced our total CO_2e emissions (scope 1 and 2) from 32,150 tonnes in 2009 to 26,233 tonnes in 2012; a reduction of over 18%. As our business has grown, we have significantly reduced our CO_2e intensity against inflation adjusted sales at constant currency, from 56.4 tonnes per £m of sales in 2009 to 39.6 tonnes per £m of sales in 2012; a reduction of nearly 30%. Between 2011 and 2012 our CO_2e intensity fell 12% from 45.2 tonnes to 39.6 tonnes per £m of inflation adjusted sales, at constant currency.

Using externally verified methodology we calculate that the energy saving products purchased from Spirax Sarco in 2012 could reduce our customers' CO_2e emissions by as much as 4.9 million tonnes annually. With our scope 1 and 2 emissions amounting to just 26,233 tonnes across the Group in 2012, our business has a significant net gain in reducing carbon emissions. Expressing this from a shareholder perspective, we calculate a net carbon benefit of approximately 62.5kg per Ordinary share in issue in 2012*.

Since 2008, the Group has reported its carbon footprint to the Carbon Disclosure Project in the UK. In 2012 we were awarded a carbon disclosure index of 69 (2011 : 65), from a maximum possible score of 100, reflecting a year-on-year improvement. The carbon disclosure index reflects:

- The extent to which a company measures its carbon emissions
- The comprehensiveness of the information that it provides on climate-related actions
- The depth of information given on the issues climate change presents to the business
- Whether a company uses a third party for external verification of its data.

Energy efficiency

Increased energy efficiency is essential to reducing our carbon footprint and is central to the Group's sustainability agenda.

Much has been done to reduce energy consumption, with several notable success stories. Throughout the Group, staff awareness campaigns have been used effectively to encourage individuals to switch off non-essential equipment when not in use. For example, in Spirax Sarco Korea, adjusting indoor room temperatures, setting screen savers on all computers and laptops, and switching off lights at lunchtime has made significant base load savings.

Although not directly reporting on scope 3 emissions, we recognise that we have a responsibility to improve energy efficiency and reduce emissions in all aspects of our business operations, including the transportation of our manufactured products. We have made significant progress towards increased energy efficiency in the intra-Group transportation of goods. Shorter internal supply chains have been created through the unification of manufacturing into one Cheltenham site. In addition, contracts have been negotiated to streamline transportation across Europe through the use of a single freight forwarder (we previously used 28) and two carriers within the UK (previously 18).

* Net carbon savings per share are based on the average number of shares in circulation divided by the net savings in carbon emissions between our operations and the estimated savings made by our customers. Net savings in carbon emissions are based on scope 1 and scope 2 emissions only and do not include scope 3 emissions such as deliveries made by third party freight forwarders and emissions associated with our supply chain. Carbon savings are based on the sale of selected product lines and the emissions those products avoid through their use in a typical year.

Total Group CO_2e emissions (scope 1 and 2) tonnes

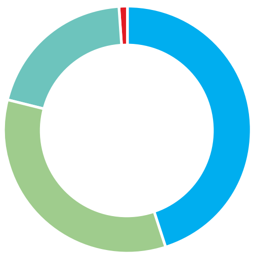
2009	32,150
2010	29,579
2011	29,392
2012	26,233

CO_2e intensity tonnes per £m of inflation adjusted sales, at constant currency

2009	56.4
2010	48.0
2011	45.2
2012	39.6

Greenhouse gas (GHG) emissions inventory

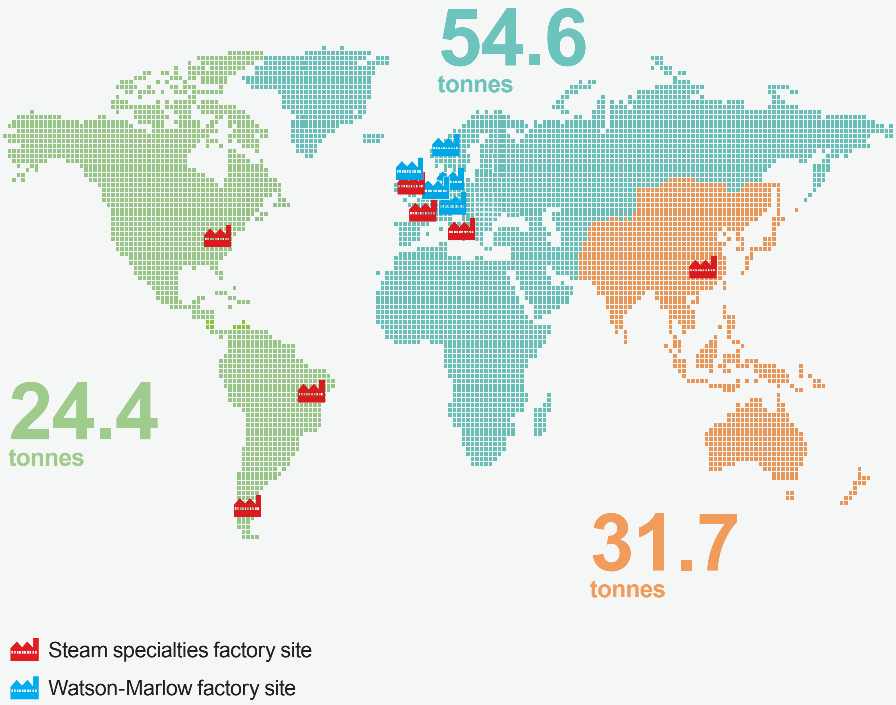
Electricity	45%
Business travel	34%
Natural gas	20%
Other	1%



US energy efficiency success

Spirax Sarco Inc, in Blythewood, South Carolina was recently commended by the US Department of Energy for its energy efficiency accomplishments during 2012. Furthermore, as a founding partner of the US Department of Energy's Better Buildings, Better Plants Program, Spirax Sarco has joined over 100 other industrial firms in the US in a voluntary pledge to reduce the energy intensity of their manufacturing operations by 25% in 10 years.

Regional CO_2e emission intensity in tonnes per £m of sales



Regional CO_2e emission intensity

The geographical distribution of our business operations predominantly accounts for regional variations in CO_2e emission intensity. While we have major manufacturing plants strategically located in all market regions, EMEA contains eight of the Group's 12 major manufacturing facilities, as well as significantly more operating companies than the other two regions.

Packaging

Spirax Sarco is successfully incorporating sustainability initiatives and reducing our environmental impact in innovative ways in the packaging of our products. Within the UK, environmentally friendly, 100% recyclable, inflatable AirPack protective packaging is now used wherever possible. AirPack reduces storage and shipping costs through its compact size and lightweight design and is fully recyclable or reusable by our customers.

Throughout the Group we aim to ensure that all packaging is responsibly sourced. For example, most cardboard packaging is made from recycled material and is fully biodegradable so that it can be safely disposed of by the customer.

In addition, wooden pallets used in the UK are produced using a species of fast growing northern European pine. Each pallet is designed to be collapsible, saving storage and transportation costs, and is nail-less, being constructed using stainless steel hinges, so that it can be assembled and disassembled for repeated use.

Saving energy and preventing landfill during a UK soil decontamination project

When contaminated land specialist Provectus decided to take a novel approach to decontaminating the soil from an old printing works, Spirax Sarco provided the steam system expertise to turn their ideas into reality.

Through many years of industrial use, the site in Somerset had been contaminated with toluene, a flammable solvent. Developers were looking to extract the chemical from the soil so that the land could be used safely for housing.

Spirax Sarco engineers devised a series of trombone-shaped coils, laid flat across one of the old concrete factory floors. Several thousand metres of pipework were used to provide a heating area large enough to efficiently treat the batches of soil that were piled on top.

The soil was heated using steam, and the vapour that was emitted was captured and passed through a system of activated carbon beds that absorbed the toluene and discharged clean air into the atmosphere.

Our solution successfully decontaminated the site in only four weeks, prevented the soil being sent to landfill and had higher energy and water efficiency than traditional decontamination methods.

'We'd never seen a project like this and neither had the Environment Agency personnel who inspected the operation', explained Provectus Director, Steve Langford. 'We had cleaned up the first batch of soil within two weeks and the site is now suitable for even the most sensitive developments – residential housing with gardens. I'm more than happy with the support we got from Spirax Sarco, which helped us to complete the project so quickly and efficiently.'

Waste management and recycling

Reducing the amount of waste sent to landfill is essential for increasing sustainability. Recycling schemes are in operation across the Group and we have dedicated contractors to pro-actively manage waste, serving to minimise our environmental impact.

Water management

We recognise that clean water is a valuable resource that should be managed effectively to minimise our environmental impact. It is our aim to improve our water management across the Group. As part of this drive to use water more effectively, during the construction of the new Technology Centre in the UK, we installed a 2,000 litre rainwater harvesting tank which is used to flush lavatories at the site.

ISO 14001:2004 certification

ISO 14001:2004 is an international standard relating to environmental management. Certification to the standard provides assurance to the managers and employees of a company, as well as external stakeholders, that the environmental impact of a business is being managed and improved. The certification process is rigorous, requiring external auditing against prescribed standards, including waste management and energy consumption. During 2012, five additional operating companies achieved the certification, meaning that 59% of our employees now work in a location with ISO 14001:2004 in place, an increase from 47% in 2011.

We are committed to increasing the number of our operations with ISO 14001:2004 approval, and a number of our operating companies are either awaiting certification or are implementing the procedures necessary to acquire it.

Helping our customers to become more environmentally sustainable

Our primary contribution to sustainability is to develop technologies and products with an increasingly lower environmental impact. We have the capability to respond to several of the major environmental challenges, through the provision of low-emissions, low-carbon and renewable energy solutions.

We use methodology, externally verified by AEA Group, to calculate the quantity of CO_2e emissions saved by our customers as a result of purchasing our energy saving products. We calculate that the energy saving products we sold during 2012 will save our customers approximately 4.9 million tonnes of CO_2e annually. Put another way, for every tonne of CO_2e emissions (scope 1 and 2) that we produced during our business operations in 2012, our customers could save as much as 187 tonnes of CO_2e annually.

The Group is dedicated to supplying exceptional quality products and solutions which meet the requirements of our customers in a manner consistent with high environmental and ethical standards. These principles form an integral part of the Group's management processes and operations throughout the world.

Employees working in operations with ISO 14001:2004 certification %

	%
2011	47
2012	59

Energy savings at Northumbrian Water

Spirax Sarco recently helped Northumbrian Water to halve the energy it uses to raise steam at its Bran Sands anaerobic digestion plant in Teesside, UK. Mr Errington, of Northumbrian Water, stated, 'Spirax Sarco are very good at what they do. They're very helpful and very knowledgeable and we get a good response from them. The energy savings equate to about 50%.' Northumbrian Water was so impressed by the service and solution provided by Spirax Sarco that they plan to work with us while constructing a new plant at Howden.

Our communities

Helping in our communities

The Group encourages its employees to be involved in contributing their time and resources towards improving the quality of life in the communities in which they live and work. We have a keen sense of our community obligations and encourage a positive approach to our community relations, organising community events and activities worldwide.

Charitable donations

The Spirax Sarco Group Charitable Trust ('Trust') meets regularly throughout the year to determine its donations to registered charities in the UK and worldwide.

The Trust focuses its donations in the following major areas: social services (particularly for the less advantaged, disabled or abused), education, health care, arts and the environment. In addition, it also makes donations to charities that support recovery efforts following natural disasters.

This year the Trust made 45 donations, ranging from £750 to £15,000, in accordance with its charitable donations policy, to a total value of £132,000.

Donations made by the Trust included £10,000 to Open Door, a local Cheltenham charity founded for the relief of poverty, hardship and distress among the homeless. Winston's Wish, a national charity that helps children to rebuild their lives following the death of a parent or sibling, received a donation of £5,000, while the National Star College, which provides further education, training and development for young people aged 16 to 25 with complex physical, sensory or learning disabilities, received £15,000.

In addition to donations made by the Trust, our operating companies worldwide made many donations to local charities and social organisations. Charitable donations made by our operating companies amounted to £40,000 during 2012, giving a total of £172,000 across the Group.

As well as the charitable donations made by the Trust and our operating companies, our people have independently undertaken many fundraising events to raise money for a wide range of worthwhile causes. Examples from the UK include donations to the Frenchay Unit Neuro Club, based on a children's ward of the Bristol Royal Infirmary and to the British Heart Foundation.

Spirax Sarco Korea service club

In Spirax Sarco Korea there is a club called 'Help' which reaches out to the disabled and less fortunate in the local community through giving time and money to help those in need.

During winter, the club members deliver coal and welfare packages to those less fortunate than themselves.

Group charitable Trust donations (2008-2012) £'000

2008	81,000
2009	86,000
2010	112,000
2011	132,000
2012	132,000

Design a bike event, US

Spirax Sarco Inc sponsored a bicycle charity event for the Boys and Girls Club of the Midlands in Blythewood, South Carolina. Over 150 employees assembled and decorated bicycles for 18 excited children.

At the end of the event the children arrived to pick up their new bikes. Stephen Gow, Director of Marketing, commented, 'Giving back to the community was a great experience. All the employees had a lot of fun.'

Watson-Marlow sponsors technology challenge at local school

As part of its aim to encourage engineers of the future, Watson-Marlow Pumps Group has teamed up with Falmouth School to organise an Annual Computing Challenge.

The Annual Computing Challenge proves that there is a wealth of talent in Cornwall's schools, which Watson-Marlow is proud to help nurture. The education of young people in IT and technology is vital for building up a strong base of engineers that can grow the UK's technological expertise in the future.

In the first year of the competition, students at the local secondary school were challenged to create a computer game or app. The competition proved hugely successful, attracting entries of a very high standard.

The winning entry was created by Gareth Willets, who devised a clever homage to the retro game 'Asteroids'.

Other top entries included a maze-type platform game and an Android app that delivers the latest news on West Ham United Football Club.

Watson-Marlow donated the competition's prize: a Computing Challenge Cup, plus £100 in Amazon vouchers, and also invited the finalists to visit its Falmouth facility, to find out more about how the Company operates and the ways in which it prioritises technology and computing.

The Falmouth School competition is just one of a number of technology-based projects that Watson-Marlow sponsors in local schools, helping to encourage the next generation of engineers and technicians.

Children's Day, Mexico

Mexico's Children's Day, also known as 'El Día del Niño', is a unique festivity, full of laughter and play, when adults are reminded of the importance of childhood and children teach us how joyful and simple life can be.

Spirax Sarco, Mexico organised a special celebration and party for the children of its employees with the theme of a 'Big Top Circus Party'.

A highlight of the party for many of the guests was a 'Grand Tour' of the plant. One attendee noted, 'Spirax Sarco is not just a company, or a great place to work, it is a great family!'

Our workplaces

Spirax Sarco is a major international employer. In December 2012, the Group, including our joint venture in India, employed over 5,000 people in more than 100 countries.

Communications

We communicate with our people through a wide variety of channels, including regular face-to-face team briefings, conference calls and a number of intranet sites. Feedback is sought on the effectiveness of our communications and surveys have been instituted in many of our businesses to gauge the morale of our people and what is important to them. Our aim is to ensure that all our employees are informed about, and engaged in, their part of the business locally while having a deeper understanding of the Group overall and its future direction.

Talent and development

As a Group whose purpose is to deliver products and services that help provide our customers with effective solutions, it is second nature to make the health and wellbeing of our own employees a priority. We continue to support our people through training and development, so that they can grow professionally and meet the evolving challenges of our industry. During 2012 we delivered 12,059 days of training to our 2,128 customer facing employees, across the Group; an average of over one week of training per person.

In 2011 we announced the launch of our Spirax Sarco Leadership Academy and, in 2012, 12 of our future leaders attended courses designed to help them learn new skills and prepare for increasing responsibility within the organisation. The two week course, run by the Ashridge Business School, is a Company-specific version of Ashridge's Advanced Management Programme. The course demands a significant investment in our people, but we recognise that achieving optimal business results is related to the expertise of our managers. Key topics covered on the course include: working with people, driving growth and innovation, and delivering results.

Those who attended the Leadership Academy saw immediate benefits of the training they received.

'Thanks to the course we will be able to build our management and leadership capabilities. Most of what I have learnt on the course is immediately applicable to my role and it is the most demanding course I have ever been on.'
Filip Prochazka, General Manager, Czech Republic and Slovakia

'To be involved in the course was a unique experience for me; to work with colleagues from other countries and share ideas and knowledge was an invaluable experience.'
Mario Montano, National Sales Manager, Mexico

It is not just our senior employees who benefit from our investment in people. In the UK, we launched our online appraisal software in time for completion of the 2012 appraisals. This will help us to ensure that we have a consistent and fair way to appraise our employees and identify their professional development needs, while supporting our move towards a performance culture. It is our aim to roll out this software globally.

In 2012 we launched our Knowledge Sustainability Programme to provide continued technical and sales training for all our sales and service engineers. The Programme is designed to co-ordinate global training delivery and enhance the technical expertise of all our customer facing employees, with the aim of increasing sales. To achieve our objectives we are:

- delivering more training across the Group
- consolidating, organising and expanding our library of training materials to address our needs with regards to products, customer processes and sales skills
- multiplying and sharing training materials across the Group to support local training initiatives with global consistency.

Objectives 2 and 3 will be further developed in 2013 through the launch of a new online training tool, ensuring that even more of our employees worldwide will have access to much improved training.

Employee survey, Spirax Sarco Italy
A recent survey of Spirax Sarco employees in Italy established that 99% of workers found informational meetings, held by senior managers, helpful. As a result of the survey it was decided to hold regular meetings with all employees to update them on Company objectives, projects and news.

Spirax Sarco, Mexico – a great place to work
This year Spirax Sarco has been awarded 3rd place in the 'Best Place to Work Regional Ranking' for the northeast of Mexico, moving up from 8th place last year. The Company has also been certified as a 'Great Place to Work' in Mexico.

Engaging with our staff through the 'GEM' concept

At Watson-Marlow Pumps we encourage a culture of continuous improvement across our operations. At the heart of this is our Global Excellence in Manufacturing (GEM) initiative that brings together and builds on the best systems, initiatives and policies from across our Group.

GEM is people-led. We are improving our business through empowering our employees, sharing best practice and creating an environment in which our people help to drive through initiatives. GEM is also being used to identify key performance measures and opportunities for improvement, as well as record our successes.

GEM is making an impact on the way we go about our business. At our Flexicon factory in Denmark we are engaging in active dialogue with our staff in order to find new ways of making sustainability a collective responsibility.

We believe that GEM gives our employees a voice, which is central to fostering a culture in which they feel motivated and understand the importance of sustainability, as well as improving overall efficiency within the business.

Health and safety

The health and safety of our employees is paramount. We recognise our responsibilities to ensure the well-being and safety of our employees and to maintain a safe environment for visitors and subcontractors while they are on Company premises. We obey the Health and Safety regulations of each country in which we operate, and set high standards across the Group.

All staff are instructed in the Group's Health and Safety Policy, which can also be viewed by all employees on the Company's intranet. The policy is reviewed annually by the Group Risk Management Committee, and updated to improve practice across the Group.

Some of the main principles of the policy include:

- Managers must see that everything reasonably practicable is done to prevent injury at work and maintain a safe and healthy place of work
- Training must be provided to minimise health and safety risks
- All accidents, incidents and near misses must be recorded and used to guide continual improvement.

We have a detailed management structure in place to monitor health and safety standards across the Group. Trained safety officers and committees assess their local working environment and report their findings to the General Managers who each maintain a local policy and are responsible for ensuring that processes and standards are enforced. The General Managers report to the Divisional Directors, who report directly to the Executive Director responsible for HS&E.

We apply above industry standard criteria for reporting accidents, injuries and health and safety incidents, ensuring comprehensive coverage across the Group. All incidents are reported quarterly to the Executive Director responsible for HS&E, while all major injuries, causing a person to be absent from work for three or more days, work related incidents or near miss accidents are reported immediately. Improvements made to prevent a repeat of the accident are reported within two days of the incident report.

Our commitment to health and safety ensures that we maintain a low accident incident rate. During 2012 the accident incident rate across the Group was 65 per 1,000 employees (2011 : 70 per 1,000 employees).

A total of 361 accidents, injuries or incidents were recorded during 2012. Of these, 30 were classified as 'major reportable'.* In each instance a full report was conducted and changes initiated to prevent reoccurrence.

For example, a UK apprentice experienced a case of dermatitis following time in the Training Centre. The incident report identified insufficient training and monitoring of washing regimes. Following the incident, the Training Centre have revised their induction to include more information on dermatitis and how to prevent it, and all first year apprentices are now included in a health surveillance programme so that they can be checked and monitored.

* An accident that caused a person to require three or more days absence from work; an accident resulting in death; an accident or near miss that could have resulted in death, or a recognised disease that could have been caused by their work.

Developing young talent – Spirax Sarco, UK

Spirax Sarco, UK is adopting a co-ordinated approach to replenishing its pipeline of talent for the future, by investing in a number of early years career programmes. The Company has established a partnership with the local Balcarras School, Cheltenham, and provides pupils with careers and STEMNET (Science, Technology, Engineering and Mathematics Network) events, as well as work placement opportunities.

The Company has a well-developed apprenticeship system and is an approved provider of an advanced craft and advanced technician SEMTA (Sector Skills Council for Science, Engineering and Manufacturing) pathway. At the close of 2012, Spirax Sarco had 22 apprentices on its programme, providing them with skills for successful employment.

Many undergraduate engineering students have benefited from a 'year in industry' placement with Spirax Sarco. At year-end 2012, five students were on a placement in Cheltenham. Successful individuals from the scheme are offered a bursary for the remainder of their studies and given conditional offers of employment.

Employment practices

The Group seeks to make a positive impact on the communities and environment in which our employees work, through our operations, products and services, and our interactions with our customers, colleagues and suppliers. All employees are expected to behave ethically when working for the Company and this is reflected in the detailed policies set out in both the Employee Handbook and the Group Management Code (including the Group's Anti-Bribery and Corruption Policy and Competition Policy). Ethical business practices are integral to the Company and are reflected in the practices relating to recruitment, disciplinary matters and grievances.

The Group is fully committed to the principle of equal opportunity in employment and maintains a working environment free from discrimination, victimisation, harassment or bullying. The Company ensures that all applicants and employees receive equal treatment during their recruitment, transfer, promotion and training, and in the assessment of salary and benefits irrespective of an individual's sex, race, gender reassignment, disability, sexual orientation, age, religion or belief, pregnancy or maternity, marriage or civil partnership status.

We give full and fair consideration to applications for employment made by disabled persons, having regard to their particular aptitudes and abilities. We have policies in place to facilitate the continuing employment of those who may become disabled during the period in which they are employed by the Company, and disabled persons are entitled to the same opportunities for training, career development and promotion as all other Company employees, in line with our 'Dignity at Work' and 'Equal Opportunities' policies.

Anti-bribery and corruption

We are proud of Spirax Sarco's corporate reputation. Our Group Management Code protects our reputation by requiring fairness, honesty and transparency in everything we do. We expect everyone within the Group to meet the standards set out in our Code to:

- Comply with laws, regulations and Group standards
- Reject bribery and corruption
- Conduct business in a fair manner
- Treat customers fairly
- Maintain confidentiality of information
- Report with accuracy and honesty
- Act responsibly towards our people, communities and the environment.

We raise employee awareness of the Group Management Code through our induction programme and by requiring everyone to understand, accept and sign up to the Code.

The Group has an Anti-Bribery and Corruption Policy which forms part of the Group Management Code. It applies to all operating companies and all Directors, officers and employees of the Group.

It is Group policy to conduct its business free of any bribery or corruption. The Group will not enter into contractual relationships with third parties who are known to engage in corrupt practices and will not engage in the giving or receiving of bribes or favours.

All existing and new directors, senior managers and employees who have regular contact with customers or suppliers, and are therefore at risk of bribery and corruption, must take part in the newly introduced anti-bribery online training arranged by the Group. At the conclusion of the 'anti-bribery@work' training, they must pass a test to demonstrate their understanding of the Group's Anti-Bribery and Corruption Policy. The Policy and the online training are available in 15 different languages and are available to all employees.

If an employee thinks the Policy is not being observed they have a duty and an obligation to report the issue in accordance with the Group's Anti-Bribery and Corruption Policy. All such reports will be investigated appropriately.

Measures are in place to ensure complaints are treated confidentially to the fullest extent possible. Employees raising legitimate concerns in good faith will be protected to the fullest extent possible. The Group will not permit retaliation of any kind against any employee for making good faith reports about an actual or suspected violation of this Policy.

In 2012, the Group clarified its Gifts, Hospitality and Entertainment Policy which sets out the Group's position on the giving and receiving of gifts, hospitality and entertainment and employees' responsibilities under this Policy. This Policy complements the Anti-Bribery and Corruption Policy and it aims to ensure transparency, provide clarity on acceptable behaviour and comply with relevant anti-bribery and corruption legislation.

The aim of the Policy is to ensure the highest standards of integrity are maintained and that there can be no suggestion of an improper motive behind an offer or acceptance of a gift or hospitality, or of undue influence on the recipient.

Each operating company must keep an up to date register of all gifts and entertainment/hospitality, given or received, that exceed £100 per person for gifts, or £250 per person for entertainment/hospitality.

The Register of Gifts and Hospitality shall be provided to the internal auditor and external auditor on request.

FTSE4Good

Spirax-Sarco Engineering is a constituent of the FTSE4Good UK Index

FTSE Group confirms that Spirax-Sarco Engineering plc has been independently assessed according to the FTSE4Good criteria and has satisfied the requirements to become a constituent of the FTSE4Good Index Series. Created by the global index company FTSE Group, FTSE4Good is an equity index series that is designed to facilitate investment in companies that meet globally recognised corporate responsibility standards. Companies in the FTSE4Good Index Series have met stringent environmental, social and governance criteria, and are positioned to capitalise on the benefits of responsible business practice.

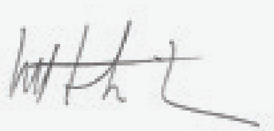
Managing the business responsibly

Setting out the Board's approach to governance and corporate culture.

Quick reference guide to the contents of the Governance section

Chairman's introduction to governance

At Spirax-Sarco Engineering plc we remain committed to high standards of corporate governance. This is central to the continued strong performance of the business in a manner which is sustainable in the long-term and to maintain the confidence of shareholders.



Bill Whiteley
Chairman

We believe that good governance is about managing the business effectively and in a way that is honest, transparent and accountable.

On the following pages, we set out our approach to governance. We explain how the Board and its Committees are structured, how they operate and what they have done during the year, as well as how their effectiveness is evaluated. We support the Government's efforts to encourage more effective narrative reporting and we ensure that our reporting on governance matters is comprehensive, clear and well-structured. We aim for reporting that is relevant and accessible.

As required by the Listing Rules of the Financial Services Authority, our Governance Report explains how the Group has applied the principles and complied with the provisions of the UK Corporate Governance Code 2010 (Code). The table on pages 75 to 79 sets out, on a provision by provision basis, our compliance with the Code.

We have satisfied the requirements of the Code in 2012 and up to the date of approval of the Annual Report.

The new UK Corporate Governance Code 2012 applies to the Group from 1st January 2013 and we will report under this code in future Annual Reports, although many of the requirements in the 2012 code are embedded in this year's Annual Report.

Other statutory and regulatory disclosures required under DTR 7.2.6 can be found on page 81.

Mr Bullock, the Senior Independent Director and Remuneration Committee Chairman, discusses in his introduction to the Remuneration Report, on page 60, our approach to executive remuneration. This is a topic which has been the subject of debate and we appreciate that it is important to our shareholders. Therefore, we have placed considerable emphasis in this Annual Report on the clarity of the Remuneration Report.

During 2012 it has been particularly important to keep in touch with our principal investors and to ensure we have a better ongoing dialogue with them.

Mr Bullock has met with investors and shareholder representative bodies on remuneration. We have listened to ensure that we understand the views of our shareholders. This active discussion develops a better understanding of mutual objectives and will continue to be a focus going forward.

As a Board, we have ultimate responsibility for the Group's performance and for overseeing the management of risk. We acknowledge that shareholders look to us to promote the long-term success of the Group and, as Chairman, I recognise that it is my role to provide the leadership to enable it to do so effectively. This year the effectiveness of the Board was subject to an externally facilitated independent review by Dr Tracy Long of Boardroom Review Limited. The details of this review are set out on page 51. The effectiveness of the Board is reviewed on an annual basis and it is the Board's intention to undertake an independent external review at least once every three years.

The Board takes seriously its responsibility for promoting the Group's values and, in particular, for ensuring that all employees and everyone associated with the Group are aware of their responsibility to act lawfully and conduct themselves in accordance with high standards of business integrity. These values are embedded in our Group Management Code. A strong anti-corruption culture has long been at the centre of the Group's values. The UK Bribery Act 2010 saw the introduction of an Anti-Bribery and Corruption Policy and its implementation across the Group. We have built on this Policy during 2012 by introducing specific policies on gifts and hospitality, and dealing with third parties. In January 2013 we also introduced a comprehensive training programme called 'anti-bribery@work' across the Group. As part of the programme all Directors and employees who work with customers and suppliers, approximately 2,400 in total, are required to pass a test. The training will be refreshed and repeated periodically. The principle that no employee or representative should be involved or implicated in any way in corrupt practices, and the training and tools to ensure that this principle is applied, are firmly embedded throughout the Group.

A further area of focus for us in 2012 was a review of our arrangements with our external auditor. With support from the Audit Committee, the Board satisfied itself that KPMG Audit Plc is both effective and independent. Following the publication of revised guidance by the Financial Reporting Council, we have taken the opportunity to review and update our policy on auditor independence and we explain the revised policy in more detail in the section on audit and accountability on page 53.

Good corporate governance has always been an important matter for the Board and, combined with our clear and consistent strategy, the Group is well equipped to continue generating value for shareholders. I look forward to meeting you at our Annual General Meeting on Thursday, 9th May 2013.

Bill Whiteley
Chairman

The Boardroom

- Chairman
- Executive Directors
- Independent Non-Executive Directors

Bill Whiteley
Chairman
- Senior management experience
- Engineering
- International

David Meredith
Finance Director
- Finance and accounting
- Engineering
- Pensions

Neil Daws
Executive Director Asia Pacific and Supply
- Manufacturing
- Engineering
- Health, safety and environmental

Nick Anderson
Executive Director EMEA
- Engineering
- International operations
- Sales management

Jay Whalen
Executive Director WMP
- Engineering
- Sales and marketing
- International business development

Mark E Vernon
Group Chief Executive
- Experienced CEO
- Engineering
- International

Gareth Bullock
Senior Independent Director
Non-Executive Director
- Banking
- Risk
- Remuneration
- International skill

Krishnamurthy Rajagopal
Independent
Non-Executive Director
- Engineering
- Senior management experience
- International

Trudy Schoolenberg
Independent
Non-Executive Director
- Engineering
- Product development
- Oil and petrochemical

Clive Watson
Independent
Non-Executive Director
- Finance
- Business planning
- Engineering

Directors' biographies are set out on pages 46 and 47.

Board of Directors

Bill Whiteley BSc, FCMA (64)
Chairman

Committees

Nomination (Chairman)

Experience

Joined the Group as an independent Non-Executive Director in 2002 and was appointed Chairman in 2009. Until his retirement in 2008 Mr Whiteley was Chief Executive of Rotork plc, where he had been a Director since 1984. He is Chairman of Brammer plc and Hill & Smith Holdings PLC and Senior Independent Director of Renishaw plc. Mr Whiteley has been awarded an honorary Doctorate of Engineering by the University of Bath.

Mark E Vernon BSc (Hons) (60)
Group Chief Executive

Committees

Nomination, Risk Management (Chairman)

Experience

Joined the Group in 2003 as President of the Group's steam business in the US. Mr Vernon was appointed to the Board in 2006, became Chief Operating Officer in 2007 and Group Chief Executive in 2008. Mr Vernon is a Non-Executive Director of Senior plc and, with effect from February 2013, Liqtech International, Inc. Mr Vernon has had a long career in industrial engineering, serving previously as Group Vice-President of Flowserve's Flow Control Business Unit, Group Vice-President of Durco International and President of Valtek International, a global controls business.

Gareth Bullock MA (59)
Independent Non-Executive Director
Senior Independent Director

Committees

Audit, Nomination, Remuneration (Chairman)

Experience

Joined the Group as an independent Non-Executive Director in 2005. Mr Bullock has had a career in banking, having retired from the Board of Standard Chartered PLC in 2010 following roles in Technology and Operations, Strategy and Northeast Asia. He was most recently responsible for Africa, Middle East, Europe and the Americas as well as for the Risk function. Mr Bullock also currently serves as a Non-Executive Director of Tesco PLC and Global Market Group Ltd, and is a Trustee of the British Council.

Krishnamurthy Rajagopal FREng, CEng, FIET, FIMechE, FIE, FCMI, PhD (59)
Independent Non-Executive Director

Committees

Audit, Nomination, Remuneration

Experience

Joined the Group as an independent Non-Executive Director in 2009. Dr Rajagopal is a Non-Executive Director of WS Atkins plc, Bodycote plc and e2v technologies plc. He also serves as Chairman of UMI³ Ltd. On completing his Doctorate in 1980, he became Manufacturing Systems Manager for Edwards High Vacuum (part of the BOC Group plc) before being appointed Operations Director. Dr Rajagopal was later appointed Managing Director of the Vacuum Technology Division, prior to being named Chief Executive of BOC Edwards in 1998 and Executive Director of the BOC Group plc in 2000. He retired from BOC Group plc in 2006.

Trudy Schoolenberg PhD (54)
Independent Non-Executive Director

Committees

Audit, Nomination, Remuneration

Experience

Joined the Group in August 2012 as an independent Non-Executive Director. Dr Schoolenberg most recently served as Vice-President of Global Research & Development at Wartsila Oy, the world leader in land and marine power systems. Prior to that, she worked for 21 years for Royal Dutch Shell plc and held several senior management positions, including Deputy Site Manager and Production Manager of the Shell Pernis refinery in the Netherlands, the largest refinery in Europe, and also served as Head of Strategy for Shell Chemicals. Dr Schoolenberg is currently a Non-Executive Director of COVA, the agency responsible for maintaining the Dutch strategic oil and petrochemical reserves.

Clive Watson B Comm (Acc), ACA, CTA (55)
Independent Non-Executive Director

Committees

Audit (Chairman), Nomination, Remuneration

Experience

Joined the Group as an independent Non-Executive Director in 2009. Mr Watson is an Executive Director and Group Finance Director of Spectris plc. He held several tax and finance roles before joining Black & Decker in 1988 as Director of Tax and Treasury Europe, and was later appointed Vice-President of Business Planning and Analysis in the US. He then joined Thorn Lighting as Group Finance Director before working for Borealis as Chief Financial Officer and Executive Vice-President of Business Support. Mr Watson joined Spectris plc in 2006 as Chief Financial Officer.

David Meredith FCMA, CGMA (53)
Finance Director

Committees

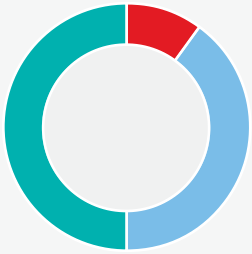
Risk Management

Experience

Joined the Group in 1988 as Group Accountant. Mr Meredith was appointed to the Board as Finance Director in 1992. He trained as an accountant with Redman Heenan International, a specialist engineering group, and was appointed Accountant at their Heenan Drives Limited subsidiary. Mr Meredith later joined English & American Reinsurance Company where he held finance positions prior to joining the Group.

Balance of Non-Executive and Executive Directors

Chairman	1
Non-Executive Directors	4
Executive Directors	5



Neil Daws CEng, FIMechE (50)
Executive Director Asia Pacific and Supply

Committees

Risk Management

Experience

Joined the Group in the UK in 1978. Mr Daws has wide manufacturing experience within the Group, having held positions in production and design engineering prior to being named as UK Supply Director. Mr Daws was appointed to the Board in 2003 and is now responsible for Asia Pacific and Supply, including the Company's Supply operations in the UK and France, together with the Group's health, safety and environmental matters.

Nick Anderson BS Civil Engineering, MBA (52) Executive Director EMEA

Committees

Risk Management

Experience

Joined the Group in 2011 as Director EMEA for the Group's steam specialties business and was appointed to the Board in March 2012. Mr Anderson has wide industry experience and worked for several subsidiaries of the Smiths Group plc. Prior to joining Spirax Sarco, he was Vice-President of John Crane Asia Pacific and, previously, President of John Crane Latin America based in Miami, Florida. Mr Anderson also held senior positions with Alcoa Aluminio in Argentina and the Foseco Minsep Group plc in Brazil before joining the Smiths Group plc.

Jay Whalen BA, MBA (56)
Executive Director

Committees

Risk Management

Experience

Joined the Group in 1991 as President of Watson Marlow Inc. in the US and was appointed to the Board in March 2012. Mr Whalen was named Sales and Marketing Director of the global Watson-Marlow pump business in 2002 and in 2010 was appointed to his current position of President, Watson-Marlow Pumps. Prior to joining Watson-Marlow, Mr Whalen was Vice-President Operations for Harvard Apparatus.

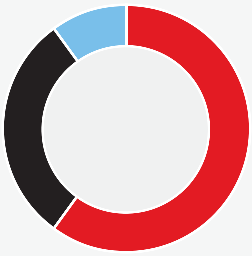
Corporate governance report

Board tenure

	0-3 years	3
	3-6 years	2
	6-9 years	3
	9+ years	2

Board nationality

	British	6
	American	3
	Dutch	1



Board composition

Mr Whiteley leads the Board as Chairman. He also chairs the Nomination Committee. The Chairman's other significant commitments are set out in his biography on page 46.

Mr Vernon leads the business as Group Chief Executive and has Board responsibility for the steam specialties business in the Americas. He also chairs the Risk Management Committee.

Mr Meredith is the Finance Director.

Mr Daws is the Executive Director for the steam specialties business in Asia Pacific and the steam specialties Supply operations in the UK and France.

Mr Anderson is the Executive Director for the steam specialties business in Europe, the Middle East and Africa (EMEA).

Mr Whalen is the Executive Director for the Watson-Marlow peristaltic pumps business.

Mr Bullock is an independent Non-Executive Director, our Senior Independent Director and Chairman of our Remuneration Committee.

Dr Rajagopal is an independent Non-Executive Director.

Dr Schoolenberg is an independent Non-Executive Director.

Mr Watson is an independent Non-Executive Director and Chairman of our Audit Committee.

Mr Anderson and Mr Whalen joined the Board on 15th March 2012 as Executive Directors.

Dr Schoolenberg joined the Board on 1st August 2012 as an independent Non-Executive Director. Her broad industrial engineering background, proficiency in new product development and experience in Europe will benefit the further development of the Group's successful international business.

The Board is supported by Mr Robson, who was appointed on 1st July 2012 as General Counsel and Company Secretary.

At the Annual General Meeting (AGM) to be held on 9th May 2013, shareholders will be asked to elect to the Board our new Non-Executive Director, Dr Schoolenberg. All other Directors will offer themselves for annual re-election.

Details of the experience of the Directors, biographical information and their roles are set out on pages 46 and 47.

Director development

Directors attend formal training seminars to update their knowledge and duties. The Board is regularly updated on changes to relevant laws and regulations. Non-Executive Directors are invited to attend Group conferences, which provide information on new product development and sales and marketing initiatives. Business presentations are given at Board meetings to enable a review of new product development, regional operations, business strategies and employee development.

An induction pack is provided to new appointees to the Board and induction procedures include site visits, briefings by senior managers and meetings with major shareholders.

In 2012 Mr Daws attended the Advanced Management Programme at Harvard Business School.

Board attendance

Details of the number of Board and Committees Meetings, and individual attendance by Director for 2012, are set out in the table below.

Board attendance Board member	Board	Audit Committee	Nomination Committee	Remuneration Committee	Risk Management Committee
Number of meetings	**7**	**3**	**4**	**3**	**2**
W.H. Whiteley[1]	7	N/A	3	N/A	N/A
M.E. Vernon	7	N/A	4	N/A	2
D.J. Meredith	7	N/A	N/A	N/A	2
N.H. Daws[2]	6	N/A	N/A	N/A	2
N.J. Anderson[3]	5	N/A	N/A	N/A	2
J.L. Whalen[3]	5	N/A	N/A	N/A	2
G.R. Bullock[1]	7	3	3	3	N/A
K. Rajagopal	7	3	4	3	N/A
G.E. Schoolenberg[4]	3	1	1	1	N/A
C.G. Watson[1]	7	3	3	3	N/A

[1] Absence due to Nomination Committee considering Director's re-appointment.
[2] Absence due to attendance at the Advanced Management Programme at Harvard Business School.
[3] Appointed to Board on 15th March 2012 and member of Risk Management Committee prior to that date.
[4] Appointed to Board on 1st August 2012.

N/A means not applicable.

Approach to governance

Governance helps us to:

- Ensure our shareholders receive a good return on their investment
- Behave with integrity as colleagues, making sure that each feels valued, motivated and rewarded
- Treat our customers, suppliers and local communities properly
- Respect the environment.

Board activities in 2012

We aim to embed governance practices throughout the Group so that they become an integral part of running a successful business. In the adjacent diagram we have given examples of the Board's focus during 2012. The Board agendas are linked to the fundamentals of a trusted brand, a clear strategic plan, strong leadership, motivated employees and satisfied customers, together with the necessary checks and balances. We focus on long-term plans for our businesses, the issues that matter on the ground, and what our management and people are doing day-to-day. The Board spends 40% of its time ensuring the Group's operations and risk management controls are effective. During 2012 the Board also regularly reviewed the Group's performance and satisfied itself that, despite difficult trading conditions, management was on track in delivering the strategic business plan. In addition, the Board concentrated its efforts on product development and ensuring the Group was benefiting from its supply consolidation initiatives. The Board also regarded engagement with shareholders on governance, remuneration and trading as a significant issue and was appraised of progress on a regular basis.

Compliance with the Code

The governance rules which apply to the Group for 2012 are found in the Code. Meeting the requirements of the Code is achieved through the application of the principle 'comply or explain'. It is expressly stated in the Code that the Code is not a rigid set of rules and that an alternative to following a provision is justified, in particular circumstances, if good governance can be achieved by other means. The Group's compliance in 2012 with each provision of the Code is set out in the table on pages 75 to 79.

The table shows that the Group complied with every Code provision except the balance of the Board between Executive and Non-Executive Directors (Code provision B.1.2). There are currently five Executive and four independent Non-Executive Directors, excluding the Non-Executive Chairman. The Board is pleased to take this opportunity to thoroughly explain its reasons for this structure and, in doing so, meets the requirements of the Code to comply or explain. The Board also wishes to explain why the composition of the Board is justified in the circumstances and how good governance is still achieved.

Board focus during 2012

Operations and risk	40%
Strategy	20%
Governance and shareholders	20%
Finance	10%
People and succession	5%
New product development	5%

The Group operates a predominantly direct sales business model, a strategy that has been at the heart of the Group's success over many years. The need for a direct presence in every market of any size leads to a trading structure with many relatively small operations – the Group currently has over 50 operating companies in 36 countries and operates in more than 100 countries. Our business philosophy is to empower the General Managers of our local companies to maximise the opportunities in each market, whilst ensuring there is appropriate oversight, control and integration.

Effective Board oversight and control of this necessarily flat organisation structure with many small components is, we believe, best achieved by having knowledgeable Executive Directors on the Board providing direct first-hand operational input to the Chairman and Non-Executive Directors. The three Executive Directors, in addition to the Group Chief Executive and the Finance Director, are responsible for the EMEA and the Asia Pacific/Supply divisions for the steam specialties business, and for the Watson-Marlow peristaltic pumps business. They have detailed knowledge of their respective divisions and their presence on the Board enables the Chairman and independent Non-Executive Directors to have regular access to the operations of the Group. Executive Directors also gain valuable experience of wider business issues across different divisions, regions and functional areas, which we believe enhances the Group's succession planning process. Having a number of Executive Directors on the Board manages the risk of over-reliance on limited Executive Director opinion.

The Board has a well-balanced blend of experienced, independently-minded Non-Executive Directors who provide robust challenge. The practical conduct of Board meetings is such that, even though there are five Executive Directors and four independent Non-Executive Directors (excluding the Non-Executive Chairman), the views of the Non-Executive Directors are given due weight and a collective approach to decision-making is adopted. The Board considers that it has the appropriate balance of skills, experience, independence and knowledge to enable it to discharge its duties and responsibilities effectively and that expanding its size by the appointment of another Non-Executive Director, simply to meet the balance criteria, will have the effect of the Board becoming unwieldy. Nevertheless, the Board recognises that this is an important matter to shareholders, and will ensure it is subject to continuous review.

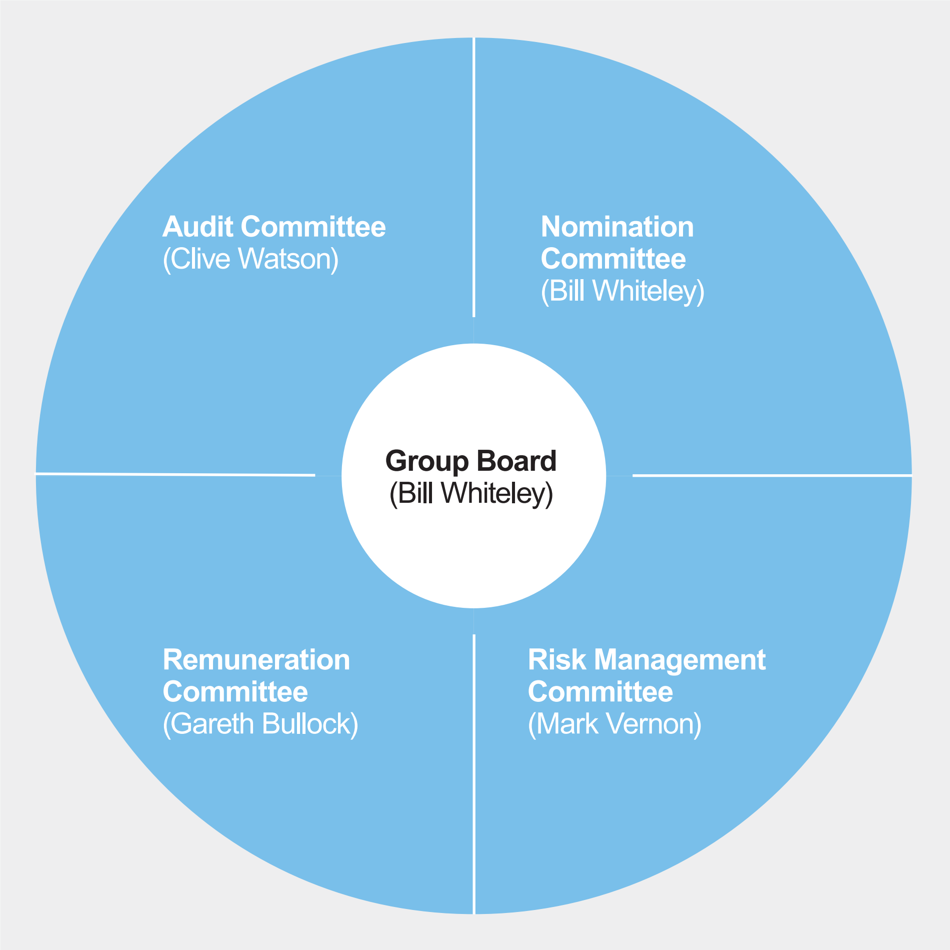
The Group has an excellent track record in delivering sustained growth in shareholder value and £1,000 invested in January 2003 produced a total shareholder return, as at 31st December 2012, of £7,488 (+649%). In the latest five-year period, total shareholder return has increased by 201% and the share price has risen from under £9 to over £22 at the end of 2012, all underpinned by the Group's good governance practices over many years.

The external review of Board effectiveness conducted recently by Dr Long, and described in more detail on page 51, concluded that the Board functions effectively and that its decision-making process is excellent. It is also important to point out that including the Non-Executive Chairman (who was independent on appointment) balances the Board and the Non-Executive Chairman has a casting vote in the event of a deadlock. In providing this detailed explanation the Board considers that the Group satisfies the requirements of the Code to comply or explain.

The Board is committed to the changes to the Code in relation to board diversity. The Board has set measurable objectives and will monitor progress on diversity. Diversity is discussed in more detail in the Nomination Committee's Report on page 54.

Governance structure

Our governance structure is best illustrated by the diagram set out below.



Chairman's responsibilities

- Managing the business of the Board and facilitating the participation of each Director
- Safeguarding robust Corporate Governance processes and the development and maintenance of governance policies
- Facilitating constructive debate and discussion on Board agenda items and ensuring that alternative viewpoints are considered
- Maintaining appropriate contact, in conjunction with the Group Chief Executive, with shareholders and in stock market related matters
- Providing for regular evaluation and feedback of the performance of each Director and the Board
- Ensuring effective succession planning for Directors
- Interfacing with regulatory bodies which may require access to the Chairman
- Working successfully with the Group Chief Executive to ensure performance objectives are achieved

Group Chief Executive's responsibilities

- Managing the Group's business and the effective stewardship of capital, technical and human resources including senior management succession planning
- Ensuring appropriate internal controls for risk management
- Developing and recommending corporate and business strategy for Board approval
- Maintaining direct contact with shareholders and dealing with stock market related matters
- Providing leadership to the Group's most senior executives in their management of functional activities
- Recommending to the Board major changes in the organisational structure of the Group
- Ensuring that the Group complies with all appropriate legislation
- Directing the Group's internal and external communications
- Performance of the Group in meeting its short, medium and long-term objectives

Governance structure

The Board Committees and functions are listed below along with an overview of their activities and the main person responsible. The terms of reference for the Committees are published on the Group's website, www.spiraxsarcoengineering.com.

Group Board

Mr Whiteley

The Board relies on Executive management to run the business, monitors management activities and holds them accountable against targets and standards. The Board also approves long-term corporate and strategic plans after a full review and assessment of market and technology trends, business drivers and risks. Having a senior management team that is capable of executing the strategic plans is a key focus.

The formal schedule of matters reserved for the Board's decision is available on the Group's website, www.spiraxsarcoengineering.com.

Key matters include:

- The approval of corporate and strategic business plans
- The approval of the annual and interim results
- Interim management statements
- Acquisitions
- Major capital expenditure
- Director appointments
- Major litigation.

The Non-Executive Directors provide independent challenge and review, bringing wide experience, specific expertise and a fresh, objective perspective.

The Board meets as often as is necessary to discharge its duties. In 2012 the Board met seven times. All Directors are expected to attend all Board meetings and relevant Committee meetings unless prevented by prior commitments, illness or a conflict of interest. Directors unable to attend specific Board or Committee meetings are sent the relevant papers and asked to provide comments in advance of the meetings to the Chairman of the Board or Committee, as appropriate. In addition, all Board and Committee members receive copies of the minutes of meetings as a matter of course.

The Directors' attendance record at Board and Committee meetings is set out on page 48. The Non-Executive Directors meet without the Executive Directors present to discuss the Executive Directors' performance and other matters. The Senior Independent Director, Mr Bullock, is available to discuss concerns with shareholders, in addition to the normal channels of the Chairman, Group Chief Executive or the Finance Director.

The Board has a conflicts of interest policy and has put in place procedures for the disclosure and review of any potential or actual conflicts.

Committee composition

The Non-Executive Directors play an important governance role in the detailed work they carry out on our Committees on behalf of the Board. All the Non-Executive Directors are determined by the Board to be independent in character and judgement, in compliance with the Code.

The General Counsel and Company Secretary supports the Committee Chairmen in making sure members are equipped for informed decision-making and that they allocate their time to the right subjects.

The Board has satisfied itself that at least one member of the Audit Committee, namely Mr Watson, has recent and relevant financial experience and is confident that the collective experience of its members enables it to be effective. The Audit Committee also has access to the financial expertise of the Group, the external and internal auditors and can seek further professional advice at the Company's expense, if required.

The Board has delegated specific responsibility to the four Board Committees, being the Audit Committee, the Nomination Committee, the Risk Management Committee and the Remuneration Committee.

Audit Committee

Mr Watson

Monitors the integrity of the financial statements and reviews the effectiveness of internal controls and external audit.

Nomination Committee

Mr Whiteley

Recommends Board appointments and reviews succession plans.

Risk Management Committee

Mr Vernon

Ensures that risk management is meaningful, relevant and focused on improving the business.

Remuneration Committee

Mr Bullock

Recommends remuneration strategy and framework to attract, retain and reward senior executives, determines annual Executive Director remuneration and approves awards under the Group's Performance Share Plan.

Further information on each of the Committees' activities during the 12 month period to 31st December 2012 is set out in pages 52 to 74.

Board effectiveness

In 2012, we commissioned an independently facilitated Board effectiveness review conducted by Dr Long of Boardroom Review Limited. Dr Long does not have any other connection with the Group. Our aim was to capture open and constructive feedback from Board members which would:

- Provide insight into our effectiveness
- Point to actions for improving our performance
- Establish a benchmark for measuring future progress.

In accordance with the provisions of the Code, we did not have to carry out the external review until 2013. However, based on the positive feedback from the Board and the fact that we had three new Directors join during the year, we decided to proceed earlier.

The review was carried out in accordance with the guidance in the Code. Our approach involved a Board observation, one-to-one interviews with all Directors, individual feedback meetings and a Board discussion. Each participant was asked to evaluate the Board and its Committees. Subjects covered included the work of the Board, the Board environment and the Board's use of time. Directors were asked for their views on our shareholder engagement and relationships and how these relationships might be improved. Views were sought on the Board's input into strategy discussions, governance and compliance, risk management and succession planning. Views were also sought on the Board culture and the relationships with senior management as well as how new Board members are selected and inducted.

The review was based on a careful analysis of the Board's approach to its work, its contribution to the Group's success, and its preparation for the future.

Dr Long commended the Board for its many strengths including its culture, chairmanship, clarity of strategy and shareholder communication.

During 2013, the Board plans to continue to:

- Review the strategic planning cycle
- Drive the agenda on succession planning and development of senior managers
- Be actively engaged on diversity
- Increase the awareness of Group best practice, particularly with regard to risk management
- Formalise Committee feedback to the Board
- Review the schedule of Board and Committee meetings across the year.

Audit Committee

Clive Watson
Chairman

Role of the Committee

The key responsibility of the Committee is to review the effectiveness of the Company's financial reporting and controls. Accordingly the Committee is authorised by the Board to:

- Monitor and review the integrity and the audit of the Company's financial results statements
- Oversee the Company's relationship with its external auditor including reviewing their independence
- Agree the fees and terms of appointment of the external auditor including quality and effectiveness.
- Consider the output of the procedures used to manage risk within the Company
- Review the Company's internal controls
- Consider the management letter from the external auditor on its review of the effectiveness of internal controls
- Agree the work plan of internal audit and review the resulting output from that plan
- Review significant finance and tax matters.

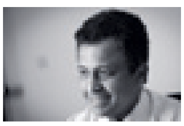
How the Committee spent its time during the year

Results review	25%
External audit	20%
Internal audit	20%
Finance and tax reviews	20%
Risk management and controls	15%

Membership and attendance

Committee member	Attendance
Number of meetings	**3**
C.G. Watson	3
G.R. Bullock	3
K. Rajagopal	3
G.E. Schoolenberg[1]	1

[1] Appointed 1st August 2012.


The Committee met three times in 2012. Both the internal and external auditors attend its meetings and have direct access to its Chairman.

Significant areas of review by the Committee in the year included principal risks, including provisions, current and deferred taxation, and the valuation of accounts receivables and inventories; reviews of significant control matters as they arose; and key judgement areas in the financial statements, including pensions, provisions and acquisitions.

The Committee reviews the effectiveness of internal audit, tracks their findings and the responsiveness of management to any issues identified. As a safeguard, at each meeting the Committee holds separate meetings with the external and internal auditors, without management present, to discuss their respective areas and any issues arising from their audits.

During the year the Committee received reports from external and internal auditors on the major findings of their work and progress of management follow up. We received assurance on going concern, counterparty risks, pension valuation and risk management.

Auditor

The effectiveness of our external auditor is vital in underpinning the Group's internal controls and the integrity of our systems, and to enable us to recommend the re-appointment of KPMG Audit Plc. The Committee judges them on the quality of their audit findings, management's response and stakeholder feedback. We check their independence by making sure they are sufficiently challenging in their work. We also set the audit and non-audit fees and ensure that our auditor engagement policy is adhered to when commissioning non-audit work.

Although KPMG Audit Plc has been in place since the 1950s, periodic changes to audit partners are made at a Group and country level in accordance with the relevant professional and regulatory standards in order to protect independence and objectivity and provide fresh challenge to the business. Such changes are planned carefully to ensure that the Group benefits from continuity of staffing without incurring undue risk or inefficiency.

To assess the effectiveness of the auditor the Committee reviewed:

- The external auditor's fulfilment of the agreed audit plan and variations from it
- The auditor's report of major issues arising during the course of the audit
- The results of the annual survey completed by local management teams of the service levels provided by the external auditor.

The Committee is satisfied with the auditor's effectiveness and independence, and the degree of diligence and professional scepticism brought to bear. As such, the Committee has not considered it necessary during 2012 to conduct a tender process for the appointment of its auditor. Having carried out the review described above, and having satisfied itself that the external auditor remains independent and effective, the Committee has recommended to the Board that the auditor be re-appointed for 2013.

The Committee has noted the revisions to the UK Corporate Governance Code introduced by the Financial Reporting Council (FRC) in September 2012 and, in particular, the recommendation to put the external audit out to tender at least every ten years. The FRC has proposed non-binding suggested transitional arrangements with respect to audit tendering, including a suggestion that tendering should normally fit the five yearly cycle of partner rotation. The Committee will take this guidance into account when considering these tendering arrangements, which will continue to focus on the effectiveness and independence of the auditor.

The Committee, with the approval of the Board, has put in place policies that restrict the types and the amount of non-audit work that can be carried out by the external auditor. The Committee is provided with a report of all non-audit work carried out by the external auditor and a full breakdown of fees related to non-audit work. A summary of the fees is contained in note 6 on page 97. The policies, restrictions and reporting requirements allow the Committee to ensure that auditor objectivity and independence is maintained.

In accordance with the International Standard on Auditing (UK and Ireland) 260 and the Ethical Statement issued by the Accounting Practices Board, the external auditor has confirmed, in writing to the Directors, its independence as auditor of the Company.

As is normal practice, the Committee carried out a thorough review in preparation for the Group's interim and preliminary financial results.

Financial reporting

Through discussion with management and the external auditor, the Committee determined that the key judgements with risk of misstatement of the Company's financial statements related to provisions, current and deferred taxation, and the valuation of accounts receivables and inventories.

These issues were discussed with management during 2012 and with the auditor when reviewing and agreeing the audit plan and also at the conclusion of the audit of the financial statements.

After reviewing the presentations and reports from management and consulting with the auditor, the Committee is satisfied that the financial statements appropriately address the critical judgements and key estimates, both in respect of the amounts reported and the disclosures. The Committee is also satisfied that the significant assumptions used for determining the value of assets and liabilities have been appropriately scrutinised, challenged and are sufficiently robust.

Review of financial statements

Over the course of 2012 the Committee considered many components of business performance in order to ensure it has a full understanding of the operations of the Group.

Examples of processes the Committee uses include:

- Reviews of the processes undertaken in determining the position adopted in key judgement areas including pensions, provisions and acquisitions
- Risk areas as described above
- Receipt of regular strategy reports from the Group Chief Executive and operational reports from the Divisional Directors
- Requesting members of management to attend Committee meetings to provide updates on operational and strategic matters
- Reviews of the budget and operational plan.

Through these processes and its monitoring of the effectiveness of controls, internal audit and risk management, the Committee is able to maintain a good understanding of business performance, key areas of judgement and decision-making processes within the organisation.

Nomination Committee

Bill Whiteley
Chairman

Role of the Committee

The primary responsibilities of the Committee are to make appropriate recommendations to the Board for the appointment, re-appointment or replacement of Directors, to keep under review the structure and composition of the Board, to recommend any proposed changes to the Board and to consider succession planning arrangements for Directors.

In making recommendations for appointments to the Board, the Committee has regard to the overall balance of the skills, knowledge and experience of Board members against the current and perceived future requirements of the Group and to the benefits of diversity, including gender.

How the Committee spent its time during the year

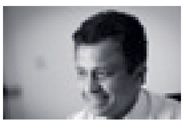
Succession planning	50%
Recruitment	20%
Diversity	20%
Board and Committee composition	10%

Membership and attendance

Committee member	Attendance
Number of meetings	**4**
W.H. Whiteley[1]	3
M.E. Vernon	4
G.R. Bullock[1]	3
K. Rajagopal	4
G.E. Schoolenberg[2]	1
C.G. Watson[1]	3

[1] Absence due to Nomination Committee considering Director's re-appointment.
[2] Appointed 1st August 2012.





A great deal of time and effort was put into finding our new Non-Executive Director, Dr Schoolenberg, in 2012. We worked with our external consultants, Korn/Ferry Whitehead Mann, defining our needs and reviewing prospective candidates. Korn/Ferry Whitehead Mann do not have any other connection with the Company. We managed a thorough, orderly search and interviewed rigorously. The appointment of Dr Schoolenberg was recommended to the Board.

We also recommended the appointment of Mr Anderson and Mr Whalen as Executive Directors. Mr Whalen was appointed internally whilst Egon Zehnder International assisted with the search for an additional Executive Director which resulted in Mr Anderson being selected. Egon Zehnder International do not have any other connection with the Company.

We have given increased focus to leadership development through robust succession planning and have strengthened our performance management culture. We seek to ensure that we have a high performing workforce and that we better identify tomorrow's leaders. Those individuals demonstrating high potential are included in our senior management development plan, which is an important part of our overall leadership succession planning.

Career plans for those individuals are reviewed regularly and the Executive Directors meet frequently to review organisational staffing requirements against career planning of high-potential leaders.

In relation to diversity, the Group seeks to have Directors who, in addition to relevant technical and commercial expertise, meet the highest standards of judgement, critical-thinking and openness. We believe that the Board's perspective and approach is greatly enhanced through gender, age and cultural diversity and it is our policy to consider overall Board balance and diversity when appointing new Directors. The diagram on page 48 illustrates the diverse range and nationalities of our Board which is particularly relevant given the broad international reach of the Group. On gender, we appointed Dr Schoolenberg as a Non-Executive Director during 2012 and, subject to appointing Directors of the highest calibre and relevant expertise, we plan to increase female representation on the Board when vacancies arise. Our aim on Board diversity is to have 25% female directors by 2016.

However, all appointments will continue to be made on merit. To achieve this target we will ensure that female candidates are considered routinely as part of the recruitment process. We will also encourage the progress of females in senior positions throughout the Group. We are pleased to report that we do have a number of females in senior positions including the Europe and Middle East Sales and Marketing Director of Watson-Marlow Pumps, the Chief Financial Officer and Chairman of Watson-Marlow Ltd and a Regional General Manager in the Spirax Sarco EMEA Division. We are also constantly improving the intake of female professionals from universities to ensure an improved talent pipeline for senior leadership roles in the future.

Risk Management Committee

Mark Vernon
Chairman

Role of the Committee

The Committee ensures that the Group has operating policies and procedures covering everything from financial planning and reporting, capital expenditure, project governance and information security to business continuity, employee performance management and how we do business. Detailed policies and procedures are in place to ensure the accuracy and reliability of financial reporting and the preparation of consolidated financial statements. The Committee is responsible for risk management, compliance and regulation.

How the Committee spent its time during the year

Internal controls	25%
Group policies	20%
Risk management framework	20%
Anti-bribery	15%
Competition compliance	10%
Business continuity	10%

Membership and attendance

Committee member	Attendance
Number of meetings	**2**
M.E. Vernon	2
D.J. Meredith	2
N.H. Daws	2
N.J. Anderson[1]	2
J.L. Whalen[1]	2

[1] Appointed to the Board on 15th March 2012 and member of Risk Management Committee prior to that date.




The following executives are also members of the Risk Management Committee: Group Human Resources Director, Group Business Development Director, Group Information Systems Director, Divisional Director – Americas and the General Counsel and Company Secretary.

Our approach and appetite for risk

Our aim is to build a sustainable business through consistent, profitable growth and to ensure that our customers and shareholders trust us. We recognise that creating shareholder value is the reward for taking acceptable risks. The effective understanding, acceptance and management of risk is fundamental to the long-term success of the Group.

Our approach is encapsulated in the principles of our risk management policy:

- To understand the nature and extent of risks facing the Group
- To accept and manage within the business those risks which our employees have the skills and expertise to understand and leverage
- To assess and transfer or avoid those risks which are beyond our appetite for risk
- By consideration of materiality, to establish the authority levels within the Group at which decisions on acceptance and mitigation of these risks are taken.

The risk review process

We have adopted an integrated approach to our risk management, independent assurance and internal controls to ensure greater linkage across our review and assessment of risk. Internal controls and risk management are designed to limit the chance of failure to achieve corporate objectives. Independent assurance is provided by the external auditor and internal audit.

The Committee has accountability for overseeing the risk management processes and procedures, and reports to the Board on the principal risks facing the Group. The Committee also monitors the mitigating actions put in place by the relevant divisions and Group companies to address the identified risks.

The Group Chief Executive, Mr Vernon, chairs the Committee. The members of the Committee are set out in the adjacent table.

External consultants are involved in the review every three years, with the last review taking place in 2011.

Each operating company is required, at a local level, to undertake a formal review of the risks which impact on its business at least twice a year. The reviews are consolidated into Group-wide risk reports which are maintained and reviewed by the Risk Management Committee on a regular basis.

The result is that the Group has in place a robust risk management process to identify, evaluate and manage the principal risks that could impact on the Group's performance.

The principal risks and the product of the 2012 review are set out on pages 58 and 59.

Internal controls

The Board has overall responsibility for the system of internal controls and for reviewing its effectiveness, whilst the role of management is to implement Board policies on risk and control. There is an ongoing review process for identifying and managing risks faced by the Group which has been in place for 2012 and up to the date of approval of the Annual Report. The review covers and assesses the effectiveness of all material controls, including financial, operational and compliance controls and risk management systems. This ensures that proper accounting records have been maintained, that financial information used within the business is reliable and that the consolidated accounts preparation and financial reporting process comply with all relevant regulatory reporting requirements. The system of internal controls is designed to manage, rather than eliminate, the risk of failure to achieve the business objectives.

The Board believes from its annual reviews that the system of internal controls is embedded in the business and regular review allows for assessment of new and changing risks in the Group's business.

In pursuing these objectives, internal controls can provide only reasonable and not absolute assurance against material misstatement or loss.

As required by the UK Listing Authority, the Group has complied throughout the year and up to the date of the Annual Report with the Code provisions on internal controls.

All operating companies are required annually to complete self-certification questionnaires regarding compliance with the policies, procedures and minimum requirements for an effective system of internal controls.

Self-certification is given by both the General Manager and the Finance Manager of each operation.

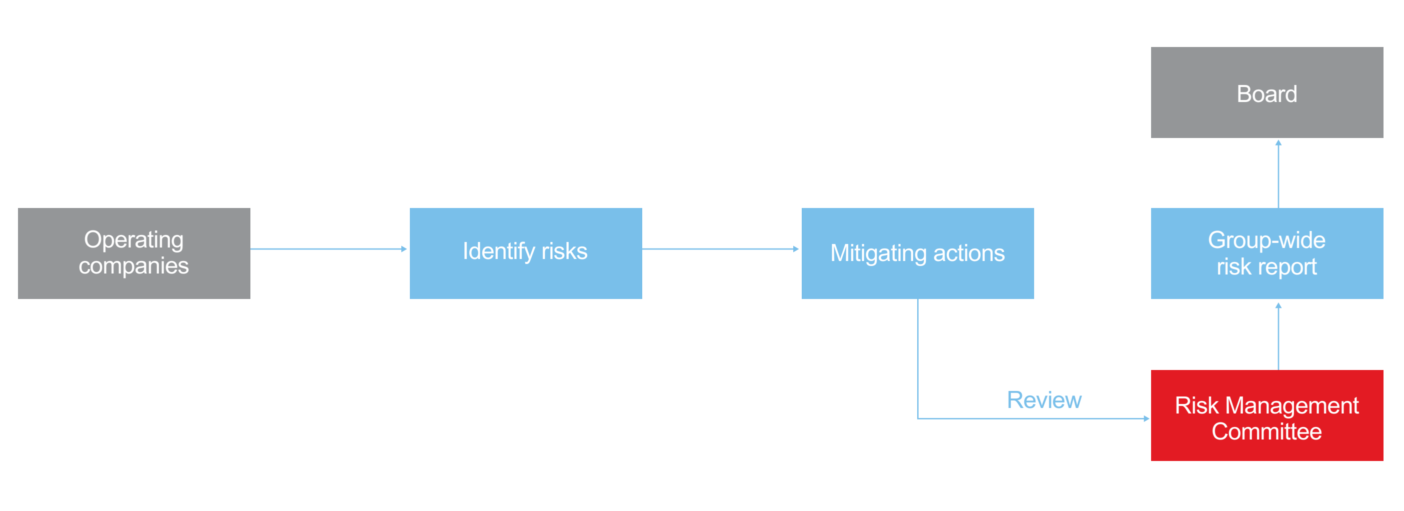
Internal audit

The Board has an established internal audit function which allows each of the Group operating companies to be audited at least every three years and those judged to be in higher risk territories will be audited more frequently. All businesses acquired by the Group are subject to internal audit within one year from the date of acquisition. Internal audit resource is supplemented by experienced, qualified accounting staff from principal Group operating companies and a professional auditing firm, BDO International. Reports are made to the Audit Committee and the Board as a whole. Whilst there were some areas for local improvement identified in the internal audit reports, no significant matters were raised in the reports made in the operating companies audited during the year.

As explained by the Chairman, in his introduction to Governance on pages 44 and 45, we have built on our strong anti-corruption culture and our Anti-Bribery and Corruption Policy by introducing new specific policies and a comprehensive training programme called 'anti-bribery@work'. The programme has been trialled and introduced in operating companies with the roll-out nearly completed at the date of the Annual Report. At the end of the roll-out, approximately 2,400 employees will have taken part.

The Committee has ensured compliance with centrally documented control procedures on such matters as capital expenditure, information and technology security and legal and regulatory compliance. We also introduced a new Competition Policy to ensure the Group conducts its business in accordance with the competition laws of all the countries in which it operates.

Risk management structure



Important developments in the year
Our risk management approach is subject to continuous review and updating to take account of new and developing issues which might impact our business objectives. The following actions have been undertaken during the year to address significant developments:

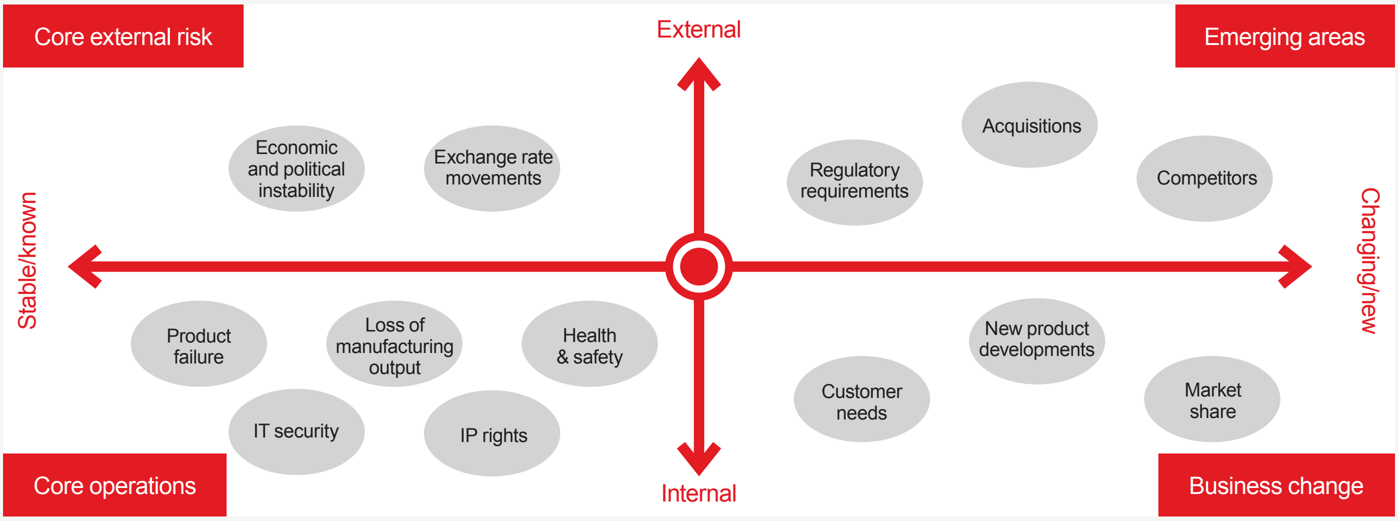
- Introduction of new specific Anti-Bribery and Corruption policies and 'anti-bribery@work' programme
- All the Group-wide risk reports have been updated
- We have managed the financial pressures on our home markets by continuing to grow our presence in emerging markets
- The diverse range of economic, geopolitical and accidental external global events has prompted a review and updating of disaster management and business continuity planning across the Group
- We have reviewed and improved our global insurance cover with particular emphasis on lower deductibles and higher cover levels for our growing international businesses.

To achieve an overview of the risks facing the business as set out in the Group-wide risk reports, the Committee categorised the risks as follows:

- External to our business
- Core to our day-to-day operation
- Related to business change activity
- Those that could emerge in the future.

The Committee then mapped the risks in the Group-wide risk reports to these categories, which is set out in the 'risk radar' diagram below. This analysis informed the determination of the principal risks set out on pages 58 and 59.

Mapping of risks to risk reports



Principal risks

A summary of the principal risks, their likely impact and an explanation of how the Group mitigates each risk is set out in the table below. The direction of change in particular risks during the year is explained in the 'Principal Risk' column and illustrated by the arrow in the 'Change' column. Finally, we have also set out the relevance of the risk to our strategy.

Please note that the 'Change' column shows the change in the risk and not the mitigation of the risk.

Principal risk	Change	Impact	Mitigation	Relevance to strategy
Economic and political instability: The Group operates worldwide. Economic and political instability creates risks for our locally based direct operations. The Group has reviewed country, credit, liquidity and currency risks and, in particular, those arising from European debt issues. The risk has increased as a result of the deterioration in some European economies and the general world economic outlook.	↑	• Fluctuations in profit from significant currency movements • Reduced profit due to impact on customers from economic problems • Potential redenomination of local currency, devaluation and high inflation.	• Compliance with Group Treasury Policy • Strong internal controls with internal audit and appropriate insurance • Resilient business model (as explained in the Business Review on page 17). • Well spread business – approximately 10% of Group sales originate in the higher risk countries of Greece, Ireland, Italy, Portugal and Spain. Sales in Greece are immaterial.	Broaden our global presence
Breach of regulatory requirements: The Group operates in a large number of countries across the world and is subject to many different laws and regulations, including the UK Bribery Act, the US Foreign and Corrupt Practices Act, health and safety, competition laws and local quality regulations. Breaching these laws and regulations could have serious consequences. This risk has increased in the year as sales in Asia Pacific have risen.	↑	• Fines and regulatory action and resultant reduced profit • Damage to reputation • Diversion of management time.	• Robust internal controls, policies and procedures and Group Management Code • Establish strong ethical culture supported by communication and training • Review of commercial arrangements and regulatory requirements with appropriate professional advice • Maintain local quality accreditations.	Create strong market positions
Non-compliance with health, safety and environmental legislation: The Group places great emphasis on health, safety and environmental issues in relation to our employees and operations, and those of our customers, suppliers and communities so as to avoid the risk of major health, safety or environmental problems.	→	• Damage to reputation • Reduced profit due to fines, compensation and clean-up costs • Enforcement action by regulatory authorities.	• Compliance with legislation and codes of best practice • Regular audits, checks and reporting to management and the Board on health, safety and environmental issues • Ongoing training • In the course of appointing a Senior Group Health and Safety Manager.	Create strong market positions
Failure to respond to technological developments or customer needs: The Group has significantly increased R&D resources and risks, this being ineffective if we fail to respond to development and customer needs or if we fail to manage and protect our intellectual property.	→	• Failure to achieve expected return on the R&D investment • Reduced profit • Loss of market share • Loss of intellectual property.	• Maintain market knowledge and monitor competitor developments, making effective use of our direct field sales force • Maintain investment in R&D programmes • Maintain appropriate intellectual property registrations, taking enforcement action where appropriate.	Generate consistent organic growth Deliver solutions to reduce energy usage

There may be other risks and uncertainties which are unknown to the Group or which could become material in the future. These risks may cause the Group's results to vary materially from historic and expected results.

Principal risk	Change	Impact	Mitigation	Relevance to strategy
Risk of product failure: The Group provides a wide range of products into many different plants and industries many of which are in critical parts of our customers' processes. A risk exists that products are wrongly specified or installed, fail, or contain design or manufacturing faults. This risk has increased during the year as a result of the Group providing more fully integrated solutions.	↑	• Damage to customer relationships • Reduced profit due to increased costs to correct the problems caused at customers' plants • Litigation following product liability claim.	• Products designed and tested to international standards and strict quality procedures • Training of sales/installation staff • Appropriate conditions of sale and contractual restrictions on liability • Insurance cover.	Create strong market positions Deliver solutions to reduce energy usage
Loss of manufacturing output at any Group factory: The Group manufactures most of the products we sell in eight main factory units which supply our sales operations worldwide. Loss of manufacturing output at any important plant risks serious disruption to sales operations. This risk has reduced in the year due to the realisation of the Group's manufacturing strategy of regionalising the manufacturing base.	↓	• Reduced sales and profit due to inability to meet customer orders • Loss of market share • Damage to reputation.	• Group manufacturing strategy to regionalise manufacturing base and increase resilience • Business continuity planning and disaster recovery plans • Stocks of components and finished products in sales companies • Regular and comprehensive back-ups of IT systems • Use of insurance audits/ inspections and business interruption insurance.	Broaden our global presence
Defined benefit pension deficit: Defined benefit pension schemes carry risks in relation to investment performance, security of assets, longevity and inflation. Total defined benefit pension liabilities represent approximately 52% of total Group assets. This risk has reduced in the year as a result of the operation of the Mercer 'Dynamic De-Risking Solution'.	↓	• Increase in liabilities • Increase in pension costs and cash contributions • Fluctuations in pension fund asset and liability values.	• Use of independent professional advisers and custodians for defined benefit pension schemes • Pension scheme de-risking strategy to automatically reduce equity exposure and increase matching assets at pre-agreed trigger points.	
Failure to realise acquisition objectives: The Group's strategy is focused on organic growth complemented by acquisitions (as explained in the Business Review on page 17). We risk failing to achieve the expected return on investment if acquisitions are not properly identified, executed and integrated.	→	• Failure to achieve expected return on investment • Assumption of unexpected liabilities.	• Evaluation of potential targets against Strategic Plan and acquisition criteria • Project management disciplines • Appropriate due diligence by Group personnel and external advisers covering commercial, legal, accounting and environmental issues.	Grow market share Deliver solutions to reduce energy usage

Remuneration report

Remuneration Committee

Gareth Bullock
Chairman

Role of the Committee

The main responsibility of the Committee is to set executive remuneration policies covering salary and benefits, performance-based variable reward, pensions and the terms of service agreements. The Committee is authorised by the Board to:

- Determine the specific remuneration packages for the Group Chief Executive and the Executive Directors
- Set targets for the Company's performance-based variable reward schemes and determine achievement against those targets, exercising discretion as appropriate where provided by scheme rules
- Monitor and advise the Board on any major changes in employee benefit structures throughout the Group
- Appoint and seek advice from appropriate consultants in respect of Executive Director remuneration.

Please note that sections 2.1, 2.2, 2.3.3, 3.1 to 3.6, 4.1 and 4.2 of this Remuneration Report have been subject to audit.

How the Committee spent its time during the year

Pay policy	20%
Executive pay	20%
Directors' contracts	20%
Bonus target setting	10%
Bonus achievement	10%
PSP target setting	10%
PSP achievement	10%

Membership and attendance

Committee member	Attendance
Number of meetings	**3**
G.R. Bullock	3
K. Rajagopal	3
G.E. Schoolenberg[1]	1
C.G. Watson	3

[1] Appointed 1st August 2012.

1. Introductory letter

"We remain committed to maintaining a strong link between the Company's performance, the creation of long-term shareholder value and the level of remuneration received by the Executive Directors."

As Chairman of the Remuneration Committee I am pleased to present to you our Remuneration Report in respect of the financial year ended 31st December 2012. As a Committee, we are acutely aware of the ongoing debate taking place with respect to executive pay. We support the UK Government's plans to simplify disclosure and improve the clarity of explanations on how executive remuneration is linked to Company performance and shareholder interests. To that end, we have sought to adopt many aspects of the draft UK Government guidelines in our Remuneration Report in 2012, while also complying with the requirements of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008.

In this Remuneration Report we set out details of our pay policy along with how it was implemented in 2012. However, I would firstly like to take this opportunity to explain the main activities of the Committee in 2012, and summarise the context within which our decisions were made.

Business performance

As reported in the Chairman's Statement on page 4 of this Annual Report, the Company made further progress during 2012 and achieved another year of record sales, profit and cash generation. The total dividend for the year increased by 8%, extending our dividend record to 45 years.

Our remuneration policy is designed to ensure that a significant percentage of senior management pay is based on the achievement of demanding performance targets and is therefore 'at risk'. The maximum pay out in the annual bonus plan and long-term incentive scheme is only available as a result of significant outperformance by the business. Although we achieved good results in 2012, overall macro-economic conditions were difficult and some of the more demanding performance targets established in the annual bonus plan and Performance Share Plan (PSP) were not fully met.

This Remuneration Report for 2012 illustrates clearly the linkage between business performance and pay.

The Committee is satisfied that there is strong alignment between Company performance and remuneration of the Executive Directors.

Appointment of new Executive Directors to the Board

In March 2012 the Board appointed Mr Anderson and Mr Whalen as Executive Directors. In light of their appointment to the Board, the Committee reviewed their remuneration packages on appointment to ensure they were aligned with our remuneration policy.

Review of Executive Directors' service agreements

We undertook a review of the service agreements during 2012 and have now agreed consistent terms with all the Executive Directors. Where a payment is made in lieu of notice on termination, the payment of a sum in respect of lost future bonus opportunity is now subject to the Committee's discretion to reduce the amount to reflect unsatisfactory performance. In addition, the Committee will have the power to exercise discretion to reduce or waive the payment of an accrued bonus on termination if an individual's performance is unsatisfactory ensuring that no payments made to a departing Executive Director could be classified as a 'payment for failure'. Finally, any accrued bonus or payment in respect of lost future bonus paid on termination will be subject to clawback. Full details are set out on page 65 of this Annual Report.

Looking forward

For many years, we have sought to ensure a strong link between the Company's strategy, the performance delivered, the creation of long-term shareholder value and the level of remuneration received by the Executive Directors. We intend to continue with a remuneration policy that rewards fairly, recognises achievements and maintains the ability of the Group to recruit and retain the best talent in the interests of all our shareholders.

Gareth Bullock
Chairman, Remuneration Committee

2. Our remuneration policy

"Our strategy is to enhance value to shareholders through consistent growth in earnings and dividends per share."

The Company's remuneration policy is designed to:

- Provide a strong alignment between the achievement of strategic objectives and the delivery of value to shareholders
- Ensure that Executive Directors' remuneration packages allow the Group to attract and retain Executive Directors of the calibre required to meet the Group's strategic objectives both in the long and the short-term
- Provide material performance-related rewards through the use of the Annual Bonus Plan and the Company's PSP
- Ensure a significant percentage of the package remains 'at risk'. The Annual Bonus Plan rewards achievement against challenging profit and Return on Capital Employed (ROCE) targets for the year and awards under the Company's PSP only vest against challenging relative Total Shareholder Return (TSR) and Earnings Per Share (EPS) targets over a three-year period.

  The Committee considers that payout at maximum levels under these Plans will be as a result of significant outperformance by the business, with substantial levels of return for investors.

The Committee believes that the current remuneration structure is well aligned to the remuneration policy and Company strategy.

The metrics that we have incorporated into both the short and long-term incentive plans are guided by the Company's KPIs below.

The Annual Bonus Plan, PSP and Employee Share Ownership Plan (ESOP) (Incentive Plans) reward financial performance, both absolute and relative, to ensure that there is clear and demonstrable pay for performance, which we seek to illustrate in the balance of the Remuneration Report.

In developing and reviewing the Company's remuneration policy for Executive Directors and other senior executives, the Committee is sensitive to the views of shareholders and to the relationship between the arrangements for Executive Directors and those of other employee groups.

The Committee will:

- Seek the views of investors. It is as a result of this feedback that the Committee has amended Executive Directors' service agreements during 2012 and sought to improve the clarity of our remuneration reporting
- Consider the general base salary increase for the broader UK employee population when determining the annual salary increase for the Executive Directors.

The Committee also determines the principles and policy of remuneration which shall apply to the Group's senior managers. The responsibility for determining the precise compensation package to meet local practice and performance lies with the Group Chief Executive and the responsible Executive Director.

Aligning remuneration with KPIs

Profitability	Group operating profit (annual)
Strong returns	ROCE (annual)
Strong comparative share performance	Relative TSR (long-term)
Profit growth	EPS growth (long-term)

2.1 2013 Remuneration policy

The tables below summarise our remuneration policy with effect from 1st January 2013. This is unchanged from 2012, apart from where noted.

2.1.1 Fixed elements of remuneration

Element and purpose	Operation	Change from 2012
Executive Directors		
Base salary To attract, retain and motivate high calibre executives	Reviewed annually by the Committee. Reviews take account of Company and individual performance, changes in responsibility and levels of increase for the broader UK employee population. Reference is also made to median levels within our comparator group[1]. The Committee considers the impact of any base salary increase on the total remuneration package.	An average 2.3% increase for all Executive Directors in 2013. Base salaries effective 1st January 2013: M.E. Vernon: £500,000 (2.0%) D.J. Meredith: £307,000 (3.0%) N.H. Daws: £280,000 (2.2%) N.J. Anderson: £266,000 (2.3%) J.L. Whalen: $394,000 (2.1%) This is similar to the average increase for the broader UK employee population of some 2% and takes into consideration the other factors noted.
Benefits To provide market competitive benefits	The Company provides: • Company car and associated running costs or cash allowance in lieu • Life assurance • Disability insurance • Private health insurance • Telecommunications equipment • Tax treaty adjustment[2] (not tax equalisation) • Reimbursement of reasonably incurred expenses (including those linked to relocation and repatriation).	No change
Pension[3] To offer market competitive levels and to aid retention of executives	The Company provides: • M.E. Vernon and J.L. Whalen (US nationals) Total benefit of 25% of base salary comprising - Participation in US defined benefit plan, at the time of participation - Balance paid in cash on pro-rated pension, at the time of payment • D.J. Meredith and N.H. Daws - Participation in the UK defined benefit pension scheme - Cash alternative of 25% of base salary offered • N.J. Anderson - Total benefit of 25% of base salary comprising contribution to a private pension plan or cash alternative.	No change
Chairman and Non-Executive Directors		
Fees To attract and retain high calibre individuals by offering market competitive fee levels	The Chairman is paid a single fee for all of his responsibilities. The Non-Executive Directors are paid a basic fee. The chairmen of the main Board Committees and the Senior Independent Director are paid an additional fee to reflect their extra responsibilities. The Company reimburses reasonably incurred expenses. Fees for the Non-Executive Directors are reviewed every year by the Board, with reference to UK market levels. The Chairman's fee is reviewed every year by the Board, with reference to UK market levels.	The Chairman's fee has been increased by 2.1% and the Non-Executive Directors' base fee by 2.3% in 2013. Fees effective 1st January 2013: *Basic fees* Chairman: £143,000 Non-Executive Directors' base fee: £44,500 *Additional fees* Senior Independent Director: £2,000 Audit/Remuneration Committee Chairmen: £8,500

[1] The pay benchmarking comparator group comprises companies that the Committee has identified as relevant comparators given the nature of their business, size and geographic exposure. The constituents will change from time-to-time but will remain subject to the same selection criteria.

In respect of the 2013 review, the comparator group comprised 16 companies, namely: Bodycote, Chemring, Cookson, Fenner, Halma, IMI, Laird, Meggitt, Melrose, Morgan Crucible, Renishaw, Rotork, Senior, Spectris, Ultra Electronics and Weir Group. Against this comparator group, the Company is positioned between median and upper quartile with respect to market capitalisation, and between lower and median quartile with respect to revenue. The same comparator group is used to assess the market competitiveness of annual bonus and long-term incentive opportunity.

[2] Mr Vernon pays UK taxes under his service agreement. While in transition between his US and UK home locations Mr Whalen is liable for appropriate tax payments in both the US and the UK. The Company reimburses these Directors only for any additional double tax they might be liable for as a result of being subject to US and UK tax. This corresponds to the US tax payable for days worked in the US where these Directors suffer double taxation. Over the last five years these amounts in respect of Mr Vernon have never exceeded $40,000. Mr Whalen has not incurred any double taxation and therefore no payments have been made to Mr Whalen under this arrangement to 31st December 2012.

[3] Further information regarding pension can be found on pages 69 and 70 of this Remuneration Report.

2.1.2 Variable elements of remuneration

Element and purpose	Operation	Change from 2012
Executive Directors		
Annual Bonus To incentivise and reward for delivery of the Group's and Divisional financial performance	Executive Directors participate in the Annual Bonus Plan. Targets are reviewed annually to ensure continuing alignment with strategy. Bonus levels are determined following year-end by the Committee based on performance against targets. Bonus is payable entirely in cash. **Levels** Maximum: 100%, Target: 60% **Performance** Bonus is based entirely on the achievement of challenging financial objectives, which have been chosen as they are clearly aligned with our strategy. *Group roles* Group Operating Profit (65%) + Group ROCE (35%) *Divisional roles – Steam specialties* Group Operating Profit (35%) + Group ROCE (35%) + Divisional Operating Profit (30%) *Divisional role – Watson-Marlow* Group Operating Profit (15%) + Group ROCE (35%) + Divisional Operating Profit (50%) The above metrics are adjusted to reflect certain non-operating items including the amortisation of acquisition-related intangible assets and exceptional reorganisation costs, and to reflect the inclusion of our Associate company in India. Bonus is subject to clawback for up to three years following payment at the discretion of the Committee. Circumstances might include financial misstatement, erroneous calculations determining bonus payments or gross misconduct.	No change has been made to the performance metrics or their respective weightings.
Performance Share Plan To incentivise and reward for delivery of the Group's performance over the long-term and to provide alignment with shareholders' interests	The Committee makes an annual conditional award of shares to each Executive Director. Prior to award, the Committee reviews the performance targets for each measure to ensure they remain sufficiently stretching. For financial measures this includes a review of analysts' forecasts. **Levels** 100% of salary **Performance** Vesting is based on two performance measures, which have been chosen as they are clearly aligned with our strategy: 60% TSR performance relative to a comparator group 40% aggregate EPS relative to target aggregate EPS Performance is measured over a three-year period. Clawback provisions apply for awards made from 2012.	No change has been made to the performance metrics or their respective weightings. The EPS performance range will be reviewed ahead of awards being made in 2013 and disclosed next year.
Employee Share Ownership Plan To offer all eligible UK-based employees the opportunity to build a shareholding in a tax-efficient way	UK-based Executive Directors (excluding Mr Vernon and Mr Whalen) are eligible to participate in the ESOP (an HMRC approved Share Incentive Plan) **Levels** Maximum annual investment: £1,500 Potential for up to a 1:1 matching award from the Company and dividend shares (can be reinvested)	No change

2.1.3 Other elements of our remuneration policy

In addition, the Company has guidelines for Executive Directors with respect to share ownership requirements and external directorships.

- Following appointment to the Board, Executive Directors are expected to accumulate a shareholding worth 100% of salary in the Company. It is expected that on vesting all PSP shares (net of tax) will be retained until the required shareholding is achieved and that this level of shareholding should be retained for the duration of the appointment. The Committee can exercise discretion in implementing this policy where personal circumstances make it appropriate to do so. For details of Directors' shareholdings please see pages 73 and 74 of this Remuneration Report.
- Directors are permitted to hold external directorships. None of the Executive Directors hold a directorship on a FTSE 100 company. In line with this policy, Mr Vernon served as a Non-Executive Director at Senior plc during the year, for which he received and retained total fees of £39,240. On 25th February 2013 Mr Vernon became a Non-Executive Director of Liqtech International, Inc.

When appointing external hires into executive roles, the Committee will continue to act in the best interests of shareholders when determining remuneration, in line with the stated policy.

2.2 Total remuneration opportunity

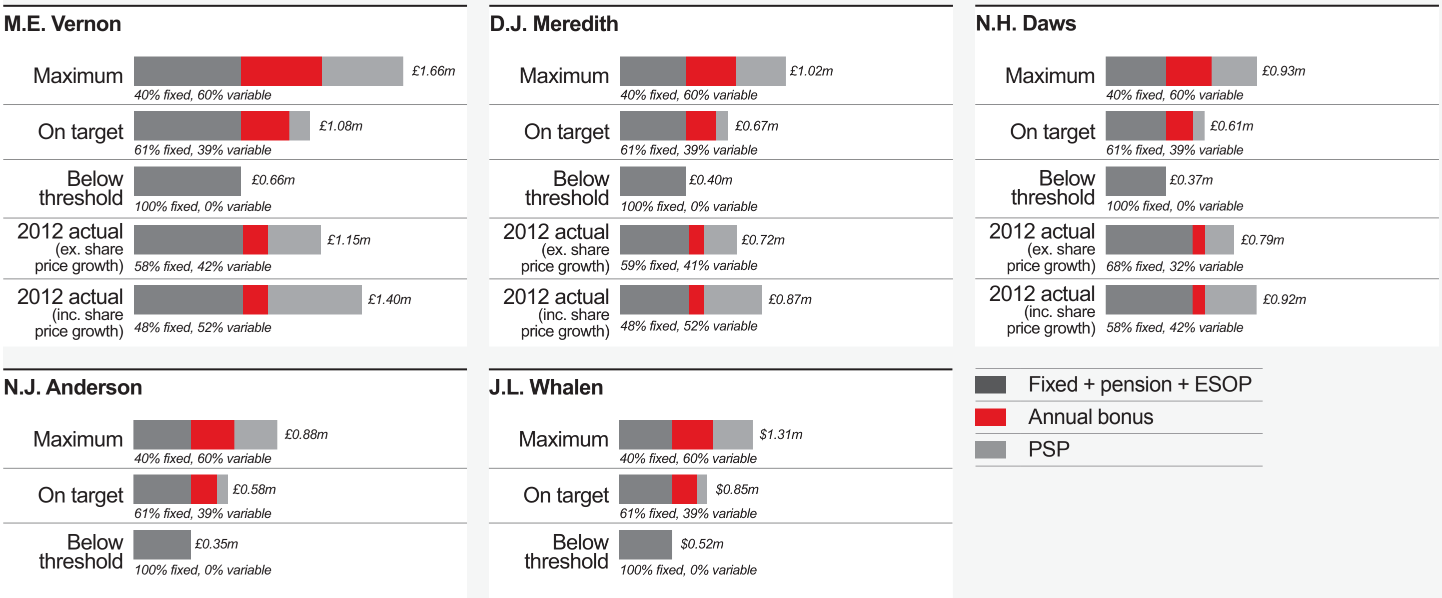
Under the remuneration policy, a significant portion of remuneration is variable and depends on the Company's performance. Below we illustrate how the total pay opportunity for the Executive Directors varies under three performance scenarios: maximum, 'on target', and below threshold. In addition, for the three Executive Directors who served for the full 12 months of the 2012 financial year, the charts below show a comparison of forward looking policy with the actual remuneration for 2012 including and excluding share price appreciation in respect of the PSP element. Participants do not accrue dividends over the performance period.

The scenarios are defined as follows:

Element	Forward looking policy			2012 actual
	Below threshold	On target	Maximum	
Fixed pay, benefits and ESOP	Fixed pay and ESOP does not vary with performance and comprises: • 2013 base salary • Benefits, assumed to be worth 6.5% of salary • Pension, assumed to be worth 25% of salary • ESOP participation of £1,500 for eligible Executive Directors			Details of 2012 fixed pay and participation in the ESOP can be found on page 71
Annual bonus (% of salary)	0%	60%	100%	28% to 36% of salary in 2012 (see page 67)
Performance Share Plan[1] (% of salary at award)	0%	25%	100%	74.6% of awards granted in 2010 vest (see page 68) The impact of share price appreciation on vesting awards is set out in the graphs.

[1] A level of 25% vesting for 'on target' performance is equivalent to threshold performance under the PSP, which the Committee believes to be a fair assumption for 'on target' performance adopting the Financial Reporting Council's recommendations set out in their March 2013 publication 'Lab project report: Reporting of pay and performance'.

In section 3 of this report we set out further details of pay in respect of 2012.



2.3 Directors' service agreements and termination

2.3.1 Executive Directors

As noted in the Committee Chairman's opening letter, in 2012 Executive Directors' service agreements were reviewed and brought into line with best practice following feedback from our shareholders. On signing the revised service agreements, there were no payments made, nor were there changes to any other aspects of the Executive Directors' pay to compensate for the lost rights. The changes were as follows:

- Where a payment is made in lieu of notice on termination, the payment of a sum in respect of lost future bonus opportunity (based on an average of the preceding three years' bonus payments) is now subject to the Company's discretion to reduce the amount to reflect performance on the part of the Executive Director which is considered by the Committee to be unsatisfactory. Bonus payments, if any, will only be made at the discretion of the Committee after taking into account individual performance in order to ensure that there will be no 'payments for failure'. In any event, any payments will also be subject to the clawback provisions in the rules.
- Save as set out in the table below, the Company has discretion to make the termination payments in instalments and such instalments will be reduced to take account of required mitigation by the Executive Director.

While the Executive Directors' service agreements continue to include a provision to deal with termination on a change of control, in the event of an offer being made, shareholders have discretion to accept the offer or not. The decision to recommend acceptance, or not, is a matter for the Board of Directors and the Committee is of the clear view that the change of control provision within the Executive Directors' service agreements would have no influence on the voting pattern of those Directors.

The service agreements for all Executive Directors can be terminated at 12 months' notice by either party. The table below sets out key provisions relating to termination of employment from the Executive Directors' service agreements and from the incentive plan rules. It also sets out key provisions relating to change of control. Executive Directors' service agreements may be terminated without notice and without payment of compensation on the occurrence of certain events, such as termination for gross misconduct.

Service agreement and incentive plan provisions relating to termination	
Salary and benefits	• Appointments can be terminated with immediate effect and, in lieu of the unexpired notice period, the Company can make a series of monthly payments in respect of salary, benefits and pension provision (or at the Company's discretion, a lump sum). Any monthly payments would be reduced to take account of amounts received from alternative employment, in line with the mitigation provisions. • In addition, on termination Mr Vernon and Mr Whalen are entitled to relocation expenses in accordance with Company policy.
Annual bonus	• There is no automatic entitlement to accrued bonus on termination. The Committee will exercise their discretion to determine whether any bonus is payable, taking into account individual performance. No payment will be made in circumstances that amount to a 'payment for failure'. • Amounts payable are subject to clawback provisions in the rules.
Performance Share Plan	• If an Executive Director ceases to be employed before the end of the three-year performance period, the relevant awards lapse except as noted below: - Awards made within six months of employment ceasing will always lapse. - Where employment terminates due to death, disability, retirement or redundancy, each relevant award of shares vests subject to the performance condition measured at the earliest practicable date, pro-rated based on the time served during the performance period. When notice is issued by the Company and is not for cause, the Committee applies the approach as described above, but has discretion to reduce the number of shares vesting to zero. • Amounts payable are subject to clawback provisions in the rules.
Employee Share Ownership Plan	• All appropriate shares shall be transferred as soon as practicable following cessation of employment.
Service agreement and incentive plan provisions relating to change in control	
Salary and benefits	• In the event of termination following a change in control, the amount due (as described above) is payable in one lump sum.
Annual bonus	• Termination within 12 months following a change in control will result in the payment of a lump sum equal to the average of the last three years' annual bonus (or a shorter period if service as an Executive Director is less than three years).
Performance Share Plan	• Following a change in control, each relevant award of shares vests subject to the performance condition measured at the earliest practicable date, pro-rated based on the time served during the performance period.
Employee Share Ownership Plan	• All shares shall be transferred as soon as practicable following a change in control.

2.3.2 Chairman and Non-Executive Directors

The Chairman and Non-Executive Directors have letters of appointment with the Company for an initial period of three years, subject to annual re-election at the AGM. Appointments may be terminated by the Company or individual with one month's notice. The appointment letters for the Chairman and Non-Executive Directors provide that no compensation is payable on termination, other than accrued fees and expenses.

2.3.3 Directors' terms of service
The tables below set out the dates on which each Director was initially appointed, their latest service agreement or letter of appointment and their notice period. All Directors are subject to election (if newly appointed in the year) or re-election at the next AGM.

Directors' service agreements and letters of appointment

	Appointment date	Agreement	Notice period
Executive Directors			
M.E. Vernon	01.07.06	09.05.12	12 months
D.J. Meredith	19.06.92	17.08.12	12 months
N.H. Daws	01.06.03	25.09.12	12 months
N.J. Anderson	15.03.12	08.05.12	12 months
J.L. Whalen	15.03.12	17.04.12	12 months

	Appointment date	Letter	Notice period
Chairman and Non-Executive Directors			
W.H. Whiteley	26.07.02	15.05.12	1 month
G.R. Bullock	02.05.05	15.05.12	1 month
K. Rajagopal	10.02.09	15.12.11	1 month
G.E. Schoolenberg	01.08.12	12.07.12	1 month
C.G. Watson	17.07.09	15.05.12	1 month

3. Director remuneration in 2012

3.1 Base salary and fees
The following table sets out the 2012 base salary for each of the Executive Directors.

	2012	2011	Increase
M.E. Vernon	£490,000	£470,000	4.3%
D.J. Meredith	£298,000	£287,000	3.8%
N.H. Daws	£274,000	£250,000	9.6%
N.J. Anderson	£260,000	N/A	–
J.L. Whalen	$386,000	N/A	–

The increases for Mr Vernon and Mr Meredith were similar to the average increase for UK employees for 2012 and also took into account market positioning, Company and individual performance and returns to shareholders over the period.

Mr Daws' salary was reviewed with effect from 2012 to take into account the changes to his role effective in October 2011 when he became responsible for the UK and French Supply operations, in addition to the Asia Pacific steam specialties business. While he relinquished responsibility for the Latin American steam specialties business, overall his role increased substantially and the Committee are of the view that his revised salary is appropriate for this increased scope of his role.

Mr Anderson's and Mr Whalen's salaries were set on appointment to the Board.

The following table sets out the 2012 fees for the Chairman and Non-Executive Directors. Pay for the Chairman and Non-Executive Directors does not vary with performance.

	Basic fees	Additional fees	Total fees
W.H. Whiteley	£140,000	£0	£140,000
G.R. Bullock[1]	£43,500	£10,500	£54,000
K. Rajagopal	£43,500	£0	£43,500
G.E. Schoolenberg[2]	£43,500	£0	£18,125
C.G. Watson[1]	£43,500	£8,500	£52,000

[1] Mr Bullock received £2,000 in respect of his duties as Senior Independent Director and £8,500 in respect of his role as Chairman of the Remuneration Committee. Mr Watson received £8,500 in respect of his role as Chairman of the Audit Committee.

[2] Dr Schoolenberg was appointed to the Board on 1st August 2012 and therefore her total fee is pro-rated.

3.2 Annual bonus

The annual bonus plan rewards Executive Directors for financial performance both at Group level and, where appropriate, for the Division for which they are responsible.

	2012 measures
M.E. Vernon D.J. Meredith	Group operating profit (65%) Group ROCE (35%)
N.H. Daws N.J. Anderson	Group operating profit (35%) Group ROCE (35%) Divisional operating profit (30%)
J.L. Whalen	Group operating profit (15%) Group ROCE (35%) Divisional operating profit (50%)

Achievement of target performance results in a bonus of 60% of salary, increasing to 100% of salary for maximum performance.

In spite of challenging times, 2012 was a good year for the Group which delivered earnings growth, maintained a strong operating profit margin and increased dividends to shareholders. Nonetheless, the annual bonus payments to Executive Directors were below target.

This reflects the stretching targets that the Committee determines each year for the Executive Directors, in order to incentivise above target performance. The table below summarises the achieved performance in 2012 in respect of each of the measures used in the determination of annual bonus, together with an indication of actual performance relative to target.

Performance assessment in 2012

	Actual performance[1]	Below threshold	Below target	Target	Above target	Maximum
Group operating profit	£138m		✓			
Group ROCE	39.3%		✓			
Asia Pacific and Supply operating profit	£51m		✓			
EMEA operating profit	£38m		✓			
Watson-Marlow operating profit	£39m		✓			

[1] These metrics use actual results adjusted to reflect certain non-operating items and the inclusion of our Associate company in India to comply with the bonus plan rules.

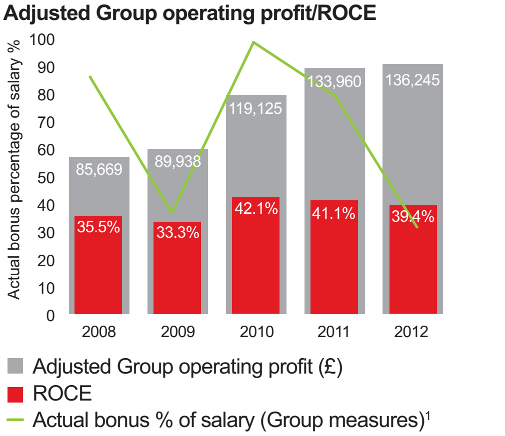
As a result of this performance in 2012, the following bonuses were achieved:

	Bonus achieved	Bonus (% of salary)
M.E. Vernon	£155,280	31.69%
D.J. Meredith	£94,436	31.69%
N.H. Daws	£76,939	28.08%
N.J. Anderson[1]	£61,573	29.77%
J.L. Whalen[1]	$111,125	36.19%

[1] Pro-rated for appointment on 15th March 2012.

The following graph provides a five-year summary of bonus outcomes against the performance of Group operating profit and ROCE. This illustrates the strong historical alignment between pay and performance.

Adjusted Group operating profit/ROCE



[1] Calculated in accordance with the metrics in 2.1.2 on page 63.

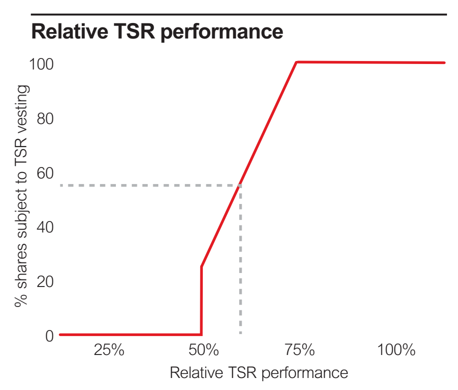
3.3 Performance Share Plan

3.3.1 Awards vesting for 2010 – 2012

In 2010 the Executive Directors received share awards under the Performance Share Plan, with vesting subject to EPS growth and relative TSR performance. The diagrams below set out details of the performance tests that applied, along with the actual performance during the period 1st January 2010 to 31st December 2012.

Relative TSR performance (60% of award)

Over the three-year period to 31st December 2012, the Company delivered a total shareholder return of 104.7%. This ranked at the 61st percentile relative to the comparator group.

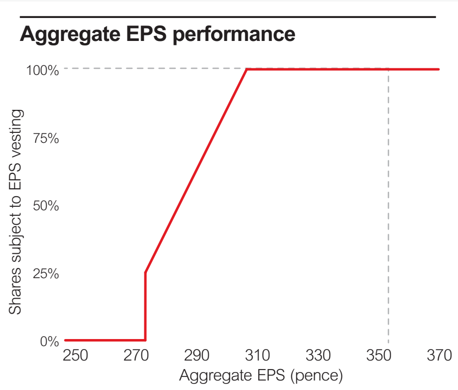


	Performance	Payout
Threshold	Median	25%
Maximum	Upper quartile	100%
Actual	61st percentile	58%

The comparator group for the purpose of measuring relative TSR performance comprises 26 similar companies, namely: BAE Systems, Bodycote, Charter International, Chemring Group, Chloride Group, Cobham, Cookson Group, Domino Printing Services, Fenner, Halma, IMI, Laird, Meggitt, Melrose, Morgan Crucible, Qinetiq, Renishaw, Rexam, Rolls-Royce, Rotork, Smith (DS), Smiths, Spectris, Tomkins, Ultra Electronics and Weir.

Aggregate EPS performance (40% of award)

Over the three-year period to 31st December 2012, the Company delivered aggregate adjusted EPS of 357.2p. Adjusted EPS was 82.2p in 2009 and so this equated to growth of approximately 20.1% per annum over the three years.



	Performance	Payout
Threshold	272.1p	25%
Maximum	304.9p	100%
Actual	357.2p	100%

EPS is derived from the audited Annual Report for the relevant financial year but adjusted to exclude any non-operating items shown separately on the face of the Company's profit and loss account.

Awards vesting for 2010-2012

In respect of the 2010 awards, actual performance for the combined relative TSR and aggregate EPS resulted in 74.6% of shares vesting.

	Award	Vesting[1]	Lapsed	Value on vesting
M.E. Vernon	31,332	23,362	7,970	£577,742
D.J. Meredith	19,472	14,519	4,953	£359,055
N.H. Daws	17,086	12,740	4,346	£315,060
N.J. Anderson	N/A	N/A	N/A	N/A
J.L. Whalen	N/A	N/A	N/A	N/A

[1] Awarded in the form of nil cost options.

3.3.2 Awards made for 2012 – 2014

Executive Directors were awarded the following number of shares on 9th March 2012. Face values are shown as a percentage of salary, based on the share price at date of award (2106.0p). Performance will be measured following completion of the three-year performance period on 31st December 2014, which will determine the percentage of awards vesting.

	Shares awarded	Face value (% of salary)
M.E. Vernon	23,029	100%
D.J. Meredith	14,055	100%
N.H. Daws	13,058	100%
N.J. Anderson[1]	11,633	100%
J.L. Whalen[1]	5,983	60%

[1] Prior to appointment to the Board.

In respect of awards made to Executive Directors under the Performance Share Plan in 2012, vesting is dependent on TSR and EPS as follows:

Relative TSR performance (60% of award)

	Performance	Payout
Threshold	Median	25%
Maximum	Upper quartile	100%

The comparator group for the purpose of measuring relative TSR performance comprises 25 similar companies based on the same selection criteria as previous awards. Since 2010 Charter International, Chloride, Laird and Tomkins have been removed and Oxford Instruments, RPC and Senior have been added.

Aggregate EPS performance (40% of award)

	Performance	Payout
Threshold	RPI +3% CAGR	25%
Maximum	RPI +9% CAGR	100%

EPS is as defined in previous years.

The same performance metrics will apply for awards to be made in 2013.

3.4 Employee Share Ownership Plan (ESOP)

All eligible Executive Directors participated in the ESOP during the year. Mr Anderson joined the Group in September 2011 and under the rules of the ESOP was only eligable to participate with effect from 1st October 2012.

No employee's entitlement under the ESOP is subject to performance conditions as the aim of the ESOP is to encourage increased shareholding in the Company by all eligible UK employees.

3.5 Pension

The following information is consistent with the presentation used last year and sets out the disclosures under the UKLA Listing Rules and the Companies Act 2006.

Mr Meredith and Mr Daws are members of an HM Revenue & Customs (HMRC) registered, contributory defined benefit pension scheme based on 1/60th of pensionable salary for each year of pensionable service to 31st March 2011. With effect from 1st April 2011 they elected to build up benefits at a lower rate of 1/80th accrual without having to make contributions. They accrue pro-rata additional service at a rate which gives a further two and a half years of service at age 62½. At retirement they are entitled to commute a proportion of their pension for a tax free cash lump sum payment within HMRC limits. They may retire on an actuarially reduced pension on early retirement with the Company's consent, provided they have attained age 55, or are retiring on ill-health grounds at an earlier age. No consent is required for retirement on or after age 60 and no early retirement reduction is applied to the scale pension on retirement at or after age 60.

Details of Mr Meredith's and Mr Daws' pensions are set out in the table below.

	Age attained at 31.12.12	Old pensionable salary	New pensionable salary	Accrued pension at 31.12.11 £pa	Accrued pension at 31.12.12 £pa	Change in accrued pension during the year £pa	Change in accrued pension during the year[1] £pa	Transfer value of change in accrued pension[1] £	Transfer value of accrued pension at 31.12.11 £	Transfer value of accrued pension at 31.12.12 £	Change in total transfer value £
D.J. Meredith	53	287,000	298,000	131,204	140,434	9,230	5,174	88,000	2,284,000	2,342,000	58,000
N.H. Daws	50	250,000	274,000	122,365	138,165	15,800	12,018	181,000	1,853,000	2,010,000	157,000

[1] Net of inflation at a rate of 3.1% per annum.

The following additional information supplements this:

- Dependant's pension: on death-in-service, a spouse's pension equal to one-half of pension, based on pensionable service to the date of death, is payable. On death after payment of the pension commences, a spouse's pension of one-half of pension entitlement at the date of death, ignoring commutation and any early retirement actuarial reduction, is payable. In addition Mr Meredith's and Mr Daws' pensions are guaranteed to be paid for five years from retirement.
- Early retirement rights: after leaving the service of the Company, there is the right to draw the accrued pension at any time after age 60 with no reduction.
- Pension increases: pensions are subject to annual increases in line with the annual rise in the RPI subject to a maximum of 5% per annum. The Trustees and the Company have the discretion to apply a greater increase.
- Other discretionary benefits: there are no discretionary practices which are taken into account in calculating transfer values on leaving service.

Mr Vernon and Mr Whalen are members of the Spirax Sarco Inc. defined benefit plan. The benefit paid under normal retirement from the US defined benefit plan is a single life annuity equal to the number of years of service multiplied by the sum of 1.0% of pensionable salary up to social security covered compensation, plus 1.45% of pensionable salary in excess of social security covered compensation. Final average salary is the average of the highest pensionable pay for any five consecutive years prior to retirement up to a ceiling. Both Mr Vernon's and Mr Whalen's final average salary is higher than the salary ceiling as at 31st December 2012.

Details of Mr Vernon's and Mr Whalen's pensions are set out in the table below.

	Age attained at 31.12.12	Accrued pension at 31.12.11 pa	Accrued pension at 31.12.12 pa	Change in accrued pension during the year pa	Change in accrued pension during the year[1] pa	Transfer value of change in accrued pension[1]	Transfer value of accrued pension at 31.12.11	Transfer value of accrued pension at 31.12.12	Change in total transfer value
M.E. Vernon	59	£17,282	£18,791	£1,509	£1,165	£11,032	£140,315	£177,943	£37,628
J.L. Whalen	56	$64,105[2]	$67,972	$3,867	$2,849	$22,450	$487,080[2]	$535,605	$48,525

[1] Net of inflation at a rate of 2.0% per annum.

[2] Mr Whalen was appointed to the Board on 15th March 2012; therefore accrued pension and transfer value at start of year are actual values as at 15th March 2012 and not 31st December 2011.

The following additional information supplements this:

- Dependant's pension: on death-in-service, a spouse's pension equal to one-half of pension, based on pensionable service to the date of death, is payable. After payment of the pension commences the accrued pension shown has no attaching spouse's pension. However at retirement there is the option to reduce their own pension to provide for a spouse's pension after death.
- Early retirement rights: after leaving the service of the Company, there is the right to draw their accrued pension at any time after age 65 with no reduction. There is the right to commence their pension earlier if they meet the age and service requirements, with the pension being reduced. The annual reductions for early retirement are 3% for each year from age 65 to age 60 and 5% for each year from age 60 to earliest retirement age.
- Pension increases: the pension has no guaranteed increases. Spirax Sarco Inc. has the discretion to provide increases.
- Other discretionary benefits: Mr Vernon benefited from an amount in lieu of contributions to a UK defined contributions pension scheme. The total amount paid by the Group was £112,344. Mr Whalen benefited from Company contributions to a US defined contribution pension plan and to a 401k plan totalling $28,675.

Mr Anderson received contributions to a private pension plan or cash alternative: aggregate of 25% of base salary.

The following pension payments were made during the year:

	Pension payments
M.E. Vernon	£112,344
N.J. Anderson	£51,707
J.L. Whalen	$28,675

A lump sum death-in-service benefit of four-times pensionable salary is provided for all Executive Directors.

3.6 Total remuneration

3.6.1 2012 Total remuneration for Directors

The following table sets out details of the Directors' emoluments and complies with the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008. No Directors have waived, or agreed to waive in future, any emoluments.

	Base salary/fees[1]	Benefits[2]	Annual bonus[3]	Total emoluments (excluding pension) 2012	Total emoluments (excluding pension) 2011	Pension[4]	PSP 2010- 2012[5]	ESOP	Single figure[6] 2012	Single figure[6] 2011
M.E. Vernon	£490,000	£44,002	£155,280	£689,282	£848,235	£135,644	£577,742	N/A	£1,402,668	£1,504,195
D.J. Meredith	£298,000	£18,981	£94,436	£411,417	£524,179	£103,480	£359,055	£1,500	£875,452	£997,265
N.H. Daws	£274,000	£17,298	£76,939	£368,237	£437,333	£240,360	£315,060	£1,500	£925,157	£850,390
N.J. Anderson[7]	£206,829	£9,950	£61,573	£278,352	N/A	£51,707	N/A	£375	£330,434	N/A
J.L. Whalen[7,8]	$307,061	$32,677	$111,125	$450,863	N/A	$85,655	N/A	N/A	$536,518	N/A
W.H. Whiteley	£140,000	N/A	N/A	£140,000	£140,000	N/A	N/A	N/A	£140,000	£140,000
G.R. Bullock	£54,000	N/A	N/A	£54,000	£54,000	N/A	N/A	N/A	£54,000	£54,000
K. Rajagopal	£43,500	N/A	N/A	£43,500	£43,500	N/A	N/A	N/A	£43,500	£43,500
G.E. Schoolenberg[7]	£18,125	N/A	N/A	£18,125	N/A	N/A	N/A	N/A	£18,125	N/A
C.G. Watson	£52,000	N/A	N/A	£52,000	£52,000	N/A	N/A	N/A	£52,000	£52,000

[1] Base salary earned during the financial year ending 31st December 2012.

[2] Benefits include private health insurance, provision of telecommunications equipment, provision of a Company car or cash allowance in lieu of a Company car and, for Mr Vernon, a payment relating to the tax treaty adjustment (not tax equalisation – see page 62).

[3] Annual bonus cash element awarded in relation to the financial year ending 31st December 2012. Mr Vernon and Mr Meredith received 31.69% of base salary. Mr Daws and Mr Anderson received 28.08% and 29.77% of base salary respectively. Mr Whalen received 36.19% of base salary.

[4] Mr Vernon receives an amount in lieu of contributions to a UK defined contributions pension scheme. Mr Vernon and Mr Whalen are both members of the Spirax Sarco Inc. defined benefit plan. Mr Meredith and Mr Daws are both members of a UK defined benefit pension scheme. Mr Anderson receives contributions to a private pension plan or cash alternative: aggregate of 25% of base salary. When including the value of defined benefit pensions, a multiplier of 20 has been applied to the change in accrued pension during the year, net of inflation.

[5] The awards for Mr Vernon, Mr Meredith and Mr Daws vested on 5th March 2013. The share price at date of vesting was 2473.0p. The performance period was 1st January 2010 to 31st December 2012, which falls within the financial year. Overall, 74.6% of the shares vested with the balance lapsing.

[6] This is the sum of base salary, benefits, annual bonus, pension, PSP and ESOP.

[7] Mr Anderson and Mr Whalen were appointed to the Board on 15th March 2012. Dr Schoolenberg was appointed to the Board on 1st August 2012. Remuneration in the above table is calculated from these dates.

[8] Mr Whalen is a US resident who works in the US and the UK. He is paid in US dollars.

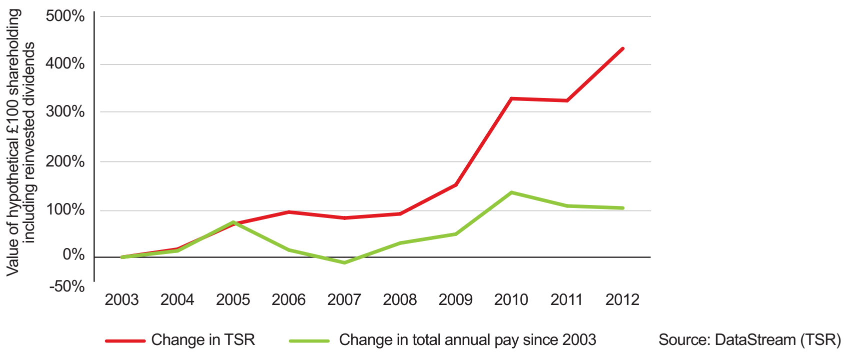
3.6.2 Historical ten-year TSR performance relative to the Group Chief Executive's single figure remuneration

The graph below compares the single figure remuneration of the Group Chief Executives of the Company over the last ten years, relative to the returns delivered to shareholders.

For the purpose of calculating the value of remuneration of the Group Chief Executive, data has been collated on a basis consistent with the 'single figure methodology' as currently defined by the Department for Business, Innovation & Skills (it also aligns with the data presented in section 3.6.1 above). In respect of 2008, when Mr Vernon succeeded Mr Steel, the part-year remuneration for each individual has been added together. Total Shareholder Return (TSR) is the change in value of a hypothetical £100 holding from 2003, based on one-month trading day averages in respect of each year.

As this analysis shows, total remuneration has been well aligned over the last ten years and the rate of increase of returns to shareholders has significantly outpaced growth in remuneration.

10 year historical TSR performance relative to change in Group Chief Executive's single figure remuneration (see 3.6.1) since 2003 %

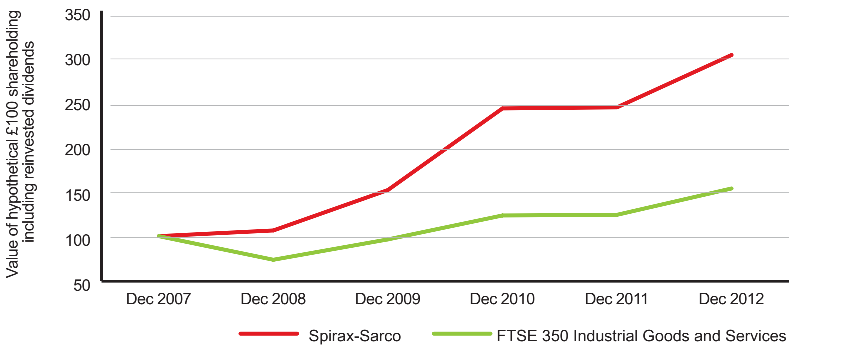


Source: DataStream (TSR)

3.7 TSR performance graph

The adjacent graph demonstrates the growth in value of a £100 investment in the Company to the FTSE 350 Industrial Goods and Services Supersector over the last five years. This comparison is chosen as it is the Supersector within which the Company is classified and it is a broad equity market index including companies of a similar size, complexity and sector.

Historical five-year TSR performance



Source: DataStream

3.8 Distribution statement

The table below demonstrates the relative importance of total remuneration spend relative to total employee numbers, profit before tax and dividends payable in respect of the year.

	2012	2011	Change
Total pay spend	£228m	£220m	3.6%
Headcount	4,706	4,683	0.5%
Profit before tax	£128m	£132m	-3.5%
Dividends payable	£41m	£38m	8.7%
Special dividend payable	£78m	–	–

4. Outstanding share interests

4.1 Summary of awards outstanding

4.1.1 Spirax-Sarco Engineering plc Share Option Schemes

The interests of Executive Directors are set out below. No options were granted to Executive Directors during the year and no options held by Executive Directors lapsed during the year.

The options granted to Mr Whalen were made before his appointment to the Board. The performance condition requires an increase in EPS of more than 9% greater than the increase in the UK RPI over the three year period from 1st January in the year the grant was made. If the condition is not met at the end of the three year period, the option will lapse. The auditor is asked to confirm whether the performance condition has been met.

There are no interests to disclose in relation to the other Executive Directors.

The mid-market price of the Ordinary shares on 31st December 2012 was 2268.0p. During the period from 1st January 2012 to 31st December 2012 the Ordinary mid-market share price ranged between 1858.0p and 2334.0p.

	Balance 01.01.12	Granted	Exercised	Lapsed	Balance 31.12.12	Option price (p)	Market price on exercise (p)	2012 Gain arising on exercise (£)	Date from which first exercisable	Expiry date
J.L. Whalen	7,500	0	7,500	0	0	1019.6	2141.0	84,105	26.03.10	26.03.17
	7,500	0	7,500	0	0	959.0	2203.0	93,300	12.03.11	12.03.18
	6,000	0	6,000	0	0	765.0	2203.0	86,280	11.03.12	11.03.19
	7,500	0	0	0	7,500	1369.0	–	–	26.03.13	26.03.20
	7,500	0	0	0	7,500	1873.0	–	–	18.03.14	18.03.21
Total	**36,000**	**0**	**21,000**	**0**	**15,000**			**263,685**		

4.1.2 Spirax-Sarco Engineering plc Performance Share Plan

The interests of Executive Directors are set out below.

	Date of award				Balance 01.01.12	Vested 06.03.12[1]	Lapsed 06.03.12[1]	Awarded 09.03.12[5, 6]	Balance 31.12.12
	11.03.09[1, 6]	26.03.10[2, 6]	18.03.11[3, 6]	01.09.11[4, 6]					
M.E. Vernon	41,176	31,332	25,093	–	97,601	24,376	16,800	23,029	79,454
D.J. Meredith	25,588	19,472	15,323	–	60,383	15,148	10,440	14,055	48,850
N.H. Daws	22,450	17,086	13,347	–	52,883	13,290	9,160	13,058	43,491
N.J. Anderson	–	–	–	8,500	8,500	–	–	11,633	20,133
J.L. Whalen	–	–	–	–	0	–	–	5,983	5,983

[1] The mid-market price of the shares on 11th March 2009 was 758.0p. 59.2% of the awards vested as the performance conditions applicable to those awards were partly met. During the performance period 1st January 2009 to 31st December 2011, the EPS performance of the Company was above the maximum target and the TSR performance ranked the Company at the 52nd percentile resulting in 32% of this element of the award vesting. The awards vested on 6th March 2012 and the mid-market price of the shares on that date was 2006.0p.

[2] The mid-market price of the shares on 26th March 2010 was 1390.0p. The period over which performance conditions are measured is 1st January 2010 to 31st December 2012. There are two performance conditions governing vesting of this award: 60% of the award is subject to a TSR test which requires the Company to rank at median relative to a comparator group of 26 companies for 25% of this portion of the award to vest, increasing to full vesting for ranking at the upper quartile; 40% of the award is subject to an EPS test which requires growth of 5% per annum for 25% of this portion of the award to vest, increasing to full vesting for growth of 11% per annum.

[3] The mid-market price of the shares on 18th March 2011 was 1860.3p. The period over which performance conditions are measured is 1st January 2011 to 31st December 2013. There are two performance conditions governing vesting of this award: 60% of the award is subject to a TSR test which requires the Company to rank at median relative to a comparator group of 25 companies for 25% of this portion of the award to vest, increasing to full vesting for ranking at the upper quartile; 40% of the award is subject to an EPS test which requires growth of RPI +3% CAGR per annum for 25% of this portion of the award to vest, increasing to full vesting for growth of RPI +9% CAGR per annum.

[4] The mid-market price of the shares on 1st September 2011 was 1845.0p. The period over which performance conditions are measured is 1st January 2011 to 31st December 2013. Details of the performance test attached to this award are set out in note 3 above.

[5] The mid-market price of the shares on 9th March 2012 was 2106.0p. This was applied in determining the number of shares subject to the awards granted on 9th March 2012. The period over which performance conditions are measured is 1st January 2012 to 31st December 2014. Details of the performance conditions attached to this award are set out on page 69 of this report.

[6] The 2010 and 2012 TSR comparator groups are set out on pages 68 and 69 of this Remuneration Report. In 2009 Fenner and Laird were not comparators, but Hampson Industries and VT Group were. In 2011 Charter International, Chloride and Tomkins were removed and Oxford Instruments, RPC and Senior were added. All other comparators are unchanged.

4.1.3 Spirax-Sarco Engineering plc Employee Share Ownership Plan (ESOP)

The interests of eligible Executive Directors are set out below.

	Balance 01.01.12	Partnership shares purchased[1]	Matching shares awarded[1]	Dividend shares awarded[2]	Balance 31.12.12	Period of qualifying conditions[3]
D.J. Meredith	5,496	81	81	73	5,731	3 years
N.H. Daws	5,496	81	81	73	5,731	3 years
N.J. Anderson	0	0	0	0	0	N/A

[1] Partnership shares were purchased, at a price of 1832p, and Matching shares were awarded on 8th October 2012. The mid-market price of the shares on that date was 2012.0p.

[2] 73 Dividend shares were awarded on 18th May 2012, on which date the mid-market price of the shares was 1982.0p. No Dividend shares were awarded on 9th November 2012.

[3] Partnership shares are not subject to qualifying conditions. No Matching shares or Dividend shares were released from the ESOP or forfeited during the year.

4.2 Total interests in shares

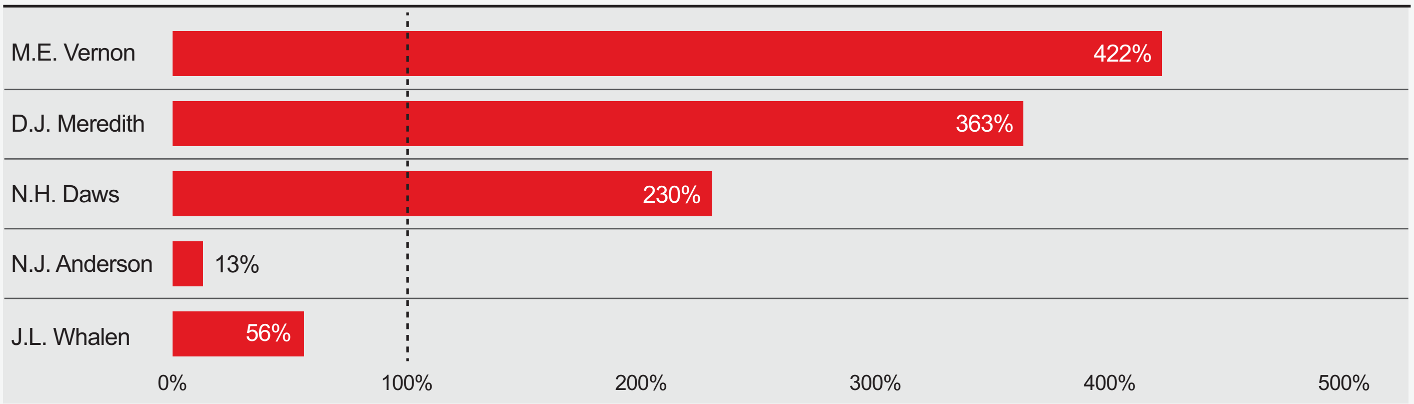
The following table summarises the total interests of the Directors in shares of Spirax-Sarco Engineering plc as at 31st December 2012 and 6th March 2013. These cover beneficial and conditional interests. No Director had any dealings in the shares of the Company between 31st December 2012 and 6th March 2013. Unexercised share options under the Global Share Option scheme are excluded but nil cost options under the PSP are included.

	Beneficial	PSP	ESOP	Conditional total	Total 31.12.12	Total 06.03.13[1]
W.H. Whiteley	11,884	N/A	N/A	N/A	11,884	11,884
M.E. Vernon	91,232	79,454	N/A	79,454	170,686	162,716
D.J. Meredith	47,647	48,850	5,731	54,581	102,228	97,275
N.H. Daws	27,772	43,491	5,731	49,222	76,994	72,648
N.J. Anderson	1,525	20,133	0	20,133	21,658	21,658
J.L. Whalen	6,000	5,983	N/A	5,983	11,983	11,983
G.R. Bullock	1,250	N/A	N/A	N/A	1,250	1,250
K. Rajagopal	2,000	N/A	N/A	N/A	2,000	2,000
G.E. Schoolenberg	1,000	N/A	N/A	N/A	1,000	1,000
C.G. Watson	2,636	N/A	N/A	N/A	2,636	2,636

[1] The reduction in shareholding at 6th March 2013 for Mr Vernon, Mr Meredith and Mr Daws is as a result of 74.6% of the 2010 PSP award vesting and the balance of the award therefore lapsing. For full details, please see page 68.

4.3 Progress towards share ownership guideline

The following chart sets out the Executive Directors' progress towards the share ownership guideline of 100% of salary. The value of the shareholding is taken at 31st December 2012 as a percentage of 2012 base salary.



Share ownership guideline is 100% of base salary

5. Operation of the Remuneration Committee in 2012

5.1 Membership and attendance

Each of the Committee members is an independent Non-Executive Director and thus brings independence to consideration of all aspects of Board remuneration and the application of professional advice to matters relating to remuneration.

The Committee is chaired by Mr Bullock, and the members comprise Dr Rajagopal, Dr Schoolenberg and Mr Watson, all of whom are independent Non-Executive Directors.

In 2012 the Committee met three times. Dr Schoolenberg attended the one meeting held following her appointment to the Committee; the remaining members attended all three meetings.

5.2 Advisors to the Committee

During 2012 the Committee sought advice and information from Mr Whiteley, the Chairman, Mr Vernon, the Group Chief Executive and Mr Richardson, the Group Human Resources Director. None of the invitees participated in any discussions regarding their own remuneration or fees. The General Counsel and Company Secretary acts as Secretary to the Committee.

In addition the Committee received external advice from Towers Watson and Herbert Smith Freehills.

- Towers Watson is appointed by the Committee and provided advice on general remuneration matters and the drafting of the 2012 Remuneration Report. Towers Watson is a signatory of the Remuneration Consultants Group Code of Conduct
- Herbert Smith Freehills is appointed by the Company and provided advice to the Committee on Executive Directors' service agreements and share plans.

5.3 Shareholder engagement

At the AGM in 2012, the advisory vote on the 2011 Directors' Remuneration Report received 68.5% votes in favour. The key issues that were raised related to provisions in the Executive Directors' service agreements and the quality of disclosure with respect to base salary increases and bonus payments.

As discussed earlier in this Report, the Committee has since reviewed Executive Directors' service agreements and addressed concerns with respect to the quality of disclosure.

5.4 Approval

This Remuneration Report has been approved by the Board of Directors of Spirax-Sarco Engineering plc.

Signed on behalf of the Board of Directors

Gareth Bullock
Chairman, Remuneration Committee
6th March 2013

Statement of compliance

As required by the Listing Rules of the Financial Services Authority this Statement of Compliance explains how the Company applies the principles and complies with the provisions of the UK Corporate Governance Code 2010 (Code). The Code can be found on the Financial Reporting Council's website at www.frc.org.uk/Our-Work/Codes-Standards/Corporate-governance.

The Group has complied with the detailed provisions of the Code throughout 2012, with the exception of provision B.1.2, Composition of the Board. We have explained in detail our reasons on pages 49 and 76 and set out our alternative practice to achieve good governance. The Code is not a rigid set of rules and the Code recognises that an alternative to following a provision may be justified in particular circumstances where good governance is still achieved.

We have addressed each Code principle in the table below.

COMPLIANCE WITH THE UK CORPORATE GOVERNANCE CODE 2010

	Code of Best Practice – Principles	Group Compliance Statement
A	**DIRECTORS**	
1	**The role of the Board** Every company should be headed by an effective board, which is collectively responsible for the long-term success of the company.	The Directors' responsibilities are outlined in the Corporate Governance Report on page 49. The Board meets regularly on a formal basis plus additional ad hoc meetings as necessary.
2	**Division of responsibilities** There should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business. No one individual should have unfettered powers of decision.	Responsibility is clearly split between the Chairman and the Group Chief Executive. The Chairman is responsible for managing the business of the Board, safeguarding corporate governance and chairing the Board. The Group Chief Executive has responsibility for corporate and business strategy, managing the Group's businesses and the effective stewardship of capital, technical and human resources. A detailed explanation of their respective responsibilities is set out on page 50.
3	**The Chairman** The chairman is responsible for leadership of the board and ensuring its effectiveness on all aspects of its role.	The Chairman sets the Board's agenda and ensures that adequate time is available for the discussion of all agenda items. The Chairman promotes a culture of openness and debate. He also ensures constructive relations between the Executive Directors and the Non-Executive Directors. The Chairman ensures effective communication with shareholders. A detailed explanation of the Chairman's responsibilities is set out on page 50.
4	**Non-Executive Directors** As part of their role as members of a unitary board, non-executive directors should constructively challenge and help develop proposals on strategy.	The Non-Executive Directors scrutinise the performance of management, monitor the reporting of performance and assist in the development of strategy. The Senior Independent Director is available to shareholders if they have concerns that contact through the normal channels has failed to resolve matters. The Chairman holds meetings with the Non-Executive Directors without the Executive Directors present where considered appropriate. The Senior Independent Director meets with the Non-Executive Directors without the Chairman being present on such occasions as he considers appropriate.

COMPLIANCE WITH THE UK CORPORATE GOVERNANCE CODE 2010

	Code of Best Practice – Principles	Group Compliance Statement
B	EFFECTIVENESS	
1	**The composition of the Board** The board and its committees should have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively.	All the Non-Executive Directors other than the Non-Executive Chairman are considered by the Board to be independent of the management of the Company and free from any business or other relationship which could materially interfere with the exercise of their independent judgement. The Directors have a combination of business and industry expertise which is suited to the nature of the Company. During 2012 there were five Executive and four independent Non-Executive Directors, excluding the Non-Executive Chairman. The Board is pleased to take this opportunity to explain its reasons for this structure and, in doing so, meets the requirements of the Code to comply or explain. The Board also wishes to explain why it is justified in the circumstances and how good governance is still achieved. The Group operates a predominantly direct sales business model, a strategy that has been at the heart of the Group's success over many years. The need for a direct presence in every market of any size leads to a trading structure with many relatively small operations – the Group currently has over 50 operating companies in 36 countries and operates in more than 100 countries. Our business philosophy is to empower the General Managers of our local companies to maximise the opportunities in each market, whilst ensuring there is appropriate oversight, control and integration. Effective Board oversight and control of this necessarily flat organisation structure with many small components is, we believe, best achieved by having knowledgeable Executive Directors on the Board providing direct first-hand operational input to the Chairman and Non-Executive Directors. The three Executive Directors, in addition to the Group Chief Executive and the Finance Director, are responsible for the EMEA and the Asia Pacific/Supply divisions for the steam specialties business, and for the Watson-Marlow peristaltic pumps business. They have detailed knowledge of their respective divisions and their presence on the Board enables the Chairman and independent Non-Executive Directors to have regular access to the operations of the Group. Executive Directors also gain valuable experience of wider business issues across different divisions, regions and functional areas, which we believe enhances the Group's succession planning process. Having a number of Executive Directors on the Board manages the risk of over-reliance on limited Executive Director opinion. The Board has a well-balanced blend of experienced independently-minded Non-Executive Directors who provide robust challenge. The practical conduct of Board meetings is such that, even though there are five Executive Directors and four independent Non-Executive Directors (excluding the Non-Executive Chairman), the views of the Non-Executive Directors are given due weight and a collective approach to decision-making is adopted. The Board considers that it has the appropriate balance of skills, experience, independence and knowledge to enable it to discharge its duties and responsibilities effectively and that expanding its size by the appointment of another Non-Executive Director, simply to meet the balance criteria, will have the effect of the Board becoming unwieldy. Nevertheless, the Board will routinely reconsider the balance and skills of Executive Directors and Non-Executive Directors. The Group has an excellent track record in delivering sustained growth in shareholder value and £1,000 invested in January 2003 produced a total shareholder return, as at 31st December 2012, of £7,488 (+649%). In the latest five-year period, total shareholder return has increased by 201% and the share price has risen from under £9 to over £22 at the end of 2012, all underpinned by the Group's good governance practices over many years. The external review of Board effectiveness conducted recently by Dr Long, and described in more detail on page 51, concluded that the Board functions effectively and that its decision-making process is excellent. It is also important to point out that including the Non-Executive Chairman (who was independent on appointment) balances the Board and the Non-Executive Chairman has a casting vote in the event of a deadlock. In providing this detailed explanation the Board considers that the Group satisfies the requirements of the Code to comply or explain.

COMPLIANCE WITH THE UK CORPORATE GOVERNANCE CODE 2010

	Code of Best Practice – Principles	Group Compliance Statement
B	**EFFECTIVENESS**	
2	**Appointments to the Board** There should be a formal, rigorous and transparent procedure for the appointment of new directors to the board.	The Nomination Committee is comprised our four independent Non-Executive Directors, the Group Chief Executive and the Chairman, and is responsible for identifying and nominating the best candidates to fill Board vacancies having due regard for the balance of skills and experience. The Group seeks to have Directors who, in addition to relevant technical and commercial expertise, meet the highest standards of judgement, critical-thinking and openness. We believe that the Board's perspective and approach is greatly enhanced through gender, age and cultural diversity and it is our policy to consider overall Board balance and diversity when appointing new Directors. The diagram on page 48 illustrates the diverse range and nationalities of our Board which is particularly relevant given the broad international reach of the Group. On gender, we appointed Dr Schoolenberg as a Non-Executive Director during 2012 and, subject to appointing Directors of the highest calibre and relevant expertise, we plan to increase female representation on the Board when vacancies arise. Our aim on Board diversity is to have 25% female directors by 2016. However, all appointments will continue to be made on merit. To achieve this target we will ensure that female candidates are considered routinely as part of the recruitment process. We will also encourage the progress of females in senior positions throughout the Group. We are pleased to report that we do have a number of females in senior positions including the Europe and Middle East Sales and Marketing Director of Watson-Marlow Pumps, the Chief Financial Officer and Chairman of Watson-Marlow Ltd and a Regional General Manager in the Spirax Sarco EMEA Division. We are also constantly improving the intake of female professionals from universities to ensure an improved talent pipeline for senior leadership roles in the future.
3	**Commitment** All directors should be able to allocate sufficient time to the company to discharge their responsibilities effectively.	The Board ensures that on appointment, and thereafter, all Directors have sufficient time to carry out their duties.
4	**Development** All directors should receive induction on joining the board and should regularly update and refresh their skills and knowledge.	Directors attend formal training seminars to update their knowledge and duties. The Board is regularly updated on changes to relevant laws and regulations. Non-Executive Directors are invited to attend Group conferences, which provide information on new product development, sales and marketing initiatives. Business presentations are given at Board meetings to enable a review of new product development, regional operations, business strategies and employee development. An induction pack is provided to new appointees to the Board and induction procedures include site visits, briefings by senior managers and meetings with major shareholders. The Board has extensive experience and possesses the relevant skills and knowledge to perform its duties. In 2012 Mr Daws, Executive Director Asia Pacific and Supply, attended the Advanced Management Programme at Havard Business School.
5	**Information and support** The board should be supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties.	The Board is supplied with management accounts, detailed operational reviews and other appropriate papers on a timely basis prior to each meeting. All Directors have access to the advice and services of the General Counsel and Company Secretary and all Directors are able to take independent professional advice, if necessary, at the Company's expense.

Statement of compliance
continued

COMPLIANCE WITH THE UK CORPORATE GOVERNANCE CODE 2010

	Code of Best Practice – Principles	Group Compliance Statement
B	**EFFECTIVENESS continued**	
6	**Evaluation** The board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors.	The Board conducts an annual review of its effectiveness and that of each Board Committee and Board member. The performance of the Chairman is assessed annually by the Non-Executive Directors led by the Senior Independent Director. The performance of the Group Chief Executive is assessed annually by the Chairman. In 2012, we commissioned an independently facilitated Board review conducted by Dr Long of Boardroom Review Limited. The details of this review, including our objectives, findings and action plan, are set out in full on page 51.
7	**Re-election** All directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance.	All Directors are subject to election or annual re-election by shareholders at the AGM.
C	**ACCOUNTABILITY**	
1	**Financial and business reporting** The board should present a balanced and understandable assessment of the company's position and prospects	The Annual Report seeks to present a clear understanding of the business model and the Company's strategy, and a fair, balanced and easily understood assessment of the Group's performance, including guidance on its future prospects. The Directors continue to report in the annual and half-yearly financial statements that the business is a going concern.
2	**Risk management and internal control** The board is responsible for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives. The board should maintain sound risk management and internal control systems.	The Company operates a risk management and internal control process which is reviewed at least annually by the Board and which is explained in detail on pages 55 to 57.
3	**Audit Committee and auditor** The board should establish formal and transparent arrangements for considering how they should apply the corporate reporting and risk management and internal control principles and for maintaining an appropriate relationship with the company's auditor.	The Audit Committee, comprising the Non-Executive Directors, meets at least three times a year. The Chairman and Finance Director are invited to attend. The Audit Committee also meets separately with the Company's auditor without the other Directors present. A detailed explanation of the Audit Committee and its work is set out in the Governance section on pages 52 and 53.

COMPLIANCE WITH THE UK CORPORATE GOVERNANCE CODE 2010

	Code of Best Practice – Principles	Group Compliance Statement
D	**REMUNERATION**	
1	**The level and components of remuneration** Levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose. A significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance.	The Company has set a remuneration policy that is designed to attract, retain and motivate high calibre individuals, structuring remuneration so as to reflect corporate and individual performance against stretching targets that promote the long-term success of the Company. A detailed explanation is given in the Remuneration Report starting on page 60.
2	**Procedure** There should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors. No director should be involved in deciding his or her own remuneration.	Remuneration packages for individual Executive Directors are set by the Remuneration Committee after receiving appropriate information from independent sources and the Group Human Resources Director. The Remuneration Committee comprises the independent Non-Executive Directors. The Chairman, the Group Chief Executive and the Group Human Resources Director may be invited to attend the Committee's meetings. No Director is involved in determining his or her own remuneration.
E	**RELATIONS WITH SHAREHOLDERS**	
1	**Dialogue with shareholders** There should be a dialogue with shareholders based on the mutual understanding of objectives. The board as a whole has responsibility for ensuring that a satisfactory dialogue with shareholders takes place.	The Group Chief Executive and the Finance Director meet on a regular basis with the Company's major shareholders. Non-Executive Directors meet institutional shareholders on an ad hoc basis. The Chairman and the Senior Independent Director have met with investors and shareholder representative bodies on remuneration and governance and have kept the Board informed. We have listened to our shareholders to ensure that we understand their views. This active dialogue, together with other market inputs, has enabled us to provide appropriate feedback to the Board and develop a better understanding of mutual objectives. It will continue to be a focus going forward. The Chairman ensured that the views of shareholders were communicated to the Board as a whole.
2	**Constructive use of the AGM** The board should use the AGM to communicate with investors and to encourage their participation.	Shareholders are encouraged to attend our AGM and those who are unable to attend are encouraged to vote using the proxy card mailed to them. In 2012 95% of the proxy votes received were lodged electronically through the CREST system. The Chairman, and other Board members, answer questions raised by shareholders on a resolution by resolution basis. Shareholders are then invited to vote on the resolutions on the same basis by way of a polled vote. The results will be announced instantaneously using the Equiniti 'Vote Now' polling system. Immediately after the AGM, the results are also announced on the Group's website, www.spiraxsarcoengineering.com, and the London Stock Exchange. Following the AGM our Group Chief Executive makes a presentation on the Group's business and shareholders are invited to view our Steam Technology Centre.

Other statutory and regulatory disclosures

Principal activities
Spirax Sarco is a UK-based multi-national engineering group, tightly focused on its two niche businesses of steam system specialties and peristaltic pumps.

At the heart of the Group's robust and resilient business model is our worldwide direct selling approach. Working directly with customers, our sales engineers apply our application and systems knowledge, breadth of products and services, experience and global presence, to enable the Group to offer the most extensive range of engineered solutions that generate cost savings and process improvements. The business benefits from the great diversity of our end user industries; customers and geographic spread; from our significant exposure to emerging markets; the high level of replacement content in our revenue stream and a large base of industrial steam systems and peristaltic pump installations around the world that need continual upkeep and improvement.

The Spirax Sarco steam business is the global leader in the supply of engineered solutions for the design, maintenance and operation of efficient industrial and commercial steam systems. As a heat source, steam is the natural choice in most industrial processes due to its high heat-carrying capacity, the controllability of its temperature, sterility and efficiency as a heat transfer fluid. Spirax Sarco's engineered solutions are used in a wide variety of process industries including foods, beverages and brewing, pharmaceuticals, oil and petrochemicals, chemicals, mining and metals processing, plastics and textiles. The Group also provides a wide range of products, engineered packages and services for space heating, humidification, sterilisation, steam and hot water generation for hospitals, public buildings, academic institutions and commercial buildings.

The Watson-Marlow business is the world's leading specialist and largest manufacturer of peristaltic pumps, the fastest-growing pump type, and other niche pumps. Peristaltic pumps are ideal for difficult pumping applications for hygienic, abrasive or corrosive fluids that must be pumped safely, accurately and without contamination, in applications ranging from high purity biopharmaceuticals to wastewater treatment to precious metals processing.

Future development
An indication of likely future developments in the Group is given in the Business Review on page 17.

Review of the business
In the Business Review and the Finance Review on pages 26 to 29 you will find a review of the development and performance of the Group during the year including details of its financial performance and key performance indicators. A description of risk management and the principal risks facing the business is on pages 58 and 59.

Results
The Group's results for the year have been prepared in accordance with the International Financial Reporting Standards as adopted by the European Union. They are set out in the Consolidated Income Statement which appears on page 86.

Dividend
The Directors are proposing the payment of a final dividend of 37.0p (2011 : 34.2p) which, together with the interim dividend of 16.0p (2011 : 14.8p), makes a total distribution for the year of 53.0p (2011 : 49.0p). If approved at the AGM, the final dividend will be paid on 17th May 2013 to shareholders on the register at the close of business on 19th April 2013.

Special dividend and share consolidation
Following a review of the Company's capital requirements, the Board is recommending a return of cash to shareholders of £78 million in the form of a special dividend of 100.0p per share in respect of 2012 (2011 : nil) which, if approved at the AGM, will be paid on 3rd July 2013 to shareholders on the register at the close of business on 31st May 2013.

As is common with a significant return of capital to shareholders, the Board recommends that this is combined with a share consolidation. This is intended to maintain, as far as possible, the comparability of the share price, earnings per share and dividends per share before and after the special dividend, and to remove the impact of the special dividend on employee equity-based incentives. It is anticipated, therefore, that the market price of each Ordinary share should remain at a broadly similar level following the special dividend and share consolidation.

Directors' interests
The interests of the Directors in the share capital of Spirax-Sarco Engineering plc as at 31st December 2012 are set out on page 73.

Directors' and officers' insurance
The Company provides Directors' and Officers' Insurance for Board members, directors of the Group's operating companies and senior officers.

Directors' contracts
The Executive Directors' service agreements and Non-Executive Directors' letters of appointments are available for inspection by any person at the Company's registered office during normal working hours in addition to being presented at the AGM.

Appointment and replacement of Directors
The appointment and replacement of Directors is governed by the Company's Articles of Association, the Code, the Companies Act 2006 and related legislation. At the AGM, shareholders will be asked to elect to the Board our new Non-Executive Director, Dr Schoolenberg. In order to comply with the Code, all other Directors will seek re-election at the AGM and will do so thereafter on an annual basis at each future AGM.

Conflicts
Under the Companies Act 2006 and the provisions of the Company's Articles of Association, the Board is required to consider potential conflicts of interest. The Company has established formal procedures for the disclosure and review of any conflicts, or potential conflicts, of interest which the Directors may have and for the authorisation of such conflict matters by the Board. To this end the Board considers and, if appropriate, authorises any conflicts, or potential conflicts, of interest as they arise and reviews any such authorisation annually. New Directors are required to declare any conflicts, or potential conflicts, of interest to the Board at the first Board meeting after his or her appointment. The Board believes that the procedures established to deal with conflicts of interest are operating effectively.

Articles of Association
The Company's Articles of Association are available from Companies House in the UK or by writing to the General Counsel and Company Secretary at the Group's registered office in Cheltenham. Amendments to the Articles of Association can only be made by means of a special resolution at a general meeting of the shareholders of the Company.

Share capital

As at 28th February 2013 there were no treasury shares held by the Company. Details of shares issued during the year are set out in note 23 on page 107.

As at 31st December 2012 the Company's share capital was made up of Ordinary shares which each carry one vote at general meetings of the Company. Except as set out in the Articles of Association or in applicable legislation, there are no restrictions on the transfer of shares in the Company and there are no restrictions on the voting rights in the Company's shares.

The Company is not aware of any agreements entered into between any shareholders in the Company which restrict the transfer of shares or the exercise of any voting rights attached to the shares.

Powers of the Directors and purchase of own shares

Subject to the provisions of the Articles of Association, the Directors may exercise all the powers of the Company. No purchases of shares were made by the Company during the year and therefore, as at 31st December 2012, 7,781,991 shares may be purchased in accordance with the authority given by shareholders at the 2012 AGM. This authority expires at the forthcoming AGM and it is proposed that a similar authority be approved. The total number of shares in issue as at 31st December 2012 was 78,089,826.

Substantial shareholdings

The following voting rights have been notified to the Company under the requirements of the UK Listing Authority's Disclosure Rules and Transparency Rules DTR 5, which represent 3% or more of the voting rights attached to issued shares in the Company as at 28th February 2013 and 31st December 2012.

So far as can be ascertained, the holdings are beneficially held.

Constructive use of AGM and 2013 AGM

Shareholders are encouraged to attend our AGM and those who are unable to attend are encouraged to vote using the proxy card mailed to them.

In 2012, 95% of the proxy votes received were lodged electronically through the CREST system.

The Chairman, and other Board members, answer questions raised by shareholders on a resolution by resolution basis. Shareholders are then invited to vote on the resolutions on the same basis by way of a polled vote. The results are announced instantaneously using the Equiniti 'Vote Now' polling system and via the Group's website, www.spiraxsarcoengineering.com, and the London Stock Exchange. Following the AGM our Group Chief Executive makes a presentation on the Group's business and shareholders are invited to view our Steam Technology Centre.

The Notice of Meeting convening the AGM, to be held on Thursday, 9th May 2013, and an explanation of the resolutions sought, are set out in the enclosed Circular.

Significant contracts

The Company is not a party to any significant agreements that take effect, alter or terminate upon a change of control of the Company following a takeover bid.

There are provisions in the Executive Directors' service agreements which state that following a takeover or change of control, if the Executive Director's employment is terminated then both salary/benefits and a sum in respect of lost future bonus opportunity become payable as a lump sum.

The Business Review contains all the information required to comply with section 417(5) of the Companies Act 2006 and there are no contractual arrangements that need to be disclosed which are essential to the business of the Group.

Disclosure of information to auditor

As at the date of the approval of this Annual Report, as far as each Director is aware, there is no relevant audit information of which the Company's auditor is unaware. Each Director has taken all such steps as he or she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information. For these purposes, relevant audit information (as defined by Section 418(3) of the Companies Act 2006) means information needed by the Company's auditor in connection with preparing their report set out on page 84.

Auditor

The Company's auditor, KPMG Audit Plc, has indicated its willingness to continue in office, and resolutions seeking that it be re-appointed as the Company's auditor and authorising the Directors to determine its remuneration will be proposed at the forthcoming AGM.

	As at 31.12.12		As at 28.02.13	
Substantial shareholdings	Number of Ordinary shares	% of issued share capital	Number of Ordinary shares	% of issued share capital
BlackRock Investment Management (UK) Ltd	6,835,695	8.7%	7,321,158	9.4%
Sprucegrove Investment Management Ltd	4,263,859	5.5%	4,234,769	5.4%
Schroder Investment Management Ltd	3,271,661	4.2%	3,188,810	4.1%
Baillie Gifford & Co	2,989,306	3.8%	2,986,406	3.8%

Other statutory and regulatory disclosures continued

Corporate website

Please visit our website for more information, including:

- Annual Reports, webcasts and analyst presentations
- News and press releases
- Governance and policy documents
- Investor relations documents
- Details of our operating companies

Interactive Annual Report

Our interactive Annual Report is available online. It is fully searchable and downloadable, contains additional case study detail, and includes a range of videos such as a Welcome from the Group Chief Executive, the Business Model Explained, Regional and Sectional Overviews, and the Uses of Steam.

Research and development

The Group continues to devote significant resources to the development and the updating and expansion of its range of products in order to remain at the forefront of its world markets. The Group steam specialties R&D function, which is based in Cheltenham, is tasked with improving the Group's pipeline of new products, decreasing the time to launch, expanding the Group's addressable market and realising additional sales. Further information on the expenditure on R&D is contained in note 1 on page 92. The amount of R&D expenditure capitalised, and the amount amortised, in the year, are given in note 6 on page 97 and note 13 on page 101 respectively.

Creditor payment policy

The Company does not follow a specific standard or code on payment practice but has a variety of payment terms based on the following:

- Contracts have been negotiated with a number of suppliers and payments are made in accordance with the terms of these contracts
- Payment terms are disclosed on the Company's standard purchase order forms. The Company's policy is to ensure that all invoices are settled within 30 days of the receipt and agreement of a valid and complete invoice.

Treasury and foreign exchange

The Group has in place appropriate treasury policies and procedures, which are approved by the Board. The treasury function manages interest rates for both borrowings and cash deposits for the Group and is also responsible for ensuring there is sufficient headroom against any banking covenants contained within its credit facilities, and for ensuring there are appropriate facilities available to meet the Group's strategic plans.

In order to mitigate and manage exchange rate risk, the Group routinely enters into forward contracts and continues to monitor exchange rate risk in respect of foreign currency exposures.

All these treasury policies and procedures are regularly monitored and reviewed. It is the Group's policy not to undertake speculative transactions which create additional exposures over and above those arising from normal trading activity.

Fixed assets

In the opinion of the Directors, the market value of the land and buildings of the Group exceeds the book value of those assets at 31st December 2012 by approximately £12,000,000 (2011 : £12,000,000).

Donations

During the year, the Spirax-Sarco Group Charitable Trust made 45 charitable donations amounting to £132,000 (2011 : £132,000). In addition our operating companies worldwide made many donations to local charities and social organisations. The total donations across the Group amounted to £172,000.

The Company has adopted a Group Charitable Donations Policy which sets out the principles for charitable giving.

There were no political donations made during the year (2011 : nil).

Going concern

The Group's business activities, together with the main trends and factors likely to affect its future development, performance and position, and the financial position of the Group, its cash flows, liquidity position and borrowing facilities, are set out in the Business Review and Finance Review on pages 17 to 29. In addition note 1 on page 90 includes the Group's objectives, policies and processes for managing its capital, its financial risk management objectives, its financial instruments and hedging activities, its exposures to credit risk and liquidity risk.

The Group has considerable financial resources together with contracts with a diverse range of customers and suppliers across different geographic areas and industries. No one customer accounts for more than 1% of Group turnover. As a consequence, the Directors believe that the Group is well placed to manage its business risks successfully despite the current uncertain economic outlook.

The Directors, having made appropriate enquiries, consider that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future and that therefore it is appropriate to adopt the going concern basis in preparing the Annual Report.

By order of the Board of Directors
A J Robson
General Counsel and Company Secretary
6th March 2013
Spirax-Sarco Engineering plc
Registered no. 596337

Statement of Directors' responsibilities
in respect of the Annual Report and Accounts

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 applicable law and have elected to prepare the Parent Company financial statements on the same basis.

Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Parent Company and of their profit or loss for that period. 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 judgements and estimates that are reasonable and prudent
- State whether they have been prepared in accordance with IFRS as adopted by the EU
- 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 adequate accounting records that are sufficient to show and explain the Parent Company's transactions and 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 2006. 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 Corporate Governance Report, Remuneration Report and Other Statutory and Regulatory Disclosures 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 Group's website: www.SpiraxSarcoEngineering.com. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Cautionary statement

All statements other than statements of historical fact included in this document, including, without limitation, those regarding the financial condition, results, operations and businesses of Spirax-Sarco Engineering plc and its strategy, plans and objectives and the markets and economies in which it operates, are forward-looking statements. These forward-looking statements which reflect management's assumptions made on the basis of information available to it at this time, involve known and unknown risks, uncertainties and other important factors which could cause the actual results, performance or achievements of Spirax-Sarco Engineering plc or the markets and economies in which we operate to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements. Spirax-Sarco Engineering plc and its directors accept no liability to third parties in respect of this report save as would arise under English law.

Accordingly, any liability to a person who has demonstrated reliance on any untrue or misleading statement or omission shall be determined in accordance with schedule 10A of the Financial Services and Markets Act 2000. It should be noted that schedule 10A contains limits on the liability of the Directors of Spirax-Sarco Engineering plc so that their liability is solely to Spirax-Sarco Engineering plc.

Responsibility statement

We confirm that to the best of our knowledge:

- The financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- The management report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks that they face.

Signed by

David Meredith

D J Meredith
Finance Director
on behalf of the Board of Directors
6th March 2013

Report of the independent auditor

To the members of Spirax-Sarco Engineering plc

We have audited the financial statements of Spirax-Sarco Engineering plc for the year ended 31st December 2012 set out on pages 85 to 125. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU and, as regards the Parent Company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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

As explained more fully in the Statement of Directors' Responsibilities set out on page 83, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion:

- The financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31st December 2012 and of the Group's profit for the year then ended
- The Group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU
- The Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006
- The financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- The part of the Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006
- The information given in Other Statutory and Regulatory Disclosures for the financial year for which the financial statements are prepared is consistent with the financial statements
- Information given in the Corporate Governance Report set out on pages 44 to 79 with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- Adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- The Parent Company financial statements and the part of the Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- Certain disclosures of Directors' remuneration specified by law are not made; or
- We have not received all the information and explanations we require for our audit; or
- A Corporate Governance Statement has not been prepared by the Company.

Under the Listing Rules we are required to review:

- The Directors' statement, set out on page 82, in relation to going concern;
- The part of the Corporate Governance Report on pages 75 to 79 relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code published in June 2010 specified for our review; and
- Certain elements of the report to shareholders by the Board on Directors' remuneration.

John D Cain
(Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
London
6th March 2013

Statements of financial position

at 31st December 2012

	Notes	The Group 2012 £000	The Group 2011 £000	Parent Company 2012 £000	Parent Company 2011 £000
Assets					
Non-current assets					
Property, plant and equipment	12	174,836	174,648	–	–
Goodwill	13	45,855	45,347	–	–
Other intangible assets	13	43,711	39,903	–	–
Prepayments		223	148	–	–
Loans to subsidiaries	14	–	–	64,155	74,156
Investment in subsidiaries	15	–	–	48,657	47,889
Investment in associate	16	7,702	8,280	220	220
Deferred tax assets	17	40,699	37,417	824	54
		313,026	**305,743**	**113,856**	**122,319**
Current assets					
Inventories	18	103,690	116,325	–	–
Trade receivables		145,686	142,484	–	–
Due from subsidiaries		–	–	143,748	129,016
Other current assets	19	16,188	17,054	255	44
Taxation recoverable		1,317	1,973	–	–
Cash and cash equivalents	28	99,832	60,172	4,261	–
		366,713	**338,008**	**148,264**	**129,060**
Total assets		**679,739**	**643,751**	**262,120**	**251,379**
Equity and liabilities					
Current liabilities					
Trade and other payables	20	90,469	88,632	810	1,737
Bank overdrafts	28	387	4,194	–	2,573
Short-term borrowing	28	7,000	37,280	7,000	20,000
Current portion of long-term borrowings	28	7,168	73	–	–
Current tax payable		12,399	11,449	–	–
		117,423	**141,628**	**7,810**	**24,310**
Net current assets		**249,290**	**196,380**	**140,454**	**104,750**
Non-current liabilities					
Long-term borrowings	28	33,601	6,356	27,500	–
Deferred tax liabilities	17	17,003	17,941	–	–
Post-retirement benefits	27	72,663	71,925	56	2,455
Provisions	22	991	1,509	–	–
Long-term payables		1,509	4,272	–	–
Due to subsidiaries		–	–	23,941	1,277
		125,767	**102,003**	**51,497**	**3,732**
Total liabilities		**243,190**	**243,631**	**59,307**	**28,042**
Net assets	2	**436,549**	**400,120**	**202,813**	**223,337**
Equity					
Share capital	23	19,536	19,418	19,536	19,418
Share premium account		56,172	52,262	56,172	52,262
Other reserves	23	28,098	39,408	6,969	6,201
Retained earnings		331,945	288,243	120,136	145,456
Equity shareholders' funds		435,751	399,331	202,813	223,337
Non-controlling interest		798	789	–	–
Total equity		**436,549**	**400,120**	**202,813**	**223,337**
Total equity and liabilities		**679,739**	**643,751**	**262,120**	**251,379**

These accounts were approved by the Board of Directors on 6th March 2013 and signed on its behalf by:

Directors

M E Vernon D J Meredith

Consolidated income statement

for the year ended 31st December 2012

	Notes	**Adjusted 2012 £000**	**Adjustments 2012 £000**	**Total 2012 £000**	Adjusted 2011 £000	Adjustments 2011 £000	Total 2011 £000
Revenue	2	661,723	–	661,723	649,991	–	649,991
Operating costs	3	(525,478)	(10,531)	(536,009)	(516,031)	(4,462)	(520,493)
Operating profit	2	**136,245**	**(10,531)**	**125,714**	**133,960**	**(4,462)**	**129,498**
Financial expenses		(16,860)	–	(16,860)	(17,515)	–	(17,515)
Financial income		17,249	–	17,249	18,592	–	18,592
	5	**389**	**–**	**389**	**1,077**	**–**	**1,077**
Share of profit of associate		1,873	(324)	1,549	2,132	(366)	1,766
Profit before taxation	6	**138,507**	**(10,855)**	**127,652**	**137,169**	**(4,828)**	**132,341**
Taxation	8	(40,467)	3,060	(37,407)	(40,215)	1,112	(39,103)
Profit for the period		**98,040**	**(7,795)**	**90,245**	**96,954**	**(3,716)**	**93,238**
Attributable to:							
Equity shareholders		97,836	(7,795)	90,041	96,765	(3,716)	93,049
Non-controlling interest		204	–	204	189	–	189
Profit for the period		**98,040**	**(7,795)**	**90,245**	**96,954**	**(3,716)**	**93,238**
Earnings per share	10						
Basic earnings per share		125.6p		115.6p	124.8p		120.0p
Diluted earnings per share		124.1p		114.2p	123.2p		118.4p
Dividends	11						
Dividends per share				53.0p			49.0p
Special dividend per share				100.0p			–
Dividends paid during the year (per share)				50.2p			69.8p

Adjusted figures exclude certain non-operational items as detailed in note 2.

All amounts relate to continuing operations.

The notes on pages 90 to 125 form an integral part of the accounts.

Consolidated statement of comprehensive income

for the year ended 31st December 2012

	The Group 2012 £000	2011 £000
Profit for the period	90,245	93,238
Actuarial loss on post-retirement benefits	(11,818)	(18,736)
Deferred tax on actuarial loss on post-retirement benefits	2,466	5,776
Foreign exchange translation differences	(11,312)	(11,094)
Non-controlling interest foreign exchange translation differences	20	(119)
Profit/(loss) on cash flow hedges net of tax	2	(270)
Total comprehensive income for the period	**69,603**	**68,795**
Attributable to:		
Equity shareholders	69,379	68,725
Non-controlling interest	224	70
Total comprehensive income for the period	**69,603**	**68,795**

Consolidated statement of changes in equity

for the year ended 31st December 2012

Group

	Share capital £000	Share premium account £000	Other reserves £000	Retained earnings £000	Equity shareholders' funds £000	Non-controlling interest £000	Total equity £000
Balance at 1st January 2012	19,418	52,262	39,408	288,243	399,331	789	400,120
Total comprehensive income for the period	–	–	(11,310)	80,689	69,379	224	69,603
Dividends paid	–	–	–	(39,126)	(39,126)	(215)	(39,341)
Equity settled share plans net of tax	–	–	–	2,139	2,139	–	2,139
Issue of share capital	118	3,910	–	–	4,028	–	4,028
Balance at 31st December 2012	**19,536**	**56,172**	**28,098**	**331,945**	**435,751**	**798**	**436,549**

Other reserves represent the Group's Translation, Cash flow hedge and Capital redemption reserves (see note 23).

Consolidated statement of changes in equity

for the year ended 31st December 2011

Group

	Share capital £000	Share premium account £000	Other reserves £000	Retained earnings £000	Equity shareholders' funds £000	Non-controlling interest £000	Total equity £000
Balance at 1st January 2011	19,329	48,276	50,772	260,351	378,728	796	379,524
Total comprehensive income for the period	–	–	(11,364)	80,089	68,725	70	68,795
Dividends paid	–	–	–	(54,089)	(54,089)	(77)	(54,166)
Equity settled share plans net of tax	–	–	–	1,604	1,604	–	1,604
Issue of share capital	89	3,986	–	–	4,075	–	4,075
Treasury shares reissued	–	–	–	2,260	2,260	–	2,260
Loss on the reissue of treasury shares	–	–	–	(1,972)	(1,972)	–	(1,972)
Balance at 31st December 2011	**19,418**	**52,262**	**39,408**	**288,243**	**399,331**	**789**	**400,120**

Other reserves represent the Group's Translation, Cash flow hedge and Capital redemption reserves (see note 23).

Statement of changes in equity

for the year ended 31st December 2012

Parent Company

	Share capital £000	Share premium account £000	Share-based payments £000	Capital redemption reserve £000	Retained earnings £000	Total equity £000
Balance at 1st January 2012	19,418	52,262	4,369	1,832	145,456	223,337
Total comprehensive income for the period	–	–	–	–	12,497	12,497
Dividends paid	–	–	–	–	(39,126)	(39,126)
Equity settled share plans net of tax	–	–	–	–	1,309	1,309
Issue of new share capital	118	3,910	–	–	–	4,028
Investment in subsidiaries in relation to share options granted	–	–	768	–	–	768
Balance at 31st December 2012	**19,536**	**56,172**	**5,137**	**1,832**	**120,136**	**202,813**

Statement of changes in equity

for the year ended 31st December 2011

Parent Company

	Share capital £000	Share premium account £000	Share-based payments £000	Capital redemption reserve £000	Retained earnings £000	Total equity £000
Balance at 1st January 2011	19,329	48,276	3,728	1,832	100,089	173,254
Total comprehensive income for the period				–	98,374	98,374
Dividends paid	–	–	–	–	(54,089)	(54,089)
Equity settled share plans net of tax	–	–	–	–	794	794
Issue of new share capital	89	3,986	–	–	–	4,075
Treasury shares reissued	–	–	–	–	2,260	2,260
Loss on the reissue of treasury shares	–	–	–	–	(1,972)	(1,972)
Investment in subsidiaries in relation to share options granted	–	–	641	–	–	641
Balance at 31st December 2011	**19,418**	**52,262**	**4,369**	**1,832**	**145,456**	**223,337**

Cash flow statements

for the year ended 31st December 2012

	Notes	The Group 2012 £000	The Group 2011 £000	Parent Company 2012 £000	Parent Company 2011 £000
Cash flows from operating activities					
Profit before taxation		127,652	132,341	12,773	93,702
Depreciation, amortisation and impairment		24,971	20,828	–	–
Dividends received		–	–	(17,954)	(100,461)
Share of profit of associates		(1,549)	(1,766)	–	–
Equity settled share plans		2,815	2,182	1,309	796
Net finance (income)		(389)	(1,077)	(929)	(273)
Exchange adjustments		–	–	–	221
Operating cash flow before changes in working capital and provisions		153,500	152,508	(4,801)	(6,015)
Change in trade and other receivables		(8,020)	(10,084)	(213)	–
Change in amounts due from subsidiaries		–	–	(3,978)	(67,140)
Change in amounts due to subsidiaries		–	–	22,214	–
Change in inventories		8,631	(22,561)	–	–
Change in provisions and post-retirement benefits		(6,974)	(10,915)	(2,306)	(3,288)
Change in trade and other payables		(181)	(297)	(473)	(430)
Cash generated from operations		146,956	108,651	10,443	(76,873)
Interest paid		(1,478)	(1,381)	(803)	(267)
Income taxes paid		(37,941)	(33,433)	(1,864)	1,864
Net cash from operating activities		**107,537**	**73,837**	**7,776**	**(75,276)**
Cash flows from investing activities					
Purchase of property, plant and equipment		(23,384)	(42,814)	–	–
Proceeds from sale of property, plant and equipment		2,720	5,560	–	–
Purchase of software and other intangibles		(6,116)	(3,424)	–	–
Development expenditure capitalised		(2,911)	(2,717)	–	–
Acquisition of businesses		(4,501)	(3,387)	–	–
Interest received		1,272	1,048	1,702	79
Dividends received		1,454	1,461	17,954	100,461
Net cash used in investing activities		**(31,466)**	**(44,273)**	**19,656**	**100,540**
Cash flows from financing activities					
Proceeds from issue of share capital		4,028	4,075	4,028	4,075
Proceeds from reissue of treasury shares		–	288	–	288
Repaid borrowings		(26,468)	(18,346)	(15,573)	–
New borrowings		29,537	23,687	27,500	–
Change in finance lease liabilities	28	1,267	(76)	–	–
Dividends paid (including minorities)		(39,341)	(54,166)	(39,126)	(54,089)
Net cash used in financing activities		**(30,977)**	**(44,538)**	**(23,171)**	**(49,726)**
Net change in cash and cash equivalents	28	45,094	(14,974)	4,261	(1,889)
Cash and cash equivalents at beginning of period		55,978	73,496	–	1,889
Exchange movement		(1,627)	(2,544)	–	–
Cash and cash equivalents at end of period	28	**99,445**	**55,978**	**4,261**	–
Borrowings and finance leases		(47,769)	(43,709)	(34,500)	(22,573)
Net cash	28	**51,676**	**12,269**	**(30,239)**	**(22,573)**

Notes to the Accounts

1 Accounting policies

Basis of preparation

The Parent Company and consolidated accounts have been prepared in accordance with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) that have been adopted by the European Union (EU).

The preparation of accounts in conformity with IFRS requires the Directors to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experiences and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. As further explained below, the most significant effect on the financial statements from accounting policies requiring judgement are in the areas of research and development (R&D), and revenue.

The major judgements made in respect of R&D are those in assessing whether an intangible asset arises from the development phase of a product development project, i.e.:

i) The technical feasibility of completing the product so it will be ready for sale

ii) The market for the product and the future sales that the product will generate

iii) Assessing the costs directly attributable to the individual product during its development.

The Group has a very wide product range and the general nature of product development is that of a number of modest sized projects. The value of capitalised development costs is disclosed in note 13.

The judgements used in respect of revenue are explained in the revenue accounting policy on page 93 below.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. The key areas where estimates have been used and assumptions applied are in provisions, impairment testing of goodwill and intangible assets, and in assessing the defined benefit pension scheme liabilities. More details of the estimates used and assumptions applied in relation to impairment testing of goodwill and intangible assets are given in note 13 and those in relation to assessing defined benefit scheme liabilities in note 27.

The Group has considerable financial resources together with a diverse range of products and customers across wide geographic areas and industries. As a consequence, the Directors believe that the Group is well placed to manage its business risks successfully despite the current uncertain economic outlook.

Further information on the Group's business activities, performance and position, together with the financial position of the Group, its capital structure and cash flow are included in the business review and financial review on pages 17 to 29. In addition, note 31 to the financial statements discloses details of the Group's financial risk management and credit facilities.

The consolidated accounts are presented in pounds sterling, which is the Company's functional currency, rounded to the nearest thousand.

There were no revisions to adopted IFRS that became applicable in 2012 which had a significant impact on the Group's financial statements.

There are a number of new standards, amended standards and interpretations that are not yet effective for the year ended 31st December 2012, but that will be effective for 2013. IAS 1 Presentation of Financial Statements amends the presentation of Other Comprehensive Income to require items to be presented on the basis of whether subsequently they are potentially reclassifiable to the Income Statement. IAS 19 Employee Benefits requires the financing on post-retirement benefits to be calculated on the net surplus or deficit using an 'AA' corporate bond rate and all administrative and investment expenses to be recognised in the Income Statement. This will be effective for 2013 and will require restatement of the 2012 comparative figures, the effect of which is illustrated in note 27 on page 109. The Group does not consider that any other standards, amendments or interpretations issued by the IASB, but not yet applicable, will have a significant impact on the financial statements.

1 Accounting policies continued

Basis of accounting

(i) Subsidiaries

The Group accounts include the results of the Company and all its subsidiary undertakings. Subsidiaries are entities controlled by the Group. Control exists when the Group 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 accounts of subsidiaries are included in the consolidated accounts from the date that control commences until the date that control ceases.

(ii) Associates

Associates are those entities for which the Group has significant influence, but not control, over the financial and operating policies. The accounts include the Group's share of the total recognised income and expense of associates on an equity accounted basis, from the date that significant influence commences until the date that significant influence ceases.

(iii) Transactions eliminated on consolidation

Intragroup balances, and any unrealised gains and losses or income and expenses arising from intragroup transactions, are eliminated in preparing the accounts. Unrealised gains arising from transactions with associates are eliminated to the extent of the Group's interest in the entity.

(iv) Company

Under Section 408 of the Companies Act 2006 the Company is exempt from the requirement to present its own income statement.

Foreign currency

(i) On consolidation

The assets and liabilities of foreign operations are translated into sterling at exchange rates ruling at the balance sheet date. The revenues, expenses and cash flows of foreign operations are translated into sterling at average rates of exchange ruling during the year. Where the notes to the Group accounts include tables reconciling movements between opening and closing balances, assets and liabilities are translated at balance sheet rates and revenue and expenses are translated at average rates with the exchange differences arising being disclosed separately.

Exchange differences arising from the translation of the net investment in foreign operations are taken to a separate translation reserve within equity. They are recycled and recognised in the income statement upon disposal of the operation. In respect of all foreign operations, any differences that have arisen before 1st January 2004, the date of transition to IFRS, are not presented as a separate component of equity.

(ii) Foreign currency transactions

Transactions in foreign currencies are translated to the respective currencies of the Group entities at the foreign exchange rate at the date of the transaction. Monetary assets and liabilities at the balance sheet date denominated in a currency other than the functional currency of the entity are translated at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. 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. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated at foreign exchange rates ruling at the dates fair value was determined.

Cash flow hedges

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a highly probable forecasted transaction, the effective part of any gain or loss on the derivative financial instrument is recognised in other comprehensive income and presented in the Cash flow hedge reserve. The associated gain or loss is removed from equity and recognised in the income statement in the period in which the transaction to which it relates occurs.

Property, plant and equipment

Items of property, plant and equipment are stated at cost or deemed cost, less accumulated depreciation.

Certain items of property, plant and equipment that had been revalued to fair value prior to 1st January 2004, the date of transition to IFRS, are measured on the basis of deemed cost, being the revalued amount at the date of that revaluation.

Depreciation is charged to the income statement on a straight-line basis at rates which write down the value of assets to their residual values over their estimated useful lives. Land is not depreciated. The principal rates are as follows:

Freehold buildings	1.5%	Office equipment	12.5–33.3%
Plant and machinery	10–12.5%	Motor vehicles	20%
Office furniture and fittings	10%	Tooling and patterns	10%

The depreciation rates are reassessed annually.

1 Accounting policies continued

Intangible assets

(i) Goodwill

All business combinations after 1st January 2004 are accounted for by applying the acquisition method. Goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired. Goodwill is stated at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is not amortised but is tested annually for impairment (see note 13 for more detail). In respect of acquisitions prior to 1st January 2004, goodwill is included on the basis of its deemed cost, which represents the amount recorded under previous UK Generally Accepted Accounting Practice (GAAP).

(ii) R&D

Expenditure on R&D is charged to the income statement in the period in which it is incurred except that development expenditure is capitalised where the development costs relate to new or substantially improved products that are subsequently to be released for sale and will generate future economic benefits. The expenditure capitalised includes staff costs and related expenses. Capitalised development expenditure is stated at cost less accumulated amortisation (see below) and any impairment losses.

(iii) Other intangible assets

Intangible assets other than goodwill that are acquired by the Group are stated at cost less accumulated amortisation (see below) and any impairment losses. Annual impairment tests are performed on acquired intangible assets by comparing the carrying value with the recoverable amount, being the higher of the fair value less cost to sell and value in use, discounted at an appropriate discount rate, of future cash flows in respect of intangible assets for the relevant cash generating unit. More detail is given in note 13.

(iv) Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill, from the date they are available for use. Goodwill is tested for impairment annually. The principal amortisation rates are as follows:

Capitalised development costs	20%	Manufacturing designs and core technology	10%
ERP systems and software	12.5–20%	Non compete undertakings	50%
Customer relationships	20%		
Brand names and trademarks	10–20%		

Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of inventories includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity. Cost also includes transfers from equity of any gain or loss on qualifying cash flow hedges of foreign currency purchases of inventories.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits with an original maturity usually 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 purpose of the cash flow statements.

Going concern

The statement on the going concern assumption is included within corporate governance on page 82.

Employee benefits

(i) Defined contribution plans

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

(ii) Defined benefit plans

The costs of providing pensions under defined benefit schemes are calculated in accordance with the advice of qualified actuaries and spread over the period during which benefit is expected to be derived from the employees' services. The Group's net obligation in respect of defined benefit pensions is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods. That benefit is discounted at rates reflecting the yields on AA credit rated corporate bonds that have maturity dates approximating the terms of the Group's obligations to determine its present value. Pension scheme assets are measured at fair value at the balance sheet date. Actuarial gains and losses, differences between the expected and actual returns, and the effect of changes in actuarial assumptions are recognised in the statement of comprehensive income in the year they arise. Any scheme surplus (to the extent it is considered recoverable) or deficit is recognised in full in the balance sheet.

The cost of other post-employment liabilities are calculated in a similar way to defined benefit pension schemes and spread over the period which benefit is expected to be derived from the employees' services, in accordance with the advice of qualified actuaries.

(iii) Employee share plans

Incentives in the form of shares are provided to employees under share option and share award schemes. The fair value of these options and awards at their date of grant is charged to the income statement over the relevant vesting periods with a corresponding increase in equity. The value of the charge is adjusted to reflect expected and actual levels of options and share awards vesting.

(iv) Long-term share incentive plans

The fair value of awards is measured at the date of grant and the cost spread over the vesting period. The amount recognised as an expense is not adjusted to reflect market based performance conditions, but is adjusted for non-market based performance conditions.

1 Accounting policies continued

Revenue

Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer, which is typically on delivery. For service contracts, revenue is recognised at the point of customer acceptance. Revenue from projects is recognised as income in proportion to the stage of completion of the transaction at the balance sheet date. Judgements can be required to assess the stage of completion, although in the vast majority of projects the position is relatively easy to identify. Projects where a stage of completion assessment is needed typically involve the sale of products, installation and commissioning, which are usually separately identified elements in the project order.

No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due or associated costs, or there is the possibility of return of the goods. No revenue is recognised if there is significant continuing management involvement with the goods.

As soon as the outcome of a project or service contract can be estimated reliably, revenue and expenses are recognised in the income statement in proportion to the stage of completion of the project or service contract. An expected loss on a project or service contract is recognised immediately in the income statement.

Leases

(i) Operating leases

Payments made under operating leases are charged to the income statement on a straight-line basis over the term of the lease.

(ii) Finance leases

Leases where the Group assumes substantially all of the risks and rewards of ownership are classified as finance leases as if the asset had been purchased outright. Assets acquired under finance leases are recognised as assets of the Group and the capital and interest elements of the leasing commitments are shown as obligations in creditors. Depreciation is charged on a consistent basis with similar owned assets or over the lease term if shorter. The interest element of the lease payment is charged to the income statement on a basis which produces a consistent rate of charge over the period of the liability.

Taxation

The tax charge comprises current and deferred tax. Income tax expense is recognised in the income statement unless it relates to items recognised directly in equity or in other comprehensive income, when it is also recognised in equity or other comprehensive income respectively. Current tax is the expected tax payable on the profit for the year and any adjustments in respect of previous years using tax rates enacted or substantively enacted at the reporting date. Deferred tax is recognised using the balance sheet liability method, providing for temporary differences arising between the tax base of assets and liabilities, and their carrying amounts in the accounts. Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax is provided using rates of tax that have been enacted or substantively enacted at the balance sheet date or the date that the temporary differences are expected to reverse. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Share capital

When share capital recognised as equity is repurchased, the amount of the consideration paid, including directly attributable costs, is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity.

Share options granted to subsidiary employees

The Parent Company grants share options over its own Ordinary shares directly to employees of subsidiary companies. These employees provide services to the subsidiary companies. The cost of these shares is not recharged and therefore the fair value of the share options granted is recognised as a capital contribution to the subsidiary companies. This is accounted for as an increase in investments with a corresponding increase in a non-distributable component of equity.

2 Segmental reporting

As required by IFRS 8, Operating Segments, the following segmental information is presented in a consistent format with management information considered by the Board.

Analysis by location of operation
2012

	Gross revenue £000	Inter-segment revenue £000	Revenue £000	Total operating profit £000	Adjusted operating profit £000	Adjusted operating margin %
Europe, Middle East & Africa	272,342	39,509	232,833	29,951	36,691	15.8%
Asia Pacific	170,548	3,645	166,903	43,816	43,933	26.3%
Americas	143,040	5,524	137,516	24,398	26,249	19.1%
Steam Specialties business	585,930	48,678	537,252	98,165	106,873	19.9%
Watson-Marlow	124,958	487	124,471	34,975	36,798	29.6%
Corporate expenses				(7,426)	(7,426)	
	710,888	49,165	661,723	125,714	136,245	20.6%
Intra Group	(49,165)	(49,165)				
Total	**661,723**	**–**	**661,723**	**125,714**	**136,245**	**20.6%**

2011

	Gross revenue £000	Inter-segment revenue £000	Revenue £000	Total operating profit £000	Adjusted operating profit £000	Adjusted operating margin %
Europe, Middle East & Africa	291,440	41,335	250,105	41,754	42,461	17.0%
Asia Pacific	152,813	5,712	147,101	37,795	37,795	25.7%
Americas	141,661	7,283	134,378	25,686	27,397	20.4%
Steam Specialties business	585,914	54,330	531,584	105,235	107,653	20.3%
Watson-Marlow	119,391	984	118,407	32,379	34,423	29.1%
Corporate expenses				(8,116)	(8,116)	
	705,305	55,314	649,991	129,498	133,960	20.6%
Intra Group	(55,314)	(55,314)				
Total	**649,991**	**–**	**649,991**	**129,498**	**133,960**	**20.6%**

Net revenue generated by Group companies based in the USA is £114,472,000 (2011: £109,807,000), in the UK £64,281,000 (2011: £66,091,000) and the rest of the world £482,970,000 (2011: £474,093,000).

The total operating profit for the period includes non-operational items, as analysed below:

2012

	Exceptional restructuring costs £000	Release of deferred consideration accrual on acquisition £000	Amortisation of acquisition-related intangible assets £000	Acquisition and disposal costs £000	Total £000
Europe, Middle East & Africa	(6,667)	647	(488)	(232)	(6,740)
Asia Pacific	(117)	–	–	–	(117)
Americas	(203)	–	(1,624)	(24)	(1,851)
Steam Specialties business	(6,987)	647	(2,112)	(256)	(8,708)
Watson-Marlow	(205)	–	(1,618)	–	(1,823)
	(7,192)	**647**	**(3,730)**	**(256)**	**(10,531)**

The exceptional restructuring costs, primarily in Europe, relate to cost reduction actions to reduce the underlying cost base in markets experiencing persistently difficult economic conditions.

2 Segmental reporting

2011

	Amortisation of acquisition-related intangible assets £000	Acquisition and disposal costs £000	Total £000
Europe, Middle East & Africa	(458)	(249)	(707)
Asia Pacific	–	–	–
Americas	(1,711)	–	(1,711)
Steam Specialties business	(2,169)	(249)	(2,418)
Watson-Marlow	(1,875)	(169)	(2,044)
	(4,044)	**(418)**	**(4,462)**

Share of profit of associates

	2012 Adjusted £000	2012 Total £000	2011 Adjusted £000	2011 Total £000
Europe, Middle East & Africa	–	–	–	–
Asia Pacific	1,873	1,549	2,132	1,766
Americas	–	–	–	–
Steam Specialties business	1,873	1,549	2,132	1,766
Watson-Marlow	–	–	–	–
	1,873	**1,549**	**2,132**	**1,766**

Net financing income and expense

	2012 £000	2011 £000
Europe, Middle East & Africa	(1,522)	1,140
Asia Pacific	422	(117)
Americas	394	312
Steam Specialties business	(706)	1,335
Watson-Marlow	(213)	(531)
Corporate	1,308	273
	389	**1,077**

Net assets

	2012 Assets £000	2012 Liabilities £000	2011 Assets £000	2011 Liabilities £000
Europe, Middle East & Africa	216,461	(98,547)	225,513	(99,655)
Asia Pacific	115,314	(20,430)	109,098	(17,282)
Americas	108,264	(30,841)	112,203	(35,082)
Watson-Marlow	97,852	(15,814)	97,376	(14,320)
	537,891	(165,632)	544,190	(166,339)
Liabilities	(165,632)		(166,339)	
Deferred tax	23,696		19,476	
Current tax payable	(11,082)		(9,476)	
Net Cash	51,676		12,269	
Net assets	**436,549**		**400,120**	

Non-current assets in the UK were £84,188,000 (2011: £78,123,000).

2 Segmental reporting continued

Capital additions and depreciation, amortisation and impairment

	2012		2011	
	Capital additions £000	Depreciation, amortisation and impairment £000	Capital additions £000	Depreciation, amortisation and impairment £000
Europe, Middle East & Africa	16,609	10,067	22,945	6,834
Asia Pacific	7,363	4,251	7,894	3,468
Americas	7,224	5,872	10,260	5,803
Watson-Marlow	5,360	4,781	5,038	4,723
	36,556	**24,971**	**46,137**	**20,828**

Capital additions include property, plant and equipment of £24,607,000 (2011: £39,662,000) and other intangible assets of £11,949,000 (2011: £6,475,000) of which £2,406,000 (2011: £214,000) relates to acquired intangibles from acquisitions in the period. Capital additions split between the UK and rest of the world are UK £16,328,000 (2011: £20,031,000), rest of the world £20,228,000 (2011: £26,106,000). Depreciation, amortisation and impairment includes the profit on disposal of fixed assets of £273,000 (2011: £2,948,000).

3 Operating costs

	2012 Adjusted £000	Total £000	2011 Adjusted £000	Total £000
Change in stocks of finished goods and work in progress	7,088	7,088	(12,068)	(12,068)
Raw materials and consumables	173,477	173,477	193,825	193,825
Staff costs (note 4)	220,761	227,953	220,113	220,113
Depreciation, amortisation and impairment	21,241	24,971	16,784	20,828
Other operating charges	102,911	102,520	97,377	97,795
	525,478	**536,009**	**516,031**	**520,493**

Total depreciation and amortisation includes amortisation of acquisition-related intangible assets of £3,730,000 (2011: £4,044,000). Operating costs include exchange difference costs of £1,031,000 (2011: £953,000). Other operating charges include acquisition and disposal costs of £256,000 (2011: £418,000).

4 Staff costs and numbers

The aggregate payroll costs of persons employed by the Group were as follows:

	2012 £000	2011 £000
Wages and salaries	183,031	175,260
Social security costs	30,898	31,253
Other pension costs	14,024	13,600
	227,953	**220,113**

The average number of persons employed by the Group (including Directors) during the year was as follows:

	2012 Number	2011 Number
United Kingdom	1,292	1,319
Overseas	3,414	3,364
	4,706	**4,683**

5 Net financing income and expense

	2012 £000	2011 £000
Financial expenses		
Bank and other borrowing interest payable	(1,478)	(1,381)
Interest on pension scheme liabilities	(15,382)	(16,134)
	(16,860)	(17,515)
Financial income		
Bank interest receivable	1,272	1,048
Expected return on pension scheme assets	15,977	17,544
	17,249	18,592
Net financing income	**389**	**1,077**
Net pension scheme financial income	595	1,410
Net bank interest	(206)	(333)
Net financing income	**389**	**1,077**

6 Profit before taxation

Profit before taxation is shown after charging:

	2012 £000	2011 £000
Depreciation of tangible fixed assets held under finance leases	106	42
Hire of plant and machinery	672	660
Other operating leases	4,765	5,228
R&D	8,990	8,726

Auditor's remuneration	2012 £000	2011 £000
Audit of these financial statements	127	124
Amounts receivable by the Company's auditor and its associates in respect of:		
Audit of financial statements of subsidiaries of the Company	1,082	952
Audit related assurance services	54	57
Taxation compliance services	289	293
Other tax advisory services	122	356
All other services	113	45
	1,787	**1,827**

7 Directors' emoluments

Directors represent the key management personnel of the Group under the terms of IAS 24: Related Party Disclosures. Total remuneration is shown below.

Further details of salaries and short-term benefits, post-retirement benefits and share plans and long-term share incentive plans are shown in the Directors' Remuneration Report on pages 60 to 74. The share-based payments charge comprises a charge in relation to the Performance Share Plan and the Employee Share Ownership Plan (as described in note 27 on page 115).

	2012 £000	2011 £000
Salaries and short-term benefits	2,338	2,543
Post-retirement benefits	234	306
Share-based payments	800	769
Total	**3,372**	3,618

8 Taxation

	2012 £000	2011 £000
Analysis of charge in period		
UK corporation tax		
Current tax on income for the period	750	796
Adjustments in respect of prior periods	621	(231)
	1,371	565
Double taxation relief	(750)	(796)
	621	(231)
Foreign tax		
Current tax on income for the period	38,018	35,562
Adjustments in respect of prior periods	(455)	2
	37,563	35,564
Total current tax charge	38,184	35,333
Deferred tax – UK	(1,219)	(491)
Deferred tax – Foreign	442	4,261
Tax on profit on ordinary activities	**37,407**	**39,103**

Reconciliation of effective tax rate

	2012 £000	2011 £000
Profit before tax	**127,652**	**132,341**
Tax using the UK corporation tax rate of 24.5% (2011: 26.5%)	31,274	35,069
Effect of higher/(lower) overseas tax rates	5,618	4,115
Associated companies	(379)	(468)
Non-deductible expenditure	1,666	785
Overprovided in prior years	(687)	(229)
Other reconciling items	(85)	(169)
Total tax in income statement	**37,407**	**39,103**

The Group's tax charge in future years is likely to be affected by the proportion of profits arising and the effective tax rates in the various territories in which the Group operates.

The UK corporation tax charge is calculated after deducting tax allowable deficit reduction cash contributions to the UK post-retirement benefit schemes of £7,500,000 (2011: £7,900,000) covering all employees in the UK defined benefit schemes.

The Government's autumn statement on 5th December 2012 announced that the UK corporation tax rate will reduce to 21% by 2014. A reduction in the rate from 26% to 25% (effective from 1st April 2012) was substantively enacted on 5th July 2011, and further reductions to 24% (effective from 1st April 2012) and 23% (effective from 1st April 2013) were substantively enacted on 26th March 2012 and 3rd July 2012 respectively. This will reduce the company's future current tax charge accordingly. The deferred tax asset at 31st December 2012 has been calculated based on the rate of 23% substantively enacted at the balance sheet date. It has not yet been possible to quantify the full anticipated effect of the announced further 2% rate reduction, although this will further reduce the Company's future current tax charge and reduce the Company's deferred tax asset accordingly.

No UK tax (after double tax relief for underlying tax) is expected to be payable on the future remittance of the retained earnings of overseas subsidiaries.

9 Profit for the financial year attributable to shareholders

Profit dealt with in the accounts of Spirax-Sarco Engineering plc was £14,120,000 (2011: £96,643,000). Dividends from subsidiary undertakings of £16,500,000 (2011: £99,000,000) and dividends from associate companies of £1,454,000 (2011: £1,461,000) are included in this amount.

10 Earnings per share

	2012 £000	2011 £000
Profit attributable to equity shareholders	**90,041**	**93,049**
Weighted average shares in issue	77,905,823	77,557,190
Dilution	913,544	1,016,946
Diluted weighted average shares in issue	**78,819,367**	**78,574,136**
Basic earnings per share	**115.6p**	**120.0p**
Diluted earnings per share	**114.2p**	**118.4p**
Adjusted profit attributable to equity shareholders	**97,836**	**96,765**
Basic adjusted earnings per share	**125.6p**	**124.8p**
Diluted adjusted earnings per share	**124.1p**	**123.2p**

The dilution is in respect of unexercised share options and the Performance Share Plan.

11 Dividends

	2012 £000	2011 £000
Amounts paid in the year		
Final dividend for the year ended 31st December 2011 of 34.2p (2010: 30.0p) per share	26,640	23,213
Special dividend for the year ended 31st December 2011 of nil (2010: 25.0p) per share	–	19,383
Interim dividend for the year ended 31st December 2012 of 16.0p (2011: 14.8p) per share	12,486	11,493
	39,126	**54,089**
Amounts arising in respect of the year		
Interim dividend for the year ended 31st December 2012 of 16.0p (2011: 14.8p) per share	12,486	11,493
Proposed final dividend for the year ended 31st December 2012 of 37.0p (2011: 34.2p) per share	28,893	26,579
Proposed special dividend for the year ended 31st December 2012 of 100.0p (2011: nil) per share	78,090	–
	119,469	**38,072**

The proposed final dividend and special dividend are subject to approval by shareholders at the Annual General Meeting and have not been included as a liability in these accounts.

12 Property, plant and equipment

	The Group				
	Land and buildings				
	Freehold £000	Leasehold £000	Plant and machinery £000	Fixtures, fittings, tools and equipment £000	Total £000
Cost or deemed cost:					
At 1st January 2011	97,810	16,365	133,557	61,546	309,278
Exchange adjustments	(1,539)	839	(1,589)	(628)	(2,917)
	96,271	17,204	131,968	60,918	306,361
Additions	11,836	847	20,238	6,741	39,662
Disposals	(1,574)	(55)	(8,643)	(3,941)	(14,213)
At 31st December 2011	**106,533**	**17,996**	**143,563**	**63,718**	**331,810**
Depreciation:					
At 1st January 2011	18,170	451	90,739	44,365	153,725
Exchange adjustments	(344)	12	(1,060)	(574)	(1,966)
	17,826	463	89,679	43,791	151,759
Charged in year	1,735	374	9,745	4,878	16,732
Disposals	(374)	(10)	(7,298)	(3,647)	(11,329)
At 31st December 2011	**19,187**	**827**	**92,126**	**45,022**	**157,162**
Net book value:					
At 31st December 2011	**87,346**	**17,169**	**51,437**	**18,696**	**174,648**

12 Property, plant and equipment continued

	The Group				
	Land and buildings				
	Freehold £000	Leasehold £000	Plant and machinery £000	Fixtures, fittings, tools and equipment £000	Total £000
Cost or deemed cost:					
At 1st January 2012	106,533	17,996	143,563	63,718	331,810
Exchange adjustments	(1,871)	(588)	(2,737)	(1,234)	(6,430)
	104,662	17,408	140,826	62,484	325,380
Additions	4,385	1,239	10,556	8,427	24,607
Disposals	(1,577)	(179)	(9,481)	(6,318)	(17,555)
At 31st December 2012	**107,470**	**18,468**	**141,901**	**64,593**	**332,432**
Depreciation:					
At 1st January 2012	19,187	827	92,126	45,022	157,162
Exchange adjustments	(347)	(7)	(1,137)	(836)	(2,327)
	18,840	820	90,989	44,186	154,835
Charged in year	1,835	552	10,245	5,213	17,845
Disposals	(405)	(64)	(8,463)	(6,152)	(15,084)
At 31st December 2012	**20,270**	**1,308**	**92,771**	**43,247**	**157,596**
Net book value:					
At 31st December 2012	**87,200**	**17,160**	**49,130**	**21,346**	**174,836**

Included in the above are finance leases with a net book value of £1,728,000 (2011: £354,568).

13 Goodwill and other intangible assets

	The Group				
	Acquired intangibles £000	Development £000	Software and other intangibles £000	Total intangibles £000	Goodwill £000
Cost or valuation:					
At 1st January 2011	40,886	13,395	22,681	76,962	45,125
Exchange adjustments	(2,168)	(43)	(262)	(2,473)	1,109
	38,718	13,352	22,419	74,489	46,234
Additions	214	2,727	3,534	6,475	140
Disposals	–	–	(213)	(213)	–
At 31st December 2011	**38,932**	**16,079**	**25,740**	**80,751**	**46,374**
Amortisation:					
At 1st January 2011	9,149	8,299	17,417	34,865	1,140
Exchange adjustments	(585)	(28)	(252)	(865)	(113)
	8,564	8,271	17,165	34,000	1,027
Charged/impairment in year	4,044	1,523	1,477	7,044	–
Disposals	–	–	(196)	(196)	–
At 31st December 2011	**12,608**	**9,794**	**18,446**	**40,848**	**1,027**
Net book value:					
At 31st December 2011	**26,324**	**6,285**	**7,294**	**39,903**	**45,347**

13 Goodwill and other intangible assets continued

	The Group				
	Acquired intangibles £000	Development £000	Software and other intangibles £000	Total intangibles £000	Goodwill £000
Cost or valuation:					
At 1st January 2012	38,932	16,079	25,740	80,751	46,374
Exchange and other adjustments	(2,137)	(261)	(423)	(2,821)	(783)
	36,795	15,818	25,317	77,930	45,591
Additions	2,406	2,892	6,651	11,949	1,243
Disposals/impairment	–	(272)	(262)	(534)	–
At 31st December 2012	**39,201**	**18,438**	**31,706**	**89,345**	**46,834**
Amortisation:					
At 1st January 2012	12,608	9,794	18,446	40,848	1,027
Exchange adjustments	(1,786)	(131)	(277)	(2,194)	(48)
	10,822	9,663	18,169	38,654	979
Amortisation and impairment	3,730	1,794	1,875	7,399	–
Disposals	–	(178)	(241)	(419)	–
At 31st December 2012	**14,552**	**11,279**	**19,803**	**45,634**	**979**
Net book value:					
At 31st December 2012	**24,649**	**7,159**	**11,903**	**43,711**	**45,855**

Development
All capitalised development costs arise from internal product development.

Acquired intangibles
The disclosure by class of acquired intangible assets is shown in the tables below.

	The Group				
	Customer relationships £000	Brand names and trademarks £000	Manufacturing designs and core technology £000	Non-compete undertakings and other £000	Total acquired intangibles £000
Cost or valuation:					
At 1st January 2011	25,327	7,196	5,981	2,382	40,886
Exchange and other adjustments	(1,368)	(365)	(325)	(110)	(2,168)
	23,959	6,831	5,656	2,272	38,718
Additions	107	–	–	107	214
Disposals/impairment	–	–	–	–	–
At 31st December 2011	**24,066**	**6,831**	**5,656**	**2,379**	**38,932**
Amortisation:					
At 1st January 2011	4,832	1,561	1,472	1,284	9,149
Exchange adjustments	(349)	(98)	(96)	(42)	(585)
	4,483	1,463	1,376	1,242	8,564
Amortisation and impairment	1,841	1,089	579	535	4,044
Disposals	–	–	–	–	–
At 31st December 2011	**6,324**	**2,552**	**1,955**	**1,777**	**12,608**
Net book value:					
At 31st December 2011	**17,742**	**4,279**	**3,701**	**602**	**26,324**

13 Goodwill and other intangible assets continued

	The Group				
	Customer relationships £000	Brand names and trademarks £000	Manufacturing designs and core technology £000	Non-compete undertakings and other £000	Total acquired intangibles £000
Cost or valuation:					
At 1st January 2012	24,066	6,831	5,656	2,379	38,932
Exchange and other adjustments	(1,348)	(357)	(324)	(108)	(2,137)
	22,718	6,474	5,332	2,271	36,795
Additions	1,370	–	330	706	2,406
Disposals/impairment	–	–	–	–	–
At 31st December 2012	**24,088**	**6,474**	**5,662**	**2,977**	**39,201**
Amortisation:					
At 1st January 2012	6,324	2,552	1,955	1,777	12,608
Exchange adjustments	(906)	(315)	(298)	(267)	(1,786)
	5,418	2,237	1,657	1,510	10,822
Amortisation and impairment	1,233	810	917	770	3,730
Disposals	–	–	–	–	–
At 31st December 2012	**6,651**	**3,047**	**2,574**	**2,280**	**14,552**
Net book value:					
At 31st December 2012	**17,437**	**3,427**	**3,088**	**697**	**24,649**

Impairment

In accordance with the requirements of IAS 36, Impairment of Assets, goodwill is allocated to the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the business combination that gave rise to the goodwill as analysed in the table below.

	2012 Goodwill £000	2011 Goodwill £000
Spirax-Sarco Mexicana	8,874	8,636
Flexicon A/S Denmark	7,691	7,955
MasoSine	6,890	7,064
Spirax Sarco Inc USA	3,155	3,325
M & M product unit	2,971	3,047
Alitea product unit	2,614	2,594
UK Supply product unit	1,929	1,977
Spirax Inter Valf Turkey	1,803	1,783
Spirax-Sarco S A S France	1,301	1,334
Watson-Marlow South Africa	1,098	1,206
Other cash-generating units	7,529	6,426
	45,855	**45,347**

13 Goodwill and other intangible assets continued

The goodwill balance has been tested for annual impairment on the following basis:

- The carrying values of goodwill have been assessed by reference to value in use. These have been estimated using cash flows based on forecast information for the next financial year which has been approved by the Board and in the case of recent acquisitions on detailed annual forecasts
- The key assumptions on which the impairment tests are based are the discount and growth rates and the forecast cash flows
- Pre-tax discount rates range from 10–13%
- Growth rates vary between 3-10% depending on detailed forecasts
- No impairments were identified as a result of this exercise.

The principal value in use assumptions for the Spirax-Sarco Mexicana S A goodwill balance were as follows:

- Long-term revenue growth of 5–6%
- Pre-tax discount rate of 13%.

The principal value in use assumptions for the Flexicon A/S Denmark goodwill balance were as follows:

- Long-term revenue growth of 4–5%
- Pre-tax discount rate of 13%.

The principal value in use assumptions for the MasoSine goodwill balance were as follows:

- Long-term revenue growth of 2.5–3.5%
- Pre-tax discount rate of 13%.

Sensitivity analysis shows that if long-term revenue growth assumptions are lowered by 1% and pre-tax discount rates raised by 1%, no impairment would arise.

14 Loans to subsidiaries

	Parent Company	
	2012 £000	2011 £000
Cost:		
At 1st January	75,198	32,193
(Repayment)/loans	(10,001)	43,005
At 31st December	65,197	75,198
Amounts written off:		
At 1st January and 31st December	(1,042)	(1,042)
Net book value:		
At 31st December	**64,155**	**74,156**

15 Investment in subsidiaries

	Parent Company 2012 £000	Parent Company 2011 £000
Cost:		
At 1st January	48,883	48,242
Share options issued to subsidiary company employees	768	641
At 31st December	49,651	48,883
Amounts written off:		
At 1st January and 31st December	(994)	(994)
Net book value:		
At 31st December	**48,657**	**47,889**

Investments are stated at cost less provisions for any impairment in value.

Details relating to subsidiary undertakings are given on the inside back cover. Except where stated all classes of shares were 100% owned by the Group at 31st December 2012. The country of incorporation of the principal Group companies is the same as the country of operation with the exception of companies operating in the United Kingdom which are incorporated in Great Britain. Eirdata Environmental Services Ltd is incorporated in the Republic of Ireland. All are in the fluid control business except Spirax-Sarco Investments Ltd, Spirax-Sarco Overseas Ltd, Spirax-Sarco America Ltd, Sarco International Corp, Watson-Marlow Bredel Holdings BV, Spirax-Sarco Engineering SL, Spirax-Sarco Engineering BV and Spirax-Sarco Investments BV which are investment holding companies.

16 Investment in associate

	The Group 2012 £000	The Group 2011 £000
Cost of investment	3,194	3,194
Share of retained profit	4,508	5,086
	7,702	**8,280**

Summarised aggregated financial information (total business)

	2012 £000	2011 £000
Revenue	22,379	24,063
Profit for the period	3,802	4,327
Assets	14,324	13,945
Liabilities	3,309	2,432

Details of the Group's associate at 31st December 2012 are as follows:

Name of associate	Country of incorporation and operation	Proportion of ownership interest and voting power held	Principal activity
Spirax-Marshall Ltd	India	49.3%	Manufacturing and selling

17 Deferred tax assets and liabilities

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	The Group					
	Assets		Liabilities		Net	
	2012 £000	2011 £000	**2012 £000**	2011 £000	**2012 £000**	2011 £000
Accelerated capital allowances	1,855	1,258	(5,433)	(5,873)	(3,578)	(4,615)
Provisions	5,299	4,661	(185)	(91)	5,114	4,570
Losses	4,470	3,275	(36)	–	4,434	3,275
Inventory	3,017	2,888	(1,658)	(1,565)	1,359	1,323
Pensions	23,854	21,999	(2,374)	(1,339)	21,480	20,660
Other temporary differences	2,204	3,336	(7,317)	(9,073)	(5,113)	(5,737)
Tax assets/(liabilities)	**40,699**	**37,417**	**(17,003)**	**(17,941)**	**23,696**	**19,476**

Movement in deferred tax during the year
2011

	The Group					
	1st January 2011 £000	Recognised in income £000	Recognised in OCI £000	Recognised in equity £000	Acquisitions £000	31st December 2011 £000
Accelerated capital allowances	(5,323)	726	(18)	–	–	(4,615)
Provisions	8,475	(3,606)	(299)	–	–	4,570
Losses	1,510	1,847	(82)	–	–	3,275
Inventory	(602)	1,914	11	–	–	1,323
Pensions	17,584	(2,700)	5,776	–	–	20,660
Other temporary differences	(120)	(1,951)	28	(578)	(3,116)	(5,737)
	21,524	**(3,770)**	**5,416**	**(578)**	**(3,116)**	**19,476**

2012

	The Group					
	1st January 2012 £000	**Recognised in income £000**	**Recognised in OCI £000**	**Recognised in equity £000**	**Acquisitions £000**	**31st December 2012 £000**
Accelerated capital allowances	(4,615)	1,040	(3)			(3,578)
Provisions	4,570	550	(6)			5,114
Losses	3,275	1,108	51			4,434
Inventory	1,323	35	1			1,359
Pensions	20,660	(1,646)	2,466			21,480
Other temporary differences	(5,737)	(310)	(50)	1,011	(27)	(5,113)
	19,476	**777**	**2,459**	**1,011**	**(27)**	**23,696**

17 Deferred tax assets and liabilities continued

Movement in deferred tax during the year

2011

	Parent Company			
	1st January 2011 £000	Recognised in income £000	Recognised in equity £000	31st December 2011 £000
Other temporary differences	424	(371)	1	54
	424	**(371)**	**1**	**54**

2012

	Parent Company			
	1st January 2012 £000	**Recognised in income £000**	**Recognised in equity £000**	**31st December 2012 £000**
Other temporary differences	54	864	(94)	824
	54	**864**	**(94)**	**824**

18 Inventories

	The Group	
	2012 £000	2011 £000
Raw materials and consumables	35,650	39,657
Work in progress	17,308	23,318
Finished goods and goods for resale	50,732	53,350
	103,690	**116,325**

19 Other current assets

	The Group		**Parent Company**	
	2012 £000	2011 £000	**2012 £000**	2011 £000
Other receivables	8,877	8,770	–	–
Prepayments and accrued income	7,311	8,284	255	44
	16,188	**17,054**	**255**	**44**

20 Trade and other payables

	The Group		**Parent Company**	
	2012 £000	2011 £000	**2012 £000**	2011 £000
Trade payables	27,529	30,287	–	–
Bills of exchange payable	221	580	–	–
Social security	4,190	4,891	–	–
Other payables	30,285	24,459	347	176
Accruals	28,244	28,415	463	1,561
	90,469	**88,632**	**810**	**1,737**

21 Obligations under finance leases

	The Group			
	Minimum lease payments		Present value lease payments	
	2012 £000	2011 £000	2012 £000	2011 £000
Amount payable				
Within 1 year	510	73	485	65
1–5 years inclusive	911	84	850	81
After 5 years	–	–	–	–
	1,421	157	1,335	146
Add future finance charges			86	11
Minimum lease payments	1,421	157	1,421	157
Less: Due for settlement in <1 year	510	65	510	65
Due for settlement in >1 year	911	92	911	92

22 Provisions

	The Group	
	Warranty and other provisions	
	2012 £000	2011 £000
Provisions at 1st January	1,509	912
Exchange adjustments	(70)	27
	1,439	939
Change in the year	(448)	570
Provisions at 31st December	**991**	**1,509**

Provisions include non-current product warranties charged against profit from operations that are expected to be incurred after 2012.

23 Called up share capital and reserves

	The Group		Parent Company	
	2012 £000	2011 £000	2012 £000	2011 £000
Ordinary shares of 25p each:				
Authorised 120,000,000	30,000	30,000	30,000	30,000
Allotted, called up and fully paid 78,089,826 (2011: 77,674,152)	19,536	19,418	19,536	19,418

415,674 shares were issued pursuant to the Spirax-Sarco Engineering Share Schemes for a consideration of £4,028,000 received by the Company.

At 31st December no treasury shares were available for use in connection with the Group's Employee Share Schemes.

150 senior employees of the Group have been granted options on ordinary shares under the Share Option Scheme and Performance Share Plan (details in note 27).

Other reserves in the Consolidated statement of changes in equity on page 87 are made up as follows:

	2012 £000	2011 £000
Translation reserve	26,617	37.929
Cash flow hedge reserve	(351)	(353)
Capital redemption reserve	1,832	1.832
Total other reserves	**28,098**	**39,408**

Translation reserve
The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries, including gains or losses on net investment hedges.

Cash flow hedge reserve
The reserve records the cumulative net change in the fair value of forward exchange contracts where they are designated as effective cash flow hedge relationships.

Capital redemption reserve
This reserve records the historical repurchase of the Group's own shares.

24 Return on capital employed

	The Group 2012 £000	The Group 2011 £000
Capital employed		
Property, plant and equipment	174,836	174,648
Prepayments	223	148
Inventories	103,690	116,325
Trade receivables	145,686	142,484
Other current assets	16,188	17,054
Tax recoverable	1,317	1,973
Trade and other payables	(90,469)	(88,632)
Current tax payable	(12,399)	(11,449)
Capital employed	**339,072**	**352,551**
Average capital employed	**345,812**	**325,647**
Operating profit	125,714	129,498
Adjustments (note 2)	10,531	4,462
Adjusted operating profit	**136,245**	**133,960**
Return on capital employed	**39.4%**	**41.1%**

25 Capital commitments

	The Group 2012 £000	The Group 2011 £000	Parent Company 2012 £000	Parent Company 2011 £000
Capital expenditure contracted for but not provided	1,883	1,709	–	–

26 Operating lease obligations

	The Group 2012 £000	The Group 2011 £000
Commitments under non-cancellable leases due as follows:		
Within 1 year	4,471	3,795
1–5 years inclusive	9,783	6,676
After 5 years	282	869
	14,536	**11,340**

Operating leases are primarily in respect of property, plant and equipment.

27 Employee benefits

Pension plans – The Group

The Group is accounting for pension costs in accordance with International Accounting Standard 19.

The disclosures shown here are in respect of the Group's Defined Benefit Obligations. Other plans operated by the Group were either Defined Contribution plans or were deemed immaterial for the purposes of IAS 19 reporting.

The total expense relating to the Group's Defined Contribution pension plans in the current year was £6,832,000 (2011: £6,809,000).

Of the Defined Benefit plans, the plans in the UK and USA hold most of the liability. The post-retirement mortality assumptions in respect of these plans may therefore be considered material. The main UK scheme assumes that post-retirement mortality follows the SAPS standard tables, with improvements based on the 2009 CMI Core Projections with a 1.5% long-term trend. This basis gives a life expectancy of 23 years and 25 years respectively for a male and female currently aged 65. These figures reflect the generally recognised trend of increased longevity. The USA schemes use the RP-2000 BC mortality table with AA scale projected for 12 years. Life expectancy under this table is 18 years and 20 years respectively for a male and female currently aged 65. These assumptions are regularly reviewed in light of scheme specific experience and more widely available statistics.

The financial assumptions used at 31st December were:

	Assumptions weighted by value of liabilities % per annum			
	UK pensions		Overseas pensions and medical	
	2012	2011	**2012**	2011
Rate of increase in salaries	3.6	3.8	3.3	3.3
Rate of increase in pensions	2.8	2.9	1.7	1.6
Rate of price inflation	2.9	3.1	2.3	2.7
Discount rate	4.6	5.0	3.7	4.4
Medical trend rate			5.0	5.0

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions which, due to the timescale covered, may not necessarily be borne out in practice.

	Assumptions weighted by value of assets % per annum			
	UK pensions		Overseas pensions and medical	
	2012	2011	**2012**	2011
Expected rate of return on assets (weighted average)	6.2	7.2	7.3	7.4
Equities	7.5	7.9	8.3	8.3
Bonds	3.1	4.6	2.9	3.2
Other	6.1	6.5	7.9	7.3

The market value of the schemes' assets, which are not intended to be realised in the short-term and may be subject to significant change before they are realised, at 31st December 2012 were:

	UK pensions		Overseas pensions and medical		Total	
	2012 £000	2011 £000	**2012 £000**	2011 £000	**2012 £000**	2011 £000
Equities	161,735	150,261	20,076	17,210	181,811	167,471
Bonds	76,448	64,411	9,311	6,616	85,760	71,027
Other	11,485	9,174	1,547	3,730	13,031	12,904
Total market value in aggregate	**249,668**	**223,846**	**30,934**	**27,556**	**280,602**	**251,402**

The actual return on plan assets was £26.0 million (2011: £5.5 million).

27 Employee benefits continued

The amounts recognised in the consolidated balance sheet are determined as follows:

	UK pensions		Overseas pensions and medical		Total	
	2012 £000	2011 £000	2012 £000	2011 £000	2012 £000	2011 £000
Fair value of schemes' assets	249,668	223,846	30,934	27,556	280,602	251,402
Present value of funded schemes' liabilities	(288,566)	(262,590)	(47,879)	(46,448)	(336,445)	(309,038)
(Deficit) in the funded schemes	(38,898)	(38,744)	(16,945)	(18,892)	(55,843)	(57,636)
Present value of unfunded schemes' liabilities	–	–	(16,820)	(14,289)	(16,820)	(14,289)
Retirement benefit liability recognised in the balance sheet	(38,898)	(38,744)	(33,765)	(33,181)	(72,663)	(71,925)
Related deferred tax asset	9,335	9,686	10,924	10,646	20,259	20,332
Net pension liability	**(29,563)**	**(29,058)**	**(22,841)**	**(22,535)**	**(52,404)**	**(51,593)**

The movements in the Defined Benefit Obligation (DBO) recognised in the balance sheet during the year were:

	UK pensions		Overseas pensions and medical		Total	
	2012 £000	2011 £000	2012 £000	2011 £000	2012 £000	2011 £000
Defined benefit obligation at beginning of year	(262,590)	(250,918)	(60,737)	(52,420)	(323,327)	(303,338)
Current service cost	(5,426)	(5,097)	(1,766)	(1,694)	(7,192)	(6,791)
Interest cost	(12,884)	(13,567)	(2,498)	(2,567)	(15,382)	(16,134)
Contributions by members	(650)	(603)	0	–	(650)	(603)
Actuarial (loss)/gain	(16,773)	(12,841)	(4,921)	349	(21,694)	(12,492)
Actual benefit payments	9,846	8,529	2,784	2,124	12,630	10,653
Settlement, curtailment	–	–	–	–	–	–
Experience (loss)/gain	(89)	11,907	(37)	(6,110)	(126)	5,797
Currency (loss)/gain	–	–	2,476	(419)	2,476	(419)
Defined benefit obligation at end of year	**(288,566)**	**(262,590)**	**(64,699)**	**(60,737)**	**(353,265)**	**(323,327)**

The movements in the fair value of plan assets during the year were:

	UK pensions		Overseas pensions and medical		Total	
	2012 £000	2011 £000	2012 £000	2011 £000	2012 £000	2011 £000
Value of assets at beginning of year	223,846	212,604	27,557	27,306	251,403	239,910
Expected return on assets	13,997	15,575	1,980	1,969	15,977	17,544
Actuarial gain/(loss)	8,571	(8,973)	1,431	(3,068)	10,002	(12,041)
Contributions paid by employer	12,450	12,566	3,990	3,227	16,440	15,793
Contributions paid by members	650	603	–	–	650	603
Actual benefit payments	(9,846)	(8,529)	(2,784)	(2,124)	(12,630)	(10,653)
Settlement, curtailment	–	–	–	–	–	–
Currency gain/(loss)	–	–	(1,240)	246	(1,240)	246
Value of assets at end of year	**249,668**	**223,846**	**30,934**	**27,556**	**280,602**	**251,402**

The estimated employer contributions to be made in 2013 are £15,137,000.

27 Employee benefits continued

The history of experience adjustments is as follows:

	2012 £000	2011 £000	2010 £000	2009 £000	2008 £000
Defined benefit obligation at end of year	(353,265)	(323,327)	(303,338)	(284,910)	(244,159)
Fair value of schemes' assets	280,602	251,402	239,910	211,147	170,442
Retirement benefit liability recognised in the balance sheet	(72,663)	(71,925)	(63,428)	(73,763)	(73,717)
Experience adjustment on schemes' liabilities	(126)	5,797	(984)	(1,695)	(11,140)
As a percentage of schemes' liabilities	0.0%	1.8%	0.3%	0.6%	4.6%
Experience adjustment on schemes' assets	10,002	(12,041)	10,454	26,012	(60,771)
As a percentage of schemes' assets	3.6%	4.8%	4.4%	12.3%	35.7%

The expense recognised in the Group income statement was as follows:

	UK pensions		Overseas pensions and medical		Total	
	2012 £000	2011 £000	2012 £000	2011 £000	2012 £000	2011 £000
Current service cost	(5,426)	(5,097)	(1,766)	(1,694)	(7,192)	(6,791)
Settlement, curtailment and termination benefits	–	–	–	–	–	–
Interest on schemes' liabilities	(12,884)	(13,567)	(2,498)	(2,567)	(15,382)	(16,134)
Expected return on schemes' assets	13,997	15,575	1,980	1,969	15,977	17,544
Total expense recognised in income statement	**(4,313)**	**(3,089)**	**(2,284)**	**(2,292)**	**(6,597)**	**(5,381)**

The expense is recognised in the following line items in the Group income statement:

	2012 £000	2011 £000
Operating costs	(7,192)	(6,791)
Financial expenses	(15,382)	(16,134)
Financial income	15,977	17,544
Total expense recognised in income statement	**(6,597)**	**(5,381)**

Statement of comprehensive income (OCI)

	UK pensions		Overseas pensions and medical		Total	
	2012 £000	2011 £000	2012 £000	2011 £000	2012 £000	2011 £000
Actuarial amount recognised in OCI	(8,291)	(9,907)	(3,527)	(8,829)	(11,818)	(18,736)
Deferred tax on actuarial amount recognised in OCI	1,602	2,414	864	3,362	2,466	5,776
Cumulative loss recognised in OCI at beginning of year	(45,311)	(37,818)	(11,231)	(5,764)	(56,542)	(43,582)
Cumulative loss recognised in OCI at end of year	(52,000)	(45,311)	(13,894)	(11,231)	(65,894)	(56,542)

For the financial year commencing 1st January 2013, the Group will adopt IAS 19 revised 2011. On adoption the interest cost and expected return on assets disclosed in the Income Statement for all defined benefit pension plans will be based on discount rate assumptions. This is different from the IAS 19 standard used in these financial statements (IAS revised 2008) which uses discount rates to set the interest cost, but a return on assets assumption to calculate the expected return on assets. If IAS 19 revised 2011 had been used in the 2012 financial statements, the expected return on assets recognised in the Group Income Statement would have been £3,559,000 lower at £12,418,000.

The treatment of administrative and investment expenses under IAS 19 revised 2011 will also change. If IAS 19 revised 2011 had been used for the 2012 financial statements the current service charge cost recognised in the Group Income Statement would have been £114,000 higher at £7,306,000.

The changes under IAS 19 revised 2011 described above have no impact on the post-retirement benefits liability that is recognised in the Group Statement of Financial Position.

27 Employee benefits continued

Sensitivity analysis

The effect on the defined benefit obligation at 31st December 2012 of an increase or decrease in key assumptions is as follows:

	UK pensions £'000	Overseas pensions and medical £000	Total £000
Increase/(decrease) in pension deficit			
Discount rate assumption being 0.25% higher	(14,000)	(2,000)	(16,000)
Discount rate assumption being 0.25% lower	14,000	3,000	17,000
Inflation assumption being 0.25% higher	12,000	1,000	13,000
Inflation assumption being 0.25% lower	(11,000)	(1,000)	(12,000)

The effect of an increase of one percentage point and the effect of a decrease of one percentage point in the assumed medical trend rates is as follows:

	Overseas pensions and medical		Total	
	1% increase £000	Overseas 1% decrease £000	1% increase £000	Total 1% decrease £000
Aggregate of service cost and interest cost components of post-retirement medical plans	0	(0)	0	(0)
Accumulated post-employment benefit obligation for medical costs	23	(20)	23	(20)

Pension plans – Parent Company

The Parent Company is accounting for pension costs in accordance with International Accounting Standard 19.

The disclosures shown here are in respect of the Parent Company's Defined Benefit Obligations. Other plans operated by the Parent Company were Defined Contribution plans.

The total expense relating to the Parent Company's Defined Contribution pension plans in the current year was £29,163 (2011: £22,066).

The post-retirement mortality assumptions in respect of the Parent Company Defined Benefit Scheme follows the SAPS light tables, with improvements based on the 2009 CMI Core Projections with a 1.5% long-term trend. This basis gives a life expectancy of 24 years and 26 years respectively for a male and female currently aged 65. These figures reflect the generally recognised trend of increased longevity. These assumptions are regularly reviewed in light of scheme specific experience and more widely available statistics.

27 Employee benefits continued

The financial assumptions used at 31st December were:

	Assumptions weighted by value of liabilities % per annum	
	UK pensions	
	2012	2011
Rate of increase in salaries	3.6	4.6
Rate of increase in pensions	2.8	2.9
Rate of price inflation	2.9	3.1
Discount rate	4.6	5.0

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions, which, due to the timescale covered, may not necessarily be borne out in practice.

	Assumptions weighted by value of assets % per annum	
	UK pensions	
	2012	2011
Expected rate of return on assets (weighted average)	6.2	7.2
Equities	7.5	7.9
Bonds	3.1	4.6
Other	6.1	6.5

The market value of the scheme's assets, which are not intended to be realised in the short-term and may be subject to significant change before they are realised, at 31st December 2012 were:

	UK pensions	
	2012 £000	2011 £000
Equities	31,686	29,921
Bonds	14,799	12,722
Other	3,109	2,102
Total market value in aggregate	**49,594**	**44,745**

The actual return on plan assets was £4.5 million (2011: £0.7 million).

The amounts recognised in the consolidated statement of financial position are determined as follows:

	UK pensions	
	2012 £000	2011 £000
Fair value of scheme's assets	49,594	44,745
Present value of funded scheme's liabilities	(49,650)	(47,200)
Retirement benefit liability recognised in the statement of financial position	(56)	(2,455)
Related deferred tax	–	–
Net pension liability	**(56)**	**(2,455)**

The movements in the Defined Benefit Obligation (DBO) recognised in the statement of financial position during the year were:

	UK pensions	
	2012 £000	2011 £000
Defined benefit obligation at beginning of year	(47,200)	(52,594)
Current service cost	(329)	(397)
Interest cost	(2,305)	(2,826)
Contributions from members	(10)	(28)
Actuarial (loss)	(1,996)	(2,716)
Actual benefit payments	2,196	4,004
Experience (loss)/gain	(6)	7,357
Defined benefit obligation at end of year	**(49,650)**	**(47,200)**

27 Employee benefits continued

The movements in the fair value of plan assets during the year were:

	UK pensions	
	2012 £000	2011 £000
Value of assets at beginning of year	44,745	45,055
Expected return on assets	2,785	3,287
Actuarial gain/(loss)	1,711	(2,579)
Contributions paid by employer	2,539	2,958
Contributions from members	10	28
Actual benefit payments	(2,196)	(4,004)
Value of assets at end of year	**49,594**	**44,745**

The estimated employer contributions to be made in 2013 are £2,964,000.

The history of experience adjustments is as follows:

	2012 £000	2011 £000	2010 £000	2009 £000	2008 £000
Defined benefit obligation at end of year	(49,650)	(47,200)	(52,594)	(51,000)	(43,200)
Fair value of scheme's assets	49,594	44,745	45,055	39,793	31,934
Retirement benefit (liability) recognised in the balance sheet	(56)	(2,455)	(7,539)	(11,207)	(11,266)
Experience adjustment on scheme's liabilities	(6)	7,357	(1)	32	(4,184)
As a percentage of scheme's liabilities	0.0%	15.6%	0.0%	0.1%	9.7%
Experience adjustment on scheme's assets	1,711	(2,579)	2,320	4,611	(11,031)
As a percentage of scheme's assets	3.5%	5.8%	5.1%	11.6%	34.5%

The expense recognised in the Group income statement was as follows:

	UK pensions	
	2012 £000	2011 £000
Current service cost	(329)	(397)
Interest on scheme's liabilities	(2,305)	(2,826)
Expected return on scheme's assets	2,785	3,287
Total income recognised in income statement	**151**	**64**

Statement of comprehensive income (OCI)

	UK pensions	
	2012 £000	2011 £000
Actuarial (loss)/gain recognised in OCI	(291)	2,062
Deferred tax on actuarial amount recognised in OCI	–	–
Cumulative loss recognised in OCI at beginning of year	(13,266)	(15,328)
Cumulative loss recognised in OCI at end of year	(13,557)	(13,266)

For the financial year commencing 1st January 2013, the Parent Company will adopt IAS 19 revised 2011. On adoption the interest cost and expected return on assets disclosed in the Income Statement for the defined benefit pension plan will be based on discount rate assumptions. This is different from the IAS 19 standard used in these financial statements (IAS revised 2008) which uses discount rates to set the interest cost, but a return on assets assumption to calculate the expected return on assets. If IAS 19 revised 2011 had been used in the 2012 financial statements, the expected return on assets recognised in the Income Statement would have been £539,000 lower at £2,246,000.

The treatment of administrative and investment expenses under IAS 19 revised 2011 will also change. If IAS 19 revised 2011 had been used for the 2012 financial statements the current service charge cost recognised in the Income Statement would have been £4,000 higher at £333,000.

The changes under IAS 19 revised 2011 described above have no impact on the post-retirement benefits liability that is recognised in the Statement of Financial Position.

27 Employee benefits continued

Share-based payments – The Group

Disclosures of the share-based payments offered to employees are set out below. More detail on each scheme is given in the Remuneration Report on pages 60 to 74. The charge to the income statement in respect of share-based payments is made up as follows:

	2012 £000	2011 £000
Share Option Scheme	805	673
Performance Share Plan	1,272	764
Employee Share Ownership Plan	738	745
Total expense recognised in income statement	**2,815**	2,182

a) Share Option Scheme

The Group operates equity settled share option schemes for employees. Awards are determined by the Remuneration Committee whose objective is to align the interests of employees with those of shareholders by giving an incentive linked to added shareholder value. Options are subject to performance conditions, which if met make the options exercisable between the third and tenth anniversary of the date of grant. For options granted from 1995 to 2001 the performance condition is an increase in EPS of more than 6% greater than the increase in the UK Retail Price Index over a consecutive three-year period between grant and ten years from date of grant. From and including the 2002 options, the increase in EPS was revised to 9% greater than the increase in the UK Retail Price Index over a three-year consecutive period and from 2007 the performance condition needs to be met over the three-year period from 1st January prior to the date of the grant. If the condition is not met at the end of the three-year period the option will lapse.

The share options granted have been measured by Towers Watson, using the Present Economic Value (PEV) valuation methodology. The relevant disclosures in respect of the share option scheme grants are set out below. No options were granted in 2012.

	2008 Grant	2009 Grant	2010 Grant	2011 Grant
Grant date	12th March	11th March	26th March	18th March
Exercise price	959.0p	765.0p	1366.0p	1873.0p
Number of employees	71	70	75	87
Shares under option	311,700	223,500	290,000	350,000
Vesting period	3 years	3 years	3 years	3 years
Expected volatility	20%	25%	25%	25%
Risk-free interest rate	4.3%	2.5%	3.5%	3.1%
Expected dividend yield	3.0%	3.5%	2.5%	2.5%
Fair value	211.7p	145.5p	341.7p	442.9p

The number and weighted average exercise prices of share options are as follows:

Option (exercise price)	Outstanding at start of year	Granted during year	Exercised during year	Lapsed during year	Outstanding at end of year
2003 grant (394.5p)	15,000				15,000
2004 grant (541.9p)	18,000				18,000
2005 grant (686p)	42,433		(8,343)		34,090
2006 grant (960p)	49,475		(18,825)		30,650
2007 grant (1019.6p)	92,482		(32,726)		59,756
2008 grant (959.0p)	137,900		(65,377)		72,523
2009 grant (765.0p)	192,500		(133,500)		59,000
2010 grant (1366.0p)	270,500		(5,000)		265,500
2011 grant (1873.0p)	350,000		(5,500)		344,500
	1,168,290	–	**(269,271)**	**–**	**899,019**
Weighted average exercise price	£12.76		£8.88		£13.93
Weighted average contractual life remaining					6.1 years

Performance conditions in respect of all exercisable shares have been met. The number of shares exercisable at 31st December 2012 is 289,019 (2011: 355,290). The weighted average share price during the period was £20.96 (2011: £18.74).

27 Employee benefits continued

b) Performance Share Plan

Awards under the Performance Share Plan are made to Executive Directors and other senior managers and take the form of contingent rights to acquire shares, subject to the satisfaction of a performance target. To the extent that they vest, awards may be satisfied in cash, in shares or an option over shares. For awards granted up to 2007 the performance target is based on the Company's total shareholder return (TSR) relative to the TSR of other companies included in the FTSE All-Share Industrial Engineering Sector over a three-year performance period where awards will vest on a sliding scale. All shares within an award will vest if the Company's TSR is at or above the upper quartile. 25% will vest if the TSR is at the median and the number of shares that will vest will be calculated pro-rata on a straight line basis between 25% and 100% if the Company's TSR falls between the median and the upper quartile. No shares will vest if the Company's TSR is below the median. The performance criteria for awards from 2008 onwards are split into two separate parts. The vesting of the first part, amounting to 60% of the award, is based on the existing TSR measure. The vesting of the second part, amounting to 40% of the award, is subject to achievement of a target based on aggregate EPS over a three-year performance period. For the 2008 to 2010 awards, 25% will vest if the compound growth in EPS is equal to 5% and 100% will vest if the compound growth in EPS is equal to or exceeds 11%, there is pro-rata vesting for actual growth between these rates. For awards made in 2011, 25% will vest if the compound growth in EPS is equal to the growth in the UK Retail Price Index plus 3% and 100% will vest if the compound growth in EPS is equal to or exceeds the growth in the UK Retail Price Index plus 9%, there is pro-rata vesting for actual growth between these rates.

Shares awarded under the Performance Share Plan have been valued by Towers Watson, using the Monte Carlo simulation valuation methodology. The relevant disclosures in respect of the Performance Share Plan grants are set out below.

	2008 Grant	2009 Grant	2010 Grant	2011 Grant	**2012 Grant**
Grant date	12th March	11th March	26th March	18th March	9th March
Mid market share price at grant date	959.0p	765.0p	1366.0p	1873.0p	2106.0p
Number of employees	5	5	5	5	89
Shares under scheme	131,540	128,146	99,983	78,588	179,980
Vesting period	3 years	3 years	3 years	3 years	3 years
Probability of vesting	65.4%	69.1%	69.5%	69.2%	66.5%
Probability of ceasing employment before vesting	–	–	–	–	–
Fair value	627.2p	528.6p	949.4p	1296.1p	1400.5p

c) Employee Share Ownership Plan

UK employees are eligible to participate in the Employee Share Ownership Plan (ESOP). The aim of the ESOP is to encourage increased shareholding in the Company by all UK employees and so there are no performance conditions. Employees are invited to join the ESOP when an offer is made each year. Individuals save for 12 months during the accumulation period and subscribe for shares at the lower of the price at the beginning and the end of the accumulation period under HMRC rules. The Company provides a matching share for each share purchased by the individual.

Shares issued under the ESOP have been measured by Towers Watson, using the Present Economic Value (PEV) valuation methodology. The relevant disclosures in respect of the Employee Share Ownership Plans are set out below.

	2008 Grant	2009 Grant	2010 Grant	2011 Grant	**2012 Grant**
Grant date	1st October	1st October	1st October	1st October	1st October
Exercise price	908.8p	1039.7p	1808.7p	1832.0p	2100.3p
Number of employees	985	944	955	1,012	1,017
Shares under scheme	80,087	69,788	41,584	45,327	41,703
Vesting period	3 years	3 years	3 years	3 years	3 years
Expected volatility	20.0%	25.0%	25.0%	25.0%	25%
Risk free interest rate	3.8%	0.6%	0.6%	0.6%	0.2%
Expected dividend yield	3.0%	3.5%	2.5%	2.5%	2.5%
Fair value	953.3p	1093.7p	1922.6p	1934.6p	2228.5p

The accumulation period for the 2012 ESOP ends in September 2013, therefore some figures are projections.

27 Employee benefits continued

Share-based payments – Parent Company

Disclosures of the share-based payments offered to employees of the Parent Company are set out below. The description and operation of each scheme is the same as outlined in the Group disclosure set out above.

a) Share Option Scheme

The equity settled share options issued to employees of the Parent Company are charged in the Parent Company's income statement. The relevant disclosures in respect of the share option scheme grants are set out below. No options were granted in 2012.

	2008 Grant	2009 Grant	2010 Grant	2011 Grant
Grant date	12th March	11th March	26th March	18th March
Exercise price	959.0p	765.0p	1366.0p	1873.0p
Number of employees	1	1	1	5
Shares under option	3,500	2,500	4,000	19,000
Vesting period	3 years	3 years	3 years	3 years
Expected volatility	20%	25%	25%	25%
Risk-free interest rate	4.3%	2.5%	3.5%	3.1%
Expected dividend yield	3.0%	3.5%	2.5%	2.5%
Fair value	211.7p	145.5p	341.7p	442.9p

The number and weighted average exercise prices of share options are as follows:

Option (exercise price)	Outstanding at start of year	Granted during year	Exercised during year	Lapsed during year	Outstanding at end of year
2005 grant (686p)	1,862				1,862
2007 grant (1019.6p)	2,131				2,131
2008 grant (959p)	3,500		(422)		3,078
2009 grant (765.0p)	2,500				2,500
2010 grant (1366.0p)	4,000				4,000
2011 grant (1873.0p)	19,000				19,000
	32,993	**–**	**(422)**	**–**	**32,571**
Weighted average exercise price	£15.09		£9.59		£15.16
Weighted average contractual life remaining					7.1 years

Performance conditions in respect of all exercisable shares have been met. The number of shares exercisable at 31st December 2012 is 9,571 (2011: 7,493).

b) Performance Share Plan

The relevant disclosures in respect of the Performance Share Plan grants are set out below.

	2008 Grant	2009 Grant	2010 Grant	2011 Grant	**2012 Grant**
Grant date	12th March	11th March	26th March	18th March	9th March
Mid market share price at grant date	959.0p	765.0p	1366.0p	1873.0p	2106.0p
Number of employees	5	5	5	5	9
Shares under scheme	131,540	128,146	99,983	78,588	84,230
Vesting period	3 years	3 years	3 years	3 years	3 years
Probability of vesting	65.4%	69.1%	69.5%	69.2%	66.5%
Probability of ceasing employment before vesting	–	–	–	–	–
Fair value	627.2p	528.6p	949.4p	1296.1p	1400.5p

28 Analysis of changes in net cash

	The Group			
	At 1st January 2012 £000	Cash flow £000	Exchange movement £000	At 31st December 2012 £000
Current portion of long-term borrowings	(73)			(7,168)
Non-current portion of long-term borrowings	(6,356)			(33,601)
Short-term borrowings	(37,280)			(7,000)
Total borrowings	**(43,709)**			**(47,769)**
Comprising:				
Borrowings	(43,552)	(3,069)	273	(46,348)
Finance leases	(157)	(1,267)	3	(1,421)
	(43,709)	**(4,336)**	**276**	**(47,769)**
Cash and cash equivalents	60,172	41,328	(1,668)	99,832
Bank overdrafts	(4,194)	3,766	41	(387)
Net cash and cash equivalents	**55,978**	**45,094**	**(1,627)**	**99,445**
Net cash	**12,269**	**40,758**	**(1,351)**	**51,676**

The present value of finance lease payments are shown in note 21 on page 107.

29 Related party transactions

The Group	2012 £000	2011 £000
Sales to associated companies	567	732
Dividends from associated companies	1,454	1,461
Amounts due from associated companies at 31st December	47	21

Parent Company	2012 £000	2011 £000
Dividends received from subsidiaries	16,500	99,000
Dividends received from associates	1,454	1,461
Loans and amounts due from subsidiaries at 31st December	143,748	203,172
Amounts due to subsidiaries at 31st December	23,941	1,277

The transactions above were priced on an arm's length basis and on standard business terms.

30 Purchase of businesses

2012

	Acquisitions		
	Book value £000	Fair value adj £000	Fair value £000
Fixed assets			
Intangibles	–	2,406	2,406
	–	2,406	2,406
Current assets			
Inventories	324	–	324
	324	–	324
Total assets	324	2,406	2,730
Current liabilities			
Deferred tax	–	27	27
Total liabilities	–	27	27
Total net assets	324	2,379	2,703
Goodwill	–	–	1,243
Total	**–**	**–**	**3,946**
Satisfied by			
Cash paid	–	–	2,439
Deferred consideration	–	–	1,507
	–	–	**3,946**

Cash outflow for acquired businesses in the Cash Flow statements (page 89):

Cash consideration (for the current year and deferred consideration on prior years' acquisitions)	4,501
Net cash outflow	**4,501**

1 The acquisition of the desuperheater business from UK based Transvac Systems Ltd was completed on 24th July 2012. The acquisition method of accounting has been used. Consideration of £595,000 was paid during 2012 following completion. Separately identified intangibles are recorded as part of the fair value adjustment. The goodwill recognised represents the opportunity to accelerate the growth in sales of desuperheaters around the Group by capitalising on Transvac's expertise in this area. No deferred tax liability has been created in respect of intangible assets acquired because tax relief will be available over the assets useful life.

2 The acquisition of the distribution rights of Watson-Marlow Bredel products in Denmark and Poland was made on 1st October 2012. The acquisition method of accounting has been used. Consideration of £214,000 was paid on completion. Separately identified intangibles are recorded as part of the fair value adjustment. The goodwill recognised represents the opportunity to sell a wider range of the Group's existing products to the acquired customer base to fully utilise the Group's applications expertise to expand sales.

3 The acquisition of the business and certain assets of the steam specialty business, Termodinámica, based in Chile was completed on 14th December 2012. The acquisition method of accounting has been used. Consideration of £1,631,000 was paid on completion, the balance will be paid over the next 12 months subject to certain performance conditions being met. Separately identified intangibles are recorded as part of the fair value adjustment. The goodwill recognised represents the opportunity to take direct control of the sale of the Group's products and services in the important Chilean market. No deferred tax liability has been created in respect of intangible assets acquired because tax relief will be available over the assets' useful life.

30 Purchase of businesses continued

2011

	Acquisitions Book value £000	Fair value adj £000	Fair value £000
Fixed assets			
Intangibles	–	214	214
Total assets	–	214	214
Current liabilities			
Deferred tax	–	33	33
Total liabilities	–	33	33
Total net assets	–	181	181
Goodwill			140
Total			**321**

Satisfied by	
Cash paid	**321**

Cash outflow for acquired businesses in the Cash Flow statements (page 89):	
Cash consideration (for the current year and deferred consideration on prior years' acquisitions)	3,387
Net cash outflow	**3,387**

1 The acquisition of the distribution rights of Watson-Marlow Flexicon products in the Netherlands was made on 21st March 2011. The acquisition method of accounting has been used. Consideration of £196,000 was paid following completion. Separately identified intangibles are recorded as part of the fair value adjustment. The goodwill recognised represents the opportunity to sell a wider range of the Group's existing products to the acquired customer base and to fully utilise the Group's applications expertise to expand sales.

2 The acquisition of the distribution rights of Watson-Marlow MasoSine products in Italy was made on 12th August 2011. The acquisition method of accounting has been used. Consideration of £125,000 was paid following completion. Separately identified intangibles are recorded as part of the fair value adjustment. The goodwill recognised represents the opportunity to sell a wider range of the Group's existing products to the acquired customer base and to fully utilise the Group's applications expertise to expand sales.

31 Derivatives and other financial instruments

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. The Group has various other financial instruments such as trade debtors and trade creditors, which arise directly from its 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 currency risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below. These policies have remained fundamentally unchanged since the beginning of 2000.

Credit risk
The Group sells products and services to customers around the world and its customer base is extremely varied in size and industry sector. The Group operates credit control policies to assess customers' credit ratings and provides for any debt that is identified as non-collectable. Historically losses from trade receivables have been low.

Interest rate risk
The Group borrows in desired currencies at both fixed and floating rates of interest as appropriate to the purposes of the borrowing.

Liquidity risk
The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of overdrafts, loans and finance leases as appropriate.

Foreign currency risk
The Group has operations around the world and therefore its balance sheet can be affected significantly by movements in the rate of exchange between sterling and various other currencies particularly the US dollar and euro. The Group seeks to mitigate the effect of this structural currency exposure by borrowing in these currencies where appropriate while maintaining a low cost of debt.

The Group also has transactional currency exposures principally as a result of trading between Group companies. Such exposures arise from sales or purchases by an operating unit in currencies other than the unit's functional currency. Net cash flows between any two currencies of less than £1 million per annum would not usually be considered sufficiently material to warrant forward cover. Forward cover is not taken out more than 24 months in advance or for more than 90% of the next 12 months' and 60% of the following 12 months' forecast exposure.

31 Derivatives and other financial instruments continued

Interest rate risk profile of financial liabilities

The interest rate profile of the financial liabilities of the Group as at 31st December was as follows:

2011

	The Group			
	Total £000	Fixed rate financial liabilities £000	Floating rate financial liabilities £000	Financial liabilities on which no interest is paid £000
Euro	31,568	135	12,565	18,868
US dollar	2,544	–	323	2,221
Sterling	31,061	–	22,573	8,488
Other	37,476	22	12,285	25,169
	102,649	**157**	**47,746**	**54,746**

2012

	The Group			
	Total £000	**Fixed rate financial liabilities £000**	**Floating rate financial liabilities £000**	**Financial liabilities on which no interest is paid £000**
Euro	17,052	72	387	16,593
US dollar	1,841	–	–	1,841
Sterling	43,093	1,348	34,500	7,245
Other	43,984	–	11,849	32,135
	105,970	**1,420**	**46,736**	**57,814**

In respect of fixed rate financial liabilities, the interest rate for euro financial liabilities is 4.1% fixed for 3 years.

2011

	The Parent			
	Total £000	Fixed rate financial liabilities £000	Floating rate financial liabilities £000	Financial liabilities on which no interest is paid £000
Euro	–	–	–	–
US dollar	–	–	–	–
Other (sterling)	22,749	–	22,573	176
	22,749	**–**	**22,573**	**176**

2012

	The Parent			
	Total £000	**Fixed rate financial liabilities £000**	**Floating rate financial liabilities £000**	**Financial liabilities on which no interest is paid £000**
Euro	–	–	–	–
US dollar	–	–	–	–
Other (sterling)	34,847	–	34,500	347
	34,847	**–**	**34,500**	**347**

The benchmark rates for the floating rate financial liabilities are as follows:

US dollar	}	LIBOR
Euro		LIBOR/EURIBOR

31 Derivatives and other financial instruments continued

Terms and debt repayment schedule

The terms and conditions of outstanding loans were as follows:

	Currency	Nominal interest rate	Year of maturity	2012 Carrying value £000	2011 Carrying value £000
Unsecured bank facility	CZK	LIBOR + 1%	2012	–	753
Unsecured bank facility	€	2.18%	2013	75	773
Unsecured bank facility	€	1.95%	2013	312	297
Unsecured bank facility	€	LIBOR + 2%	2012	–	11,500
Unsecured bank facility	NOK	6.50%	2012	–	18
Unsecured bank facility	Won	3.22%	2012–2017	4,655	5,027
Unsecured bank facility	$	1.25%	2012	–	323
Unsecured bank facility	YEN	0.95%	2013	5,336	6,272
Unsecured bank facility	DKK	5.82%	2012	–	210
Unsecured bank facility	£	1.67%	2013	7,000	2,573
Unsecured bank facility	£	1.78%	2015	27,500	20,000
Unsecured bank facility	RAND	8.5%	2012-2016	1,857	–
Finance leases	RMB	–	2012-2016	5	17
Finance leases	€	4.10%	2012-2015	75	135
Finance leases	£	–	2012-2016	1,341	5
				48,156	**47,903**

Interest rate risk profile of financial assets

The interest rate profile of the financial assets of the Group as at 31st December was as follows:

2011

	The Group		
	Total £000	Floating rate financial assets £000	Financial assets on which no interest is earned £000
Sterling	14,076	212	13,864
Euro	49,710	5,895	43,815
US dollar	31,669	5,482	26,187
RMB	22,804	10,496	12,308
Other	93,167	22,745	70,422
	211,426	**44,830**	**166,596**

2012

	The Group		
	Total £000	**Floating rate financial assets £000**	**Financial assets on which no interest is earned £000**
Sterling	18,024	4,536	13,488
Euro	50,305	4,682	45,623
US dollar	40,602	17,404	23,198
RMB	43,938	29,406	14,532
Other	101,526	24,819	76,707
	254,395	**80,847**	**173,548**

2011

	The Parent		
	Total £000	Floating rate financial assets £000	Financial assets on which no interest is earned £000
Sterling	–	–	–
Other	–	–	–
	–	**–**	**–**

31 Derivatives and other financial instruments continued

2012

	The Parent		
	Total £000	Floating rate financial assets £000	Financial assets on which no interest is earned £000
Sterling	4,261	4,261	–
Other	–	–	–
	4,261	**4,261**	**–**

Financial assets on which no interest is earned comprise trade and other receivables and cash at bank and in hand.

Floating rate financial assets comprise cash placed on money market deposit mainly at call and three month rates. The average rate of interest received on sterling deposits during the year was 0.6% (2011: 0.75%).

Currency exposures

As explained above, the Group's objectives in managing the currency exposures arising from its net investment overseas (in other words, its structural currency exposures) are to maintain a low cost of debt while partially hedging against currency depreciation. All gains and losses arising from these structural currency exposures are dealt with in the statement of total comprehensive income.

Transactional (or non-structural) exposures give rise to net currency gains and losses that are recognised in the income statement. Such exposures include the monetary assets and monetary liabilities in the Group balance sheet that are not denominated in the operating (or 'functional') currency of the operating unit involved. At 31st December the currency exposures in respect of the Euro was a net monetary liability of (£543,000) (2011 net monetary liability: £1,121,000) and in respect of the US dollar a net monetary asset of £7,961,000 (2011: £6,533,000).

At 31st December the percentage of debt to net assets, excluding debt was 0.65% (2011: 14.6%) for the Euro and 0.0% (2011: 1.0%) for the US dollar.

Maturity of financial liabilities

The Group's financial liabilities at 31st December mature in the following periods:

2011

	The Group					
	Trade and other payables £000	Overdrafts £000	Short-term borrowings £000	Finance leases £000	Long-term borrowings £000	Total £000
In six months or less, or on demand	54,746	4,241	26,059	36	–	85,082
In more than six months but no more than 12	–	–	11,697	37	–	11,734
In more than one year but no more than two	–	–	–	68	6,345	6,413
In more than two years but no more than three	–	–	–	10	–	10
In more than three years but no more than four	–	–	–	3	–	3
In more than four years but no more than five	–	–	–	3	–	3
In more than five years	–	–	–	–	–	–
Total contractual cash flows	**54,746**	**4,241**	**37,756**	**157**	**6,345**	**103,245**
Balance sheet values	**54,746**	**4,194**	**37,280**	**157**	**6,272**	**102,649**

31 Derivatives and other financial instruments continued

2012

	The Group					
	Trade and other payables £000	Overdrafts £000	Short-term borrowings £000	Finance leases £000	Long-term borrowings £000	Total £000
In six months or less, or on demand	57,814	391	7,005	210	6,113	71,533
In more than six months but no more than 12	–	–	–	300	770	1,070
In more than one year but no more than two	–	–	–	316	1,610	1,926
In more than two years but no more than three	–	–	–	300	31,194	31,494
In more than three years but no more than four	–	–	–	295	1,392	1,687
In more than four years but no more than five	–	–	–	–	518	518
In more than five years	–	–	–	–	–	–
Total contractual cash flows	**57,814**	**391**	**7,005**	**1,421**	**41,597**	**108,228**
Balance sheet values	**57,814**	**387**	**7,000**	**1,421**	**39,348**	**105,970**

In May 2012 a three-year £40 million revolving credit facility was negotiated at LIBOR plus 1.25% plus fees.

2011

	The Parent					
	Trade and other payables £000	Overdrafts £000	Short-term borrowings £000	Finance leases £000	Long-term borrowings £000	Total £000
In six months or less, or on demand	176	2,599	20,202	–	–	22,977
Total contractual cash flows	**176**	**2,599**	**20,202**	**–**	**–**	**22,977**
Balance sheet values	**176**	**2,573**	**20,000**	**–**	**–**	**22,749**

2012

	The Parent					
	Trade and other payables £000	Overdrafts £000	Short-term borrowings £000	Finance leases £000	Long-term borrowings £000	Total £000
In six months or less, or on demand	347	–	7,005	–	–	7,352
In more than six months but no more than 12	–	–	–	–	–	–
In more than one year but no more than two	–	–	–	–	–	–
In more than two years but no more than three	–	–	–	–	28,968	28,968
In more than three years but no more than four	–	–	–	–	–	–
In more than three years but no more than four	–	–	–	–	–	–
In more than four years but no more than five	–	–	–	–	–	–
In more than five years	–	–	–	–	–	–
Total contractual cash flows	**347**	**–**	**7,005**	**–**	**28,968**	**36,320**
Balance sheet values	**347**	**–**	**7,000**	**–**	**27,500**	**34,847**

Cash flow hedge

The Group uses forward currency contracts to manage its exposure to movements in foreign exchange rates. The forward contracts are designated as hedging instruments in a cash flow hedging relationship. At 31st December the Group had contracts outstanding to purchase €1,016,000 with US dollars, £534,000 with US dollars, Swedish SEK1,547,000 with US dollars and Danish DKK 471,000 with US dollars. The fair values at the end of the reporting period were £1,558,000 (2011: £27,059,000). The fair value of cash flow hedges falls into the Level 2 category of the fair value hierarchy in accordance with IFRS 7.

Borrowing facilities

The Group has various borrowing facilities available to it. The undrawn committed facilities available at 31st December in respect of which all conditions precedent had been met at that date were as follows:

	The Group	
	2012 £000	2011 £000
Expiring in one year or less	14,555	15,937
Expiring in more than two years but no more than three	12,500	–
	27,055	15,937

	The Parent	
	2012 £000	2011 £000
Expiring in one year or less	8,000	7,427
Expiring in more than two years but no more than three	12,500	–
	20,500	7,427

31 Derivatives and other financial instruments continued

Fair values of financial assets and financial liabilities

Fair values of financial assets and liabilities at 31st December are not materially different from book values due to their size or the fact that they were at short-term rates of interest. Fair values have been assessed as follows:

- Derivatives
  Forward exchange contracts are marked to market using year-end exchange rates
- Interest-bearing loans and borrowings
  Fair value is calculated based on discounted expected future principal and interest cash flows
- Finance lease liabilities
  The fair value is estimated as the present value of future cash flows, discounted at market interest rates for homogeneous lease agreements. The estimated fair values reflect change in interest rates
- Trade and other receivables/payables
  For receivables/payables with a remaining life of less than one year, the notional amount is deemed to reflect the fair value.

Sensitivity analysis

In managing interest rate and currency risks the Group aims to reduce the 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.

At 31st December, it is estimated that a general increase of one percentage point in interest rates would increase the Group's profit after tax and equity by approximately £250,000 (2011: £150,000).

At the year-end borrowings totalled £48,156,000 consequently, in respect of financial liabilities, the Group is not significantly at risk from increases in interest rates.

For the year ended 31st December 2012, it is estimated that a decrease of one percentage point in the value of sterling weighted in relation to the Group's profit and trading flows would have increased the Group's profit before tax by approximately £1,800,000 (2011: £1,600,000). The effect can be very different between years due to the weighting of different currency movements. Forward exchange contracts have been included in this calculation.

The credit risk profile of trade receivables

The ageing of trade receivables at the reporting date was:

	Gross 2012 £000	**Impairment 2012 £000**	Gross 2011 £000	Impairment 2011 £000
Not past due date	110,322	(214)	104,038	(539)
0-30 days past due date	18,193	(280)	20,600	(184)
30 days – one year past due date	21,885	(4,220)	21,795	(3,226)
More than one year	4,840	(4,840)	5,001	(5,001)
	155,240	**(9,554)**	**151,434**	**(8,950)**

Based on past experience the Group believes no further impairment allowance is required for receivables that are past their due date.

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

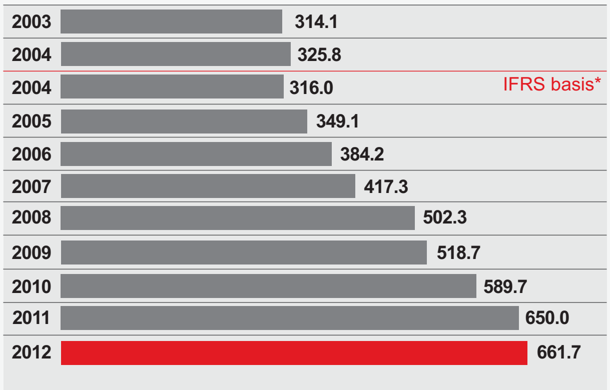
	2012 £000	2011 £000
Balance at 1st January	8,950	10,118
Movement in impairment	604	(1,168)
Balance at 31st December	**9,554**	**8,950**

Financial Summary 2003-2012

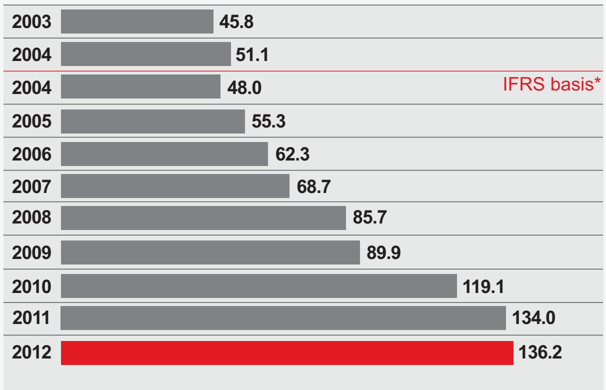
	2003 £000	2004 £000	Prepared under IFRS 2004 £000	Prepared under IFRS 2005 £000
Revenue	314,087	325,833	315,991	349,100
Operating profit	45,750	51,100	47,956	55,170
Operating profit (adjusted)	–	–	47,956	55,345
Operating profit margin (adjusted)	14.6%	15.7%	15.2%	15.9%
Profit before taxation	44,564	50,836	48,704	56,959
Profit before taxation (adjusted)	–	–	48,704	57,134
Profit after taxation	29,426	33,682	32,442	38,187
Dividends in respect of the year	15,028	16,102	16,196	18,318
Net assets	163,816	182,013	166,286	198,246
Earnings per share (basic)	38.5p	43.4p	43.1p	50.0p
Earnings per share (adjusted)	–	–	43.1p	50.2p
Dividends in respect of the year (per share)	20.1p	21.4p	21.4p	23.8p
Special dividend (per share)	–	–	–	–
Return on capital employed (note 25)	28.3%	31.0%	27.2%	30.4%

* The results for 2004 to 2012 have been prepared under International Financial Reporting Standards, prior year figures are shown as originally reported including 2004 for reference. Adjusted items exclude non-operating items (see note 2 on page 94).

Revenue £m

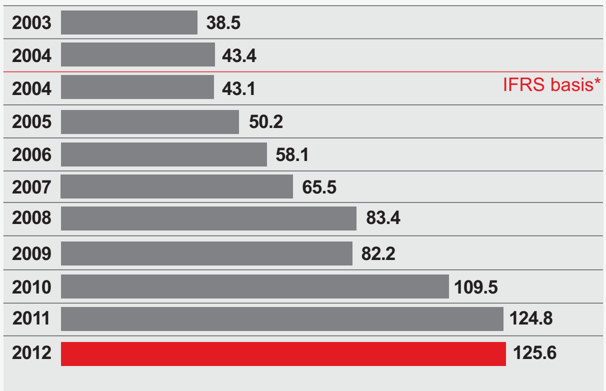


Operating profit (adjusted)* £m

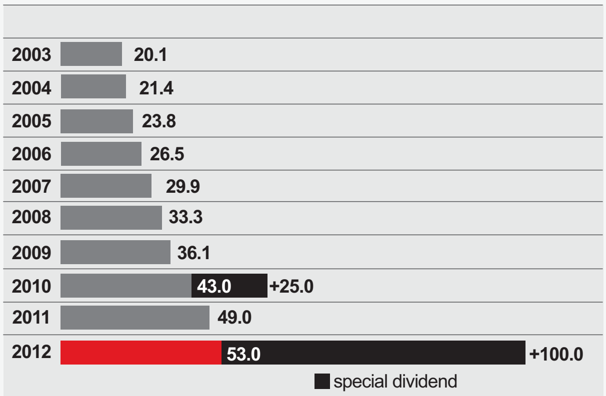


	Prepared under IFRS						
	2006 £000	2007 £000	2008 £000	2009 £000	2010 £000	2011 £000	2012 £000
Revenue	384,249	417,317	502,316	518,705	589,746	649,991	**661,723**
Operating profit	61,941	68,336	81,028	76,522	121,396	129,498	**125,714**
Operating profit (adjusted)	62,291	68,720	85,669	89,938	119,125	133,960	**136,245**
Operating profit margin (adjusted)	16.2%	16.5%	17.1%	17.3%	20.2%	20.6%	**20.6%**
Profit before taxation	65,344	72,163	85,162	76,415	123,493	132,341	**127,652**
Profit before taxation (adjusted)	65,694	72,796	90,146	90,196	121,613	137,169	**138,507**
Profit after taxation	44,066	49,190	59,788	53,091	86,654	93,238	**90,245**
Dividends in respect of the year	20,038	22,754	25,668	27,569	52,624	38,072	**119,469**
Net assets	199,722	242,965	296,006	307,364	379,524	400,120	**436,549**
Earnings per share (basic)	57.7p	64.7p	78.0p	69.6p	112.5p	120.0p	**115.6p**
Earnings per share (adjusted)	58.1p	65.5p	83.4p	82.2p	109.5p	124.8p	**125.6p**
Dividends in respect of the year (per share)	26.5p	29.9p	33.3p	36.1p	43.0p	49.0p	**53.0p**
Special dividend (per share)	–	–	–	–	25.0p	–	**100.0p**
Return on capital employed	32.2%	33.6%	35.5%	33.3%	42.1%	41.1%	**39.4%**

Earnings per share (adjusted)* p



Dividends per share p



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Allen & Overy LLP

Important dates

Annual General Meeting	9th May 2013

Final dividend*

Ordinary shares quoted ex-dividend	17th April 2013
Record date for final dividend	19th April 2013
Final dividend payable	17th May 2013

Special dividend*

Record date for special dividend	31st May 2013
Existing Ordinary shares marked ex-entitlement to special dividend	3rd June 2013
Special dividend payable	3rd July 2013

* Subject to shareholder approval at the AGM.

Spirax Sarco worldwide

Steam specialties

EMEA

Belgium
Spirax-Sarco N V

Czech Republic
Spirax Sarco spol sro

Denmark
Spirax-Sarco Ltd (Branch)

Finland
Spirax Oy

France
Spirax-Sarco SAS

Germany
Spirax-Sarco GmbH
Hygromatik GmbH

Ireland
Eirdata Environmental Services Ltd

Italy
Spirax-Sarco Srl
M & M International Srl
Colima Srl

Netherlands
Spirax-Sarco Engineering BV
Spirax-Sarco Investments BV

Norway
Spirax-Sarco AS

Poland
Spirax Sarco Sp Zoo

Portugal
Spirax Sarco Equip Ind Lda

Russia
Spirax-Sarco Engineering LLC

South Africa
Spirax-Sarco South Africa (Pty) Ltd

Spain
Spirax Sarco SA
Spirax-Sarco Engineering SL

Sweden
Spirax-Sarco AB

Switzerland
Spirax-Sarco AG

Turkey
Spirax Inter Valf Sanayi ve Ticaret
Ltd Sirketi

United Kingdom
Spirax-Sarco Ltd
Spirax-Sarco America Ltd
Spirax-Sarco Investments Ltd
Spirax-Sarco Overseas Ltd

Americas

Argentina
Spirax Sarco SA

Brazil
Spirax Sarco Ind e Com Ltda

Canada
Spirax Sarco Canada Ltd

Chile
Spirax-Sarco Chile Ltda

Mexico
Spirax-Sarco Mexicana SAPI DE CV

USA
Spirax-Sarco Inc
Sarco International Corp

Asia Pacific

Australia
Spirax-Sarco Pty Ltd

China
Spirax Sarco Engineering (China) Ltd

India
Spirax-Marshall Ltd (49.3%)

Japan
Spirax-Sarco Ltd (Branch)

Malaysia
Spirax-Sarco Sdn Bhd

New Zealand
Spirax Sarco Ltd

Philippines
Spirax-Sarco Philippines, Inc

Singapore
Spirax-Sarco (Private) Ltd

South Korea
Spirax-Sarco (Korea) Ltd (97.5%)

Taiwan
Spirax Sarco Co Ltd

Thailand
Spirax Sarco (Thailand) Ltd

Watson-Marlow Pumps

Australia
Watson-Marlow Pty Ltd

Belgium
Watson-Marlow N V

Brazil
Watson-Marlow Bredel Ind
e Com de Bombas Ltda

Denmark
Watson-Marlow Flexicon A/S

France
Watson-Marlow SAS

Germany
Watson-Marlow GmbH

India
Watson-Marlow India Private Ltd

Italy
Watson-Marlow Srl

Mexico
Watson-Marlow S de RL de C V

Netherlands
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Watson-Marlow Bredel Holdings BV
Watson-Marlow BV

New Zealand
Watson-Marlow Ltd

Poland
Watson-Marlow Sp Zoo

Russia
Watson-Marlow LLC

Singapore
Watson-Marlow Pte Ltd

South Africa
Watson-Marlow Bredel S A (Pty) Ltd

Sweden
WM Alitea A B

Switzerland
Watson-Marlow Ltd (Branch)

United Kingdom
Watson-Marlow Ltd

USA
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