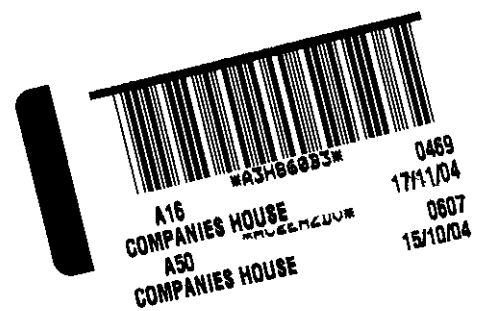


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Swallowfield plc

Report and Accounts

2004



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# swallowfield in china

The official opening of our Shanghai office

# chairman's statement

**Chairman**  
**J S Espey**

## Results

I am very pleased to report that trading in the second half of the year was in line with the expectations I presented in my report of 26 February 2004 and, shows a healthy turnaround from last year's results.

In our strategic update of 6 April 2004, we presented a restructuring plan aimed at increasing annual profit before tax during 2005 by £0.4m at a cost of £0.4m.

Accordingly, we have now charged this year's profit and loss account with £0.4m of restructuring costs, as predicted.

Excluding these costs, profit before tax increased by 60% from £1.0m to £1.6m on an 11% reduction in turnover.

Including restructuring costs, profit before tax increased by 19% to £1.2m.

The objectives that we set ourselves for the financial year were to improve operating margins, reduce overhead costs and to drive a big improvement in the profitability of the cosmetics business. We have achieved these objectives, against a background of a weak market and continued pricing pressure, by concentrating on our product development strengths, cost efficiencies, improved pricing control and improved customer service.

Turnover in the Cosmetics business reduced by 11% from £13.8m to £12.2m but last year's operating loss of £0.8m was improved to a break-even position. This represents a very creditable turnaround of £0.8m in terms of operating profit during the year. The business was profitable before the impact of corporate overheads.

Turnover in the Aerosol business declined by 11% from £40.8m to £36.5m whilst operating profit fell by 11% from £2.2m to £2.0m. During the year, we launched a new bag-on-valve product and produced significant volumes of this for a major customer. Our investment in plant and machinery made during 2003 helped to ensure the success of this project.

## Cash and Net Debt

Net debt at the year end was broadly unchanged on the previous year even though trade working capital increased significantly. This increase, arising from debtors, was primarily due to a single customer contract with extended payment terms, offset in part by extended supplier terms on components purchased for this same contract. This is more fully explained in the Financial Review.

As outlined in our interim report, during the year we restructured our financing arrangements to better align our facilities with the Group's funding requirements, and to reduce our interest rate margin by 0.25%.

## Corporate Governance

We continue to strengthen our approach to Corporate Governance and, in accordance with best practice, have described our approach to the new Combined Code within this year's Corporate Governance statement. We have also published terms of reference for the Audit, Remuneration and Nomination Committees on our web site and have issued a whistle-blowing policy to our employees.

# chairman's statement

## Strategic Update

As announced on 6 April 2004, we have completed the first phase of our strategic review of the business, which was directed at actions to increase the profitability of the Cosmetics business, and improve the total profitability of the Group. The long-term target we have set ourselves is to achieve a return on shareholders' equity of 12% by 30 June 2006, and 15% by 30 June 2009. Excluding restructuring costs, the return on shareholders equity for the current year was 9%.

On the same date, we announced that we would be opening a procurement office in the Peoples' Republic of China. I am pleased to say that this office is now operational, and we plan to increase the resources directed to this office, in order to speed up the benefits we expect to receive. Whilst the cost of this office will be in the region of £0.4m per annum, we anticipate the investment should begin to break even in the 4th quarter of our 2005 financial year and to generate net savings in the year ended 30 June 2006.

In our strategic plan, we include the acquisition of businesses that have complementary product capabilities, and that provide us with the opportunity to obtain synergistic benefits with our current customer base. As ever, we continue to be discerning in terms of the financial returns required from any such acquisition, and whilst we have examined a number of opportunities, financial prudence mitigated against further action.

## Looking Forward

We do not anticipate any improvement in the market for personal care products over the next 12 months and expect consumer spending on our products to remain subdued. The pricing pressure we have experienced over the past few years is likely to continue in most areas of our business, as retailer competition continues to squeeze the supply chain and the impact of Far Eastern sourcing intensifies.

Despite this background, we plan to raise shareholder returns by driving down total input costs, improving manufacturing efficiencies, presenting new and exciting product ranges and improving our pricing strategies.

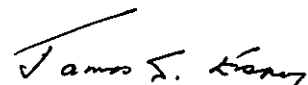
Following the high levels of the previous two years, we have significantly reduced our expenditure on fixed assets in the year just ended. During the coming year, we expect an affordable increase in capital expenditure as we restart our longer term investment plans aimed at cost reduction and the enhancement of good manufacturing practices across the Group.

We expect that the split of profitability between the first and second halves of the current financial year will be more balanced than the year just ended, but as ever, this is dependent on the final dates for new product launches. The first two months of the new financial year have been slightly ahead of last year and, despite our expectations for an unhelpful market background, we are positive for the future as we continue to use our acknowledged skills to best advantage.

## Dividend

Our policy over the last 18 months has been to maintain dividend payments, notwithstanding short-term reductions in the level of dividend cover. We continue to believe that our medium-term aim of pursuing a progressive dividend policy is correct, but recognise that in the short term we must continue to rebuild the level of dividend cover and increase the strength of our balance sheet. Therefore, the Board is proposing to pay a final dividend of 2.0p per share making a total dividend of 4.8p per share for the year, unchanged from that paid in the previous year. If approved at the Annual General Meeting, the final dividend will be paid on 29 October 2004 to shareholders on the register at 15 October 2004. The shares will go ex-dividend on the 13 October 2004.

The past year has been one of great challenge in our business. These results are a credit to all of our employees and managers and would not have been possible without their hard work and commitment. We would like to extend our thanks to them.



**J S Espey**  
Chairman  
9 September 2004

# operating review

**Group Managing Director**  
**J A Wardell**

## **Results**

Our trading results for the financial year ended 30 June 2004 finished in line with expectations and included a strong recovery in the second half of the year as projected.

This improvement in profitability is a credit to the management and workforce on both sites who have made big strides in implementing the action plan I outlined in last year's Operating Review. These results have confirmed the appropriateness of the actions undertaken.

## **Action Plan Update**

During the last financial year, we worked hard on both sites to reduce costs and improve operating efficiencies. The new capacity, which came on stream at our Wellington factory was timely, as we produced considerable quantities of a new and unique product using a bag-on-valve system with a compressed air propellant. Our success in executing the action plan is all the more impressive given the weak market background and the increasing complexity of our product range.

In the Cosmetics business, we specifically set out to make a significant reduction in overheads without adversely affecting overall customer service levels. I am pleased to confirm this was wholly successful and greatly contributed to the turnaround in profitability.

Recently, we opened an office in Shanghai, in the Peoples' Republic of China, to more effectively purchase components and finished goods. We see this as a key action aimed at helping to maintain our competitiveness in the colour cosmetics and gift markets.

We continue to examine new business available to us and strive to use our core strengths in product design and manufacture to win this business with added values and better margins. This is supported by our continuing review of working methods to unlock further ongoing reductions in our overhead cost base.

## **Market Background**

Sales of toiletries and cosmetics, in our traditional marketplaces of Europe and North America, remain flat in unit volume terms and we believe that any reported increase in retail sales value comes from a widening of retailer margins.

At any one time, we have a number of interesting enquiries for new products. We have noticed that customers are more uncertain about launching new products. Consequently, fewer of these enquiries are launched on the original planned dates. Introducing new products into the current market is increasingly difficult and success is much harder to come by.

Our gift business remains strong, but is subject to competition from South East Asian manufacturing sources. We continue to use our core skills to add value and maintain our profitability in this sector.

Whilst we note considerable over-capacity in Europe for the manufacture of toiletries and cosmetics, it is the increasing quantity of goods manufactured in the Far East which is having the greatest impact on prices. It is worth noting that most toiletries and cosmetics manufactured on a global basis are still sold in the European and North American markets. Far Eastern

# operating review

manufacture represents an increasing level of importation into these areas.

## **Bideford**

After absorbing its share of Group overhead costs, our colour cosmetics operation on the Bideford site achieved a break-even situation. This represents a very encouraging turnaround in the business and is a fine reflection of the effort put in by the management and workforce.

We have been successful in winning the supply of new product ranges and have seen strong sales from a number of these. We are particularly pleased about the success of the Pout colour cosmetics brand which we manufacture on behalf of the brand owner. This range is now being sold internationally with increasing success.

The results at Bideford are particularly good when viewed against the reduction in average production run lengths, which has increased downtime and product changeovers. This results from our customers' desire to reduce stock levels throughout their supply chain. We see this trend as a positive challenge and continue to invest in ideas and equipment to improve our efficiency and flexibility.

## **Wellington**

In the toiletries business at Wellington, we have been purposeful in driving our strategy for focusing on higher margin business and improved operating efficiencies. Operating profit of £2.0m compared with £2.2m in the prior year, although showing a slight decline, is a

strong result when viewed against the drop in turnover and the 17.5 million reduction in production units. We have been successful in reducing our dependency on high volume, low margin business.

We continue to develop a range of new products and new ideas and believe we are at the forefront of the Aerosol market. Our innovative approach to design and investment keeps us at the head of this particular packaging stream. In relation to comments about the difficult market, it remains important for us to build on and make best use of our innovative skills in this sector.

## **Strategic Review**

We have registered, perhaps even more than in previous years, an increasing demand from our customers for lower cost goods and we continually seek to align our business to take account of this. Like all manufacturers, we are continually bombarded with changing legislation, new accounting standards, labour laws and other regulatory changes, all of which make manufacturing in the UK increasingly difficult.

We remain undeterred, however, and know that there are many positive steps that we can still take to improve our profitability. We intend to offset continued price erosion by improved international procurement, exercises in value engineering on specific products and the use of selective offshore manufacturing where demanded. The recent strategic review of the business indicates that a gradual, but definite, change of position is needed, as we continue to improve and secure our status

as the outsourcer of choice for customers requiring high quality, desirable, toiletry and cosmetic products.

We are expanding our China office to broaden the range of products that we can buy through our chosen partners. We will also maintain our ability to offer the widest range of the most desirable product types from our current UK manufacturing facilities.

## **Future Objectives**

Changing business patterns, faster communications and modern life styles, mean an increased pressure for us to produce our products more cheaply and more flexibly, but we are confident of an ongoing and increasing consumer demand for our products and services.

Good cash and working capital management remains of utmost importance in everything that we do. Going forward, we must seek to protect our customer base, by providing superb service levels whilst using lower levels of working capital.

Our future objective is to expand the business using our inherent skills. We will seek to manufacture our products to best effect from sources chosen by our product management teams. We will continue to retain and build high-level skills and knowledge right across our business, which will be required even more in the future.



**J A Wardell**

Group Managing Director  
9 September 2004

# financial review

Group Finance Director  
I A Mackinnon

## Results

This year, to more fully explain the results, we have adopted a multi-column profit and loss account format. This format has been designed to allow the ongoing operating results to be shown separately from the impact of restructuring costs, which are described more fully below.

Profit after tax, before the impact of exceptional restructuring costs, has increased by 52% from £0.7m to £1.1m and earnings per share, on the same basis, have increased from 6.4p to 9.7p.

The net interest charge for the year reduced by 6% to £0.4m, due to a combination of lower average base rate levels, a reduction in the interest rate margin we pay our bankers, which is explained below, and a decrease in average net debt levels.

The tax rate for the period was 30% compared to 26% last year. This increase is primarily due to a reduction in the utilisation of overseas tax losses. An analysis of this charge is set out in Note 8 to the accounts. The actual tax charge is equal to the effective UK rate as reductions to prior year tax charges are offset by unrelieved overseas losses and the impact of permanent disallowables. Neither the unrelieved overseas tax charge nor the reductions to prior year charges should recur next year, and overall we anticipate our tax rate rising slightly.

## Restructuring

In our strategic plan update of 6 April 2004, we announced a series of restructuring actions designed to generate overhead savings of £0.4m in the next financial year, and £0.5m annually thereafter. The cost of this restructuring plan totals approximately £0.4m, and this has been charged against this year's profit and loss account. As at 30 June 2004, £0.1m had been spent, with the remainder to be spent in 2005.

Part of the restructuring plan involved the creation of a single, customer-facing organisation from our two UK subsidiaries, Aerosols International Limited and Cosmetics Plus Limited. At the year end, the assets and liabilities of these two subsidiaries were consolidated into Swallowfield plc, and the year end balance sheet of the company shows the impact of these changes.

## Debt and Cashflow

At the year end, net debt, at £8.8m, remained broadly unchanged from the previous year end and, as a result, gearing decreased from 75% to 73%. Trade debtors increased by £4.9m during the year as the Group undertook a large contract on extended payment terms. This was, however, partly offset by improved supplier terms on components relating to that business and accordingly trade creditors increased by £4.1m.

As anticipated, our capital expenditure was significantly reduced from the high levels of the previous two years. We anticipate an affordable increase in the level of capital expenditure next year.

During the year, we restructured our banking facilities to provide an improved match to our current and ongoing borrowing requirements. At the same time we were able to reduce the interest rate margin we pay our bankers by around 0.25%. At the year-end, we had undrawn facilities totalling £3.6m; this is explained more fully in note 19 to the accounts.

## Accounting Standards

There have been no changes to Accounting Standards during the year which impact the Group Accounts, but we are currently in the process of readying ourselves for the change to International Accounting Standards. Our first reporting year using International Accounting Standards will be for the year ending

# financial review

30 June 2006, and our interim report to be issued in February/March 2006 will be the first report issued to shareholders using the new accounting standards. We expect to be able to provide shareholders with an analysis of the impact of this change in next year's annual report and accounts.

## Pension Fund Accounting

The Group has continued to adopt the transitional arrangements for FRS17, *Retirement Benefits* and the results of this are described in Note 27 to the accounts. The most recent FRS17 valuation, as at 30 June 2004, indicates a deficit of £3.6m before the impact of deferred taxation, and £2.5m net of deferred taxation. The improvement seen in equity markets during the last 12 months has been offset by a continued reduction in inflation adjusted discount rates. Real discount rates have reduced by a further 0.3% this year in addition to the 0.35% decline witnessed in the previous year. The impact of a reduced discount rate is to increase the present value of liabilities in the scheme.

The last triennial valuation of the scheme undertaken at 5 April 2002 indicated that the scheme was 119.6% funded on the Government minimum funding rate basis, and 101.7% funded on an ongoing basis, although these valuations are likely to have weakened considerably since. The next triennial valuation is due as at 6 April 2005 and should be available in September 2005. We do not anticipate any increase in the funding rate before that date, but it is likely that contributions may rise subsequently.

## Financial Instruments

The Group's financial instruments, other than derivatives, comprise bank loans, finance leases and hire purchase contracts, cash and short-term deposits.

The main purpose of these financial instruments is to raise finance to fund the Group's operations. The Group has various other financial instruments such as trade debtors and trade creditors that arise directly from its operations.

It has been the Group's policy that no trading in financial instruments be undertaken.

The major financial risks faced by the Group are foreign currency risk, credit risk, interest rate risk and funding risk.

## Foreign Currency Risk

Transactional currency exposures exist from buying and selling in currencies other than the subsidiaries' reporting currencies. During the year we continued our hedging activity to minimise the impact of changes in exchange rates. This activity is limited to a maximum of 100% of the balance sheet exposure at any point in time and as noted above we do not trade in these instruments. At the balance sheet date approximately 33% of our net euro exposure on 30 June was hedged at a rate of £:€1.5118.

## Credit Risk

The Group controls credit risk by entering into transactions with counter parties having good credit ratings. Exceptions to this, which occur infrequently, are dealt with on a case-by-case basis and no material bad debts were incurred during the year.

## Interest Rate Risk

The Group policy is to fund its operations through a mixture of retained earnings, bank borrowings, finance leases and hire purchase contracts. During the period under review 60% of borrowings were at floating rates of interest and 40% at fixed rates of interest. It has been Group policy to accept a degree of risk provided interest rate exposure remained within a certain

range. On 17 September 2002 the Group entered into a five year base rate swap for £3m at a fixed rate of 4.92%. This was done to reduce the Group's exposure to changes in interest rates and to take advantage of the relatively low long-term rates then available.

## Funding Risk

The Group's policy is to ensure that borrowing facilities are sufficient to meet operating and investment requirements taking into account the nature and timing of the Group's cash flows, and to maintain good cash management controls so as not to exceed these facilities. Regular dialogue is maintained with the banks, and cash flow forecasts are closely monitored.

## Going Concern

The Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the accounts.



## I A Mackinnon

Group Finance Director  
9 September 2004

# health, safety and environmental report

**Group Operations Director  
B J Williamson**

I am pleased to present the Group's third annual report on health, safety and environmental matters.

## Health and Safety

Continuous improvement of health and safety performance remains one of the Company's most important business objectives. The accident statistics all show an improving trend for 2004, demonstrating the effectiveness of our systems and our approach to health and safety management. The number of major and minor accidents our people have suffered at work is at a three year low, with no major accidents occurring at the Bideford site. For the Group the total number of major accidents per 100,000 employees was less than one third that of our industry sector average using the standard industry measure.

All employees participate in regular safety training sessions and the subjects covered during 2004 were safe handling of dangerous substances (European week for safety and health topic 2003) and safe lifting and carrying with an emphasis on minimising the risk of back injury.

Health and safety related investment during 2004 included segregation and installation of new sprinkler systems in the finished goods warehouse to minimise the risk of rapid spread of fire, installation of new emergency escape lighting at the Wellington site and purchase of new mechanical handling equipment. All new equipment purchased complies with the essential health and safety requirements of the appropriate EU Directives and EN/ISO standards.

The physical and mental health of employees has not been overlooked. Wellington staff have the opportunity to join the local sports centre at a significantly reduced corporate rate which will hopefully serve to improve staff fitness and morale and all employees have access to a free, confidential BUPA stress counselling help-line.

## Environmental

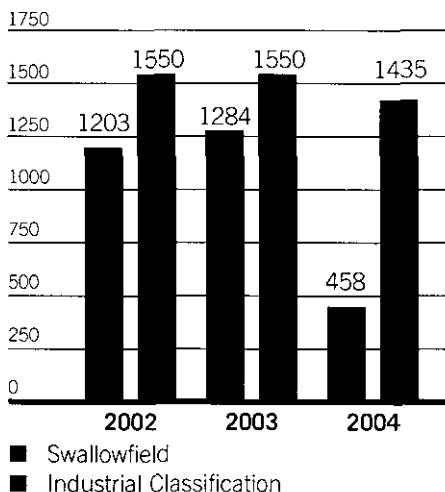
The Swallowfield Board agreed to amend the Company's environmental policy to commit to establishing an Environmental Management System (EMS) compliant with ISO 14001 by the end of calendar year 2005. This revised policy has been published and is available on the internet. A plan for the staged implementation of the EMS has been established and an external specialist environmental consultant is assisting implementation teams for both sites. ISO 14001 certification will demonstrate our commitment to reducing our overall impact on the local and global environment.

We are currently investigating the Environmental Aspect and Impact Analysis of our activities. This has led us to carrying out a detailed analysis of energy and water consumption at the Wellington site. In addition we are investigating working in partnership with waste management contractors to significantly increase the proportion of waste (including waste metal, cardboard, paper and plastic) that is recycled.

*Brian Williamson*

**B J Williamson**  
Group Operations Director  
9 September 2004

**Accident Incident Rate\***



\* Number of over 3 day accidents divided by the number of employees multiplied by 100,000

# board of directors

**James Espey, BCom MBA PhD**  
*Chairman*

Aged 61, James joined the Company in June 2000, bringing with him over 30 years' experience in the international consumer goods industry. Formerly Chairman of Seagram Distillers UK plc, he currently holds non-executive Directorships with Fuller Smith & Turner plc and A.G. Barr plc. In addition, he is Chairman of International Business Development and External Affairs for White & MacKay and Chairman of three private companies.

**Brian Williamson, MA Cantab**  
*Group Operations Director*

Aged 47, Brian joined the Company in January 2000, having previously been Managing Director of the European Aerosols business of CarnaudMetalbox. Prior to this he was Managing Director of Avimo Alvis Aerospace in Singapore.

**Tony Wardell, M Inst Pkg**  
*Group Managing Director*

Aged 58, Tony joined the business in 1963 and has held a number of senior positions, becoming a Director and General Manager of Aerosols International in 1984. In 1986 he led the management buy-out from Cadbury Schweppes and was appointed Managing Director. He is a trustee of Somerset Community Foundation.

**Richard Organ, MA Oxon**  
*Independent non-executive Director*

Aged 52, Richard joined the Company in 1996 and acted as interim Chairman from October 1999 to May 2000. He is considered by the Board to be the senior independent non-executive Director. He is currently Chairman of Dinkie Heel plc, having previously held senior positions with Jaeger and C & J Clark Ltd.

**Ian Mackinnon, BSc Hons FCA**  
*Group Finance Director*

Aged 40, Ian joined the Company in January 2000, having previously held senior finance roles with Invensys plc and Raychem Corporation. He worked for three years as a Chemical Engineer before qualifying as a Chartered Accountant. He is a member of the South West Regional Council of the CBI.

**Shena Winning, BA Hons FCA**  
*Independent non-executive Director*

Aged 50, Shena joined the Company in 2003 as an independent non-executive Director. Formerly a Director of Carpetright plc, she brings with her over 20 years' experience gained in the retail sector. Shena chairs the Audit Committee.

# directors' report

The Directors submit their report together with audited accounts for the year ended 30 June 2004.

## Results & Dividends

The Group profit attributable to shareholders amounted to £816,000 for the year to 30 June 2004 (2003: £718,000). The Directors propose a final dividend of 2.0p (2003: 2.0p) per ordinary share which, together with an interim dividend of 2.8p (2003: 2.8p) per ordinary share paid on 27 May 2004, makes a total of 4.8p (2003: 4.8p) per ordinary share for the year. Payment of the proposed final dividend, if approved at the Annual General Meeting, will be made on 29 October 2004 to shareholders registered at the close of business on 15 October 2004.

## Review of the Business and Future Developments

The principal activities of the Group are the formulation and manufacture of aerosol and non-aerosol products for retail distributors, the contract-filling of aerosols and the formulation and manufacture of cosmetic pencils and other cosmetic

products. A review of the business and future developments is set out in the reports on pages 3 to 12.

## Research and Development

The Group develops formulations for new products using its own laboratories and technical staff.

## Disabled Employees

The Group always carefully considers an application for employment by any disabled person. If an employee becomes disabled, it is standard practice to offer an alternative job in all but the most extreme circumstances and to provide retraining where necessary. The Group's training, development and promotion policies provide for equal opportunities for minority groups, including the disabled.

## Employee Involvement

The policy of informing and consulting with employees has continued by means of regular briefing groups and consultative committees. Employees are encouraged to present their views and suggestions in respect of the Group's performance. All

employees are formally advised of the Group's progress at least once a year, and manager and employee representatives are invited to share detailed performance figures on a quarterly basis.

## Supplier Payment Policy

The Group endeavours to ensure that payments to suppliers are made in accordance with those terms and conditions agreed between the Group and its suppliers. The Group does not follow any specific code or standard. At 30 June 2004, the Group had an average of 88 days purchases outstanding in trade creditors.

## Donations

During the year, the Group made charitable donations amounting to £3,750 (2003: £5,914). No contributions were made for political purposes.

## Auditors

Ernst & Young LLP have expressed their willingness to continue in office as auditors and a resolution proposing their reappointment will be presented at the Annual General Meeting.

# directors' report

## Directors and their Interests

The Directors who served during the year and their interests in the Company's share capital are as follows:

	30 June 2004		1 July 2003	
	Ordinary shares	Options to subscribe	Ordinary shares	Options to subscribe
J S Espey	45,000	—	45,000	—
J A Wardell	1,082,651	—	1,082,651	75,000
(i) 104,255	104,255	—	(i) 104,255	—
I A Mackinnon (i)	25,020	50,000	25,020	95,000
R T Organ	182,790	—	182,790	—
B J Williamson	13,415	60,000	13,415	110,000
S J Winning	25,000	—	25,000	—

(i) Non-beneficial

In accordance with the Articles of Association, J A Wardell and I A Mackinnon retire by rotation at the Annual General Meeting and, being eligible, offer themselves for re-election.

Details of the Directors' Service Contracts can be found on page 18.

Directors' shareholdings have not changed since the year end.

## Substantial Shareholdings

Except as disclosed under Directors and their Interests for J A Wardell, at 23 August 2004 notification had been received of the following holdings of ordinary shares of the Company required to be recorded in the register under Section 211 of the Companies Act 1985:

	Number of ordinary shares held	% of issued ordinary share capital
3i	1,524,000	13.5%
Western Selection	1,000,000	8.9%
R & A Persey	927,900	8.2%
Jupiter Asset Management	605,000	5.4%
Hunter Hall Investment Management	590,633	5.2%
A P & T M Dowsett	413,680	3.7%
M A Wardell	370,769	3.3%

# directors' report

## General Meeting

At the Annual General Meeting to be held on 14 October 2004, resolutions 8, 9, 10 and 11 will be special business. Further details of the following resolutions are set out in the notice of meeting on pages 49 and 50.

### a) Authority to allot shares

Resolution 8 seeks approval to renew the general authority of the Directors under Section 80 of the Companies Act 1985 to allot new shares. This general authority is, however, limited to the allotment of shares representing one third of the present issued share capital in addition to the allotment of shares to satisfy existing employee share options. If approved, the authority will expire at the conclusion of the next Annual General Meeting.

Resolution 9 seeks approval for renewal of the authority given at last year's Annual General Meeting to permit the Directors to allot for cash, otherwise than by rights issues, or to satisfy existing employee share options, shares representing 5% of the issued share capital. If approved, the authority will expire at the conclusion of the next Annual General Meeting.

### b) Purchase of own shares

Resolution 10 seeks approval for renewal of the authority given at last year's Annual General Meeting to permit the Company, subject to certain limitations, to purchase its own shares on the London Stock Exchange. The authority is limited to 1,125,000 ordinary shares or just under 10% of the issued share capital. The Directors consider it advantageous for them to be able to respond promptly should circumstances

arise in which they consider such a purchase would result in an increase in earnings per share and would be in the best interests of the Company.

c) *Amendment to Articles of Association*  
Resolution 11 seeks approval to amend the Articles of Association of the Company in order to resolve a technical conflict between the existing Articles of Association of the Company and the Combined Code in respect of the retirement and re-election of directors.

The Combined Code states that all directors should retire and be subject to re-election at intervals of no more than three years.

Due to the recent change of the Company's financial year end from December to June, three of the directors are required to be subject to re-election at the Annual General Meeting of the Company to be held on 14 October 2004. However, the articles of association of the Company do not allow for more than one third of the directors to retire at any one time. The current number of directors in office is six and so technically the three directors required to retire and be re-elected under the Combined Code cannot do so under the existing articles of association.

The Company proposes to deal with this technical conflict by passing a special resolution to amend the articles of association of the Company at the forthcoming Annual General Meeting. The articles of association will be amended to allow for such number of directors to retire from office by rotation as may from time to time be required, in order to comply with the Combined Code, providing that a minimum

of two directors shall not be so required to retire by rotation.

## Statement of Directors' Responsibilities in Respect of the Accounts

Company law requires the Directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the Company and of the Group and of the profit or loss of the Group for that year. In preparing these accounts, the Directors are required to:

- a) Select suitable accounting policies and then apply them consistently;
- b) Make judgements and estimates that are reasonable and prudent; and
- c) State whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and to enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

By Order of the Board



**A A Farrer-Halls**

Secretary

9 September 2004

# directors' remuneration report

The Directors submit their remuneration report for the year ended 30 June 2004. A resolution will be put to shareholders at the Annual General Meeting on 14 October 2004 inviting them to consider and approve this report.

## **Remuneration Committee**

The members of the remuneration committee are J S Espey (Chairman), R T Organ and S J Winning.

The committee meets at least twice a year to evaluate and determine the overall remuneration package for the executive Directors. The work of the remuneration committee includes a review of the remuneration levels within the market place as necessary and particular attention is given to the remuneration levels of fully listed companies of a similar size. The individual components of the remuneration package are discussed below.

## **Remuneration Policy**

The Company's policy is to provide an overall remuneration package for executive Directors in order to attract and retain high quality executives capable of achieving the Group's objectives. The package consists of basic salary, benefits, performance-

related bonuses, pensions and share options. The individual components of the remuneration package are discussed below.

## *Basic Salary and Benefits*

Salary and benefits are reviewed annually and changes in the level of basic salary are made on the basis of the Group's performance and the performance of the individual Directors in carrying out their duties. The executive Directors received an increase in basic salary of 3% at the last review in April 2004. Benefits principally comprise a contributory pension scheme, a fully expensed car, private healthcare and permanent health insurance.

## *Performance-Related Bonuses*

The executive Directors participate in a performance-related bonus scheme that rewards them for the Group achieving specified financial targets in the year. The fixed formulae for this bonus scheme are determined in advance of each year by the remuneration committee. We do not anticipate these arrangements changing in future years. No bonus has been awarded to executive Directors for the year ended 30 June 2004.

## *Pensions*

The executive Directors are members of the Swallowfield plc Directors Retirement Benefit Scheme. This is a defined contribution scheme, which is funded with the objective of providing two-thirds of the final pensionable remuneration after 20 years' service with a specified retirement age of 60. The level of the Company's contributions varies with each member. Pensionable remuneration comprises basic salary and certain benefits as the Remuneration Committee believes this to be an important part of the remuneration package.

## *Fees*

The executive Directors of the Board determine the fees for the non-executive Directors. Fees for the non-executive directors were increased by £1,000 at the last review in April 2004.

## *Share Options*

The Company operates an approved executive share option scheme under which options based upon a percentage of the executive's salary may be granted at the market price at the date of grant. No new options were granted to the executive Directors during the year under review, and no options were exercised during the year.

# directors' remuneration report

## Service Contracts

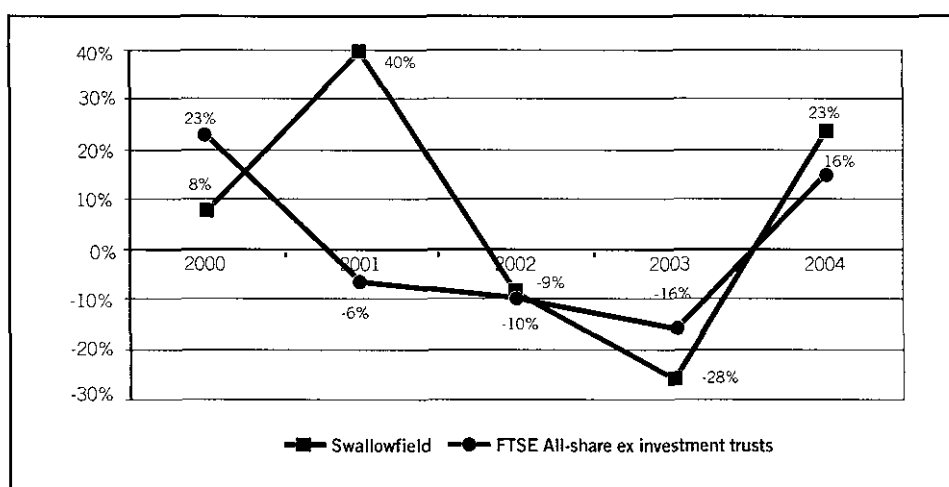
The Company's policy is for all executive Directors to have contracts of employment with 12 month notice periods. None of the non-executive Directors have service contracts, but each has a letter of appointment for a 12 month fixed term. The service contracts and letters of appointment include the following terms:

	Date of Contract	Unexpired Term Months	Notice Period Months
<b>Executive Directors</b>			
J A Wardell	1 June 1999	n/a	12
I A Mackinnon	4 January 2000	n/a	12
B J Williamson	25 January 2000	n/a	12
<b>Non-executive Directors</b>			
J S Espey	1 June 2004	9	—
R T Organ	1 July 2004	10	—
S J Winning	21 May 2004	9	—

## Performance Graph

The graph below shows the percentage change in the total shareholder return (with dividends reinvested) for each of the last five years ended 30 June of a holding of the Company's shares against the corresponding change in a hypothetical holding of shares in the FTSE All-share ex investment trusts index.

The FTSE All-share ex investment trusts index was selected as it represents a broad market index of listed trading companies.



# directors' remuneration report

## Information Subject to Audit

### Directors' Share Options

The following options have been granted to the Directors:

	Exercise Period	Exercise Price	At 1 July 2003	Lapsed During the Period	At 30 June 2004
J A Wardell	25 Apr 2004–25 Apr 2011	117.5p	75,000	(75,000)	—
I A Mackinnon	25 Apr 2004–25 Apr 2011 3 Feb 2003–3 Feb 2010	117.5p 73p	45,000 50,000	(45,000) —	— 50,000
			<b>95,000</b>	<b>(45,000)</b>	<b>50,000</b>
B J Williamson	25 Apr 2004–25 Apr 2011 3 Feb 2003–3 Feb 2010	117.5p 73p	50,000 60,000	(50,000) —	— 60,000
			<b>110,000</b>	<b>(50,000)</b>	<b>60,000</b>

All of the above are granted under the Swallowfield plc 1999 Executive Share Option Scheme.

All options have been granted as exercisable at the market price on the date of grant. The market price of shares at 30 June 2004 was 77.5p and the range during the 12 month period was 69.5p to 90.5p.

There were no share options exercised during the period nor since the year end.

During the year options over 170,000 ordinary shares lapsed due to performance conditions not being met.

### Directors' Remuneration and Pension Contributions for the year to 30 June 2004

	Basic Salary and Fees £'000	Performance-Related Benefits £'000	Performance-Related Bonuses £'000	Total Year to 30 June 2004 £'000	Total Year to 30 June 2003 £'000	Pension Year to 30 June 2004 £'000	Pension Year to 30 June 2003 £'000
<b>Executive Directors</b>							
J A Wardell	142	37	—	179	176	103	102
I A Mackinnon	88	16	—	104	103	30	29
B J Williamson	96	22	—	118	116	30	29
<b>Non-executive Directors</b>							
J S Espey	35	—	—	35	35	—	—
R T Organ	20	—	—	20	17	—	—
S J Winning (a)	20	—	—	20	3	—	—
J A Bryant-Pearson (b)	—	—	—	—	16	—	—
	<b>401</b>	<b>75</b>	<b>—</b>	<b>476</b>	<b>466</b>	<b>163</b>	<b>160</b>

(a) S J Winning was appointed on 21 May 2003.

(b) J A Bryant-Pearson served until her resignation on 21 May 2003.

Approved by the Board and signed on its behalf by



**A A Farrer-Halls**

Secretary

9 September 2004

# corporate governance

The Company is committed to high standards of corporate governance, and the Board is accountable to the Company's shareholders for maintaining these standards. This statement describes how the principles of corporate governance are applied to the Company and the Company's compliance with the provisions set out in Section 1 of the Combined Code.

## **Statement on Compliance with the Provisions of the Combined Code**

The Company has been in full compliance with the provisions set out in Section 1 of the Combined Code throughout the year.

## **Implementation of the New Combined Code**

The Company had implemented the provisions of the new Combined Code at 30 June 2004 and will be in compliance with the new code during the next financial year, with the following exceptions:

- The Company considers the Chairman to be an independent non-executive Director and, due to the size of the Company, the Chairman is a member of the Audit, Nomination and Remuneration Committees.
- Formal evaluations of the performance of the Board and the Chairman were not documented during the last 12 months but informal appraisals were undertaken.

## **Relations with Shareholders**

Communications with shareholders are given high priority. The Operating and Financial reviews on pages 7 to 11 include a detailed review of the business and future developments. There is regular dialogue with institutional shareholders including presentations after the Company's preliminary announcement of year end results. The Board also uses the Annual General Meeting to communicate with private and institutional investors and welcomes their participation. All Directors will be available to answer questions at the Annual General Meeting on 14 October 2004 and the resolutions to be proposed can be found on pages 49 and 50. The Chairman and non-executive Directors meet shareholders as requested. They also use the Company's broker and informal discussions after the Annual General Meeting to maintain open routes of communication with shareholders.

## **The Workings of the Board and its Committees**

### *The Board*

The Board currently comprises an independent non-executive Chairman, the Group Managing Director, two other executive Directors and two other independent non-executive Directors. The biographies appearing on page 13 demonstrate a range of experience and sufficient calibre to bring independent

judgement on issues of strategy, performance, resources and standards of conduct that are vital to the success of the Group. The Board is responsible to shareholders for the proper management of the Group. A statement of the Directors' responsibilities in respect of the accounts is set out on page 16 and a statement of going concern on page 11.

The Board has overall responsibility for the Group and there is a formal schedule of matters specifically reserved for decision by the Board. Each executive Director has been given responsibility for specific aspects of the Group's affairs and independent advice is available to all Directors. Appropriate training is given when Directors are appointed to the Board. The following represents a summary of matters reserved for decision by the Board:

- The approval of financial statements and significant accounting policies.
- The approval of interim and the recommendation of final dividends.
- The appointment, removal and remuneration of auditors, based on recommendations from the Audit Committee.
- Approval of circulars, listing particulars and other Stock Exchange documentation.
- Approval of the Group's strategy and annual operating budgets.

## corporate governance

- Changes relating to the Group's capital structure and financing arrangements.
- Board appointments and removals, including the Company Secretary.
- Remuneration of Directors and other senior executives.
- Terms of reference and membership of board committees.
- Major investments and divestments.
- All other matters that have a material impact on the Company in accordance with the Group's approval process.

The Board meets every four weeks to review trading performance, set and monitor strategy, approve matters reserved for decision by the Board and to ensure that adequate funding exists. All Directors are supplied with information in a manner to enable the Board to discharge its duties. The attendance at the 12 Board meetings held during 2004 for each of the Directors is as follows:

	Board Meetings	Nomination Committee	Remuneration Committee	Audit Committee
J S Espey	11	0	2	2
J A Wardell	12	0	2*	2*
I A Mackinnon	12	0	2*	2*
R T Organ	10	0	2	2
B J Williamson	12	0	1*	2*
S J Winning	11	0	2	2

\* in attendance only

### *Nomination Committee*

The Nomination Committee is chaired by the Group Chairman and includes the other two independent non-executive Directors together with the Group Managing Director. The Committee is responsible for proposing candidates for appointment to the Board, having regard to the balance and structure of the Board. In appropriate cases recruitment consultants are used to assist the process. No nominations were made during the year under review. The terms of reference of the Nomination Committee are published on the Company's web site. All Directors are subject to re-election every three years.

### *Audit Committee*

The members of the Audit Committee are S J Winning (chair), J S Espey and R T Organ. It meets at least twice a year to review the Company's accounting policies and reporting procedures, external audit reports and other relevant matters. The external auditors, Group Finance Director

and Group Managing Director are also invited to attend but are not entitled to vote. The terms of reference of the Audit Committee are published on the Company's web site. The Company receives non-audit services such as taxation and other consultancy advice from the Company's auditors. The Audit Committee assesses the independence of the external auditors by means of an internal review of relationships with the auditors together with a review of an annual report issued by the Auditors.

### *Remuneration Committee*

The Remuneration Committee is chaired by the Group Chairman and includes the other two independent non-executive Directors. The Group Managing Director and Group Finance Director attend the Remuneration Committee meetings by invitation but are not entitled to vote. The Committee reviews the terms and conditions of service of executive Directors, and ensures that salaries, bonuses and share option awards satisfy any relevant performance criteria. Further details of the Company's remuneration policies are given in the Directors' Remuneration Report on pages 17 to 19, and the terms of reference of the Remuneration Committee are published on the Company's web site.

# corporate governance

## Internal Control

The Board is responsible for the Group's system of internal control and for reviewing its effectiveness. Such a system can only provide reasonable and not absolute assurance against material misstatement or loss.

The key procedures established are as follows:

- Responsibility levels, the ethos of the Group, the delegation of authority and other control procedures, together with appropriate accounting policies, are communicated throughout the Group.
- The Group appoints experienced and professional staff of the necessary calibre, both through promotion and recruitment, to fulfil their responsibilities. The Group also carries out comprehensive training programmes.
- The Group maintains an annual budget process. The Board sets

budgets once per year and monitors actual performance against those budgets every four weeks. The Board also reviews forecasts and expectations in the light of up-to-date circumstances and takes action as appropriate.

- The Audit Committee considers significant control matters. Management letter points raised by the external auditors are discussed by the Audit Committee and are dealt with as appropriate.
- The Group maintains an expenditure approval process that ensures that the Board approves major expenditure and investments.
- The Board undertakes a review of internal controls annually.

The Group implemented the Turnbull guidance during 2000 and has continued in compliance during the year under review.

The Board has implemented the guidance

"Internal Controls: Guidance for Directors on the Combined Code", and has procedures in place for regular risk management reviews. These reviews focus on risk assessment, risk management and corrective actions, and are carried out by the main Board directly with senior managers who are actively encouraged to embed the process throughout their organisations. The reviews are conducted annually for Sales, Technical, Operations, Environmental, Finance and IT matters, and twice yearly for Health and Safety matters. The whole process is reviewed annually together with a further summary assessment of the major risks facing the business.

The Board has considered the need for an internal audit function and has concluded that, because of the size of the Group, it cannot be justified at present. The Board will review the decision next year.

# independent auditors' report

## To the Members of Swallowfield plc

We have audited the Group's financial statements for the year ended 30 June 2004 which comprise the Group Profit and Loss Account, Group Statement of Total Recognised Gains and Losses, Group and Company Balance Sheets, Group Statement of Cash Flows, and the related notes 1 to 27. These financial statements have been prepared on the basis of the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

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

## Respective Responsibilities of Directors and Auditors

The Directors are responsible for preparing the Annual Report, including the financial statements which are required to be prepared in accordance with applicable United Kingdom law and accounting standards as set out in the Statement of Directors' Responsibilities in relation to the financial statements.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards and the Listing Rules of the Financial Services Authority.

We report to you our opinion as to whether the financial statements give a true and fair

view and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or the Listing Rules regarding Directors' remuneration and transactions with the Group is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises the Chairman's Statement, Operating and Financial Reviews, Health, Safety and Environmental Report, information on Directors, Corporate Governance Statement, unaudited part of the Directors' Remuneration Report, Directors' Report, Five Year Summary and Notice of Annual General Meeting. We consider the implications for our report if we become aware of any apparent misstatement or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

## Basis of Audit Opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit

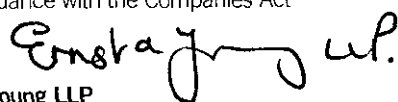
includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

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

## Opinion

In our opinion:

- the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 30 June 2004 and of the profit of the Group for the year then ended; and
- the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985.

  
Ernst & Young LLP  
Registered Auditor  
Bristol  
9 September 2004

# group profit and loss account

for the year ended 30 June 2004

	Notes	Operations		2004 £'000	2003 £'000
		before exceptional costs £'000	Exceptional costs £'000		
<b>Turnover</b>	2	48,763	—	<b>48,763</b>	54,663
Cost of sales		(40,722)	—	<b>(40,722)</b>	(46,701)
<b>Gross profit</b>		8,041	—	<b>8,041</b>	7,962
Net operating expenses	3, 4b	(6,061)	(396)	<b>(6,457)</b>	(6,543)
<b>Operating profit</b>	4a	1,980	(396)	<b>1,584</b>	1,419
Interest receivable	6	—	—	—	10
Interest payable	7	(419)	—	<b>(419)</b>	(454)
<b>Profit on ordinary activities before taxation</b>		1,561	(396)	<b>1,165</b>	975
Tax on profit on ordinary activities	8	(467)	118	<b>(349)</b>	(257)
<b>Profit attributable to shareholders</b>		1,094	(278)	<b>816</b>	718
Dividends	9	(541)	—	<b>(541)</b>	(541)
<b>Transferred to reserves</b>	22	553	(278)	<b>275</b>	177
<b>Earnings per share</b>					
— basic	10	9.7p		<b>7.2p</b>	6.4p
— diluted	10	9.7p		<b>7.2p</b>	6.4p

## group statement of total recognised gains and losses

for the year ended 30 June 2004

	2004 £'000	2003 £'000
Profit for the financial year	<b>816</b>	718

There are no gains or losses other than the profit for the financial year, or in the previous year.

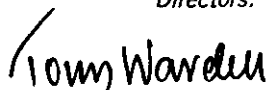
# group and company balance sheets

as at 30 June 2004

	Notes	Group		Company	
		2004 £'000	2003 £'000	2004 £'000	2003 £'000
<b>Fixed assets</b>					
Tangible assets	11	12,382	13,174	12,382	—
Investments	12	—	—	2,494	6,072
<b>Current assets</b>					
Stocks	13	7,982	7,616	7,982	—
Debtors	14	14,219	9,267	15,155	8,255
Cash at bank and in hand		94	21	7	608
		<b>22,295</b>	<b>16,904</b>	<b>23,144</b>	<b>8,863</b>
Creditors: amounts falling due within one year	15	(14,998)	(11,032)	(18,502)	(3,928)
<b>Net current assets</b>		<b>7,297</b>	<b>5,872</b>	<b>4,642</b>	<b>4,935</b>
<b>Total assets less current liabilities</b>		<b>19,679</b>	<b>19,046</b>	<b>19,518</b>	<b>11,007</b>
Creditors: amounts falling due after more than one year	16	(6,668)	(6,413)	(6,668)	(5,400)
Provisions for liabilities and charges	20	(947)	(844)	(947)	—
		<b>12,064</b>	<b>11,789</b>	<b>11,903</b>	<b>5,607</b>
<b>Capital and reserves</b>					
Called up share capital	21	563	563	563	563
Share premium	22	3,796	3,796	3,796	3,796
Revaluation reserve	22	124	138	—	—
Capital reserve	22	—	—	467	467
Profit and loss account	22	7,581	7,292	7,077	781
<b>Equity shareholders' funds</b>	23	<b>12,064</b>	<b>11,789</b>	<b>11,903</b>	<b>5,607</b>

Approved by the Board on  
9 September 2004

Directors:

  
J A Wardell

  
I A Mackinnon

# group statement of cash flows

for the year ended 30 June 2004

	Notes	2004 £'000	2003 £'000
Net cash inflow from operating activities	24a	1,897	1,069
<b>Returns on investments and servicing of finance</b>			
Interest received		—	10
Interest paid		(364)	(404)
Interest element of finance lease rentals		(55)	(50)
		(419)	(444)
<b>Corporation tax paid</b>		(190)	(534)
<b>Capital expenditure</b>			
Purchase of tangible fixed assets		(696)	(2,740)
Sale of tangible fixed assets		2	53
		(694)	(2,687)
<b>Equity dividends paid</b>		(541)	(541)
<b>Net cash inflow/(outflow) before financing</b>		53	(3,137)
<b>Financing</b>			
New loans		—	900
Repayment of loans		(32)	(97)
Capital element of finance lease rentals		(351)	(406)
		(383)	397
<b>Decrease in cash</b>	24b	(330)	(2,740)

## reconciliation of net cash flow to movement in net debt

	Notes	2004 £'000	2003 £'000
Decrease in cash		(330)	(2,740)
Cash outflow/(inflow) from changes in debt and lease financing		383	(397)
Change in net debt resulting from cash flows		53	(3,137)
New finance leases		—	(820)
Movement in net debt in the year		53	(3,957)
Net debt at 1 July		(8,834)	(4,877)
Net debt at 30 June	24b	(8,781)	(8,834)

# notes to the accounts

## **Note 1 Accounting Policies**

### *(a) Accounting convention*

The accounts are prepared under the historical cost convention, modified by the revaluation of certain freehold land and buildings, and in accordance with applicable accounting standards.

### *(b) Basis of consolidation*

The Group accounts consolidate the accounts of the Company and its subsidiary undertakings drawn up to 30 June each year. In accordance with the exemptions given by S230 of the Companies Act 1985, the Company has not presented its own profit and loss account.

### *(c) Depreciation*

Tangible fixed assets other than freehold land are depreciated over their useful lives to their estimated residual value on a straight-line basis. The principal rates of depreciation are as follows:

Plant	— 6.7% to 15% per annum
Vehicles	— 12.5% to 33% per annum
Office equipment	— 15% to 33% per annum

Freehold buildings are depreciated over their useful life on a straight-line basis, principally this is 50 years.

The carrying values of tangible fixed assets are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable.

### *(d) Foreign currencies*

Trading transactions denominated in foreign currencies are recorded in sterling at actual rates as at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are re-translated at the middle market rates ruling at the balance sheet date.

The accounts of overseas subsidiary undertakings are translated at the rates of exchange ruling at the balance sheet date. Exchange differences arising on re-translation of the net investment in overseas subsidiary undertakings are taken directly to reserves. All other exchange differences are taken to the profit and loss account.

### *(e) Goodwill*

Goodwill arising on acquisitions made prior to 1 January 1998 has been eliminated directly against reserves.

### *(f) Leasing and hire purchase commitments*

Assets obtained under finance leases and hire purchase contracts are capitalised in the balance sheet and are depreciated over their useful lives.

The interest element of the rental obligations is charged to the profit and loss account over the period of the lease and represents a constant proportion of the balance of capital repayments outstanding. The capital element of future obligations under leases and hire purchase contracts are included as liabilities in the balance sheet.

Rentals payable under operating leases are charged to the profit and loss account on a straight-line basis over the term of the lease.

# notes to the accounts

## *(g) Pension costs*

The cost of providing benefits under the Group's defined benefit pension scheme is charged over the working lives of the members. The Group also operates defined contribution schemes, contributions to which are charged to the profit and loss account as they become payable in accordance with the rules of the schemes.

## *(h) Research and development expenditure*

Expenditure is written off in the financial year in which it is incurred.

## *(i) Stocks*

Stocks are stated at the lower of cost and net realisable value. Costs are those incurred in bringing each product to its present location and condition. In the case of raw materials, cost comprises purchase costs including transport costs, calculated on a first-in, first-out basis. In the case of work in progress and finished goods, cost comprises direct material, direct labour plus attributable overheads.

Net realisable value is based on estimated selling price, less further costs expected to be incurred to completion and disposal.

## *(j) Taxation*

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more, or a right to pay less, tax in the future have occurred at the balance sheet date, with the following exceptions:

- provision is made for tax on gains arising from the revaluation of fixed assets, and gains on disposal of fixed assets that have been rolled over into replacement assets, only to the extent that, at the balance sheet date, there is a binding agreement to dispose of the assets concerned,
- provision is made for that tax that would arise on remittance of the retained earnings of overseas subsidiaries only to the extent that, at the balance sheet date, dividends have been accrued as receivable,
- deferred tax assets are recognised only to the extent that the Directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is measured on a non-discounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

## *(k) Turnover*

Turnover excludes value added tax and intra-Group sales and is stated net of discounts.

# notes to the accounts

## Note 2 Turnover and Segmental Analysis

Class of business	2004			2003		
	Turnover £'000	Profit before tax £'000	Net assets £'000	Turnover £'000	Profit before tax £'000	Net assets £'000
Aerosol products	36,520	1,986	14,820	40,835	2,223	13,923
Cosmetic products	12,243	(6)	6,398	13,828	(804)	6,780
	<u>48,763</u>		<u>21,218</u>	<u>54,663</u>		<u>20,703</u>
Operating profit before exceptional costs		1,980			1,419	
Exceptional costs		(396)			—	
Net interest payable		(419)			(444)	
Profit before tax		<u>1,165</u>			<u>975</u>	
Unallocated net liabilities			(9,154)			(8,914)
Group net assets			<u>12,064</u>			<u>11,789</u>
<b>Geographic segment</b>						
By destination:						
UK	34,049			40,410		
Continental Europe	12,545			12,043		
North America	1,393			980		
Far East	407			872		
Other	369			358		
	<u>48,763</u>			<u>54,663</u>		

Unallocated net liabilities comprise bank loans, overdrafts, finance leases, taxation and proposed dividend.

## Note 3 Exceptional Costs

An analysis of exceptional costs incurred in the year ended 30 June 2004, and their effect upon the taxation charge for the year is summarised below:

	Exceptional costs £'000	Tax credit £'000	Exceptional costs net of tax £'000
Aerosol products	285	(85)	200
Cosmetic products	111	(33)	78
	<u>396</u>	<u>(118)</u>	<u>278</u>

Exceptional costs mainly comprise fees to professional advisors and redundancy costs.

## notes to the accounts

### Note 4 Operating Profit

	2004 £'000	2003 £'000
(a) This is stated after charging:		
Depreciation of tangible fixed assets:		
Leased assets	274	225
Purchased assets	1,214	1,267
Research and development	756	834
Operating leases:		
Hire of plant and machinery	60	78
Rent of buildings	112	87
Auditors' remuneration:		
Audit services	71	55
Non-audit services	55	44
(b) Net operating expenses are analysed as follows:		
Distribution costs	2,309	2,510
Administrative expenses	4,148	4,033
	<b>6,457</b>	<b>6,543</b>

### Note 5 Staff Costs

	2004 £'000	2003 £'000
Wages and salaries	10,296	12,642
Social security costs	865	954
Other pension costs	850	983
	<b>12,011</b>	<b>14,579</b>

The average monthly number of employees, including executive Directors, during the year was:

	Number	Number
Production	537	674
Distribution	46	51
Administration	65	73
	<b>648</b>	<b>798</b>

Details of Directors' remuneration and share options are set out on pages 17 to 19.

## notes to the accounts

### Note 6 Interest Receivable

	2004 £'000	2003 £'000
Bank interest	—	10

### Note 7 Interest Payable

	2004 £'000	2003 £'000
Bank loans and overdraft	364	404
Finance lease interest	55	50
	419	454

### Note 8 Tax on Profit on Ordinary Activities

	Operations before exceptional costs £'000	Exceptional costs £'000	2004 £'000	2003 £'000
(a) Analysis of tax charge in the year				
UK corporation tax:				
— on profits of the year	482	(118)	364	250
— adjustment in respect of previous periods	(118)	—	(118)	(75)
Foreign tax:				
— on profits of the year	—	—	—	8
Total current tax	364	(118)	246	183
Deferred tax:				
Origination and reversal of timing differences:				
— on profits of the year	40	—	40	74
— adjustment in respect of previous periods	63	—	63	—
Total deferred tax	103	—	103	74
Tax on profit on ordinary activities	467	(118)	349	257

## notes to the accounts

### Note 8 Tax on Profit on Ordinary Activities *(continued)*

#### (b) Factors affecting current tax charge for the year

The tax assessed on the profit on ordinary activities for the year is slightly lower than the standard rate of UK corporation tax of 30% (2003: 30%). The differences are reconciled below:

	Operations before exceptional costs £'000	Exceptional costs £'000	2004 £'000	2003 £'000
Profit on ordinary activities before tax at 30%	468	(118)	350	293
Adjustments in respect of previous periods	(118)	—	(118)	(75)
Expenses not deductible for tax purposes	30	—	30	21
Unrelieved overseas tax losses	24	—	24	—
Capital allowances for the year in excess of depreciation	(54)	—	(54)	(64)
Other timing differences	14	—	14	6
Small companies rate adjustment	—	—	—	(6)
Higher taxes on overseas earnings	—	—	—	8
Total current tax	364	(118)	246	183

#### (c) Factors that may affect future tax charges

There are no factors which are expected to affect future tax charges.

### Note 9 Dividends

	2004 £'000	2003 £'000
May interim paid — 2.8p (2003: 2.8p) per share	316	316
Final proposed — 2.0p (2003: 2.0p) per share	225	225
	541	541

## notes to the accounts

### Note 10 Earnings per Share

	2004	2003
<b>(a) Basic</b>		
Profit on ordinary activities after taxation	£816,000	£718,000
Weighted average number of ordinary shares in issue during the year	11,256,416	11,256,416
Earnings per share	7.2p	6.4p
<b>(b) Diluted</b>		
Profit on ordinary activities after taxation	£816,000	£718,000
Basic weighted average number of ordinary shares in issue during the year	11,256,416	11,256,416
Dilutive potential ordinary shares:		
executive share options	9,285	11,424
	11,265,701	11,267,840
Diluted earnings per share	7.2p	6.4p
<b>(c) Basic excluding exceptional costs</b>		
Profit on ordinary activities after taxation	£816,000	£718,000
Exceptional costs (Note 3)	£396,000	—
Tax credit on exceptional costs	(£118,000)	—
Profit on ordinary activities after taxation excluding exceptional costs	£1,094,000	£718,000
Weighted average number of ordinary shares in issue during the year	11,256,416	11,256,416
Earnings per share	9.7p	6.4p
<b>(d) Diluted excluding exceptional costs</b>		
Profit on ordinary activities after taxation excluding exceptional costs	£1,094,000	£718,000
Basic weighted average number of ordinary shares in issue during the year	11,256,416	11,256,416
Dilutive potential ordinary shares:		
Executive share options	9,285	11,424
	11,265,701	11,267,840
Diluted earnings per share	9.7p	6.4p

## notes to the accounts

### Note 11 Tangible Fixed Assets

	Group			Company		
	Freehold land and buildings £'000	Plant and machinery £'000	Total £'000	Freehold land and buildings £'000	Plant and machinery £'000	Total £'000
Cost or valuation:						
At 1 July 2003	8,083	22,174	30,257	—	—	—
Additions	71	625	696	—	—	—
Intra Group Transfers	—	—	—	8,154	22,761	30,915
Disposals	—	(38)	(38)	—	—	—
<b>At 30 June 2004</b>	<b>8,154</b>	<b>22,761</b>	<b>30,915</b>	<b>8,154</b>	<b>22,761</b>	<b>30,915</b>
Depreciation:						
At 1 July 2003	2,164	14,919	17,083	—	—	—
Provided during the year	132	1,356	1,488	—	—	—
Intra Group Transfers	—	—	—	2,296	16,237	18,533
Disposals	—	(38)	(38)	—	—	—
<b>At 30 June 2004</b>	<b>2,296</b>	<b>16,237</b>	<b>18,533</b>	<b>2,296</b>	<b>16,237</b>	<b>18,533</b>
Net book value:						
<b>At 30 June 2004</b>	<b>5,858</b>	<b>6,524</b>	<b>12,382</b>	<b>5,858</b>	<b>6,524</b>	<b>12,382</b>
At 1 July 2003	5,919	7,255	13,174	—	—	—

The net book value of plant and machinery at 30 June 2004 included an amount of £1,657,000 (2003: £1,931,000) after depreciation charged in the year of £274,000 (2003: £225,000) in respect of assets held under finance leases.

Certain of the freehold land and buildings were revalued in 1988 on an existing use basis to a total of £785,000 (historical cost £468,000). If none of the freehold land and buildings had been revalued they would be restated at the following amounts:

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Historical cost	7,837	7,766	7,837	—
Accumulated depreciation based on cost	(2,103)	(1,986)	(2,103)	—
Net book value	5,734	5,780	5,734	—

The Group has adopted the transitional provisions contained in FRS 15 and accordingly has not updated the valuation of freehold land and buildings referred to above.

# notes to the accounts

## Note 12 Investments

	Company	
	2004 £'000	2003 £'000
Cost	7,073	7,073
Provision for permanent diminution in value of investment:		
At 1 July	(1,001)	(1,001)
Charge for the year	(3,578)	—
At 30 June	(4,579)	(1,001)
Net book value	2,494	6,072

The Group holds 100% of the voting rights and ordinary shares of the following principal subsidiary undertakings:

Name of company	Country of registration	Nature of business
Aerosols International Limited	England	Dormant
Cosmetics Plus Limited	England	Dormant
Swallowfield Consumer Products S.A.	Belgium	Dormant
Swallowfield Consumer Products Limited	England	Dormant

At the end of the financial year, the Group undertook a reorganisation of its legal entity and operational structures. This reorganisation was undertaken in order to streamline the Group's administration activities and to create a single customer facing organisation. As part of this restructure all UK operations previously part of Cosmetic Plus Limited and Aerosols International Limited were consolidated into Swallowfield plc. The carrying values of the investments held in Aerosols International Limited and Cosmetics Plus Limited were written down to reflect the net investment remaining in these entities after payment of dividends to Swallowfield plc.

## Note 13 Stocks

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Raw materials	3,722	3,222	3,722	—
Work in progress	298	549	298	—
Finished goods and goods for sale	3,962	3,845	3,962	—
	7,982	7,616	7,982	—

## notes to the accounts

### Note 14 Debtors

	Group		Company	
	2004	2003	2004	2003
	£'000	£'000	£'000	£'000
Trade debtors	13,317	8,461	13,317	—
Amounts owed by subsidiaries	—	—	956	8,255
Loans to employees	18	31	18	—
Other debtors	346	159	326	—
Prepayments and accrued income	538	616	538	—
	<b>14,219</b>	<b>9,267</b>	<b>15,155</b>	<b>8,255</b>

### Note 15 Creditors: amounts falling due within one year

	Group		Company	
	2004	2003	2004	2003
	£'000	£'000	£'000	£'000
Bank overdraft	1,858	1,455	1,858	—
Current instalments due on loans (note 18)	3	635	3	600
Obligations under finance leases (note 17)	346	352	346	—
Trade creditors	9,654	5,544	9,633	—
Amounts owed to subsidiaries	—	—	3,556	3,091
Current corporation tax	229	173	229	12
Other taxes and social security costs	676	1,179	654	—
Accruals and deferred income	2,007	1,469	1,998	—
Proposed dividend	225	225	225	225
	<b>14,998</b>	<b>11,032</b>	<b>18,502</b>	<b>3,928</b>

### Note 16 Creditors: amounts falling due after more than one year

	Group		Company	
	2004	2003	2004	2003
	£'000	£'000	£'000	£'000
Loans (note 18)	6,000	5,400	6,000	5,400
Obligations under finance leases (note 17)	668	1,013	668	—
	<b>6,668</b>	<b>6,413</b>	<b>6,668</b>	<b>5,400</b>

# notes to the accounts

## Note 17 Obligations Under Leases

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
<b>Finance leases</b>				
Amounts payable:				
Within one year	382	406	382	—
In second to fifth years inclusive	709	1,089	709	—
	<b>1,091</b>	<b>1,495</b>	<b>1,091</b>	<b>—</b>
Finance charges allocated to future periods	(77)	(130)	(77)	—
	<b>1,014</b>	<b>1,365</b>	<b>1,014</b>	<b>—</b>
Finance leases are analysed as follows:				
Current obligations	346	352	346	—
Non-current obligations	668	1,013	668	—
	<b>1,014</b>	<b>1,365</b>	<b>1,014</b>	<b>—</b>

## Operating leases

The annual commitments under non-cancellable operating leases are as follows:

	Group				Company			
	Other		Land & Buildings		Other		Land & Buildings	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Operating leases which expire:								
Within one year	12	16	3	33	12	—	3	—
In the second to fifth years inclusive	180	152	18	54	180	—	18	—
In over five years	10	4	36	—	10	—	36	—
	<b>202</b>	<b>172</b>	<b>57</b>	<b>87</b>	<b>202</b>	<b>—</b>	<b>57</b>	<b>—</b>

# notes to the accounts

## Note 18 Loans

Loans are repayable as follows:

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
After five years	4,200	3,000	4,200	3,000
Between two and five years	1,800	1,800	1,800	1,800
Between one and two years	—	600	—	600
	<b>6,000</b>	<b>5,400</b>	<b>6,000</b>	<b>5,400</b>
Within one year	3	635	3	600
	<b>6,003</b>	<b>6,035</b>	<b>6,003</b>	<b>6,000</b>
Wholly repayable within five years	3	35	3	—

Loans amounting to £6,003,000 (2003: £6,035,000) were secured by fixed and floating charges over certain of the Group's assets. Amounts payable after five years are part of a loan of £6,000,000 and bear interest at a rate of 1.00% above the UK base rate.

During the year we restructured the Group's borrowing facilities and as such this changed the repayment profile as shown above.

## Note 19 Financial Instruments

The financial review on pages 10 and 11 provides an explanation of the Group's approach to derivatives and other financial instruments. The disclosures below, apart from the analysis of currency exposures, exclude short-term debtors and creditors.

### Interest rate risk profile of financial assets and liabilities

	Group			Total £'000
	Fixed rate £'000	Floating rate £'000	No interest £'000	
<b>30 June 2004</b>				
Financial assets	—	87	7	94
Financial liabilities	3,008	5,867	—	8,875
<b>30 June 2003</b>				
Financial assets	—	13	8	21
Financial liabilities	3,008	5,847	—	8,855

Apart from £87,000 shown in financial assets, all the amounts above are denominated in pounds sterling.

Floating rate financial assets at 30 June 2004 and 30 June 2003 comprise cash surpluses that earn interest at rates based on the bank base rate.

Floating rate financial liabilities comprise sterling denominated bank loans, overdrafts and leases that bear interest at rates based on the bank base rate. In addition, the leases are subject to minimum interest rates. Fixed rate financial liabilities comprise finance leases, and a five year base rate swap for £3m at a fixed rate of 4.92%, entered into on 17 September 2002.

The weighted average interest rate on the fixed rate liabilities is 4.9% (2003: 4.9%). The weighted average period remaining at the balance sheet date for fixed rate liabilities is 3.3 (2003: 4.3) years.

## notes to the accounts

### Note 19 Financial Instruments (continued)

#### Currency exposures

Functional currency of Group operations		Net foreign currency monetary assets/(liabilities)				Total £'000
		Sterling £'000	Euro £'000	US Dollar £'000	Other £'000	
30 June 2004	Sterling	—	518	(17)	4	505
	Euro	87	—	—	—	87
	<b>Total</b>	<b>87</b>	<b>518</b>	<b>(17)</b>	<b>4</b>	<b>592</b>
30 June 2003	Sterling	—	971	(47)	4	925
	Euro	13	—	—	—	13
	<b>Total</b>	<b>13</b>	<b>971</b>	<b>(47)</b>	<b>4</b>	<b>938</b>

On 21 June 2004 (2003: 6 May 2003) the Group entered into a forward exchange contract to sell €250,000 on 7 July 2004 (2003: €450,000 on 21 July 2003), to hedge approximately 33% (2003: 33%) of the net euro exposure as at 30 June 2004 (2003: 30 June 2003).

#### Maturity of financial liabilities

	2004 £'000	2003 £'000
In one year or less or on demand	2,207	2,442
In more than one year but not more than two years	291	952
In more than two years but not more than five years	2,177	2,461
After five years	4,200	3,000
	<b>8,875</b>	<b>8,855</b>

#### Borrowing facilities

	2004 £'000	2003 £'000
Undrawn committed borrowing facilities:		
Expiring in one year or less	3,642	2,045

The undrawn committed facilities comprise the unutilised element of the Group's overdraft facility of £5.5m which is repayable on demand.

#### Fair values of financial assets and liabilities

There is no material difference between book value and fair value of either financial assets or financial liabilities at 30 June 2004 or 30 June 2003.

## notes to the accounts

### Note 20 Provisions for Liabilities and Charges

The movement in provisions for liabilities and charges is analysed as follows:

	<b>Group</b> Deferred taxation £'000	<b>Company</b> Deferred taxation £'000
At 1 July 2003	844	—
Intra-group transfer	—	947
Provided during the year	103	—
<b>At 30 June 2004</b>	<b>947</b>	<b>947</b>

Deferred tax is represented by:

	<b>Group</b>		<b>Company</b>	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Capital allowances in advance of depreciation	978	862	978	—
Other timing differences	(31)	(18)	(31)	—
	<b>947</b>	<b>844</b>	<b>947</b>	<b>—</b>

# notes to the accounts

## Note 21 Share Capital

	2004 £'000	2003 £'000
<b>Equity ordinary share capital</b>		
Authorised share capital 25,800,000 shares of 5p each	1,290	1,290
Allotted, called-up and fully paid ordinary shares		
11,256,416 (2003: 11,256,416) shares of 5p each	563	563

## Share options

No options to subscribe for shares in the Company were granted during the year or prior year.

At 30 June 2004 certain Directors and employees held options to subscribe for shares in the Company as described below:

Scheme	Date of grant	Number of shares under option	Exercise price	Normal earliest exercise date	Latest exercise date
Swallowfield plc 1999 Executive Share Option Scheme	02 February 2000	110,000	73p	February 2003	February 2010

During the year, options over 254,000 of the Company's ordinary share capital lapsed.

# notes to the accounts

## Note 22 Reserves

	Group		
	Share premium £'000	Revaluation reserve £'000	Profit and loss account £'000
At 1 July 2003	3,796	138	7,292
Revaluation reserve transfer	—	(14)	14
Retained profit for the year	—	—	275
<b>At 30 June 2004</b>	<b>3,796</b>	<b>124</b>	<b>7,581</b>

The cumulative amount of goodwill eliminated directly against reserves at 30 June 2004 as a matter of accounting policy for acquisitions made prior to 1 January 1998 is £1,632,000 (2003: £1,632,000). This goodwill would be charged in the profit and loss account in the event of disposal of the acquired businesses.

	Company		
	Share premium £'000	Capital reserve £'000	Profit and loss account £'000
At 1 July 2003	3,796	467	781
Profit for the year	—	—	6,837
Dividends	—	—	(541)
<b>At 30 June 2004</b>	<b>3,796</b>	<b>467</b>	<b>7,077</b>

Swallowfield plc received dividends from Aerosols International Limited and Cosmetics Plus Limited, following the restructuring referred to in Note 12.

Following the transfer of assets from subsidiary companies, amounts totalling £124,000 of the Company's profit and loss account is undistributable.

## Note 23 Reconciliation of Movement in Shareholders' Funds

	Group	
	2004 £'000	2003 £'000
Profit attributable to shareholders	816	718
Dividends	(541)	(541)
Net addition to shareholders' funds	275	177
Equity shareholders' funds at 1 July	11,789	11,612
Equity shareholders' funds at 30 June	12,064	11,789

# notes to the accounts

## Note 24 Notes to Statement of Cash Flows

(a) Reconciliation of operating profit to net cash inflow from operating activities:

	Operations before		Group	
	exceptional	Exceptional	2004	2003
	costs	costs	2004	2003
	£'000	£'000	£'000	£'000
Operating profit	1,980	(396)	1,584	1,419
Depreciation	1,488	—	1,488	1,492
Profit on disposal of fixed assets	(2)	—	(2)	(17)
(Increase)/decrease in stocks	(366)	(366)	(366)	1,010
(Increase) in debtors	(4,952)	—	(4,952)	(763)
Increase/(decrease) in creditors	3,886	259	4,145	(2,072)
Net cash inflow from operating activities	2,034	(137)	1,897	1,069

(b) Analysis of net debt

	1 July	Cash flow	Group	
	2003		Non-cash	30 June
	£'000		changes	2004
	£'000	£'000	£'000	£'000
Cash at bank and in hand	21	73	—	94
Bank overdraft	(1,455)	(403)	—	(1,858)
Cash	(1,434)	(330)	—	(1,764)
Loans	(6,035)	32	—	(6,003)
Finance leases	(1,365)	351	—	(1,014)
Total	(8,834)	53	—	(8,781)

## Note 25 Capital Commitments

	Group	
	2004	2003
	£'000	£'000
Contracted for but not provided	462	69

# notes to the accounts

## Note 26 Pension Arrangements

The Group operates two defined contribution pension plans and a defined benefit plan, all of which are funded by the payment of contributions to separately administered plans.

### (a) Defined contribution pension plans

The Group operates two separate defined contribution pension schemes. The Swallowfield plc Directors' Retirement Benefit Scheme is operated for Directors and senior employees and is described on page 17. The Cosmetics Plus Limited Pension Scheme is operated as a Group Personal Pension Plan.

### (b) Defined benefit pension plan

For the Aerosols International Limited defined benefit scheme the pension cost is assessed in accordance with the advice of independent qualified actuaries, using the projected unit method. The most recent valuation was conducted as at 6 April 2002. The assumptions which have the most significant effect on results are the investment rate of return at 6.9% per annum, salary growth at 5.0% per annum, price inflation at 3.0% per annum and present and future pensions to increase by 2.9% per annum on that part of the pension in excess of the members' guaranteed minimum pension.

The 2002 valuation showed that the market value of the scheme's assets was £7,003,000 and this was sufficient to cover 101.7% of the benefits that had accrued to members, after allowing for future increases in earnings. The future contributions rate of 14.5% is in accordance with the recommendation of the actuary, and is expected to maintain the funding level at 101.7% until the next valuation of the plan which is due no later than 6 April 2005. The effect of amortising this surplus over the working lives of scheme members would not be material.

## Note 27 FRS17 Retirement Benefits — Transitional Disclosures

### (a) Composition of the defined benefit scheme

The Group operates a defined benefit scheme in the UK. A full actuarial valuation was carried out as at 6 April 2002 and updated to 30 June 2004 by a qualified independent actuary. The contribution rate from October 2002 onwards was 14.5% of pensionable pay. Prior to this date the agreed contribution rate was 13.5% of pensionable pay.

The major assumptions used by the actuary were:

	2004	2003	2002
Rate of increase in salaries	5.15%	4.60%	4.75%
Rate of increase in pensions in payment	2.85%	2.60%	2.75%
Discount rate	5.75%	5.50%	6.00%
Inflation assumption	3.15%	2.60%	2.75%

## notes to the accounts

### Note 27 FRS17 Retirement Benefits — Transitional Disclosures *(continued)*

(b) The assets in the scheme and the expected rates of return

	Long-term rate of return expected at 30 June 2004	Value at 30 June 2004 £'000	Long-term rate of return expected at 30 June 2003	Value at 30 June 2003 £'000	Long-term rate of return expected at 30 June 2002	Value at 30 June 2002 £'000
Equities	7.60%	5,262	7.00%	4,892	7.00%	5,209
Bonds	5.50%	2,283	4.50%	784	5.00%	985
Other	4.50%	341	3.75%	840	3.50%	285
Total market value of assets		<b>7,886</b>		6,516		6,479
Present value of scheme liabilities		<b>(11,437)</b>		(9,769)		(8,016)
Scheme deficit		<b>(3,551)</b>		(3,253)		(1,537)
Related deferred tax asset		<b>1,065</b>		976		461
Net pension liability		<b>(2,486)</b>		(2,277)		(1,076)

(c) Amounts which would be charged to operating profit

	2004 £'000	2003 £'000
Current service cost	590	460
Past service cost	—	—
Total operating charge	<b>590</b>	460

(d) Amounts which would be debited to other finance charges

	2004 £'000	2003 £'000
Expected return on pension scheme assets	420	437
Interest on pension scheme liabilities	(575)	(477)
Net charge	<b>(155)</b>	(40)

## notes to the accounts

### Note 27 FRS17 Retirement Benefits — Transitional Disclosures *(continued)*

(e) Amounts which would be recognised in the statement of total recognised gains and losses (STRGL)

	2004 £'000	2003 £'000
Actual return less expected return on pension scheme assets	597	(831)
Experience gains and losses arising on the scheme liabilities	9	(135)
Changes in assumptions underlying the present value of the scheme liabilities	(595)	(773)
Actuarial surplus/(deficit) recognised in STRGL	11	(1,739)

(f) Movement in the deficit during the year

	2004 £'000	2003 £'000
Deficit in scheme at 1 July	(3,253)	(1,537)
Movement in the year:		
Current service cost	(590)	(460)
Contributions	436	523
Past service cost	—	—
Other finance charges	(155)	(40)
Actuarial surplus/(deficit)	11	(1,739)
Deficit in scheme at 30 June	(3,551)	(3,253)

## notes to the accounts

### Note 27 FRS17 Retirement Benefits — Transitional Disclosures *(continued)*

(g) History of experience gains and losses

	Year ended 30 June 2004	Year ended 30 June 2003	18 months ended 30 June 2002
Difference between the expected and actual return on scheme assets:			
Amount £'000	597	(831)	(2,115)
Percentage of scheme assets	7.6%	(12.8%)	(32.6%)
Experience gains/(losses) on scheme liabilities:			
Amount £'000	9	(135)	139
Percentage of the present value of scheme liabilities	0.1%	1.4%	1.7%
Total actuarial gain/(loss) recognised in statement of total recognised gains and losses:			
Amount £'000	11	(1,739)	(1,516)
Percentage of the present value of scheme liabilities	0.1%	(17.8%)	(18.9%)

(h) Reconciliations of net assets and reserves under FRS17

	Net Assets 2004 £'000	Net Assets 2003 £'000	Profit & Loss Reserve 2004 £'000	Profit & Loss Reserve 2003 £'000
<b>Group</b>				
Net assets/profit & loss reserve as stated in balance sheet	12,064	11,789	7,581	7,292
FRS17 net pension liability	(2,486)	(2,277)	(2,486)	(2,277)
Net assets/profit & loss reserve including defined benefit liabilities	9,578	9,512	5,095	5,015
<b>Company</b>				
Net assets/profit & loss reserve as stated in the balance sheet	11,903	5,607	7,077	781
FRS17 net pension liability	(2,486)	—	(2,486)	—
Net assets/profit & loss reserve including defined benefit liabilities	9,417	5,607	4,591	781

## five year summary

The following five year summary has been produced to allow improved comparisons to be made between the current results and those of prior years.

	Notes	audited Financial Year 2004 £'000	audited Financial Year 2003 £'000	unaudited Financial Year 2002 £'000	unaudited Financial Year 2001 £'000	unaudited Financial Year 2000 £'000
First day of financial year	(a)	1 July 2003	1 July 2002	17 June 2001	18 June 2000	20 June 1999
Last day of financial year	(a)	30 June 2004	30 June 2003	30 June 2002	16 June 2001	17 June 2000
Number of weeks in financial year	(b)	52	52	54	52	52
<b>Profit and Loss Account</b>						
Turnover		48,763	54,663	44,404	40,425	37,600
Adjustment to 52 week basis	(b)	—	—	(1,088)	—	—
Adjusted turnover		48,763	54,663	43,316	40,425	37,600
Operating profit		1,980	1,419	2,628	2,177	2,205
(Exceptional costs)/income		(396)	—	—	20	54
Interest		(419)	(444)	(296)	(354)	(454)
Profit before taxation		1,165	975	2,332	1,843	1,805
Taxation		(349)	(257)	(645)	(444)	(501)
Profit attributable to shareholders		816	718	1,687	1,399	1,304
Dividends		(541)	(541)	(541)	(472)	(394)
Retained earnings		275	177	1,146	927	910
<b>Balance Sheet</b>						
Fixed assets		12,382	13,174	11,142	10,228	10,516
Net current assets		7,297	5,872	6,427	6,610	5,146
Total assets less current liabilities		19,679	19,046	17,569	16,838	15,662
Long-term creditors:						
Loans and lease finance		(6,668)	(6,413)	(5,187)	(5,669)	(5,243)
Deferred tax		(947)	(844)	(770)	(716)	(720)
Provision for liabilities		—	—	—	—	(146)
Equity		12,064	11,789	11,612	10,453	9,553
Net debt		8,781	8,834	4,877	4,777	5,825
<b>Segmental Analysis</b>						
Aerosol products:						
Turnover		36,520	40,835	31,783	28,880	25,041
Operating profit		1,986	2,223	2,710	2,400	2,470
Cosmetic products:						
Turnover		12,243	13,828	11,533	11,545	12,559
Operating loss		(6)	(804)	(82)	(223)	(265)
<b>Statistics</b>						
Weighted average number of shares in issue		11,256,416	11,256,416	11,256,416	11,256,416	11,256,416
Undiluted earnings per share		7.2p	6.4p	15.0p	12.4p	11.6p
Earnings per share excluding (exceptional costs)/income		9.7p	6.4p	15.0p	11.7p	11.1p
Gearing		73%	75%	42%	46%	61%
Dividends per share		4.8p	4.8p	4.8p	4.2p	3.5p

### Notes

- (a) For 2002 and prior years the five year summary is based on previously reported interim and full year reports as adjusted for the retrospective implementation of FRS19, *Deferred Tax*. The results for each of these financial years comprised the interim results for the first half of the calendar year in which the financial year ended, together with the second half of the previous calendar year. The balance sheet and net debt numbers are those reported at the last day of the financial year.
- (b) Except for turnover, where the relevant adjustment has been shown above, no material changes would be required to the profit and loss account to adjust the financial year 2002 numbers to a 52 week basis.

# notice of meeting

Notice is hereby given that the Eighteenth Annual General Meeting of the Company will be held at the Castle Hotel, Taunton, Somerset on Thursday 14 October 2004 at 12.00 noon for the purpose of considering and if thought fit passing the following resolutions:

- 1 To receive and adopt the annual statement of accounts and the reports of the Directors and auditors for the year ended 30 June 2004.
- 2 To declare a final dividend of 2.0p per ordinary share.
- 3 To receive and adopt the Directors' Remuneration Report for the year ended 30 June 2004.
- 4 To re-elect J A Wardell as a Director.
- 5 To re-elect I A Mackinnon as a Director.
- 6 To re-appoint Ernst & Young LLP as auditors.
- 7 To authorise the Directors to fix the remuneration of the auditors.

As special business to consider and, if thought fit, pass Resolution 8 as an Ordinary Resolution and Resolutions 9, 10 and 11 as Special Resolutions.

## **8 Ordinary Resolution**

THAT the Directors of the Company be and are hereby generally and unconditionally authorised in accordance with Section 80 of the Companies Act 1985 ('the Act') to exercise all the powers of the Company to allot relevant securities (as defined in Section 80 of the Act) up to the aggregate nominal amount of £193,107. This authority shall expire at the conclusion of the next Annual General Meeting of the Company after the passing of this resolution save that the Company may before such expiry make an offer or agreement which would or might require relevant securities to be allotted after such expiry and accordingly the Directors may allot relevant securities pursuant to any such offer or agreement as if such authority had not expired; and all previous authorities under Section 80 of the Act shall henceforth cease to have effect.

## **9 Special Resolution**

THAT the Directors of the Company be and are hereby empowered under Section 95 of the Companies Act 1985 ('the Act') to allot equity securities within the meaning of Section 94 of the Act ('equity securities') for cash, pursuant to the authority under Section 80 of the Act granted by the preceding resolution, as if Section 89(1) of the Act did not apply to any such allotment, provided that this authority (which supersedes and replaces the authority granted to the Directors under Section 95 of the Act on 14 Oct 2003) shall be limited to:

- a) The allotment of equity securities in connection with a rights issue in favour of ordinary shareholders where the equity securities respectively attributable to the interests of all ordinary shareholders are proportionate (as nearly as may be) to the respective numbers of ordinary shares held by them provided that the Directors shall have the right to make exclusions or other arrangements in connection with the offer as they deem necessary or expedient:
  - (i) to deal with equity securities representing fractional entitlements; and
  - (ii) to deal with legal or practical problems arising in any overseas territory or by virtue of shares being represented by depository receipts, the requirements of any regulatory body or any stock exchange; or any other matter whatsoever;
- b) The allotment of equity securities for the purpose of any option, incentive or profit sharing scheme (whether or not an employees' share scheme as defined in the Act) being a scheme approved by the shareholders in general meeting; and
- c) The allotment (otherwise than pursuant to sub-paragraphs (a) and (b) above) of equity securities for cash up to an aggregate nominal value of £28,141.

This power shall expire at the conclusion of the next Annual General Meeting of the Company after the passing of this resolution save that the Company may before such expiry make an offer or agreement which would or might require equity securities to be allotted after such expiry and accordingly the Directors may allot equity securities pursuant to any such offer or agreement as if this power had not expired; and all previous authorities under Section 95 of the Act shall henceforth cease to have any effect.

# notice of meeting

## 10 Special Resolution

THAT the Company be and is hereby generally and unconditionally authorised in accordance with Part V of the Companies Act 1985 ('the Act'), to make market purchases (within the meaning of Section 163 of the Act) of its own ordinary shares on such terms and in such manner as the Directors of the Company shall determine provided that:

- (a) The maximum number of ordinary shares hereby authorised to be purchased is 1,125,000.
- (b) The minimum price which may be paid for each ordinary share is its nominal value exclusive of any expenses payable by the Company.
- (c) The maximum price which may be paid for each ordinary share is an amount equal to 105 per cent of the average of the closing middle market quotations for the ordinary shares of the Company (derived from the Daily Official List of the London Stock Exchange) on the five business days immediately preceding the day on which the ordinary share is purchased.

This power shall expire at the conclusion of the next Annual General Meeting of the Company after the passing of this resolution, save that the Company may after such expiry make a purchase of ordinary shares in execution of a contract of purchase that was made under and before expiry of such authority.

## 11 Special Resolution

THAT the draft article set out below be and is adopted by the Company in substitution for article 84 of its existing articles of association.

Subject to Article 90 at each Annual General Meeting such number of directors shall retire from office by rotation as may from time to time be required, in order to comply with the Combined Code, providing that a minimum of two directors shall not be so required to retire by rotation.

### By Order of the Board

**Alan Farrer-Halls**  
*Secretary*

**Swallowfield House**  
**Station Road**  
**Wellington**  
**Somerset**

**9 September 2004**

A member entitled to attend and vote at the meeting is entitled to appoint one or more proxies (whether members or not) to attend and on a poll vote instead of him/her.

Forms of proxy must be deposited at Computershare Investor Services PLC, Registrars, PO Box 1075, Bristol, BS99 3FA, not less than 48 hours before the time fixed for the meeting.

Only members entered in the register of members of the Company as at 6.00 pm on Tuesday 12 October shall be entitled to attend and vote at the above meeting. Changes to entries in the register of members after 6.00 pm on Tuesday 12 October shall be disregarded in determining the rights of a person to attend and vote at the meeting. These requirements reflect Regulation 41 of the Uncertificated Securities Regulations 2001.

The register of the Directors' interests in the capital of the Company, and copies of the Directors' contracts of service with the Company will be available for inspection at the Registered Office from the date of this notice until 14 October 2004, and at the Annual General Meeting, from 15 minutes prior to the meeting.

# Swallowfield plc form of proxy

I/We .....  
(Please use block capitals)

of .....  
.....

hereby appoint the chairman of the meeting or\* .....

As my/our proxy to attend and on a poll to vote for me/us on my/our behalf at the Annual General Meeting of the Company to be held on Thursday 14 October 2004 and at any adjournment thereof. I/We direct my/our proxy to vote on the resolutions to be proposed at the Annual General Meeting as follows:

**Resolutions**

	<i>For</i>	<i>Against</i>
1. To receive and adopt the annual report and accounts for the year ended 30 June 2004.		
2. To declare a final dividend of 2.0p per ordinary share.		
3. To receive and adopt the Directors' Remuneration Report for the year ended 30 June 2004.		
4. To re-elect J A Wardell as a Director.		
5. To re-elect I A Mackinnon as a Director.		
6. To reappoint Ernst & Young LLP as auditors.		
7. To authorise the Directors to fix the remuneration of the auditors.		
8. To authorise the Directors to allot relevant securities.		
9. As a special resolution, to authorise the Directors to issue equity securities for cash, subject to limitations.		
10. As a special resolution, to authorise the Company to purchase its own shares, subject to limitations.		
11. As a special resolution, to authorise the Company to amend its articles of association.		

Dated the ..... day of .....2004

Signature.....

Please indicate your vote by an X in the appropriate boxes. Unless otherwise indicated, the proxy will abstain or vote on all business transacted at the meeting as he/she thinks fit.

**NOTES:**

1. This form of proxy, together with any power of attorney (or certified copy thereof) under which it is signed, must be deposited at Computershare Investor Services PLC, Registrars at the address overleaf not later than 48 hours before the meeting.
2. In the case of a corporation, the proxy must be either given under its common seal or signed under the hand of an officer or attorney duly authorised.
3. In the case of a joint holding, the vote of the senior holder who tenders a vote (seniority being determined by the order in which the names are registered) will be accepted to the exclusion of the votes of the other joint holders.

\* If you wish to appoint a proxy other than the chairman of the meeting, please amend and insert the name and address of your proxy.



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**Computershare Investor Services PLC**  
**PO Box 1075**  
**BRISTOL**  
**BS99 3FA**

First fold

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# corporate directory

## Directors

J S Espey (Chairman)  
J A Wardell (Group Managing Director)  
I A Mackinnon (Group Finance Director)  
B J Williamson (Group Operations Director)  
R T Organ (non-executive Director)  
S J Winning (non-executive Director)

## Secretary

A A Farrer-Halls FCCA

## Registered Office

Swallowfield House  
Station Road  
Wellington  
Somerset  
TA21 8NL

## Stockbrokers

Rowan Dartington & Co. Ltd  
Colston Tower  
Colston Street  
Bristol  
BS1 4RD

## Registered Number

01975376

## Financial Calendar

Annual General Meeting	14 October 2004
Payment date for final dividend	29 October 2004
Interim results announcement	March 2005
Payment date for 2005 interim dividend	May 2005
Preliminary announcement of 2005 results	September 2005
2005 Annual General Meeting	October 2005

## Registrars

Computershare Investor Services PLC  
Registrars  
PO Box 82  
The Pavilions  
Bridgwater Road  
Bristol  
BS99 7NH

## Auditors

Ernst & Young LLP  
One Bridewell Street  
Bristol  
BS1 2AA

## Solicitors

Osborne Clarke  
2 Temple Back East  
Temple Quay  
Bristol  
BS1 6EG

## Bankers

National Westminster Bank plc  
12 Fore Street  
Wellington  
Somerset  
TA21 8AL

## Website Address

[www.swallowfield.com](http://www.swallowfield.com)

**Swallowfield plc**

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