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spirax sarco

Spirax Sarco provides knowledge, service and products worldwide for the control and efficient use of steam and other industrial fluids and for peristaltic pumping. Spirax Sarco's position as the world leader is founded on its long held strategy of investing for growth.

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

Spirax-Sarco Engineering plc final results

31st December	2005	2004	Change
Revenue	£349.1m	£316.0m	+10%
Operating profit	£55.2m	£48.0m	+15%
Operating profit margin	15.8%	15.2%	
Profit before taxation	£57.0m	£48.7m	+17%
Earnings per share	50.0p	43.1p	+16%
Dividends per share	23.8p	21.4p	+11%
Return on capital employed	30.4%	27.2%	
Net cash	£19.0m	£1.3m	

- Good growth in Asia and Americas
- Operating profit up 15%
- Improved operating margin of 15.8%
- Strong cash flow
- Dividend for the full year up 11%

CHAIRMAN'S STATEMENT

I am pleased to report a further good set of results for 2005. Following the progress in the first half of the year, the momentum was maintained through the second half. Sales increased 10% in the full year, operating profit was 15% ahead and pre-tax profit rose by 17% to a record £57.0 million, which includes favourable exchange movements and a small contribution from acquisitions. These trading results together with control of the balance sheet are reflected in the improved return on capital employed, the strong cash flow and the recommended 11% increase in dividend for the year.

M. Townsend, Chairman

This is the first full year's results to have been prepared under International Financial Reporting Standards (IFRS) and all comparisons are with 2004 results which have been restated to comply with IFRS.

Group sales were £349.1 million which compares with £316.0 million in 2004. Sterling was weaker against most currencies in 2005 which increased turnover on translation by £8.1 million. At constant exchange rates turnover grew by 8%; excluding acquisitions the underlying increase was 6%.

Operating profit increased to £55.2 million from £48.0 million in 2004, an increase of 15%. The effect of exchange rate movements was to increase operating profits by £2.1 million. The Group operating profit margin improved to 15.8% compared with 15.2% in 2004, the improvement largely arising from the higher sales. We strengthened our position as the world leader in providing advice and products for the efficient use of both steam and peristaltic pumps. Our businesses in the Americas and Asia made good progress but the markets in the UK and Continental Europe were, for the most part, quiet and our progress in those economies was, therefore, constrained.

Net finance income was £0.9 million which compares with a figure close to zero in 2004. This increased income results partly from the strong cash flow in the year and partly from an improved net finance income in respect of defined benefit pension funds.

The Group's share of profits of Associates increased to £0.9 million (2004: £0.7 million). The Group pre-tax profit increased by 17% to £57.0 million (2004: £48.7 million).

The tax charge at 33% was similar to 2004 and earnings per share rose to 50.0p from 43.1p, an increase of 16%.

The Board has decided to recommend a final dividend of 17.0p per share which, together with the interim dividend of 6.8p per share paid in November, makes a total dividend for the year of 23.8p. This compares with a total dividend of 21.4p per share last year, an increase of 11%. The cost of the interim and final dividends is £18.3 million, which is covered 2.1 times by earnings. No scrip alternative to the cash dividend is being offered.

On 9th June 2005 we announced the acquisition of Actuators and Controls (Pty) Limited and Proportional Control Technology (Pty) Limited, manufacturers of control valves and actuators for steam and high pressure industrial processes. Both businesses are based in Johannesburg, South Africa. The consideration was R28.9 million (£2.3 million).

On 27th June 2005 we announced the acquisition, for a consideration of US$4.5 million (£2.5 million), of the assets and business of EMCO Flow Systems of Longmont, Colorado. EMCO is a provider of flow measurement products for HVAC, industrial and commercial applications. The trading performance of these companies and the process of their integration has started well.

The Group's record of good cash generation continued and net cash balances increased by £17.7 million to £19.0 million at 31st December 2005. Net capital expenditure in the year amounted to £12.0 million which compares with £13.8 million in 2004. We continue to invest in our workforce, equipment and systems to improve our efficiency and to support our long-term growth plans. We also improved the utilisation of our existing plant. We intend, in 2006, to accelerate our contributions to the defined benefit pension schemes and to buy in some shares to help satisfy the requirements of the share-based payment schemes.

We recently announced that Graham Marchand will be retiring from the Board on 30th June 2006. Graham started work at Spirax in 1987 and came onto the Board in 1992. Throughout his time at Spirax, Graham has been responsible for many of our operating companies at first in Europe and, later, the Americas. He has helped to develop those businesses and we have to thank him for much of the growth and development in those markets in recent years.

We have also announced that we will be welcoming Mark Vernon to the Board from 1st July 2006 with responsibility for the Americas and Group Marketing. Mark, who is a US citizen, joined Spirax in 2003 to run the Spirax Sarco business in the USA. Mark has a great deal of relevant experience having worked for many years in the controls industry. We look forward to Mark making a strong contribution to the future development of the Group.

Chris Ball and Tim Fortune retired from the Board on 29th April and 12th May 2005 respectively. Both Tim and Chris gave generously of their time and talents over many years, and their energy and experience were major contributors to the Group's long and successful history of growth and profitability. The Board wishes to put on record its thanks to Tim and Chris for their contribution to the performance of the Group. I was pleased to take over the chairmanship of the Board from Tim Fortune on 12th May, at which time Bill Whiteley succeeded me as Senior Independent Director and now chairs the Remuneration and Audit Committees.

The Board was pleased to welcome Tony Scrivin as Director-Europe from 1st May 2005. Tony has many years' experience with Spirax in commercial, logistics, manufacturing and sales positions, most recently as President of Spirax Sarco Inc. in the USA and then as Controls Product Unit director.

We are also delighted that Gareth Bullock joined the Board as a non-executive director on 2nd May 2005. Gareth is a director of Standard Chartered Bank. We look forward to benefiting from his wide experience of doing business around the world, notably in Africa and Asia.

The Group's performance reflects continued management focus on our core businesses and I would like to thank, on behalf of the Board, all the teams of dedicated people in all parts of the world who have delivered the good results of the Group not only in 2005 but consistently over many years.

PROSPECTS

The results for 2005 were helped by favourable exchange movements and a broadly positive trading environment. We invested in the growth of the business and will continue to invest in sales and marketing resources and to improve efficiency. The current year has started satisfactorily and, assuming that there is no disruption to the major world economies and that currency movements do not go significantly against us, we expect that the Group will make still further progress in 2006.

M Townsend, Chairman

CHIEF EXECUTIVE'S REVIEW

In 2005, both the Spirax Sarco steam business and the Watson-Marlow Bredel peristaltic pumping business increased sales and profits. While the UK and European markets remained subdued with limited industrial investment, the business climate in Asia, the Americas and the Rest of the World was more buoyant with rising manufacturing output and industrial investment. We concentrated on developing our businesses in the expanding markets and protecting our position in the more difficult trading areas through extending our offering of products and services, and continuing to advance the product ranges both technically and by way of cost reductions. The Group produced a solid underlying performance which, with the benefit of exchange and acquisitions, gave good growth in sales and profits for the year, which was converted into a strong cash flow.

The business of the Spirax-Sarco Engineering Group remains concentrated on the industrial and commercial steam-using market and the specialist peristaltic pumping market.

Steam is the natural choice as a heat medium in many industrial processes because of its high heat carrying capacity, controllability, sterility and efficiency as a heat transfer medium. The expertise within the Spirax Sarco business is in applying our products to improve the efficiency of our customers' process heating, thereby improving the output of the process or reducing running costs, most notably energy consumption, helping to relieve the pressures on the environment.

Equally, Watson-Marlow Bredel are specialists not only in manufacturing the best and most advanced peristaltic pumps, but also in the application of those pumps to the customers' processes, the objective being to improve the performance of the end users' plant. The peristaltic pumping market is a small part of the global pumping market; it is also the fastest growing part.

M.J.D. Steel, Chief Executive

We make the specialised knowledge of our two businesses readily available to our customers to improve the efficiency of their plant, reduce energy bills and enhance the quality of their products. We make this knowledge available through extensive training programmes and through our own highly trained force of over 1,000 direct sales engineers and service engineers worldwide who build long-term partnerships with our customers. Our business is not only spread very broadly across the globe, it is also spread across virtually all manufacturing industries; no industrial sector makes up more than 10% of Group sales and no individual customer is greater than 1% of the Group's sales. Our sales engineers are trained to analyse customer problems, then to supply the solution through the application of our products. In recent years the Spirax Sarco business has expanded the product offering to include engineered systems for easier installation and guaranteed performance; we have also increased the provision of services such as energy audits and steam trap surveys to identify potential improvements to customers' systems. Because of the importance of the performance of the tubing in a pump, Watson-Marlow Bredel has in recent years brought tube extrusion in-house, most recently the production of Marprene and Bioprene tubing and this is a growing element of the peristaltic pumping business.

TRADING

Following the good progress in the first half of 2005, we continued the growth of our businesses through the second half of the year and the market conditions have been broadly positive. North American markets have remained firm. The South American economies have grown but are fragile. Continental European economies were generally slow with weak manufacturing sectors but we continued to implement our own selective growth plans. The conditions in the UK market were similar to Continental Europe and we have been focussing our sales effort on new product areas and strong marketing. By contrast, there was strong growth in the Asian markets, driven particularly by China, India and Korea. The high oil price does not yet seem to have had much adverse effect on markets generally and, for Spirax Sarco with the ability to save energy for our customers, the oil price is overall a positive factor.

Exchange rates have moved in our favour in 2005 with a small weakening of sterling. With 89% of the Group's sales being outside the UK and the majority of the Group's manufacturing resources also outside the UK, exchange is a significant factor for us. Taking the annual average exchange rates against sterling, the euro and US dollar were both slightly stronger in 2005 than 2004 but the South American and Asian currencies were stronger still - most notably the Brazilian Real and the Korean Won. The net result is that, with our mix of business, sterling was approximately 2½% weaker than in 2004. The effect was to enhance sales by £8.1 million in the year; the operating profit increase includes a positive exchange movement of £2.1 million, of which £1.5 million was translation and £0.6 million was transaction.

Turnover increased to £349.1 million from £316.0 million in 2004, an increase of 10%. At constant exchange the growth in sales was 8%, a good result which includes organic growth of 6% and a contribution from acquisitions of 2%. The organic growth was achieved in all regions except the UK, which was broadly flat. The strongest growth was in Asia and the Rest of the World, with good growth in North America too. The sales increase in Continental Europe was patchy and, in total, modest.

In the Spirax Sarco business, we made progress with a number of sales initiatives including engineered units, steam system services and controls. Sales to the oil and petrochemicals industry increased with more project work. We also increased our sales and service coverage during the year. Watson-Marlow Bredel capitalised on the recent releases of the award-winning new pump ranges which take the company well ahead of the competition and sales grew particularly well in developing markets in Asia and South America.

Operating profit for the Group increased by 15% over 2004 from £48.0 million to £55.2 million, a record for the Group. Excluding the exchange gains, the profit increase was 10%, a solid underlying performance. The profit increase was mainly achieved organically; acquisitions also added 2%. We increased productivity during the year and made progress with the resourcing of raw materials; the benefits of the latter were however outweighed by significant raw material cost increases in Europe and energy cost increases generally. We expanded our investment in sales resources in the growing markets in Asia and the Americas, largely in the form of extra sales and service engineers and sales support.

GEOGRAPHICAL ANALYSIS OF TURNOVER

We have only minority shareholdings in our operations in India and Mexico which are therefore reported outside the operating profit. They are nevertheless integral to the whole and both produced good performances in 2005.

The operating profit margin increased from 15.2% in 2004 to 15.8% in 2005, the effect of the sales increase being reduced by our continuing investment for the future. On 9th June 2005 we announced the acquisition of the Mitech group of controls companies in South Africa for £2.3 million, and on 27th June 2005 we announced the acquisition for £2.5 million of the assets and business of EMCO, a small supplier of flow meters in the USA. Both businesses have been successfully brought into the Group.

CHIEF EXECUTIVE'S REVIEW (continued)

The UK domestic market continued to be weak with lower industrial production and weak manufacturing investment. Third party sales rose marginally to £40.1 million (2004: £39.9m) with the sales growth held back by the non-repeat of a large boilerhouse project in 2004. The sales teams concentrated on market segments where there is potential to grow such as oil and petrochemicals, steam system services, hospitals, controls, OEMs, water treatment and custom tubing. Our factories were busy with strong demand from our companies overseas.

Operating profits in the UK were £10.9 million, an increase of 3% on 2004 despite significant raw material and energy cost increases.

Sales into the Continental European markets increased by 3% from £121.2 million in 2004 to £125.3 million in 2005, which was achieved against a backdrop of weak markets; the effect of exchange rate movements was relatively small. The main economies, Germany, France and Italy, have not yet shown any sustained signs of returning to growth, and industrial output and investment were generally weak, with relatively few projects. Our growth has come from increased sales of controls, heat exchanger packages and both condensate pumps and peristaltic pumps. Particular attention has also been paid to the oil and petrochemicals industry, and pulp and paper.

The growth in Continental Europe was patchy in the Spirax Sarco business. Gains were made in Scandinavia where the companies in Finland, Denmark and Norway grew sales and profits. Sales were also ahead in Italy, Spain and Switzerland but were flat in Germany. The Watson-Marlow Bredel sales increased in most markets based on the new product releases and the relatively early stages of development of our companies in some of the markets. The Hygromatik humidifier business in Germany also increased sales and profits. The main weaknesses were in the Czech Republic, France, Portugal and Sweden, the latter having produced a particularly strong performance in 2004. We set up our own trading company in Russia and sales increased well in 2005.

Our factories in France and the Netherlands were busy with demand from around the world; here too there were higher raw material and energy costs. The Bredel factory undertook a major process reorganisation which constrained profits in 2005.

Operating profits in Continental Europe increased by 6% to £18.7 million (2004: £17.8 million).

NORTH AMERICA

Turnover in North America increased by 14% from £64.1 million to £73.1 million in 2005, a good increase which was only marginally helped by exchange movements. The market in the USA was resilient in the face of the twin economic deficits and worries about consumer indebtedness.

The Spirax Sarco sales increased in the USA, helped by the EMCO acquisition which performed well in its first six months under our ownership. The growth came in energy services, engineered systems, controls and pumps; a number of product releases supported these sales initiatives. Our Canadian company produced increased sales and profits. Watson-Marlow Bredel Inc. also pushed sales ahead with particular success in sanitary applications, sales to OEMs and tubing sales.

Operating profits in the region increased 20% to £7.9 million (2004: £6.6 million) and the operating margin increased to 10.8% despite a squeeze on the gross margin due to significant product sourcing from Europe.

Although Mexico is excluded from the figures above because we have only a minority shareholding, we were pleased that the team there carried the strong growth through from 2004.

Fully automated steam trap production at Spirax Sarco Inc., Blythewood, South Carolina

CHIEF EXECUTIVE'S REVIEW (continued)

ASIA

Sales in the Asian territories increased to £65.8 million (2004: £55.3 million), a strong rise of 19%. The economies in Asia continued their growth record of the last few years and trading conditions were generally positive. Our operations pushed up both sales and profits as a result of the market activity, implementing our own sales plans and increasing our sales coverage. Project activity was also higher. The Asian currencies have generally been stronger against the US dollar, with the Korean Won being particularly strong; the main exception has been the Japanese Yen which has weakened against the US dollar and sterling thereby holding back the gross margin in Japan. At constant exchange rates there was a strong underlying sales increase of 13% in Asia. The gains in sales and profits have been widespread with the largest increases being in China, Korea and India (which is reported separately under Associates). Elsewhere there was good growth in Japan, Singapore, Taiwan and Thailand.

Operating profit for the region was £11.4 million (2004: £8.2 million), an increase of 40% which came mainly from the sales growth but the gross margins were also boosted by the stronger currencies. If the total currency effect is discounted, the underlying profit growth is still a good 24%. The operating profit margin rose from 16.2% in 2004 to 18.7% in 2005.

SOUTH AMERICA, AFRICA, AUSTRALASIA (rest of the world)

The economies were, not surprisingly for such a diverse region, rather mixed. The Australian market was quiet and in Brazil the economy slowed noticeably in the second half of the year. Against this, South Africa and Argentina were strong, although the economic fundamentals in Argentina and Brazil must give cause for concern.

Turnover in the ROW was strongly ahead at £44.8 million (2004: £35.5 million), an increase of 26%. This does include the first six months trading of the small Mitech controls companies in South Africa following their acquisition in June 2005. The effect of exchange on the sales was significant as the currencies strengthened against sterling, particularly the Brazilian Real. The underlying increase in turnover in ROW after allowing for currency movements and the acquisition was still a solid 10%. We achieved good growth in Argentina, South Africa and New Zealand. Sales in Australia were flat.

Operating profit in ROW increased by 27% to £6.2 million (2004: £4.9 million) helped by exchange and the Mitech acquisition. The South American trading margins eased slightly, which held back the margin to 13.5% for the whole region.

BALANCE SHEET AND CASH FLOW

We continue to pay close attention to the management of the balance sheet. Capital employed, comprising property, plant and equipment, inventories, debtors and creditors, increased by 7% to £188 million; at constant exchange rates the increase was 3% including the addition of £1 million in respect of the acquisitions of Mitech and EMCO during the year. Underlying working capital levels rose by under 5% compared with the 6% organic increase in sales. The value of tangible fixed assets was broadly unchanged at constant exchange rates as additions were in line with the depreciation charge for the year. Under IFRS, the deficit of £45.8 million (before deferred tax) in the defined benefit schemes is included as a liability for the first time.

Severe service control valve from newly acquired Mitech

Cash flow for the year was strong and net cash balances increased by £17.7 million to £19.0 million, underpinned by the good profit and control of capital employed. There was an unusually large inflow of £8.6 million from the issue of shares under the Group's option scheme and employee share ownership plan. This was roughly matched by the outflow of £5.9 million for acquisitions and an extra £4 million in cash contributions into the Group's defined benefit pension schemes. In 2006, we plan to make additional contributions of around £20 million to the defined benefit pension schemes, thereby reducing the deficit. In addition, in 2006, we expect to buy in up to 2 million shares to be held by the company to meet the demand for shares in respect of share options, the share ownership plan and the performance share plan.

LOOKING AHEAD

We are the world leaders in our niche markets which comprise the industrial and commercial steam-using market for the Spirax Sarco business, and the process and environmental markets for peristaltic pumps.

The worldwide steam-using market is very fragmented and although Spirax Sarco is the leading supplier to that market, we have a relatively small market share. There is good long-term potential for growth and the aim is to continue the steady increase in market share that we have achieved over the last several decades. The potential exists both in developed markets such as the USA, Japan and Germany and in the developing markets such as China, India and Russia. We will achieve the growth by applying our expert knowledge and our specialist product to improve the customers' plant performance. We will also continue to develop new products and increase our sales coverage.

The peristaltic pumping market as served by Watson-Marlow Bredel is the most rapidly growing part of the global pumping market and, although we have a relatively high market share, the potential for growth lies in displacing other pump types within the overall market. The Watson-Marlow Bredel pump range leads the world in performance, functionality and ease of use, and as the technology advances (particularly the tube and hose capability), so the possible applications for peristaltic pumps are widening. We are continuing to expand our presence in both the developing and developed markets in order to ensure that the unique and very useful qualities of the pumps are fully understood by the market.

Both the Spirax Sarco and Watson-Marlow Bredel businesses are based on the philosophy of understanding in detail the customers' process and being able to apply the product in order to give a benefit to the customer. For all these reasons we are clear that by investing in sales resources, in product development, in improved efficiencies and in training, we expect to maintain long-term growth in sales, profits and dividends as we have in the past.

Marcus Steel.

M.J.D. Steel, Chief Executive

MANUFACTURING DEVELOPMENTS

manufacturing strategy - delivering results to the group

The Spirax Sarco Supply Division performs a key role in supplying many of the products and services required by the sales organisations to deliver the Spirax Sarco business proposition. To achieve this goal the Supply Senior Management team have developed a new strategy based on working together as an integrated worldwide organisation to provide innovative, high quality products and services with competitive prices and delivery lead times.

Hence LIFE (Little Improvements from Everyone) has been initiated, an integrated programme of projects designed to deliver these goals. The ethos of the LIFE Project is to ensure that everyone is involved and has clear visibility of the benefits whilst implementation risks are reduced by planning, piloting/testing and then progressively rolling out each project. The LIFE project has so far laid solid foundations towards achieving improved service levels at reduced operating costs.

"Through the LIFE project, Supply are ensuring that the products and services we offer are exactly what our customers want to buy - innovative products of exceptional quality and value delivered on time."

projects:-

- Improving supply chain management process.
- Improving new product introduction process.
- Improving cost accounting and performance measures.
- Improved training process.
- Improving workplace organisation and visual management.

lean manufacturing

One of the first LIFE initiatives to be established is the introduction of Lean Manufacturing, an operational strategy oriented toward improving cost, quality and service by an elimination of waste in business processes. Spirax Sarco has adopted the well proven proprietary model as a framework for achieving the lean objectives following its proven track record in numerous reference companies and in our own USA facility.

The DP27 pressure reducing valve product line was selected as the lean pilot line in Cheltenham and a number of volume steam trap products were combined into a single lean production line in Châtellerault. These are now fully operational, already demonstrating many of the lean benefits. The implementations have brought substantial manufacturing lead time reductions, typically one week to less than one day. Stocks are reducing and production is showing week on week improvement.

"The introduction of Lean Manufacturing on targeted assembly lines has reduced the production lead times from one week to one day."

DP27 pressure reducing valve

Encouraged by these successes, Lean Manufacturing is being rolled out across the UK and French facilities. South America and Italy will start lean projects in 2006.

Rolling out Lean Manufacturing across Supply will take us a long way forward to our 'exceeding customer expectations' goal.

It is a significant pillar of the Supply Strategy but it is recognised that there are many other inter-related activities, which will be improved, enabling Supply to achieve its goals.

INVESTING IN PRODUCT DEVELOPMENT

the importance of research and development

An active research and development programme is the lifeblood of any long term successful organisation like Spirax Sarco. Run effectively and streamlined, it is a vital component to future-proofing our business. Product performance testing prior to product introduction is a key element of the development phase, reducing the investment risk and increasing both new product credibility and quality to the customer.

new technology

New technology such as 3D modelling, computational fluid dynamics, finite element analysis and rapid prototyping techniques allow far more rigorous testing, over a wider range of product combinations. This permits much greater performance fine-tuning than previously achievable and results in low investment risk. In business terms, this means we can offer better products and respond to market needs much quicker, ultimately giving us a greater competitive edge now and for the future.

"On a project involving over 3,000 components, our technology enabled us to design, develop, test and deliver to market far more quickly, cost effectively and accurately than we'd ever imagined possible."

3D prototype model

3d modelling sits at the heart of the research and development advantage in that it speeds up the production of component drawings and facilitates the use of many other technologies.

rapid prototyping machines build a model layer by layer out of ABS plastic. Depending on the size and complexity of the assembly or component, the model is complete in a matter of hours compared to weeks or months using traditional methods.

computational fluid dynamics is an advanced piece of software, which allows design engineers to evaluate how the fluid moves through a valve. The engineer can fine-tune the performance before committing to expensive prototypes and losing valuable time on critical new product development.

finite element analysis allows the stress within the product to be evaluated so potential problems can be anticipated and 'designed out' early on in the process.

Computational Fluid Dynamics Simulation of a control valve body.

new control valve range

The Spirax Sarco control valve has been developed using the computational fluid dynamics and rapid prototyping techniques to provide a modern valve for today's demanding industry.

The control valve has a modular design concept and incorporates many options within one body envelope. Both ANSI and EN versions share the same internals and only three pneumatic actuators are required for valves up to DN100, 4" size. This leads to a low number of components and a highly flexible system, where one valve can satisfy the needs of numerous industrial requirements. The benefit for the user is a universal control valve with an exceptionally low cost of ownership.

product features that meet the customers' demands

The new Spirax Sarco control valve offers the following benefits to our customers;

- Precise control
- Universal application
- High performance stem sealing
- Long life internals
- Rationalised spares stock holding
- Quick and easy maintenance

In summary, the Spirax Sarco control valve range is a perfect example of how the contribution of new product development technologies can give us clear market advantage.

Pneumatic actuated control valve with smart positioner

Spirax Sarco, USA has developed the Cool Blue TD-52TM thermodynamic steam trap, distinguished by its blue stainless steel insulation cover and featuring a specially engineered ceramic disc material with lower heat conductivity than conventional steel alloy caps on disc traps. The new trap offers significantly reduced life cycle energy consumption and maintenance requirements compared to conventional designs.

'Cool Blue' Steam Trap

The new Watson-Marlow 620 series pumps were launched in September 2005, having been developed in record time using Design for Six Sigma techniques to meet precisely defined customer requirements, reduce costs, and improve manufacturability. The new pumps provide higher flow and pressure capabilities, greater speed control, and enhanced ingress protection.

The new Watson-Marlow 620 high-flow process pump

INVESTING IN ENERGY SAVING SOLUTIONS

With rising energy prices impacting production costs, increasingly industry is looking for innovative ways in which to save energy, whilst reducing maintenance and production costs. Spirax Sarco's global network of specialist engineers is providing customers with solutions to this growing need. This section looks at a sample of customers who have been impressed by the innovative products and solutions available from Spirax Sarco.

compact steam trapping solution provides ease of maintenance

Spirax Sarco supplied a number of compact steam trapping stations to Hyundai Oilbank Ltd, South Korea's third largest oil refinery. Hyundai Oilbank needed to improve maintenance and ensure the solution provided was compact.

Whenever maintenance was required on the steam tracing system it was difficult to locate the isolation valves. This resulted in even the simplest of maintenance procedures taking a long time. In some cases there were insufficient isolation valves to allow maintenance procedures to be undertaken safely.

'Spirax Sarco's knowledge, combined with the additional training and services, ensured the right solution'

By understanding the customer's problems Spirax Sarco Korea was able to recommend the use of its pipeline connectors and steam traps. Spirax Sarco's knowledge, combined with the additional training and services, ensured the right solution.

Steam tracing manifold with universal connector steam traps

increased capacity and better quality pulp in Finland

Metsä-Botnia Rauma pulp plant in Finland was encountering problems with their dryer and as a result was losing drying capacity, and production. The steam heater batteries in the dryer were severely affected by corrosion causing them to leak.

Spirax Sarco was asked to complete a survey and provided a list of interesting improvements.

'In accordance with Spirax-Sarco's suggestion we installed a steam trap on each battery. We now remove condensate in a controlled way and achieve several benefits including, reduced steam consumption and no corroded batteries. We can see that primary costs per produced ton of pulp are now reduced', states Erkki Lähdesmäki, factory designer.

'In matters like this you need a real technical specialist to deviate from the mainstream' said Mr Lähdesmäki about Spirax Sarco. 'We have made many technical improvements in order to produce better quality pulp.'

Metä- Botnia Rauma pulp plant in Finland

flash steam recovery cuts energy costs by 20%

A Spirax Sarco flash steam recovery system is delivering energy savings at De Mulder & Sons in Nuneaton. The system has dramatically cut visible plumes of flash steam from the site, which is one of the UK's largest processors of meat and poultry residues.

Spirax Sarco in partnership with the customer, designed, built and delivered a complete packaged flash steam recovery system. With the major assembly work carried out by Spirax Sarco, the system was integrated with the existing plant over a normal weekend shutdown.

Due to improved system efficiency, one of the three boilers has now been taken off line. 'The boilers work closer to their optimal firing capacity, saving an extra 10% on top of the 10% saved directly by waste heat recovery', explains operations director Rob Ratcliffe.

"The boilers work closer to their optimal firing capacity, saving an extra 10% on top of the 10% saved directly by waste heat recovery "

Flash Steam recovery systems

tradition and advanced technology for the distilling trade

Spirax Sarco Italy has contributed to automating the Marzadro Distillery, whilst maintaining its traditions of producing quality grappa. The company's challenge was to increase its production potential, whilst maintaining quality.

Spirax Sarco worked with the customer to design the automation and supervision project for the plant. This focussed on reducing operating costs, manpower and energy consumption, whilst optimising plant use, and improving quality.

The new system permits total production diversification, guarantees total system reliability, while the platforms have been designed to allow for future expansion. Special attention has been paid to recycling and reducing energy consumption.

This project demonstrates how traditional methods can be combined successfully with modern plant to guarantee product quality.

Distillation area

BOARD OF DIRECTORS

1 Michael Townsend MA FCA (64) joined the Group as an independent non-executive director in 1997 and was appointed Chairman in 2005. Until his retirement in 1999 he was the Finance Director of Rolls-Royce plc. He is Chairman of the Nomination Committee and a member of the Finance Committee. He is a non-executive director of Kennel Club Services Limited.

2 Marcus Steel ACIS FCCA (60) joined Spirax Sarco in 1972 and became Finance Director of Spirax-Sarco Limited in 1978. He was appointed to the Board in 1992 as Director - Supply, and subsequently also assumed responsibility for the Americas. He was appointed Group Chief Executive in April 1998. He is a member of the Nomination and Finance Committees and Chairman of the Risk Management Committee.

3 Tony Scrivin (58) joined Spirax Sarco in 1963. He was appointed a director of Spirax-Sarco Limited in 1998 and re-appointed in 2003 on his return to the UK from Spirax Sarco Inc., USA. He was appointed to the Board in 2005 with responsibility for Europe, excluding the UK and Italy. He is a member of the Risk Management Committee.

4 Alan Black BA (Hons) (48) joined Spirax-Sarco Limited in 1981 and has worked in the UK, Austria and Korea and has run the Group's operations in Belgium, Thailand and China. He was appointed to the Board in April 1998 and is now responsible for the Spirax Sarco International operations in Asia, Australasia and Africa. He is a member of the Risk Management Committee.

5 Graham Marchand CEng MIMechE (60) joined Spirax Sarco in 1987 to run the Group's Continental European sales operations and became a director of Spirax-Sarco Limited in 1990. He was appointed to the Board in 1992 and is now responsible for the Americas, the UK and Italian markets and Group Marketing. He is a member of the Risk Management Committee.

11 Peter Smith ACIS (58) joined Spirax-Sarco Limited in 1974, became Company Secretary in 1978 and a director of Spirax-Sarco Limited in 1988. He was appointed Company Secretary to Spirax-Sarco Engineering plc in 1992 and to the Board in 1995. He is a member of the Risk Management Committee.

10 David Meredith FCMA (46) joined the Group in 1988 as Group Accountant. He was appointed to the Board as Director - Finance in 1992. He is also responsible for Watson-Marlow Bredel. He is a member of the Finance and Risk Management Committees.

9 Bill Whiteley BSc ACMA (57) joined the Group as an independent non-executive director in July 2002. He is the Chief Executive of Rotork plc. He is Chairman of the Audit and Remuneration Committees, a member of the Nomination Committee and Senior Independent Director. He is a non-executive director of Dialight plc.

8 Einar Lindh FCA (61) joined the Group as an independent non-executive director in January 2000. Until his retirement in January 2005 he was a director of Smiths Group plc. He is a member of the Audit, Nomination and Remuneration Committees. He is a non-executive director of Foseco plc.

Gareth Bullock MA (52) joined the Group as an independent non-executive director in 2005. He is a director of Standard Chartered Bank. He is a member of the Audit, Nomination and Remuneration Committees.

6 Neil Daws CEng FIMechE (43) joined Spirax-Sarco Limited in 1978 and became Product Director in 1996. He was appointed to the Board in June 2003 as Director - Supply and is responsible for product marketing, design and manufacture. He is a member of the Risk Management Committee.

DIRECTORS' REPORT

The directors of Spirax-Sarco Engineering plc have pleasure in presenting their report and the audited accounts for the year ended 31st December 2005.

RESULTS

The results of the Group for the year, which have been prepared for the first time in accordance with the International Financial Reporting Standards (IFRS), are explained in the Chairman's Statement and Chief Executive's Review on pages 2 to 9 and are set out in the Group income statement on page 38. The application and effects of IFRS are explained in Note 34 on pages 71 to 77.

DIVIDEND

An interim cash dividend of 6.8p per share (2004: 6.3p) was paid in November 2005. The directors now recommend the payment of a final dividend of 17.0p per share (2004: 15.1p). If approved at the annual general meeting the final dividend will be paid on 22nd May 2006 to shareholders on the register on 21st April 2006. The total distribution for the year will be 23.8p per share (2004: 21.4p).

BUSINESS REVIEW

A review of the operations of the Group in 2005 together with an indication of future prospects of the business is given on pages 2 to 9.

PRINCIPAL ACTIVITIES

The Group's business is the provision of knowledge, service and products, worldwide for the control and efficient use of steam and other industrial fluids and for peristaltic pumping.

BOARD OF DIRECTORS

The directors of the Company are those listed on pages 16 and 17. Mr. G. Bullock was appointed to the Board on 2nd May 2005 as a non-executive director. Mr. A. J. Scrivin was appointed to the Board on 2nd May 2005 as an executive director. In addition Mr. C. J. Ball was a director until 29th April 2005 when he retired. Mr. T. B. Fortune retired as Chairman of the Company and from the Board on 12th May 2005 when he was succeeded by Mr. M. Townsend.

In accordance with the Company's articles of association Messrs. E. Lindh and W. H. Whiteley retire and, being eligible, offer themselves for re-appointment. Mr. E. Lindh, as a non-executive director, has a letter of appointment with the Company. Mr. W. H. Whiteley, as a non-executive and Senior Independent Director, has a letter of appointment with the Company.

DIRECTORS' INTERESTS AND REMUNERATION

The interests of the directors in the share capital of Spirax-Sarco Engineering plc as at 31st December 2005 are set out below. The number of shares over which directors hold options, together with their remuneration, is detailed in the Directors' Remuneration Report on pages 28 to 35.

	Ordinary Shares of 25p each Beneficial Interests		**Ordinary Shares of 25p each Non-beneficial Interests**	
	31.12.05 (or date of retirement if earlier)	31.12.04 (or date of appointment if later)	**31.12.05 (or date of retirement if earlier)[4]**	31.12.04 (or date of appointment if later)[4]
T.B. Fortune [1]	67,723	67,723	424,288	424,288
M. Townsend	2,879	2,879	-	-
M.J.D. Steel	83,457	66,590	-	-
C.J. Ball [2]	55,877	56,989	-	-
A.D.H. Black	45,482	20,318	424,288	-
N.H. Daws	3,165	2,588	-	-
G.P. Marchand	71,474	52,525	-	-
D.J. Meredith	42,497	41,920	424,288	424,288
A.J. Scrivin [3]	17,456	11,952	-	-
P.A. Smith	65,937	65,360	424,288	424,288
G. Bullock [3]	1,250	-	-	-
E. Lindh	-	-	-	-
W. Whiteley	2,734	2,734	-	-

(1) Mr. T. B. Fortune retired from the Board on 12th May 2005.
(2) Mr. C. J. Ball retired from the Board on 29th April 2005.
(3) Messrs. G. Bullock and A. J. Scrivin were appointed to the Board on 2nd May 2005.
(4) At 31st December 2005, the Spirax Sarco pension funds held 424,288 shares in the Company. In the period from the beginning of the year until 12th May 2005 Messrs. T. B. Fortune, D. J. Meredith and P. A. Smith were trustees of these funds. With effect from 12th May 2005 Messrs. A. D. H. Black, D. J. Meredith and P. A. Smith are trustees of these funds.

There have been no changes in the number of shares held by the directors as shown above since 31st December 2005.

Mr. C. J. Ball purchased a motor car from the Company at the current market value of £20,500.

EMPLOYMENT POLICIES
Details of the Group's Employment Policies are set out on pages 24 to 26.

ANNUAL GENERAL MEETING
The notice of meeting and an explanation of resolutions 7 to 10 to be proposed at the annual general meeting are set out in the enclosed circular.

SHARE CAPITAL
Details of shares issued during the year are set out in Note 24 on page 55.

PURCHASE OF OWN SHARES
There was no purchase of shares by the Company during the year. At 31st December 2005 the number of shares which may be purchased under the shareholders' authority given at the annual general meeting in 2005 was 7,500,000 and the number of shares in issue was 76,951,907.

SHAREHOLDINGS OF 3% OR MORE
The Company received notice of material interests in 3% or more of the issued ordinary share capital of the Company as at 3rd March 2006 as set out below. So far as is known there is no other notifiable interest of 3% or more in the issued capital.

	Ordinary Shares	%
The Capital Group Companies Inc.	4,660,491	6.05
Arnhold and S Bleichroeder Advisers LLC	4,514,985	5.86
Sprucegrove Investment Management Ltd	4,416,223	5.73
Hermes Pensions Management	3,333,152	4.33
Aberforth Partners LLP	3,000,996	3.90
Morgan Stanley Investment Management	2,980,542	3.87
Legal & General Investment Management	2,870,282	3.73
NFU Mutual	2,783,363	3.61
F&C Asset Management	2,475,738	3.21
Schroder Investment Management Ltd	2,450,141	3.18

FINANCIAL INSTRUMENT RISK MANAGEMENT
The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk and foreign currency risk. More detail is set out in Note 33 on pages 68 to 71.

STATEMENT OF THE POLICY AND PRACTICE ON THE PAYMENT OF SUPPLIERS
It is the Group's policy to meet the terms of individual supply contracts and in the UK to make payment to suppliers at the end of the month following receipt of goods. In view of this, the Group does not follow any particular prescribed code.

Spirax-Sarco Engineering plc has no trade creditors.

RESEARCH AND DEVELOPMENT
The Group continues to devote significant resources to the updating and expansion of its range of products in order to remain at the forefront of its world markets. Expenditure in 2005 on research and development amounted to £4,288,000 (2004 on an IFRS basis: £4,365,000), of which an element is capitalised as explained in Note 1 on page 43.

MARKET VALUE OF LAND AND BUILDINGS
In the opinion of the directors, the market value of the land and buildings of the Group exceeds the book value of those assets at 31st December 2005 by approximately £10,000,000 (2004: £9,000,000).

GROUP CHARITABLE AND POLITICAL DONATIONS
Charitable donations amounted to £59,400 (2004: £47,982). There were no political donations (2004: nil).

AUDITORS
A resolution to re-appoint the auditors, KPMG Audit Plc, will be proposed at the annual general meeting.

CAPITAL GAINS TAX
For capital gains tax purposes the market value of the Company's ordinary shares at 31st March 1982 was 140.375p.

COMPANY INFORMATION
Further information on the Company is available on the Group web site: www.SpiraxSarcoEngineering.com

By order of the Board
P. A. Smith *Secretary*

Charlton House, Cirencester Road,
Cheltenham.

13th March 2006

CORPORATE GOVERNANCE

COMPLIANCE

Corporate governance has been and remains the responsibility of the whole Board. This statement describes how the Company applies the principles and complies with the provisions of the Combined Code and Code of Best Practice published in July 2003, which applied to the Company in respect of the financial year ended 31st December 2005. The Board considers that the Company met the requirements of the Combined Code throughout the year ended 31st December 2005. It is in compliance with the provisions of the Combined Code as set out in section 1 subject to the explanation of the ratio of executive and non-executive directors below.

The Board assesses on an on-going basis its practices to ensure continued compliance with the Combined Code and has allocated responsibility for compliance to appropriate directors or officers. Contact has been made with major shareholders to allow discussion of the Company's governance policy and strategy with the Chairman and the Senior Independent Director.

BOARD COMPOSITION AND PROCEDURES

The Board currently comprises the non-executive Chairman, three independent non-executive directors including a Senior Independent Director and seven executive directors, details of whom are set out on pages 16 and 17. The positions of Chairman, Chief Executive and Senior Independent Director are held by separate individuals and there is a clear written division of responsibility between the Chairman and the Chief Executive. This ratio of executive and non-executive directors has applied for a number of years and the Board believes that this membership is the appropriate structure for the Company. The Board is responsible for the Group's business operations and the full executive team of seven directors is present on the Board in order to provide first hand information and contributions to the running of the business. The executive directors control the Group's devolved management structure which requires local management initiative across the Group's global spread of operating companies and the broad product range and wide customer base. Board membership of the seven executives is key to the overall management of the Group which employs a flat management structure. This also provides the non-executive directors with regular direct access to the full executive management team. This is a successful mix and appointing a further four non-executive directors would make the Board very cumbersome and would not add to the quality of the Board's performance.

The Board applies an appropriate policy in the recruitment of independent non-executive directors to meet the particular requirements of the Board. Mr. G. Bullock was recruited during the year through the process conducted by the Nomination Committee and following external advice to the Company. Each of the non-executive directors, including Mr. G. Bullock, has a letter of appointment which meets the requirements of the Combined Code. The non-executive directors have all had senior executive experience and offer independent judgement on Board matters. The non-executive directors of the Company, including the Chairman, do not participate in any bonus, share option or share ownership schemes and their appointments are non-pensionable.

The Board meets formally six times per year to consider strategic developments and to review trading results and operational and business issues. All directors attended all meetings in 2005. In particular it deals with those matters reserved to it for decision. The matters reserved to the Board are posted on the Group web site: www.SpiraxSarcoEngineering.com and are as follows:-

(i) Management

- Approval of Group strategy and annual plans.
- Commitments relating to the acquisition or disposal of any company or business by the Group.
- Material or unusual contracts.
- Capital expenditure items in excess of £500,000 or such other limit agreed by the Board. Items over £250,000 but less than £500,000 are reported to each quarterly meeting of the Board.

(ii) Board Membership and Board Committees

- The formal appointment and dismissal of directors.
- Terms of reference and membership of Board Committees.

(iii) Corporate Governance/Accounting

- Approval of actions requiring public documents including circulars to shareholders, related documents and press releases.
- Approval of accounting policies or practices, including the Treasury policy.
- Individual borrowings, financial instruments, guarantees or provision of equity capital, beyond the authority of the Finance Committee.
- Approval of the content of the Annual Report and Accounts and the Interim Statement.
- Appointment and dismissal of Company Secretary.
- Through the Audit Committee, remuneration of auditors and recommendation for appointment and removal of auditors.
- Dividend policy, interim dividends and proposed final dividends.
- Any matter to be dealt with at an annual general meeting or extraordinary general meeting.

(iv) Other

- Significant alterations to existing Group Risk Management policies relating to insurance, environmental and health and safety matters.

- Changes in principal professional advisers.
- Major changes to pensions and employee share schemes operated in the Group.
- Prosecution, defence or settlement of any material litigation.

All directors receive detailed progress reports one week prior to each Board meeting.

There is provision for the non-executive directors to meet together both with and without the Chairman. Utilising a format created with the advice of Towers Perrin, the Board again carried out a rigorous board performance evaluation process in accordance with the Combined Code requirements which confirmed the effective operation of the Board.

The evaluation process comprises a review conducted by the Company Secretary and reported to the Chairman of all directors' views on the operation of the Board and the performance of the Chairman, the Chairman and Chief Executive's review of the board performance of each director, the Chairman's review of the non-executive directors and the review by Committee members and attendees of the operations of the Audit, Nomination and Remuneration Committees and the performance of the Chairman of each of those Committees.

There are procedures for individual Board members to receive induction and training as appropriate and provision to solicit independent professional advice at the Company's expense where specific expertise is required in the course of exercising their duties. All directors have access to the Company Secretary, who is responsible for ensuring compliance with appropriate statutes and regulations.

The Company continues to provide directors' and officers' insurance for Board members and the directors of Group subsidiary companies.

All directors are subject to re-appointment by shareholders at the first opportunity after their appointment and thereafter at intervals of no more than three years.

SENIOR INDEPENDENT DIRECTOR
Mr. W. H. Whiteley succeeded Mr. M. Townsend as the Senior Independent Director on 12th May 2005.

COMMITTEES
The Board delegates specific responsibility to Board committees, notably the Audit, Nomination and Remuneration Committees in line with best practice. The terms of reference for these committees are posted on the Group web site: www.SpiraxSarcoEngineering.com. Additionally the executive directors comprise the Risk Management Committee and Messrs. M. Townsend, M. J. D. Steel and D. J. Meredith comprise the Finance Committee.

(i) Audit Committee
In the period from the beginning of the year until 12th May 2005 the Audit Committee comprised Messrs. E. Lindh, M. Townsend (Chairman) and W. H. Whiteley. With effect from 12th May 2005 the Audit Committee comprised Messrs. G. Bullock, E. Lindh and W. H. Whiteley (Chairman). All members are independent in accordance with the independence criteria set out in the Combined Code. There were three meetings of the Audit Committee during the year and all members attended all meetings.

A summary of the Audit Committee's duties and responsibilities is set out on page 23.

(ii) Nomination Committee
In the period from the beginning of the year until 12th May 2005 the Nomination Committee comprised Messrs. T. B. Fortune (Chairman), E. Lindh, M. J. D. Steel, M. Townsend and W. H. Whiteley. With effect from 12th May 2005 the Nomination Committee comprised Messrs. M. Townsend (Chairman), G. Bullock, E. Lindh, M. J. D. Steel and W. H. Whiteley. There were two meetings of the Nomination Committee and all members attended both meetings.

The Nomination Committee proposes to the Board new appointments for both executive and non-executive directors and determines on an individual basis the most appropriate method of identifying suitable applicants. The Nomination Committee arranges for the executive Board members' views to be assessed before an appointment decision is made.

(iii) Remuneration Committee
In the period from the beginning of the year until 12th May 2005 the Remuneration Committee comprised Messrs. E. Lindh, M. Townsend (Chairman) and W. H. Whiteley. With effect from 12th May 2005 the Remuneration Committee comprised Messrs. G. Bullock, E. Lindh and W. H. Whiteley (Chairman). All members are independent in accordance with the independence criteria set out in the Combined Code. There were four meetings of the Remuneration Committee and all members attended all meetings.

The Company Secretary acts as Secretary to the Audit, Nomination and Remuneration Committees.

CORPORATE GOVERNANCE (continued)

The Directors' Remuneration Report presented by the Board of Directors is set out on pages 28 to 35.

SHAREHOLDER RELATIONS

The Group conducts regular dialogue with institutional shareholders and provides such information as is permitted within the guidelines of the Listing Rules. In particular major shareholders have been approached with a view to discussing the Company's governance and strategy with the Chairman and Mr. W. H. Whiteley, the Senior Independent Director. As required by major shareholders, the Senior Independent Director is available to listen to their views on any areas of concern they may have. To date, the non-executive directors have not been requested to attend a meeting with shareholders, with the exception of a single request which was met by the Chairman. Reports are made to the Board of all meetings with major shareholders and analysts, including, in particular, briefings after interim and final results.

The preliminary results announcement may be accessed by investors on the Group web site, www.SpiraxSarcoEngineering.com. The Report and Accounts will also be on the web site in due course.

All shareholders are invited to participate in the annual general meeting, where the chairmen of the Audit, Nomination and Remuneration Committees will be available to answer questions. The results of proxy votes are declared at annual general meetings after each resolution has been dealt with on a show of hands and this practice will continue at future general meetings. Details of the votes cast will be published on the Group web site, www.SpiraxSarcoEngineering.com, following the annual general meeting.

INTERNAL CONTROLS

The Board has overall responsibility for the system of internal control and for reviewing its effectiveness, whilst the role of management is to implement Board policies on risk and control. The Board reviews the effectiveness of internal controls at least annually. The reviews cover all material controls, including financial, operational and compliance controls and risk management systems. The system of internal control is designed to manage rather than eliminate the risk of failure to achieve the business objectives.

The Board believes from its reviews that the system of internal controls is embedded in the business and regular review allows for regulation of new and changing risks in the Group's business. The Board will be further reviewing its internal control systems to take account of the recently published Financial Reporting Council's revised guidance on internal controls.

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

As required by the UK Listing Authority, the Company has complied throughout the year and up to the date of this report, with the Combined Code provisions on internal controls having established the procedures necessary to implement the guidance issued by the Turnbull Committee and by reporting in accordance with that guidance.

The Company has been assessing its practices to ensure compliance with the statutory requirements to produce an Operating and Financial Review ("OFR") in respect of the financial year ending December 2006. In particular the OFR was to provide a balanced and comprehensive analysis of the development and performance of the Company including certain forward looking statements. The requirement for listed companies to produce a mandatory OFR has now been withdrawn although the Company will still be required to include a "fair review of the business" in the Directors' Report for that financial period. This review will include an analysis of the development and performance of the business and also a description of the principal risks and uncertainties facing the Company and its subsidiaries. However, the Company continues to monitor developments as regards best practice in relation to the production of OFRs and in particular the views of the Financial Reporting Council.

(i) Risk Management

The Group has operated procedures for considering risks in the normal operations of the Group and with regard to significant transactions. Strategic and annual planning also encompasses considerations of business risks. The Risk Management Committee specifically reviews any risks facing the business which could give rise to a significant loss.

The Risk Management Committee periodically reviews with external consultants the risk register and risk management process in the context of the current business structure and operations with the aim of validating the risk register and the general risk management process and identifying any additional new risks. This exercise reviews the risk magnitude and risk likelihood against the current controls and areas for improvement. The Board, on Marsh Ltd's advice, is satisfied that the system of management for significant risks is appropriate for the Company and is properly executed.

As part of the on-going process, the Group companies have reported on a six monthly basis their position with regard to implementing the identified countermeasures to address the Group's significant business risks. The six monthly returns are assessed by the Risk Management Committee. Reports are made to the Board as a whole, by the Chief Executive, for review of the risks and measures taken. Annually the executive directors carry out a reappraisal of the business risks. The Audit Committee reviews the system of reporting and monitoring and its effectiveness as a whole.

(ii) Financial

The Finance Committee of the Board considers financing and investment decisions concerning the Group, including the giving of guarantees and indemnities, and monitors policy and control mechanisms for managing treasury risk within the limits laid down by the Board.

Financial reporting systems include comprehensive annual plans approved by the Board and monthly reporting of actual results with appropriate comparisons against plan and previous year's results. Forecast operating results for the year are regularly updated. Capital investment is subject to approval under a clear policy. This includes annual plans, appropriate authorisation, detailed investment appraisal and post-investment review and due diligence requirements where businesses are being acquired.

(iii) Operational

All subsidiaries of the Group are required to complete self-certification questionnaires regarding compliance with the policies, procedures and minimum requirements for an effective system of internal control. Self certification is given by both the general manager and the finance manager of the operation.

(iv) Audit Committee

The Audit Committee has met to consider the appropriateness and effectiveness of the Group's internal controls, policies and procedures and the outcome of the external audit for the year. Its meetings are normally attended by the Director - Finance and the external auditors. There is provision for the Committee to confer with the auditors without the attendance of executive directors. The Audit Committee reviews the independence of the external auditors on an annual basis. The Committee considers in detail reports prepared by the auditors in relation to the interim and final accounts and accounting practices and developments. It also considers reports and explanations provided by the Director - Finance.

The Board has approved terms of reference for the Audit Committee meeting the requirements of the Combined Code. The Audit Committee's responsibilities include:

- monitoring the integrity of the accounts and in particular reviewing the Company's internal controls and risk management framework;
- reviewing the scope and results of the auditors' work, their independence and objectivity and audit fee, including the requirement for an internal audit function;
- recommending the appointment, re-appointment or removal of external auditors;
- reviewing the accounting policies and practices of the Company and at the end of the annual audit cycle, assessing the effectiveness of the audit process.

(v) Non-Audit Services

A policy on non-audit services provided by the auditors in line with professional practice has been established and approved by the Audit Committee. The external auditor has undertaken non-audit work (essentially in regard to taxation and acquisition due diligence) and the fees paid by the Company for it are set out in Note 6 to the accounts on page 47. The scope and extent of non-audit work undertaken by the Company's auditors is carefully controlled in line with the written terms provided by the Company to the auditors with the objective of avoiding impact on their independence and objectivity. Particularly, the auditors are prohibited from providing services in relation to valuations, recruitment, dispute resolution and accounting assistance. The Audit Committee monitors the scope of the auditors' work.

(vi) Whistle Blowing

If any employee in the Group has reasonable grounds for believing that the Business Code/Management Code is being breached by any person or group of people and does not feel able to voice the matter with his or her manager, he or she is able to contact directly the Company Secretary in Cheltenham and provide full details. The Company Secretary will ensure that (a) the circumstances are properly investigated and (b) the employment of the person contacting the Company Secretary will be protected appropriately.

INTERNAL AUDIT

The Board assessed the requirement for an internal audit function and concluded that the current arrangements, which do not require such a function, remain satisfactory.

GOING CONCERN

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

DIRECTORS' RESPONSIBILITIES

The Statement of Directors' Responsibilities is set out on page 36.

CORPORATE SOCIAL RESPONSIBILITY

For some years the Board has been reporting on Corporate Social Responsibility ("CSR") which embraces a wide range of issues and in particular focuses on social, ethical and environmental ("SEE") matters. The Board has continued to embrace and apply the general CSR principles in conducting its business in a socially acceptable way with due regard to the relationship of the Company to its employees, customers, investors, suppliers and society generally.

This report follows the practice in recent years of illustrating the Board's commitment to meeting the requirements laid down by the ABI and the reporting procedures and actions taken within the Group in this connection. The Group has developed further its awareness of CSR issues and has continued to make improvements, particularly in the areas of health and safety.

The Board achieves compliance with the principles of CSR by the management of the risks concerned. The Board seeks to achieve such management within the normal operations of the Group such that the necessary policies, systems and procedures are embedded in Group practice. The importance of involvement of employees and suppliers in meeting the standards required by the Board is inherent in our business operations in the provision of products and services to our customers. Meeting the standards required in the operation of our business as it affects communities and customers is also a specific objective reflected in our annual plans and strategic planning.

The Group's operations are carried out under the Group's long standing Business Code. A copy of this is posted on the Group web site: www.SpiraxSarcoEngineering.com. This Code formalised policies followed over many years by the Group. The main areas are as follows:-

- compliance with all applicable laws and regulations
- operation of the internal controls established by the Group
- having proper regard for all stakeholders in the business
- outlawing of bribes
- commitment to fair treatment of all employees
- recognition of all health, safety and environmental matters.

The standards required in the practical management of the Group are set out in a separate Management Code, which is an internal practical document issued by the Chief Executive with which general managers and the finance managers in each subsidiary confirm compliance for each year.

The Group also recognises that the achievement of good quality products and services, the maintenance of health and safety, and the achievement of good environmental practices, are an integral part of running the business and require consideration as part of the day to day operations of the Group and are reflected in the Group's performance.

The responsibility held by Board members for the entirety of the Group's operations, including the implementation of its policies, enables the Group's Business Code and Group policies to be applied on a consistent basis. The Group's decentralised structure provides for detailed local management of SEE matters by the general manager in each subsidiary, who reports to and is monitored by an appropriate executive director. These reporting procedures within the Group enable the executive directors, who have direct responsibility for implementing policy, to monitor, report and take any appropriate action. SEE training is part of the training provided for newly appointed directors appropriate to their experience, knowledge and previous training.

In the risk management process explained in paragraph (i) of Internal Controls, see page 22, the risks involved in not achieving appropriate SEE standards continue to be assessed and any significant risk is monitored by the Board following half yearly reports from all Group companies.

The Group considers and applies appropriate policies through the Group's Business Code in the following areas:-

(i) Employee Rights
The Group supports and applies the principles of Human Rights in its operations including equal opportunities for employees regardless of sex, race, religion, age or disability. Board members satisfy themselves that the terms of employment in subsidiaries worldwide are appropriate. The Group has a policy of non-discrimination and does not tolerate harassment in any form. The recruitment procedures throughout the Group avoid employment of underage staff. Care has been taken to provide for a culture of openness and honesty. The Group operates personnel policies designed to meet the needs of its subsidiaries and employees around the world. Channels of communication appropriate to the local operation have been established to allow employees to be properly informed and voice their views and concerns. Recognition is given to individual employees' needs and requirements throughout the Group and, where possible, flexible working arrangements are considered where the circumstances are justified. Employees are encouraged to apply their skills, knowledge and energy. The Group's management philosophy recognises employees as its most important asset.

A summary of the Group's annual accounts is made available to its employees. The Group's newsletter, with a Foreword from the Chief Executive, is distributed to all Group companies each month and is made available to employees. Individual subsidiaries have either a local newsletter or a regular communication informing employees on the progress of their company. The Group encourages the growth of employee share ownership.

(ii) Community Involvement

The Group has a Charitable Trust which donates to registered charities and additional donations are made to appropriate requests for support from bodies which are not registered charities both in the UK and in the overseas operating subsidiaries. In the latter case the decision to donate is made by the local general manager. In total the Group donates approximately £65,000 per annum to registered charities and other good causes.

The operating companies in the Group are encouraged to provide support to local communities through company donations, employee organised charitable activities, donation of equipment no longer required and through provision of information. By way of example, Spirax Sarco Ind. e. Com. Ltda. in Brazil recently donated some wheelchairs locally in Cotia in Sao Paulo.

Another example applies in India where with our partners the local company continues to support a hospital it established many years ago making provision for both company employees and the local community. Both benefit from an established welfare programme based in company provided premises supporting community initiatives, particularly for women.

(iii) Supplier Relations

The Company policy is to use suppliers of goods and services which maintain appropriate standards in their operations. Suppliers must consistently achieve the standards required by ISO 9000.

(iv) Product Stewardship

Information and support is given through appropriate technical advice to provide a solution to customers' needs with installation and after sales service being integral to the Group's business. The proper application of products and environmental and safety considerations are dealt with in detail in the technical literature made freely available by the Group.

(v) Corruption

The Company's policy outlaws corruption or anti-competitive practices. In addition to provisions within service contracts general managers, who head Group subsidiaries, are required to certify personally that all laws and regulations have been met in their territory.

(vi) Health and Safety

- The Company has a clear attitude to health and safety, which is that each operation will maintain a healthy and safe environment. In the first instance the general manager of each company has the responsibility for ensuring that this is effectively managed at the local level. Each major manufacturing site has its own Health and Safety Committee which is advised by a safety officer.

- The general managers report in a standard form the health and safety record of each subsidiary to the responsible executive director in an exercise co-ordinated and monitored by the Director - Supply. The Director - Supply is responsible for overseeing all health and safety matters in each of the Group's subsidiaries. A separate Safety Audit Committee composed of UK based directors and senior managers meets every six months to verify the performance of the UK operating companies on health and safety and environmental issues.

- The Group ensures that the necessary resources are available for health and safety training and companies within the Group seek, as necessary, professional advice regarding the implementation of safety programmes. For example, at Spirax Sarco UK an established training programme applies to new shop floor employees and is provided as a refresher to all shop floor employees every three years.

- Regular reviews are conducted to ensure that employee knowledge of health and safety matters relevant to them is up to date.

- In the UK Spirax Sarco has carried out various reviews and in particular has extended the measures for the welfare of employees by providing:

  a) Automatic External Defibrillators for use in heart attack situations. All first aiders have been trained in their use.

  b) training for all managers in the recognition and prevention of work related stress.

CORPORATE SOCIAL RESPONSIBILITY (continued)

c) training for managers and first aiders in the recognition of the symptoms of abuse of alcohol and drugs.

d) significant investment in safety equipment and new procedures for working at height.

- Further investment in noise attenuation in the UK machine shops has realised significant decibel level reduction.

- In both the UK and in France water-based paints have now completely replaced solvent-based paints and in the UK two automated and enclosed component cleaning machines have replaced the use of open-top tanks, each of which reduce emissions to the environment and reduce employees' personal exposure.

- All Group manufacturing companies have recently implemented a 5S programme to improve the work environment, focusing on safety, cleaning and organisational aspects.

(vii) Environmental

a) Environmental Benefits from the use of Group Products

The use by customers of Group products has a significant environmental benefit which outweighs the environmental issues associated with the production of the products. Certainly the environmental impact arising from the manufacture of the Group's range of steam system products is significantly less than the energy saving benefits enjoyed by customers in the application of those products. The name Spirax Sarco is synonymous with steam and its efficient use worldwide. The majority of sales are the result of helping customers to improve the efficiency of their plant and processes, reduce energy consumption and emissions and meet local safety regulations. The Group's technical advice on the application of its products and in relation to steam systems, which is freely given to customers, is the key to maximising the benefit of the products we supply. There are numerous individual examples of benefits enjoyed by customers which include improved overall boiler efficiency, improved energy efficiency of process plant and reduced consumption of water, water treatment chemicals and lower production of effluent.

Many applications for Watson-Marlow Bredel peristaltic pumps are those where environmental improvement is the main aim. They are particularly suited to applications like waste water treatment where difficult fluids have to be handled safely and reliably.

b) Policy Statement and Performance

The Group regularly reviews its written policy statement and performance with regard to environmental matters to ensure compliance with good practice and statutory regulations in all its operations and to meet corporate objectives. The Group operates its businesses with a proper concern for their impact on the environment generally and, particularly, with concern for the local communities where the Group's operations are located.

The Group, through its Board of Directors, ensures that its managers and staff are aware of the actions required to consider environmental factors and meet regulations in each of the Group's plants and the risks of failing to do so. Managers are required to take environmental considerations into account in running the business, for example in its energy efficiency, its use of appropriate materials and the design and manufacture of its products generally and in the investment in new equipment, new processes and new buildings and services.

There is a detailed procedure which lays down responsibility for ensuring that the Group's policy is carried out. Employees are also expected in their daily job to be aware of environmental considerations and draw to the attention of management any matters of possible concern or ideas for improvement.

- **Implementation**

The Director - Supply has specific environmental responsibility in relation to the Group's operations and their impact on the environment. The Group's objective is to comply with environmental laws and good practice and where non-compliance is identified to have management systems in place to ensure that this is rectified within an appropriate timeframe. The environmental policy set out above is circulated to management and to all employees.

General managers of operating companies within the Group are responsible for local compliance with the Group's policy and with local legislation. A manager within each operating company is nominated to ensure compliance. Agreed actions are implemented by the operating company overseen by the relevant executive director for that division.

- **Review**

The Group also operates a regular system of review, under which every operating company reports on environmental issues and compliance with local legislation.

The review in 2005 revealed no major problems but identified two local issues which were dealt with. Following a prescribed approach regular reviews of the Group's facilities worldwide are conducted.

Following a review the implementation of recommendations, if any, is monitored at Group level. The general manager will report through the executive director on any issues identified as is appropriate in the circumstances.

If recommendations are made then in the first instance the general manager of each company has the responsibility for ensuring that they are effectively considered and implemented where appropriate at the local level.

Where environmental upgrades are made to plant and machinery in any jurisdiction, consideration is given to implementation of such upgrades across the Group's facilities worldwide.

- **Audit Process**
  In the past the Group has utilised external environmental consultants to audit a number of manufacturing facilities and has, as a result, established an internal environmental audit process under which a senior manager assesses the environmental position in each of the major manufacturing units and reports to the local management. This process is overseen by the relevant executive director who informs the Director - Supply appropriately and is distinct from the process identified above.

- **Results**
  As a result of these processes there have been improvements in the use of solvents, chemicals and fluxes all of which have contributed to a cleaner operating environment which together with noise attenuation have benefited both employees and local residents. To comply with local regulations as to its efficiency, Spirax Sarco Ind. e. Com. Ltda. in Brazil has installed a waste water system to treat water before discharging it and an audit is carried out each six months. Also to comply with local regulations the company has developed methodologies and documentation to discharge industrial residues. A selective waste programme, practising recycling concepts, has been implemented, together with an environmental audit to ensure continuous improvement.

THE DIRECTORS' REMUNERATION REPORT

The Board presents the following report on directors' remuneration and the work and responsibilities of the Remuneration Committee.

THE REMUNERATION COMMITTEE

This Committee has been established for many years and operates under terms of reference agreed by the Board and which can be found on the Group web site: www.SpiraxSarcoEngineering.com.

In the period from the beginning of the year until his retirement from the Committee on 12th May 2005, Mr. M. Townsend was a member and Chairman of the Committee. With effect from 12th May 2005 the Committee members are Messrs. G. Bullock, E. Lindh, and W. H. Whiteley (Chairman), each of whom is an independent non-executive director.

The Committee is responsible for determining, on behalf of the Board, the Company's remuneration policy and for determining the employment conditions and remuneration packages of individual executive directors. The Committee also administers and determines the grant of options under the Group's share option schemes for executive directors and other senior employees and administers and determines the grants of awards under the Performance Share Plan.

The Committee obtains independent professional advice from Towers Perrin to ensure that the Company's remuneration policy is appropriate and competitive. Towers Perrin was appointed by the Committee and has not provided other services to the Company during the year. Mr. M. Townsend, the Company Chairman, and Mr. M. J. D. Steel, the Chief Executive, attend meetings at the invitation of the Committee to provide information requested by it. However, they do not participate in any discussions involving their own remuneration. The Company Secretary acts as Secretary to the Committee.

The Company has throughout the year complied with the provisions of The Combined Code and Code of Best Practice published in July 2003 with regard to directors' remuneration. The Committee has given full consideration to the Combined Code in establishing the remuneration policy and packages for directors.

POLICY ON EXECUTIVE DIRECTORS' REMUNERATION

The Company's policy is to reward directors competitively and on the broad principle that their remuneration should be comparable with remuneration in other similar public companies. The total remuneration package is appropriate and necessary to attract, retain and motivate directors of the calibre required to take the Company forward.

In order to align the interests of directors and shareholders, the Committee has structured the total remuneration package to provide a material performance-related element.

The structure of the directors' remuneration package has been established subject to appropriate modifications for many years and has regard to pay and conditions elsewhere in the Group.

The remuneration package comprises:-

Basic Salary

The Committee obtains independent professional advice from Towers Perrin using published information for comparable public companies. Salaries are reviewed annually on 1st January taking into account the experience, responsibility and performance of the individual.

Annual Bonus

The Company operates an annual bonus scheme for executive directors. The bonus is paid as a percentage of salary. This percentage is the sum of:-

(i) one third of the percentage increase in pre-tax profit for the year over the average pre-tax profit for the previous three years;

(ii) two thirds of the percentage increase in earnings per share for the year over the average earnings per share for the previous three years;

(iii) cash generation (expressed as a percentage of profit for the financial year) will carry a maximum of 20% bonus. Where cash inflow, as determined from the Accounts, is less than 100% of profit, no bonus will be earned under this element; where cash generated equals or exceeds 160% of profit, the full 20% will accrue with proportionate bonus being earned between 100% and 160% of profit; and

(iv) an amount derived from the change in gross margin percentage compared with that for the previous year. Where the gross margin has deteriorated by 0.5 percentage points or more, no bonus will be earned under this element; where there has been an improvement of 1.5 percentage points or more, the full allocation of 20% will accrue with proportionate bonus being earned between these limits, provided always that the gross margin percentage is above a required minimum.

There is a contractual maximum bonus payment equal to basic salary. The bonus forms an integral and regular part of the executive directors' remuneration.

The directors' remuneration report in 2004 referred to the Committee's continuing review, with professional advice, on the pension position of the executive directors including the pensionability of elements (i) and (ii) of the bonus. The Committee can now report that an amendment to the calculation of pensionable pay has been agreed with each of the relevant executive directors. Elements (i) and (ii) of any bonus earned after 31st December 2005 will not be pensionable. From 1st January 2006 an appropriate, actuarially calculated, percentage increase to basic salary has been applied, reflecting the individual director's age and expected period of service to normal retirement date. This increase will qualify as part of the directors' pensionable pay. However, the change does not apply to Mr. G. P. Marchand in view of his retirement on 30th June 2006. Mr. A. J. Scrivin, who was appointed last year, has not earned pension on the bonus payments.

Additionally the Committee plans to offer to executive directors a cash alternative to pension contributions in respect of the directors' pensionable service from 6th April 2006, i.e. "A Day" under the Inland Revenue tax regime for pensions. This cash alternative will be confirmed by the Company's actuaries. The cost of the alternative to the Company will be no greater than the cost of the pension contributions.

The Company's policy on directors' remuneration and the structure of their remuneration package are kept under review to ensure the directors' overall package remains properly competitive and shareholders will be informed of any resulting change.

Options
Spirax-Sarco Engineering 1992 UK & Global Share Option Schemes and Spirax-Sarco Engineering Approved & Global Share Option Schemes

The Company operates share option schemes which are administered by the Committee which determines the grant of options under the schemes usually once per year. These are designed to align the longer term interests of participants with those of shareholders by giving an incentive linked to added shareholder value. Following the introduction of the Performance Share Plan in 2005, it is intended that, ordinarily, executive directors will be granted awards under that plan rather than be granted options. Executive directors, senior executives and management hold options granted in previous years and it is intended that options will continue to be granted to senior executives and management. The policy is to phase options over the ten year life of the share option schemes. Options granted to each director from 1995 are subject to a performance condition which is described below.

Performance Condition for Share Option Schemes

In accordance with market practice, options granted are normally specified to be exercisable between three and ten years from the date of grant and, for grants from 1995, only if a specified performance condition is satisfied. In line with the then established market practice, the performance condition for options granted from 1995 up to 2001 requires an increase in earnings per share of more than 6% greater than the increase in the UK retail prices index over a period of three consecutive years between grant and exercise. For options granted from and including 2002 the performance condition requires an increase in earnings per share of more than 9% greater than the increase in the UK retail prices index over a period of three consecutive years between grant and exercise. The same performance condition applies to each director. The performance condition chosen was considered appropriate because it ensured increases in the earnings per share were achieved having taken account of UK inflation. In assessing whether the chosen performance condition is met the Committee arranges for the auditors to confirm the calculations made. This method of assessment is considered appropriate to confirm compliance with the condition. The performance condition requires a comparison with a factor external to the Company, namely the growth in the UK retail prices index over the performance period.

For grants from and including 2005, the performance condition will, ordinarily, need to be met over the three year period from the 1st January prior to the date of grant in order for the option to become exercisable. If the condition is not met at the end of the three year period, the option will lapse.

Details of total share options issued are set out in Note 24 on page 55. The above performance conditions apply to other relevant options granted to all participants in the share option schemes.

Performance Share Plan

A performance share plan for executive directors, senior executives and management was adopted at the 2005 annual general meeting. Awards take the form of contingent rights to acquire shares, subject to the satisfaction of a performance target. To the extent they vest, awards may be satisfied in cash or in shares. The Committee's current policy is that the maximum individual annual award will be of shares with a market value of not more than 150% of salary, although the intention is that in practice the market value of an individual award will be significantly below the maximum. Ordinarily, an eligible person will not be granted options under the Company's share option schemes and awards under the performance share plan in the same year.

THE DIRECTORS' REMUNERATION REPORT (continued)

The vesting of an award will normally be subject to the satisfaction of a performance target. The performance target applied to awards granted in 2005 is based on the Company's total shareholder return ("TSR") relative to the TSR of other companies included in the FTSE All-Share Engineering and Machinery Index over the three year period commencing with effect from 1st January 2005. Awards will vest on a sliding scale. For full vesting the Company's TSR must be at or above the upper quartile. 25% of the shares subject to an award will vest if the Company's TSR is at the median. Awards will vest on a pro-rata straight line basis between median and upper quartile performance. The same performance condition applies to each director. The FTSE All-Share Engineering and Machinery Index has ceased to exist with effect from 2006. For the awards granted in 2005, the comparator group will remain as those companies comprising that sector immediately before the start of the performance period. Additionally, for an award to vest the Committee will also, normally, need to be satisfied that the Company's underlying financial performance has been satisfactory over the three year performance period.

The performance condition chosen was considered appropriate because it is dependent on the Company's relative long term performance based on total shareholder return, it compares the Company's performance with the performance of companies in a comparator group and was the basis described to shareholders when the plan was approved by shareholders at the 2005 annual general meeting. In assessing whether the chosen performance condition is met the Committee's professional advisers will be asked to perform the necessary calculations. In calculating TSR, average share prices for the period before the beginning and end of the performance period will be used to avoid abnormal share price movements significantly affecting the calculation. Since the FTSE All-Share Engineering and Machinery Index has ceased to exist with effect from January 2006, any awards made in 2006 will be subject to the same performance condition as described above save that the Company's TSR will be compared with the TSR of other companies included in the FTSE All-Share Industrial Engineering Index. Since the Company is now included in this sector, the Committee believes that this is the appropriate comparator group.

Spirax-Sarco Engineering plc Employee Share Ownership Plan

The executive directors participate in the Employee Share Ownership Plan, as described on page 34. Participation in the Employee Share Ownership Plan is open to all eligible UK employees. No employee's entitlement under the Employee Share Ownership Plan is subject to performance conditions. This is because the aim is to encourage increased shareholding in the Company by all eligible UK employees.

There are no other long term incentives provided to directors.

Pensions

The executive directors are members of an Inland Revenue approved non-contributory defined benefit pension scheme based on 1/60th of pensionable salary, for each year of pensionable service. The maximum pension is two-thirds of pensionable salary. The executive directors accrue pro-rata additional service at a rate which gives a further two and a half years of service at their normal retirement age of 62½. This additional service does not apply to Mr. A. J. Scrivin, who has a normal retirement age of 65. Additionally Mr. G. P. Marchand accrued pro-rata additional service at a rate which gives a further nine years of service at age 60.

The scheme provides lump sum death in service benefit of four times pensionable salary. Spouses' pensions are payable where death occurs in service or in retirement. No executive director is affected by the Inland Revenue earnings cap and there are no unapproved pension arrangements in respect of directors.

Non-Executive Directors

The remuneration of non-executive directors is approved by the full Board within the limits set out in the Company's articles of association. Their remuneration reflects the amount of time spent on the Company's business. The non-executive directors do not participate in the bonus, share option or share ownership schemes and do not participate in the new Performance Share Plan. Non-executive directors' appointments are non-pensionable.

Service Contracts

The executive directors have service contracts which are subject to 12 months' notice. The service contracts provide for a normal retirement age of 62½ for each executive director, with the exception of Mr. A. J. Scrivin who has a normal retirement age of 65.

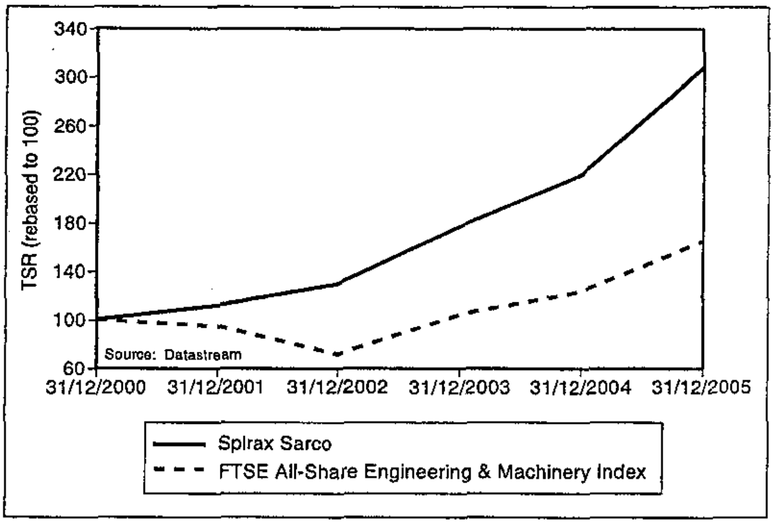
The executive directors have service contracts as follows:-

	Date of Contract	Notice Period
M.J.D. Steel	30.12.92	12 months
A.D.H. Black	18.10.98	12 months
N.H. Daws	28.05.03	12 months
G.P. Marchand	30.12.92	12 months
D.J. Meredith	30.12.92	12 months
A.J. Scrivin	15.03.05	12 months
P.A. Smith	24.12.92	12 months

The non-executive directors, including the Chairman, Mr. M. Townsend, do not have service contracts. They have appointment letters, normally for three year periods, and re-appointment is not automatic.

POLICY ON SENIOR EXECUTIVE REMUNERATION
The Committee determines the philosophy, principles and policy of remuneration which shall apply to the Group's senior executives. The responsibility for determining the precise package to meet local practice and performance lies with the Chief Executive and the responsible executive director.

TOTAL SHAREHOLDER RETURN
The performance graph illustrated shows the Company's total cumulative shareholder return for the five year period ended 31st December 2005 compared with the total cumulative shareholder return for the FTSE All-Share Engineering and Machinery Index. This comparison is selected as being the most appropriate sector for the Company's operations as the comparison automatically takes account of the impact on the Company's shares of the market's view of the engineering industry generally.



INFORMATION SUBJECT TO AUDIT
The auditors are required to report on the information contained in the remaining sections of the Report.

DETAILS OF INDIVIDUAL EMOLUMENTS

	Basic Salary/ Fees £	Benefits (1) £	Annual performance related bonus £	Total emoluments excluding pension 2005 Total £	2004 Total £
T.B. Fortune (2) (3)	28,332	153	-	28,485	77,407
M. Townsend (2)	62,480	-	-	62,480	33,000
M.J.D. Steel	322,000	15,121	131,215	468,336	424,769
C.J. Ball (4)	62,000	5,410	25,265	92,675	253,767
A.D.H. Black	182,000	14,508	74,165	270,673	241,477
N.H. Daws	163,000	12,481	66,422	241,903	199,765
G.P. Marchand	190,000	13,512	77,425	280,937	253,756
D.J. Meredith	206,000	12,619	83,945	302,564	274,035
A.J. Scrivin (5)	100,000	5,130	40,750	145,880	-
P.A. Smith	147,000	7,484	59,903	214,387	193,945
G. Bullock (2) (6)	19,000	-	-	19,000	-
E. Lindh (2)	27,000	-	-	27,000	24,000
W.H. Whiteley (2)	33,223	-	-	33,223	24,000
	1,542,035	86,418	559,090	2,187,543	1,999,921

(1) Benefits arising from employment by the Company, which relate in the main to the provision of a company car.
(2) Non-executive director.
(3) Mr. T. B. Fortune retired from the Board on 12th May 2005.
(4) Mr. C. J. Ball retired from the Board on 29th April 2005.
(5) Mr. A. J. Scrivin was appointed to the Board on 2nd May 2005 and his emoluments in the above table are calculated from this date. Total emoluments for the full year 2005 were £178,410.
(6) Mr. G. Bullock was appointed to the Board on 2nd May 2005 and his emoluments in the above table are calculated from this date.

THE DIRECTORS' REMUNERATION REPORT (continued)

Long Term Incentives

(i) Spirax-Sarco Engineering 1992 UK & Global Share Option Schemes and Spirax-Sarco Engineering Approved and Global Share Option Schemes

The interests of directors are set out below:-

	(1)	31.12.04 (or date of appointment if later*) No.	Granted during year to 31.12.05 No.	Exercised in year (4) No.	31.12.05 No.	Average exercise price per share (2) pence	Date from which exercisable (3)	Expiry date (3)
M.J.D. Steel	A	270,000	-	85,000	185,000	437.2	12.10.02	08.04.08
		270,000	-	85,000	185,000			
A.D.H. Black	A	127,500	-	87,500	40,000	468.2	14.03.06	25.03.14
	B	10,000	-	10,000	-			
		137,500	-	97,500	40,000			
N.H. Daws	A	20,000	-	-	20,000	541.9	25.03.07	25.03.14
	B	66,500	-	14,500	52,000	510.7	24.09.99	14.03.13
		86,500	-	14,500	72,000			
G.P. Marchand	A	167,500	-	97,500	70,000	569.3	24.09.99	24.12.07
		167,500	-	97,500	70,000			
D.J. Meredith	A	177,500	-	75,000	102,500	540.0	24.09.99	25.03.14
		177,500	-	75,000	102,500			
A.J. Scrivin *	B	59,500	-	39,500	20,000	540.7	24.09.99	16.06.12
		59,500	-	39,500	20,000			
P.A. Smith	A	152,500	-	112,500	40,000	468.2	14.03.06	18.08.10
		152,500	-	112,500	40,000			

* Mr. A. J. Scrivin was appointed to the Board on 2nd May 2005.

Mr. C. J. Ball retired from the Board on 29th April 2005. As at 31st December 2004, Mr. C. J. Ball held 127,500 options.

Notes

(1) Options shown on line A relate to options granted to members of the Board, whereas options shown on line B relate to options granted to individuals prior to their appointment to the Board.

The exercise prices for all options shown are lower than the middle market price of the Company's ordinary shares on 30th December 2005 (being the last trading day of the financial year).

(2) These are the weighted averages of the exercise prices for ordinary shares under option at 31st December 2005.

(3) These are the ranges of dates between which all options which have been aggregated may be exercised.

(4)

	2005 Options exercised	Option exercise price	Market price on the date options exercised	2005 Gain arising on exercise	2004 Gain arising on exercise
	No.	pence	pence	£	£
A.D.H. Black					-
	20,000	420.00000 }			
	15,000	525.00000 }			
	15,000	319.16666 }			
	20,000	397.66666 }	805.0	348,016.67	
	17,500	436.00000 }			
	5,000	739.00000 }			
	5,000	669.00000 }			
N.H. Daws					4,025.00
	7,000	420.00000 }			
	5,000	525.00000 }	714.0	32,605.00	
	2,500	611.00000 }			
G.P. Marchand					-
	15,000	420.00000 }			
	15,000	525.00000 }			
	15,000	319.16666 }	723.5	251,429.17	
	20,000	397.66666 }			
	17,500	436.00000 }			
	15,000	611.00000	730.0	17,850.00	
D.J. Meredith					30,375.00
	15,000	420.00000 }			
	15,000	319.16666 }			
	20,000	397.66666 }	797.0	254,591.67	
	25,000	611.00000 }			
A.J. Scrivin *					-
	10,000	420.00000 }			
	2,500	611.00000 }	736.0	34,725.00	
	5,000	525.00000 }			
	5,000	319.16666 }			
	10,000	397.66666 }	775.0	96,755.00	
	7,000	436.00000 }			
P.A. Smith					26,062.50
	10,000	420.00000 }			
	15,000	525.00000 }			
	15,000	319.16666 }			
	20,000	397.66666 }	710.0	229,891.67	
	17,500	436.00000 }			
	10,000	669.00000 }			
	15,000	611.00000	770.0	23,850.00	
	10.000	739.00000	816.5	7,750.00	
M.J.D. Steel					22,950.00
	40,000	420.00000 }			
	15,000	669.00000 }			
	15,000	611.00000 }	775.0	187,900.00	
	15,000	739.00000 }			
Aggregate of gains arising on exercise (Note 5)				1,485,364.18	83,412.50

* Mr. A. J. Scrivin was appointed to the Board on 2nd May 2005 and exercised the options after this date.

(5) Mr. C. J. Ball retired from the Board on 29th April 2005. Following his retirement, but in accordance with the rules of the option schemes, Mr. C. J. Ball exercised the options he held realising a gain of £325,229.17. Mr. C. J. Ball exercised options in 2004 realising a gain of £24,000.00

THE DIRECTORS' REMUNERATION REPORT (continued)

The market price of the ordinary shares on 30th December 2005 was 882.5p. During the period from 1st January 2005 to 30th December 2005 the ordinary share price ranged between 906p and 640.5p.

The Register of Directors' Interests (which is open to inspection) contains full details of directors' shareholdings and options to subscribe.

There have been no changes in the number of share options granted as shown on pages 32 and 33 since 31st December 2005.

(ii) Performance Share Plan
Under the Performance Share Plan the following awards were granted during the year to executive directors.

	Shares over which rights were granted during year	**End of the period over which the performance conditions are measured***	**Interest at 31.12.05**	**Market price of shares on 20th May 2005****
M.J.D. Steel	27,268	31.12.07	27,268	708.5p
A.D.H. Black	15,412	31.12.07	15,412	708.5p
N.H. Daws	13,803	31.12.07	13,803	708.5p
G.P. Marchand	16,090	31.12.07	16,090	708.5p
D.J. Meredith	17,445	31.12.07	17,445	708.5p
A.J. Scrivin	12,702	31.12.07	12,702	708.5p
P.A. Smith	12,448	31.12.07	12,448	708.5p

* The performance conditions are described on pages 29 and 30.
** This price is the mid market price on 20th May 2005. The date of award was 23rd May 2005.

(iii) Spirax-Sarco Engineering plc Employee Share Ownership Plan
The Company operates an Employee Share Ownership Plan in which all the executive directors are eligible to participate on the same basis as all other eligible UK employees. For the Plan period the individual director's contributions are limited to a maximum of £1,500 per annum under Inland Revenue rules. The Company provides a matching share for each share purchased under the Plan by the director which is the same basis as for other participating employees.

	Interest at 31.12.04 (or date of appointment if later*)	**Vested**	**Interest at 31.12.05 (or date of retirement if earlier**)**	**Period of qualifying conditions**
M.J.D. Steel	2,452	577	3,029	3 years
C.J. Ball **	2,452	-	2,452	3 years
A.D.H. Black	2,352	574	2,926	3 years
N.H. Daws	2,452	577	3,029	3 years
G.P. Marchand	2,452	577	3,029	3 years
D.J. Meredith	2,452	577	3,029	3 years
A.J. Scrivin *	-	504	504	3 years
P.A. Smith	2,452	577	3,029	3 years

* Mr. A. J. Scrivin was appointed to the Board on 2nd May 2005.
** Mr. C. J. Ball retired from the Board on 29th April 2005.

DIRECTORS' PENSIONS

The directors are members of defined benefit pension arrangements. The information below is consistent with the presentation used last year and sets out the disclosures under the Stock Exchange Listing Rules and the Companies Act 1985.

	Age attained at 31.12.05	Accrued pension at 31.12.04 £pa	Accrued pension at 31.12.05 £pa	Change in accrued pension during the year £pa	Change in accrued pension during the year* £pa	Transfer value of change in accrued pension* £	Transfer value of accrued pension at 31.12.04 £	Transfer value of accrued pension at 31.12.05 £	Change in total transfer value £
M.J.D. Steel	60	192,727	227,651	34,924	29,801	488,000	2,883,000	3,677,000	794,000
C.J. Ball (1)	62	129,872	134,633	4,761	2,733	48,600	2,274,000	2,344,000	70,000
A.D.H. Black (2)	48	51,230	67,637	16,407	15,045	117,000	367,000	536,000	169,000
N.H. Daws	43	55,356	72,696	17,340	15,869	92,000	319,000	466,000	147,000
G.P. Marchand	60	115,971	137,698	21,727	18,644	322,000	1,885,000	2,360,000	475,000
D.J. Meredith	46	71,751	86,419	14,668	12,761	90,000	484,000	636,000	152,000
A.J. Scrivin (3)	58	83,877	93,791	9,914	7,685	110,000	965,000	1,177,000	212,000
P.A. Smith	57	82,168	97,336	15,168	12,984	208,000	1,060,000	1,445,000	385,000

* net of deferred revaluation at a rate of 2.7% per annum (reduced accordingly for Messrs. C. J. Ball and A. J. Scrivin for the part year they were directors).

(1) Mr. C. J. Ball retired from the Board on 29th April 2005 - the transfer value at end of year relates to benefits on retirement on end of year assumptions.
(2) Benefits shown net of pensions sharing order, currently worth £25,750 per annum.
(3) Mr. A. J. Scrivin was appointed to the Board on 2nd May 2005 - the transfer value at start of year relates to the value at 2nd May 2005.

The following is additional information relating to directors' pensions:

(i) Dependant's pensions

On the death of a director in service, a spouse's pension equal to one-half of the director's pension based on pensionable service to the date of death is payable. On the death of a director after payment of the pension commences, a spouse's pension of one-half of the director's pension entitlement at the date of death, ignoring commutation and any early retirement actuarial reduction, is payable; in addition directors' pensions are guaranteed to be paid for five years from retirement.

(ii) Early retirement rights

After leaving the service of the Company, a director has the right to draw his accrued pension at any time after his 60th birthday with no reduction, with the exception of Mr. A. J. Scrivin who has a normal retirement age of 65.

(iii) Pension increases

Pensions are subject to annual increases in line with the annual rise in the RPI subject to a maximum of 5% per annum. The Trustees and the Company have the discretion to apply a greater increase.

(iv) Other discretionary benefits

There are no discretionary practices which are taken into account in calculating transfer values on leaving service.

Signed by
M. Townsend *Chairman*
on behalf of the Board

STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE ANNUAL REPORT AND ACCOUNTS

The directors are responsible for preparing the Annual Report and the Group and parent company accounts in accordance with applicable law and regulations.

Company law requires the directors to prepare Group and parent company accounts for each financial year. Under that law they are required to prepare the Group accounts in accordance with IFRS as adopted by the EU and have elected to prepare the parent company accounts on the same basis.

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

In preparing each of the Group and parent company accounts, the directors are required to:

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

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

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

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's web site: www.SpiraxSarcoEngineering.com. Legislation in the UK governing the preparation and dissemination of accounts may differ from legislation in other jurisdictions.

AUDITOR'S REPORT

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SPIRAX-SARCO ENGINEERING PLC

We have audited the Group and parent company accounts (the "accounts") of Spirax-Sarco Engineering plc for the year ended 31st December 2005 which comprise the Group Income Statement, the Group and parent company Balance Sheets, the Group and parent company Cash Flow Statements, the Group and parent company Statement of Recognised Income and Expense and the related notes. These accounts have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

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

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the accounts in accordance with applicable law and International Financial Reporting Standards (IFRS) as adopted by the EU are set out in the Statement of Directors' Responsibilities on page 36.

Our responsibility is to audit the accounts and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

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

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

We read other information contained in the Annual Report and consider whether it is consistent with the audited accounts. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the accounts. Our responsibilities do not extend to any other information.

BASIS OF AUDIT OPINION

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the accounts, and of whether the accounting policies are appropriate to the Group's and company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts 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 accounts and the part of the Directors' Remuneration Report to be audited.

OPINION

In our opinion:

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

KPMG Audit Plc KPMG Audit Plc London 13th March 2006
Chartered Accountants, Registered Auditor

GROUP INCOME STATEMENT

for the year ended 31st December 2005

	notes	2005 £000	2004 £000
Revenue	2	**349,100**	315,991
Operating costs	3	**(293,930)**	(268,035)
Operating profit	2	**55,170**	47,956
Financial expenses		**(11,450)**	(10,920)
Financial income		**12,378**	10,933
Net financing income	5	**928**	13
Share of profit of associates		**861**	735
Profit before taxation	6	**56,959**	48,704
Taxation	8	**(18,772)**	(16,262)
Profit for the period		**38,187**	32,442
Attributable to:			
Equity holders of the parent		**38,036**	32,314
Minority interest		**151**	128
Profit for the period		**38,187**	32,442
Earnings per share	10		
Basic earnings per share		**50.0p**	43.1p
Diluted earnings per share		**49.6p**	42.7p
Dividends	11		
Dividends per share		**23.8p**	21.4p
Dividends paid during the year (per share)		**21.9p**	20.4p

All amounts relate to continuing operations.

The notes on pages 42 to 77 form an integral part of the accounts.

BALANCE SHEETS

at 31st December 2005

	notes	THE GROUP 2005 £000	THE GROUP 2004 £000	PARENT COMPANY 2005 £000	PARENT COMPANY 2004 £000
ASSETS					
Non-current assets					
Property, plant and equipment	12	**85,752**	83,514	**-**	-
Goodwill	13	**15,033**	11,862	**-**	-
Other intangible assets	13	**8,357**	6,988	**-**	-
Prepayments		**396**	345	**-**	-
Loans to subsidiaries	14	**-**	-	**13,829**	11,165
Investment in subsidiaries	15	**-**	-	**47,311**	46,918
Investment in associates	16	**3,371**	2,494	**-**	-
Deferred tax	17	**18,536**	16,615	**3,256**	2,426
		131,445	121,818	**64,396**	60,509
Current assets					
Inventories	18	**64,216**	58,229	**-**	-
Trade receivables		**83,303**	76,021	**-**	-
Due from subsidiaries		**-**	-	**22,418**	22,500
Other current assets	19	**8,688**	8,388	**486**	401
Cash and cash equivalents	30	**56,929**	48,756	**39,625**	28,042
		213,136	191,394	**62,529**	50,943
Total assets		**344,581**	313,212	**126,925**	111,452
EQUITY AND LIABILITIES					
Current liabilities					
Trade and other payables	20	**46,843**	43,429	**1,908**	1,947
Bank overdrafts	30	**3,836**	4,842	**257**	1,092
Short term borrowing	30	**1,498**	-	**-**	-
Current portion of long term borrowings	30	**25,010**	8,183	**-**	-
Current tax payable	21	**7,326**	6,788	**689**	355
		84,513	63,242	**2,854**	3,394
Net current assets		**128,623**	128,152	**59,675**	47,549
Non-current liabilities					
Long term borrowings	30	**7,540**	34,432	**-**	-
Deferred tax	17	**7,728**	7,273	**-**	-
Post-retirement benefits	29	**45,807**	41,335	**5,800**	5,400
Provisions	23	**747**	644	**-**	-
Due to subsidiaries		**-**	-	**643**	643
		61,822	83,684	**6,443**	6,043
Total liabilities		**146,335**	146,926	**9,297**	9,437
Net assets	2	**198,246**	166,286	**117,628**	102,015
Equity					
Share capital	24	**19,238**	18,800	**19,238**	18,800
Share premium account		**46,154**	38,024	**46,154**	38,024
Other reserves		**7,554**	699	**1,832**	1,832
Retained earnings		**124,672**	107,957	**50,404**	43,359
Equity attributable to equity holders of the parent	25	**197,618**	165,480	**117,628**	102,015
Minority interest		**628**	806	**-**	-
Total equity		**198,246**	166,286	**117,628**	102,015
Total equity and liabilities		**344,581**	313,212	**126,925**	111,452

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

Directors

M.J.D. Steel D.J. Meredith

M.J.D. Steel

STATEMENTS OF RECOGNISED INCOME AND EXPENSE

for the year ended 31st December 2005

	THE GROUP		PARENT COMPANY	
	2005	2004	**2005**	2004
	£000	£000	**£000**	£000
Actuarial loss on post retirement benefits	**(8,974)**	3,815	**(1,935)**	919
Deferred tax on actuarial loss on post retirement benefits	**2,942**	(886)	**600**	(270)
Foreign exchange translation differences	**6,907**	(1,133)	**-**	-
Gains on cash flow hedges	**6**	-	**-**	-
Income and expense recognised directly in equity	**881**	1,796	**(1,335)**	649
Profit for the period	**38,187**	32,442	**24,788**	23,613
Total recognised income and expense for the period	**39,068**	34,238	**23,453**	24,262
Attributable to				
Equity holders of the parent	**38,917**	34,110	**23,453**	24,262
Minority interest	**151**	128	**-**	-
Total recognised income and expense for the period	**39,068**	34,238	**23,453**	24,262
Change in accounting policy:				
Adjustment in respect of adoption of IAS 32 and IAS 39 on 1st January 2005				
Adjustment to cash flow hedge reserve	**(58)**	-	**-**	-

CASH FLOWS

for the year ended 31st December 2005

		THE GROUP		PARENT COMPANY	
		2005	2004	**2005**	2004
	notes	**£000**	£000	**£000**	£000
Cash flows from operating activities					
Profit before taxation		**56,959**	48,704	**24,685**	23,502
Depreciation and amortisation		**13,151**	13,030	**-**	-
Dividends received		**-**	-	**(25,309)**	(23,616)
Share of profit of associates		**(861)**	(735)	**-**	-
Equity settled share plans		**576**	357	**238**	100
Net finance income		**(928)**	(13)	**(1,376)**	(1,754)
Operating profit before changes in working capital and provisions		**68,897**	61,343	**(1,762)**	(1,768)
Increase in trade and other receivables		**(2,814)**	(6,875)	**(88)**	(24)
Increase in amounts due from subsidiaries		**-**	-	**(4,541)**	(4,675)
Increase in inventories		**(3,224)**	619	**-**	-
Decrease in provisions and post-retirement benefits		**(4,045)**	(23)	**397**	449
Increase in trade and other payables		**1,371**	7,139	**348**	230
Increase in amounts due to subsidiaries		**-**	-	**14**	(69)
Cash generated from operations		**60,185**	62,203	**(5,632)**	(5,857)
Interest paid		**(1,677)**	(1,829)	**(420)**	(9)
Income taxes paid		**(16,789)**	(16,071)	**261**	109
Net cash from operating activities		**41,719**	44,303	**(5,791)**	(5,757)
Cash flows from investing activities					
Purchase of property, plant and equipment		**(11,692)**	(13,477)	**-**	-
Proceeds from sale of property, plant and equipment		**850**	641	**-**	-
Purchase of software		**(1,139)**	(918)	**-**	-
Development expenditure capitalised		**(1,070)**	(674)	**-**	-
Acquisition of businesses		**(5,866)**	(803)	**(780)**	(582)
Interest received		**1,860**	1,517	**1,796**	1,763
Dividends received		**351**	71	**25,309**	23,616
Net cash used in investing activities		**(16,706)**	(13,643)	**26,325**	24,797
Cash flows from financing activities					
Proceeds from issue of share capital		**8,568**	2,138	**8,568**	2,138
Repayment of borrowings	*30*	**(7,728)**	(2,330)	**-**	-
Payment of finance lease liabilities	*30*	**(372)**	(360)	**-**	-
Dividends paid (including minorities)		**(16,796)**	(15,322)	**(16,684)**	(15,289)
Net cash used in financing activities		**(16,328)**	(15,874)	**(8,116)**	(13,151)
Net increase in cash and cash equivalents	*30*	**8,685**	14,786	**12,418**	5,889
Cash and cash equivalents at beginning of period		**43,914**	29,120	**26,950**	21,061
Exchange movement		**494**	8	**-**	-
Cash and cash equivalents at end of period	*30*	**53,093**	43,914	**39,368**	26,950
Borrowings and finance leases		**(34,048)**	(42,615)	**-**	-
Net cash	*30*	**19,045**	1,299	**39,368**	26,950

NOTES TO THE ACCOUNTS

1 ACCOUNTING POLICIES

Basis of preparation

The consolidated accounts have been prepared in accordance with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) that have been adopted by the European Union (EU). In accordance with IFRS 1 'First-time Adoption of International Financial Reporting Standards' an explanation of how the transition to IFRS has affected the previously reported financial results was provided in a 2004 restatement issued on 12th July 2005.

IFRS 1 grants certain exemptions to assist companies as they change to report under IFRS. The following exemptions have been taken by the Group in preparation of its consolidated accounts for the year ended 31st December 2005:

- Financial Instruments - The Group has elected to adopt IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement' prospectively from 1st January 2005.
- Post-retirement benefits - The Group has chosen to recognise all cumulative actuarial gains and losses on defined benefit plans in equity at 1st January 2004. In preparing 2004 and 2005 financial information the directors have elected to adopt the endorsed December 2004 amendment to IAS 19 - Employee Benefits that allows actuarial gains and losses to be recognised immediately in the Statement of Recognised Income and Expense.
- Share Schemes - The transitional requirements of IFRS 2 require all share-based payment awards made after 7th November 2002 to be restated. The restatement of awards made before that date is optional but we have chosen to adopt IFRS 2 from 1st July 2001 to give greater clarity and comparibility between accounting periods.
- Business Combinations - The Group has elected to apply IFRS 3 prospectively from the date of transition to IFRS. Therefore business combinations that took place prior to 1st January 2004 have not been restated.
- Cumulative translation differences - Under IAS 21, cumulative foreign exchange movements on translation of foreign entities on consolidation should be disclosed as a seperate reserve within equity. However, for simplicity, the Group has adopted the election to reset the foreign currency translation reserve to zero as at 1st January 2004.
- Property, plant and equipment (IAS 16) - The Group has elected to cease revaluing freehold premises and to use the carrying amounts as at 1st January 2004 as 'deemed cost'.

The preparation of consolidated accounts in conformity with IFRS requires the directors to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experiences and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

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

The following adopted IFRS were available for early application but have not been applied by the Group in these accounts:

- Amendment to IAS 1 Capital Disclosures
- Amendment to IAS 39, Cash Flow Hedge Accounting of Forecast Intragroup Transactions
- Amendment to IAS 39, Fair Value Option
- Amendment to IAS 39 and IFRS 4, Financial Guarantee Contracts
- IFRS 7, Financial Instruments Disclosures
- IFRIC 4 determining whether an Arrangement contains a lease.

The company does not expect the above amendments to have any significant impact on the accounts for the period commencing 1st January 2006. With respect to financial guarantee contracts where the company enters into contracts to guarantee the indebtedness of other companies within its group, the company considers these to be insurance arrangements and accounts for them as such. In this respect the company treats the guarantee contract as a contingent liability until such time as it becomes probable that the company will be required to make a payment under the guarantee.

Basis of accounting

(i) Subsidiaries

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

(ii) Associates

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

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

(iv) Company
Under Section 230 (4) of the Companies Act 1985 the company is exempt from the requirement to present its own income statement.

Foreign currency
(i) On consolidation
The assets and liabilities of foreign operations are translated into sterling at exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated into sterling at average rates of exchange ruling during the year.

Differences arising from the changes in rates of exchange are treated as part of the trading profit where they relate to items of a trading nature. Exchange differences arising from the translation of the net investment in foreign operations are taken to a seperate translation reserve within equity. They are recycled and recognised in the income statement upon disposal of the operation. In respect of all foreign operations, any differences that have arisen before 1st January 2004, the date of transition to IFRS, are not presented as a separate component of equity.

(ii) Foreign currency transactions
Transactions in foreign currencies are translated at the foreign exchange rate at the date of the transaction. Monetary assets and liabilities at the balance sheet date denominated in a currency other than the functional currency of the entity are translated at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated at foreign exchange rates ruling at the dates fair value was determined.

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

Hedge of net investment in foreign operations
The portion of the gain or loss on an instrument used to hedge a net investment in a foreign operation that is determined to be an effective hedge is recognised directly in a separate translation reserve within equity. The ineffective portion is recognised immediately in the income statement.

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

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

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

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

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

(ii) Research and development
Expenditure on research and development is charged to the income statement in the period in which it is incurred except that, development expenditure is capitalised where the development costs relate to new or substantially improved products that are subsequently to be released for sale and will generate future economic benefits. The expenditure capitalised includes the cost of materials, direct labour and an appropriate proportion of overheads. Capitalised development expenditure is stated at cost less accumulated amortisation (see below) and any impairment losses.

(iii) Other intangible assets
Intangible assets other than goodwill that are acquired by the Group are stated at cost or fair value less accumulated amortisation (see below) and any impairment losses.

NOTES TO THE ACCOUNTS *(continued)*

1 ACCOUNTING POLICIES *(continued)*

(iv) Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets. Goodwill and intangible assets with an indefinite useful life are tested for impairment annually. The principal amortisation rates are as follows:

Capitalised development costs	20%	Manufacturing designs and core technology	10%
Computer software	12.5 - 20%	Non compete undertaking	50%
Customer relationships	20%		
Brand names and trademarks	10 - 20%		

Stocks

Stock and work in progress are valued at the lower of cost, including overheads where appropriate, and estimated net realisable value. Provision is made for slow-moving and obsolete items based on an assessment of technological and market developments and on an analysis of usage.

Cash and cash equivalents

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

Employee benefits

(i) Defined contribution plans

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

(ii) Defined benefit plans

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

The cost of other post-employment liabilities are calculated in a similar way to defined benefit pension schemes and spread over the period which benefit is expected to be derived from the employees' services, in accordance with the advice of qualified actuaries.

(iii) Employee share plans

Incentives in the form of shares are provided to employees under share option and share award schemes. The fair value of these options and awards at their date of grant is charged to the income statement over the relevant vesting periods. The value of the charge is adjusted to reflect expected and actual levels of options vesting.

(iv) Long term share incentive plans

The fair value of awards is measured at the date of grant and the cost spread over the vesting period. The amount recognised as an expense is not adjusted to reflect market based performance conditions.

Revenue

Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer. Revenue from projects or service contracts is recognised as income in proportion to the stage of completion of the transaction at the balance sheet date. The stage of completion is assessed depending on the specific circumstances of each case. No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due or associated costs, or there is the possibility of return of the goods. No revenue is recognised if there is significant continuing management involvement with the goods.

As soon as the outcome of a project or service contract can be estimated reliably, revenue and expenses are recognised in the income statement in proportion to the stage of completion of the project or service contract. An expected loss on a project or service contract is recognised immediately in the income statement.

Leases

(i) Operating leases

Payments made under operating leases are charged to the income statement on a straight-line basis over the term of the lease.

(ii) Finance leases
Leases where the Group assumes substantially all of the risks and rewards of ownership are classified as finance leases as if the asset had been purchased outright. Assets acquired under finance leases are recognised as assets of the Group and the capital elements of the leasing commitments are shown as obligations in creditors. Depreciation is charged on a consistent basis with similar owned assets or over the lease term if shorter. The interest element of the lease payment is charged to the income statement on a basis which produces a consistent rate of charge over the period of the liability.

Taxation
The tax charge shown in the income statement comprises current and deferred tax. Current tax is the expected tax payable on the profit for the year and any adjustments in respect of previous years. Deferred tax is provided in full using the balance sheet liability method, providing for temporary differences arising between the tax base of assets and liabilities, and their carrying amounts in the accounts. Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax is provided using rates of tax that have been enacted or substantively enacted at the balance sheet date.

2 SEGMENTAL REPORTING

2005
Primary Segment

Revenue by geographical location of operation	UK & Republic of Ireland £000	Continental Europe £000	North America £000	Asia £000	Rest of the world £000	Total £000
Total revenue of operation	102,479	156,050	73,220	61,263	45,949	438,961
Intra-divisional revenue	(105)	(14,095)	(603)	(565)	(894)	(16,262)
Inter-divisional revenue	(50,178)	(17,654)	(369)	(1,852)	(3,546)	(73,599)
Sales to customers	52,196	124,301	72,248	58,846	41,509	349,100
Profit from operations	**10,881**	**18,733**	**7,938**	**11,430**	**6,188**	**55,170**
Operating profit margin (based on total revenue of operation)	10.6%	12.0%	10.8%	18.7%	13.5%	12.6%
Total operating profit margin (based on total net revenue)						15.8%
Share of profit of associates	-	-	282	579	-	861
Revenue by geographical location of customers	**40,084**	**125,343**	**73,056**	**65,841**	**44,776**	**349,100**
Segment assets	64,393	90,241	40,191	41,523	31,241	267,589
Segment liabilities	(36,557)	(31,523)	(12,997)	(6,096)	(6,224)	(93,397)
						174,192
Deferred tax						10,808
Current tax payable net of tax recoverable						(5,799)
Net cash						19,045
Net assets						198,246
Capital additions, tangible and intangible, by segment	5,032	4,431	2,600	1,279	2,222	15,564
Depreciation and amortisation by segment	5,644	3,915	1,734	895	963	13,151

Secondary segment

	Spirax Sarco £000	Watson-Marlow Bredel £000	Total £000
Revenue by business operation	302,627	46,473	349,100
Segment assets	233,912	33,677	267,589
Capital additions, tangible and intangible, by segment	12,204	3,360	15,564

NOTES TO THE ACCOUNTS *(continued)*

2 SEGMENTAL REPORTING *(continued)*
2004
Primary Segment

Revenue by geographical location of operation	UK & Republic of Ireland £000	Continental Europe £000	North America £000	Asia £000	Rest of the world £000	Total £000
Analysis by operation						
Total revenue of operation	97,419	149,334	64,950	50,465	36,482	398,650
Intra-divisional revenue	-	(13,361)	(564)	(555)	(234)	(14,714)
Inter-divisional revenue	(45,843)	(16,957)	(512)	(1,234)	(3,399)	(67,945)
Sales to customers	51,576	119,016	63,874	48,676	32,849	315,991
Profit from operations	10,533	17,752	6,601	8,184	4,886	47,956
Operating profit margin (based on total revenue of operation)	10.8%	11.9%	10.2%	16.2%	13.4%	12.0%
Total operating profit margin (based on total net revenue)						15.2%
Share of profit of associates	-	-	202	533	-	735
Revenue by geographical location of customers	39,922	121,164	64,119	55,327	35,459	315,991
Segment assets	66,960	89,855	33,140	34,829	21,749	246,533
Segment liabilities	(34,830)	(30,962)	(10,721)	(4,639)	(4,253)	(85,405)
						161,128
Deferred tax						9,342
Current tax payable net of tax recoverable						(5,483)
Net cash						1,299
Net assets						166,286
Capital additions, tangible and intangible, by segment	6,920	4,312	2,475	1,033	1,204	15,944
Depreciation and amortisation by segment	5,620	4,070	1,537	1,026	778	13,031

Secondary segment

	Spirax Sarco £000	Watson-Marlow Bredel £000	Total £000
Revenue by business operation	273,065	42,926	315,991
Segment assets	215,245	31,288	246,533
Capital additions, tangible and intangible, by segment	12,427	3,517	15,944

Profit from operations figures reflect the allocation of UK incurred central support costs to the segments to which the expenses relate. This is a change from the July 2005 IFRS restatement and so 2004 segmental profit figures reflect the changes.

3 OPERATING COSTS

	2005 £000	2004 £000
Change in stocks of finished goods and work in progress	**(772)**	19
Raw materials and consumables	**93,049**	84,902
Staff costs *(note 4)*	**130,309**	118,629
Depreciation and amortisation	**13,151**	13,031
Other operating charges	**58,193**	51,454
	293,930	268,035

Amortisation of intangible assets acquired was £175,000 (2004 £nil) and amortisation of capitalised development costs was £834,000 (2004: £632,000).

4 STAFF COSTS AND NUMBERS

The aggregate payroll costs of persons employed by the Group were as follows:

	2005 £000	2004 £000
Wages and salaries	**102,966**	93,671
Social security costs	**17,657**	15,470
Other pension costs	**9,686**	9,488
	130,309	118,629

The average number of persons employed by the Group (including directors) during the year was as follows:

	2005 Number	2004 Number
United Kingdom	**1,133**	1,106
Overseas	**2,766**	2,661
	3,899	3,767

5 NET FINANCING INCOME

	2005 £000	2004 £000
Financial expenses		
Bank and other borrowing interest payable	**(1,704)**	(1,832)
Interest on pension scheme liabilities	**(9,746)**	(9,088)
	(11,450)	(10,920)
Financial income		
Bank interest receivable	**1,869**	1,518
Expected return on pension scheme assets	**10,509**	9,415
	12,378	10,933
Net financing income	**928**	13
Net pension scheme financial income	**763**	327
Net bank interest	**165**	(314)
Net financing income	**928**	13

6 PROFIT BEFORE TAXATION

Profit before taxation is shown after charging:

	2005 £000	2004 £000
Depreciation of tangible fixed assets held under finance leases	**145**	176
Audit fees (Spirax-Sarco Engineering plc £130,000 (2004: £104,000))	**818**	707
Hire of plant and machinery	**300**	286
Other operating leases	**2,706**	2,421
Research and development	**4,288**	4,365

Fees paid to the auditors of the parent company and their associates for services other than statutory audits supplied to the Company and the rest of the Group worldwide amounted to £581,000 (2004: £501,000), including amounts paid to the auditors of overseas companies of £261,000 (2004: £225,000). Fees were paid in respect of taxation services (£343,000 (2004: £366,000)) and further assurance services (£238,000 (2004: £135,000)).

7 DIRECTORS' EMOLUMENTS

Details of directors' emoluments, share plans and long term share incentive plan and pension benefits are shown in the Directors' Remuneration Report on pages 28 to 35. Directors represent the key management personnel of the Group under the terms of IAS 24: Related Party Disclosures.

8 TAXATION

	2005	2004
	£000	£000
Analysis of charge in period		
UK corporation tax		
Current tax on income for the period	**12,702**	12,164
Adjustments in respect of prior periods	**(268)**	(148)
	12,434	12,016
Double taxation relief	**(9,755)**	(8,851)
	2,679	3,165
Foreign tax		
Current tax on income for the period	**15,565**	12,752
Adjustments in respect of prior periods	**(47)**	48
	15,518	12,800
Total current tax charge	**18,197**	15,965
Deferred tax	**575**	297
Tax on profit on ordinary activities	**18,772**	16,262

Reconciliation of effective tax rate

	2005	2004
	£000	£000
Profit before tax	**56,959**	48,704
Tax using the UK corporation tax rate of 30% (2004: 30%)	**17,088**	14,611
Effect of higher overseas tax rates	**889**	1,643
Associated companies	**(258)**	(221)
Non-deductible expenditure	**827**	797
Overprovided in prior years	**(362)**	(158)
Contingencies	**300**	-
Other reconciling items	**288**	(410)
Total tax in income statement	**18,772**	16,262

Factors that may affect the future tax charges:
The Group's tax charge in future years is likely to be affected by the proportion of profits arising and the effective tax rates in the various territories in which the Group operates. No UK tax (after double tax relief for underlying tax) is expected to be payable on the future remittance of the retained earnings of overseas subsidiaries. The impact of higher tax rates on overseas earnings has reduced due to a change in the profit mix and partly due to a decrease in global tax rates.

Taxation recognised directly in equity

	2005	2004
	£000	£000
Relating to:		
Equity settled transactions	**110**	(353)
On actuarial gains and losses	**2,942**	886
	3,052	533

9 PROFIT FOR THE FINANCIAL YEAR ATTRIBUTABLE TO SHAREHOLDERS

Profit dealt with in the accounts of Spirax-Sarco Engineering plc was £24,788,000 (2004: £23,613,000). Included in this amount are dividends from subsidiary undertakings of £25,309,000 (2004: £23,616,000).

10 EARNINGS PER SHARE

	2005 £000	2004 £000
Earnings	**38,036**	32,314
Weighted average shares in issue	**76,119,005**	74,931,130
Dilution	**577,169**	781,558
Diluted weighted average shares in issue	**76,696,174**	75,712,688
Basic earnings per share	**50.0p**	43.1p
Diluted earnings per share	**49.6p**	42.7p

The dilution is in respect of unexercised share options and the performance share plan.

11 DIVIDENDS

	2005 £000	2004 £000
Amounts paid in the year		
Final dividend for the year ended 31st December 2004 of 15.1p (2003: 14.1p) per share	**11,459**	10,552
Interim dividend for the year ended 31st December 2005 of 6.8p (2004: 6.3p) per share	**5,225**	4,737
	16,684	15,289

Amounts arising in respect of the year		
Interim dividend for the year ended 31st December 2005 of 6.8p (2004: 6.3p) per share	**5,225**	4,737
Proposed final dividend for the year ended 31st December 2005 of 17.0p (2004: 15.1p) per share	**13,093**	11,459
	18,318	16,196

The proposed final dividend is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these accounts.

NOTES TO THE ACCOUNTS *(continued)*

12 PROPERTY, PLANT AND EQUIPMENT

	THE GROUP				
	Land and buildings				
	Freehold £000	Short leasehold £000	Plant and machinery £000	Fixtures, fittings, tools and equipment £000	Total £000
Cost or deemed cost:					
At 1st January 2004	49,268	1,000	79,947	41,370	171,585
Exchange adjustments	(125)	(51)	(682)	(265)	(1,123)
	49,143	949	79,265	41,105	170,462
Additions	1,323	(3)	8,734	3,627	13,681
Disposals	(110)	(24)	(2,050)	(889)	(3,073)
At 31st December 2004	50,356	922	85,949	43,843	181,070
Depreciation:					
At 1st January 2004	7,261	237	50,126	32,281	89,905
Exchange adjustments	(58)	(9)	(367)	(197)	(631)
	7,203	228	49,759	32,084	89,274
Charged in year	1,262	26	6,756	2,955	10,999
Disposals	(44)	(3)	(1,828)	(842)	(2,717)
At 31st December 2004	8,421	251	54,687	34,197	97,556
Net book value:					
At 31st December 2004	41,935	671	31,262	9,646	83,514
At 31st December 2003	42,007	763	29,821	9,089	81,680
Cost or deemed cost:					
At 1st January 2005	50,356	922	85,949	43,843	181,070
Exchange adjustments	1,205	110	1,670	1,289	4,274
	51,561	1,032	87,619	45,132	185,344
Additions	422	48	8,585	2,677	11,732
Disposals	(65)	(4)	(3,637)	(1,523)	(5,229)
At 31st December 2005	**51,918**	**1,076**	**92,567**	**46,286**	**191,847**
Depreciation:					
At 1st January 2005	8,421	251	54,687	34,197	97,556
Exchange adjustments	255	27	962	987	2,231
	8,676	278	55,649	35,184	99,787
Charged in year	1,060	31	6,885	3,222	11,198
Disposals	(17)	-	(3,222)	(1,651)	(4,890)
At 31st December 2005	**9,719**	**309**	**59,312**	**36,755**	**106,095**
Net book value:					
At 31st December 2005	**42,199**	**767**	**33,255**	**9,531**	**85,752**

Land and buildings with a book value of £3,123,000 (2004: £2,799,000) have been provided as security for a mortgage loan.

Included in the above are finance leases with a net book value of £1,517,000 (2004: £1,801,000).

13 GOODWILL AND OTHER INTANGIBLE ASSETS

	THE GROUP				
	Acquired intangibles £000	Development £000	Computer software £000	Total other intangibles £000	Goodwill £000
Cost or valuation:					
At 1st January 2004	-	3,075	10,244	13,319	11,123
Exchange adjustments	-	5	(23)	(18)	100
	-	3,080	10,221	13,301	11,223
Additions	672	682	909	2,263	639
At 31st December 2004	672	3,762	11,130	15,564	11,862
Amortisation:					
At 1st January 2004	-	615	5,517	6,132	-
Exchange adjustments	-	1	(25)	(24)	-
	-	616	5,492	6,108	-
Charged in year	-	636	1,832	2,468	-
At 31st December 2004	-	1,252	7,324	8,576	-
Net book value:					
At 31st December 2004	672	2,510	3,806	6,988	11,862
At 31st December 2003	-	2,460	4,727	7,187	11,123

	THE GROUP				
	Acquired intangibles £000	Development £000	Computer software £000	Total other intangibles £000	Goodwill £000
Cost or valuation:					
At 1st January 2005	672	3,762	11,130	15,564	11,862
Exchange adjustments	(23)	(28)	28	(23)	(68)
	649	3,734	11,158	15,541	11,794
Additions	1,601	1,078	1,153	3,832	3,239
At 31st December 2005	**2,250**	**4,812**	**12,311**	**19,373**	**15,033**
Amortisation:					
At 1st January 2005	-	1,252	7,324	8,576	-
Exchange adjustments	-	(6)	7	1	-
	-	1,246	7,331	8,577	-
Charged in year	182	838	1,419	2,439	-
At 31st December 2005	**182**	**2,084**	**8,750**	**11,016**	**-**
Net book value:					
At 31st December 2005	**2,068**	**2,728**	**3,561**	**8,357**	**15,033**

Impairment
There was no impairment of goodwill during 2005 or 2004.

For the purposes of impairment testing of goodwill, goodwill values have been compared against discounted forecast cash flows of the relevant cash-generating unit on a value in use basis. The forecasts include post tax profit increases and the corresponding cash flows. A discount rate of 10% has been applied to the calculations.

The carrying amounts of goodwill allocated to cash-generating units are as follows:

	2005 £000	2004 £000
M & M product unit	**2,511**	2,463
Alitea product unit	**2,153**	2,162
Spirax Sarco, Inc. USA	**1,869**	-
UK Supply product unit	**1,625**	1,683
Watson-Marlow Bredel, South Africa	**1,377**	1,384
Mitech product unit	**1,175**	-
Spirax-Sarco S.A.S. France	**1,096**	1,135
Other cash-generating units	**3,227**	3,035
	15,033	11,862

14 LOANS TO SUBSIDIARIES

	PARENT COMPANY	
	2005 £000	2004 £000
Cost:		
At 1st January	**12,207**	11,380
Exchange adjustments	**(14)**	166
	12,193	11,546
Loans	**2,678**	745
Repayments	**-**	(84)
At 31st December	**14,871**	12,207
Amounts written off:		
At 1st January and 31st December	**1,042**	1,042
Net book value:		
At 31st December	**13,829**	11,165

NOTES TO THE ACCOUNTS *(continued)*

15 INVESTMENT IN SUBSIDIARIES

	PARENT COMPANY	
	2005 £000	2004 £000
Cost:		
At 1st January	**47,912**	46,354
Acquisition	**393**	1,558
At 31st December	**48,305**	47,912
Amounts written off:		
At 1st January and 31st December	**994**	994
Net book value:		
At 31st December	**47,311**	46,918

Investments are stated at cost less provisions for any impairment in value.

Details relating to subsidiary undertakings are given on the back cover. Except where stated all classes of shares were 100% owned by the Group at 31st December 2005. The country of incorporation of the principal Group companies is the same as the country of operation with the exception of companies operating in the United Kingdom which are incorporated in Great Britain. Eirdata Environmental Services Ltd. is incorporated in Eire. All are in the fluid control business except Spirax-Sarco Investments Ltd., Spirax-Sarco Overseas Ltd., Sarco International Corp., Watson-Marlow Bredel Holdings B.V., Spirax-Sarco Engineering S.L., Spirax-Sarco Engineering B.V. and Spirax-Sarco Investments B.V. which are investment holding companies.

16 INVESTMENT IN ASSOCIATES

	THE GROUP	
	2005 £000	2004 £000
Cost of investment	**645**	645
Share of post-acquisition profit, net of dividends received	**2,726**	1,849
	3,371	2,494
Summarised aggregated financial information		
Revenue	**12,216**	9,842
Profit for the period	**2,023**	1,745
Assets	**10,609**	7,446
Liabilities	**2,768**	1,643

Details of the Group's associates at 31st December 2005 are as follows:

Name of associate	Country of incorporation and operation	Proportion of ownership interest and voting power held	Principal activity
Spirax-Marshall Ltd.	India	40%	Manufacturing and Selling
Spirax-Sarco Mexicana S.A.	Mexico	49%	Manufacturing and Selling

17 DEFERRED TAX ASSETS AND LIABILITIES

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	THE GROUP					
	Assets		Liabilities		Net	
	2005 £000	2004 £000	**2005 £000**	2004 £000	**2005 £000**	2004 £000
Accelerated capital allowances	**(12)**	(15)	**3,710**	3,496	**3,698**	3,481
Provisions	**(4,103)**	(4,571)	**102**	169	**(4,001)**	(4,402)
Losses	**(359)**	(205)	**5**	1	**(354)**	(204)
Stock	**(189)**	(178)	**1,276**	1,032	**1,087**	854
Pensions	**(14,027)**	(11,931)	**2,538**	2,542	**(11,489)**	(9,389)
Other timing differences	**(3,079)**	(2,834)	**3,330**	3,152	**251**	318
Tax (assets)/liabilities	**(21,769)**	(19,734)	**10,961**	10,392	**(10,808)**	(9,342)
Net off liabilities/(assets)	**3,233**	3,119	**(3,233)**	(3,119)	**-**	-
Net tax (assets)/liabilities	**(18,536)**	(16,615)	**7,728**	7,273	**(10,808)**	(9,342)

Movement in deferred tax during the year

	THE GROUP			
	1 January 2005 £000	Recognised in income £000	Recognised in equity £000	**31 December 2005 £000**
Accelerated capital allowances	3,481	78	139	**3,698**
Provisions	(4,402)	508	(107)	**(4,001)**
Losses	(204)	(140)	(10)	**(354)**
Stock	854	124	109	**1,087**
Pensions	(9,389)	210	(2,310)	**(11,489)**
Other timing differences	318	(202)	135	**251**
	(9,342)	578	(2,044)	**(10,808)**

	THE GROUP			
	1 January 2004 £000	Recognised in income £000	Recognised in equity £000	31 December 2004 £000
Accelerated capital allowances	3,433	105	(57)	3,481
Provisions	(3,919)	(444)	(39)	(4,402)
Losses	(206)	-	2	(204)
Stock	726	189	(61)	854
Pensions	(10,358)	875	94	(9,389)
Other timing differences	75	110	133	318
	(10,249)	835	72	(9,342)

Movement in deferred tax during the year

	PARENT COMPANY			
	1 January 2005 £000	Recognised in income £000	Recognised in equity £000	**31 December 2005 £000**
Pensions	1,905	119	600	**2,624**
Other timing differences	521	72	39	**632**
	2,426	191	639	**3,256**

	PARENT COMPANY			
	1 January 2004 £000	Recognised in income £000	Recognised in equity £000	31 December 2004 £000
Pensions	2,040	135	(270)	1,905
Other timing differences	248	30	243	521
	2,288	165	(27)	2,426

18 INVENTORIES

	THE GROUP	
	2005 £000	2004 £000
Raw materials and consumables	**21,902**	18,725
Work in progress	**11,049**	10,739
Finished goods and goods for resale	**31,265**	28,765
	64,216	58,229

19 OTHER CURRENT ASSETS

	THE GROUP		PARENT COMPANY	
	2005 £000	2004 £000	**2005 £000**	2004 £000
Other receivables	**3,678**	3,448	**145**	174
Prepayments and accrued income	**3,483**	3,635	**341**	227
Taxation recoverable	**1,527**	1,305	**-**	-
	8,688	8,388	**486**	401

NOTES TO THE ACCOUNTS *(continued)*

20 TRADE AND OTHER PAYABLES

	THE GROUP		PARENT COMPANY	
	2005 £000	2004 £000	**2005 £000**	2004 £000
Trade payables	**17,295**	17,105	**-**	-
Amounts owed to subsidiaries	**-**	-	**312**	298
Bills of exchange payable	**1,043**	988	**-**	-
Social security	**2,789**	2,689	**-**	-
Other creditors	**10,230**	8,925	**734**	976
Accruals	**15,486**	13,722	**862**	673
	46,843	43,429	**1,908**	1,947

21 CURRENT TAX PAYABLE

	THE GROUP		PARENT COMPANY	
	2005 £000	2004 £000	**2005 £000**	2004 £000
UK Corporation tax	**1,523**	1,963	**689**	355
Non UK tax payable	**5,803**	4,825	**-**	-
	7,326	6,788	**689**	355

22 OBLIGATIONS UNDER FINANCE LEASES

	THE GROUP			
	Minimum lease payments		Present value lease payments	
	2005 £000	2004 £000	**2005 £000**	2004 £000
Amount payable				
Within 1 year	**136**	384	**126**	356
1-5 years inclusive	**115**	219	**106**	203
After 5 years	**197**	244	**182**	226
	448	847	**414**	785
Add future finance charges			**34**	62
Minimum lease payments	**448**	847	**448**	847
Less: Due for settlement in <1 year			**126**	356
Due for settlement in >1 year			**322**	491

23 PROVISIONS

	THE GROUP	
	Warranty and other provisions	
	2005 £000	2004 £000
Provisions at 1st January	**644**	989
Exchange adjustments	**(11)**	-
	633	989
Charge for the year	**114**	-
Utilised during the year	**-**	(345)
Provisions at 31st December	**747**	644

24 CALLED UP SHARE CAPITAL

	THE GROUP		PARENT COMPANY	
	2005	2004	**2005**	2004
	£000	£000	**£000**	£000
Ordinary shares of 25p each:				
Authorised 120,000,000	**30,000**	30,000	**30,000**	30,000
Allotted, called up and fully paid 76,951,907	**19,238**	18,800	**19,238**	18,800

164,854 ordinary shares, having an aggregate nominal value of £41,214, were issued pursuant to the Spirax-Sarco Engineering plc Employee Share Ownership Plan on 6th October 2005 for a consideration of £987,475 received by the Company. 19,197 ordinary shares, having an aggregate nominal value of £4,799, were issued pursuant to the Spirax-Sarco Engineering plc Employee Share Ownership Plan in lieu of dividends of £143,589. 1,566,645 ordinary shares, having an aggregate nominal value of £391,661, were issued during the year pursuant to the Spirax-Sarco Engineering Share Option Schemes for a consideration of £7,437,018 received by the Company.

Directors and 110 other senior employees and former employees of the Group have been granted options to purchase 1,787,455 ordinary shares with an aggregate nominal value of £446,864. (Note 29).

25 SHARE CAPITAL AND RESERVES

THE GROUP

	Share capital £000	Share premium account £000	Translation reserve £000	Cash flow hedge reserve £000	Capital redemption reserve £000	Retained earnings £000	Total parent equity £000
Balance at 1st January 2004	18,690	35,996	-	-	1,832	87,292	143,810
Total recognised income and expense	-	-	(1,133)	-	-	35,243	34,110
Dividends paid	-	-	-	-	-	(15,289)	(15,289)
Equity settled share plans net of tax	-	-	-	-	-	711	711
Proceeds from issue of share capital	110	2,028	-	-	-	-	2,138
Balance at 31st December 2004	18,800	38,024	(1,133)	-	1,832	107,957	165,480

	Share capital £000	Share premium account £000	Translation reserve £000	Cash flow hedge reserve £000	Capital redemption reserve £000	Retained earnings £000	Total parent equity £000
Balance at 1st January 2005	18,800	38,024	(1,133)	-	1,832	107,957	165,480
Adjustment in respect of adoption of IAS32 and IAS39 on 1st January 2005	-	-	-	(58)	-	-	(58)
Total recognised income and expense	-	-	6,907	6	-	32,004	38,917
Dividends paid	-	-	-	-	-	(16,684)	(16,684)
Equity settled share plans net of tax	-	-	-	-	-	1,395	1,395
Proceeds from issue of share capital	438	8,130	-	-	-	-	8,568
Balance at 31st December 2005	**19,238**	**46,154**	**5,774**	**(52)**	**1,832**	**124,672**	**197,618**

PARENT COMPANY

	Share capital £000	Share premium account £000	Translation reserve £000	Cash flow hedge reserve £000	Capital redemption reserve £000	Retained earnings £000	Total parent equity £000
Balance at 1st January 2004	18,690	35,996	-	-	1,832	34,043	90,561
Total recognised income and expense	-	-	-	-	-	24,262	24,262
Dividends paid	-	-	-	-	-	(15,289)	(15,289)
Equity settled share plans net of tax	-	-	-	-	-	343	343
Proceeds from issue of share capital	110	2,028	-	-	-	-	2,138
Balance at 31st December 2004	18,800	38,024	-	-	1,832	43,359	102,015

NOTES TO THE ACCOUNTS *(continued)*

25 SHARE CAPITAL AND RESERVES *(continued)*

	Share capital £000	Share premium account £000	Translation reserve £000	Cash flow hedge reserve £000	Capital redemption reserve £000	Retained earnings £000	Total parent equity £000
Balance at 1st January 2005	18,800	38,024	-	-	1,832	43,359	102,015
Total recognised income and expense	-	-	-	-	-	23,453	23,453
Dividends paid	-	-	-	-	-	(16,684)	(16,684)
Equity settled share plans net of tax	-	-	-	-	-	276	276
Proceeds from issue of share capital	438	8,130	-	-	-	-	8,568
Balance at 31st December 2005	**19,238**	**46,154**	**-**	**-**	**1,832**	**50,404**	**117,628**

26 RETURN ON CAPITAL EMPLOYED

	THE GROUP	
	2005 £000	2004 £000
Capital employed		
Property, plant and equipment	**85,752**	83,514
Prepayments	**396**	345
Inventories	**64,216**	58,229
Trade receivables	**83,303**	76,021
Other current assets	**8,688**	8,388
Trade and other payables	**(46,843)**	(43,429)
Current tax payable	**(7,326)**	(6,788)
Capital employed	**188,186**	176,280
Average capital employed	**182,233**	176,303
Operating profit	**55,170**	47,956
Acquisition intangibles amortisation	**175**	-
	55,345	47,956
Return on capital employed	**30.4%**	27.2%

27 CAPITAL COMMITMENTS

	THE GROUP		PARENT COMPANY	
	2005 £000	2004 £000	**2005 £000**	2004 £000
Capital expenditure contracted for but not provided	**2,004**	2,438	**-**	-

28 OPERATING LEASE OBLIGATIONS

	THE GROUP	
	2005 £000	2004 £000
Commitments under non-cancellable leases due as follows:		
Within 1 year	**1,207**	1,322
1-5 years inclusive	**2,440**	2,363
After 5 years	**529**	652
	4,176	4,337

29 EMPLOYEE BENEFITS
Pension plans - The Group

The Group is accounting for pension costs in accordance with International Accounting Standard 19.

The disclosures shown here are in respect of the Group's Defined Benefit Obligations. Other plans operated by the Group were either Defined Contribution plans or were deemed immaterial for the purposes of IAS 19 reporting.

The total expense relating to the Group's Defined Contribution pension plans in the current year was £2,636,000 (2004 £2,396,000).

Of the Defined Benefit plans, the plans in the UK and USA hold most of the liability. The post-retirement mortality assumptions in respect of these plans may therefore be considered material. The UK schemes assume that post-retirement mortality follows the PMA80C00 table with a two year setback. The figures disclosed assume that a male member will survive 18 years from age 65 and a female member for 22 years. These figures reflect a detailed review of recent mortality experience amongst the membership carried out by the Actuary at the last valuation of the UK schemes. The USA schemes use the 1979 George B. Buck mortality table. These assumptions will be regularly reviewed in light of scheme specific experience and more widely available statistics.

The financial assumptions used at 31st December were:

	Assumptions weighted by value of liabilities % per annum			
	UK pensions		Overseas pensions and medical	
	2005	2004	**2005**	2004
Rate of increase in salaries	**3.7**	3.6	**3.1**	3.2
Rate of increase in pensions	**2.7**	2.6	**1.8**	1.8
Rate of price inflation	**2.7**	2.6	**2.3**	2.2
Discount rate	**4.9**	5.4	**5.1**	5.4
Medical trend rate	**-**	-	**5.0**	5.0

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions, which, due to the timescale covered, may not necessarily be borne out in practice.

	Assumptions weighted by value of assets % per annum			
	UK pensions		Overseas pensions and medical	
	2005	2004	**2005**	2004
Expected rate of return on assets (weighted average)	**7.2**	7.5	**7.0**	7.5
Equities	**7.9**	8.1	**8.3**	8.5
Bonds	**4.5**	5.0	**5.1**	5.4
Other	**5.4**	5.9	**4.7**	3.9

The market value of the schemes' assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, at 31st December 2005 were:

	UK pensions		Overseas pensions and medical		Total	
	2005 £000	2004 £000	**2005 £000**	2004 £000	**2005 £000**	2004 £000
Equities	**115,700**	97,300	**11,997**	9,633	**127,697**	106,933
Bonds	**24,800**	19,200	**4,583**	3,827	**29,383**	23,027
Other	**11,800**	7,500	**2,468**	1,907	**14,268**	9,407
Total market value in aggregate	**152,300**	124,000	**19,048**	15,367	**171,348**	139,367

The actual return on plan assets was £24.9 million (2004 £13.0 million).

29 EMPLOYEE BENEFITS *(continued)*

The effect of an increase of one percentage point and the effect of a decrease of one percentage point in the assumed medical trend rates is as follows:

	Overseas		Total	
	1% increase £000	1% decrease £000	1% increase £000	1% decrease £000
Aggregate of service cost & interest cost components of post-retirement medical plans	3	(3)	3	(3)
Accumulated post-employment benefit obligation for medical costs	21	(18)	21	(18)

The amounts recognised in the consolidated balance sheet are determined as follows:

	UK pensions		Overseas pensions and medical		Total	
	2005 £000	2004 £000	**2005 £000**	2004 £000	**2005 £000**	2004 £000
Fair value of schemes' assets	**152,300**	124,000	**19,048**	15,367	**171,348**	139,367
Present value of funded schemes' liabilities	**(178,600)**	(148,611)	**(25,640)**	(20,001)	**(204,240)**	(168,612)
(Deficit) in the funded schemes	**(26,300)**	(24,611)	**(6,592)**	(4,634)	**(32,892)**	(29,245)
Present value of unfunded schemes' liabilities	**-**	-	**(12,915)**	(12,090)	**(12,915)**	(12,090)
Retirement benefit liability recognised in the balance sheet	**(26,300)**	(24,611)	**(19,507)**	(16,724)	**(45,807)**	(41,335)
Related deferred tax asset	**7,890**	7,350	**6,523**	5,973	**14,413**	13,323
Net pension liability	**(18,410)**	(17,261)	**(12,984)**	(10,751)	**(31,394)**	(28,012)

The movements in the Defined Benefit Obligation ("DBO") recognised in the balance sheet during the year were:

	UK pensions		Overseas pensions and medical		Total	
	2005 £000	2004 £000	**2005 £000**	2004 £000	**2005 £000**	2004 £000
Defined benefit obligation at beginning of year	**(148,611)**	(140,000)	**(32,091)**	(31,194)	**(180,702)**	(171,194)
Current service cost	**(5,700)**	(6,000)	**(1,527)**	(1,383)	**(7,227)**	(7,383)
Past service cost	**-**	-	**124**	(30)	**124**	(30)
Interest cost	**(8,000)**	(7,400)	**(1,827)**	(1,675)	**(9,827)**	(9,075)
Contributions by members	**(100)**	-	**(39)**	-	**(139)**	-
Change in assumptions on DBO	**(20,700)**	(6,000)	**(2,789)**	(1,118)	**(23,489)**	(7,118)
Actual benefit payments	**4,100**	4,200	**1,846**	1,652	**5,946**	5,852
Settlement, curtailment	**-**	-	**-**	792	**-**	792
Experience gain	**411**	6,589	**-**	-	**411**	6,589
Currency (loss)/gain	**-**	-	**(2,252)**	865	**(2,252)**	865
Defined benefit obligation at end of year	**(178,600)**	(148,611)	**(38,555)**	(32,091)	**(217,155)**	(180,702)

The movements in the fair value of plan assets during the year were:

	UK pensions		Overseas pensions and medical		Total	
	2005	2004	**2005**	2004	**2005**	2004
	£000	£000	**£000**	£000	**£000**	£000
Value of assets at beginning of year	**124,000**	110,700	**15,367**	14,716	**139,367**	125,416
Expected return on assets	**9,300**	8,300	**1,284**	1,074	**10,584**	9,374
Actuarial gain/(loss)	**14,100**	3,700	**230**	(59)	**14,330**	3,641
Contributions paid by employer	**8,900**	5,500	**2,134**	2,424	**11,034**	7,924
Contributions paid by members	**100**	-	**39**	30	**139**	30
Actual benefit payments	**(4,100)**	(4,200)	**(1,846)**	(1,652)	**(5,946)**	(5,852)
Settlement, curtailment	**-**	-	**-**	(493)	**-**	(493)
Currency gain/(loss)	**-**	-	**1,840**	(673)	**1,840**	(673)
Value of assets at end of year	**152,300**	124,000	**19,048**	15,367	**171,348**	139,367

The expense recognised in the income statement was as follows:

	UK pensions		Overseas pensions and medical		Total	
	2005	2004	**2005**	2004	**2005**	2004
	£000	£000	**£000**	£000	**£000**	£000
Current service cost	**(5,700)**	(6,000)	**(1,468)**	(1,372)	**(7,168)**	(7,372)
Past service cost	**-**	-	**117**	-	**117**	-
Settlement, curtailment	**-**	-	**-**	279	**-**	279
Interest on schemes' liabilities	**(8,000)**	(7,400)	**(1,746)**	(1,688)	**(9,746)**	(9,088)
Expected return on schemes' assets	**9,300**	8,300	**1,209**	1,115	**10,509**	9,415
Total expense recognised in income statement	**(4,400)**	(5,100)	**(1,888)**	(1,666)	**(6,288)**	(6,766)

The expense is recognised in the following line items in the income statement:

	2005	2004
	£000	£000
Operating costs	**(7,051)**	(7,093)
Financial expenses	**(9,746)**	(9,088)
Financial income	**10,509**	9,415
Total expense recognised in income statement	**(6,288)**	(6,766)

Statement of recognised income and expense (SORIE)

	UK pensions		Overseas pensions and medical		Total	
	2005	2004	**2005**	2004	**2005**	2004
	£000	£000	**£000**	£000	**£000**	£000
Actuarial loss recognised in SORIE	**(6,300)**	4,400	**(2,674)**	(585)	**(8,974)**	3,815
Deferred tax on actuarial amount recognised in SORIE	**1,790**	(1,320)	**1,152**	434	**2,942**	(886)
Cumulative loss recognised in SORIE at beginning of year	**3,080**	-	**(151)**	-	**2,929**	-
Cumulative loss recognised in SORIE at end of year	**(1,430)**	3,080	**(1,673)**	(151)	**(3,103)**	2,929

Pension plans - Parent company

The parent company is accounting for pension costs in accordance with International Accounting Standard 19.

The disclosures shown here are in respect of the parent company's Defined Benefit Obligations. Other plans operated by the parent company were Defined Contribution plans.

The total expense relating to the parent company's Defined Contribution pension plans in the current year was £2,850 (2004 £2,742).

29 EMPLOYEE BENEFITS *(continued)*

The post-retirement mortality assumptions in respect of the parent company Defined Benefit Scheme follows the PMA80C00 table with a two year setback. The figures disclosed assume that a male member will survive 18 years from age 65 and a female member for 22 years. These figures reflect a detailed review of recent mortality experience amongst the membership carried out by the Actuary at the last valuation of the UK Scheme. These assumptions will be regularly reviewed in light of scheme specific experience and more widely available statistics.

The financial assumptions used at 31st December were:

	Assumptions weighted by value of liabilities % per annum	
		UK pensions
	2005	2004
Rate of increase in salaries	**3.7**	3.6
Rate of increase in pensions	**2.7**	2.6
Rate of price inflation	**2.7**	2.6
Discount rate	**4.9**	5.4

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions, which, due to the timescale covered, may not necessarily be borne out in practice.

	Assumptions weighted by value of liabilities % per annum	
		UK pensions
	2005	2004
Expected rate of return on assets (weighted average)	**7.2**	7.5
Equities	**7.9**	8.1
Bonds	**4.5**	5.0
Other	**5.4**	5.9

The market value of the schemes' assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, at 31st December 2005 were:

		UK pensions
	2005	2004
	£000	£000
Equities	**26,200**	22,200
Bonds	**5,700**	4,500
Other	**2,600**	1,600
Total market value in aggregate	**34,500**	28,300

The actual return on plan assets was £5.2 million (2004 £2.7 million).

The amounts recognised in the consolidated balance sheet are determined as follows:

		UK pensions
	2005	2004
	£000	£000
Fair value of schemes' assets	**34,500**	28,300
Present value of funded schemes' liabilities	**(40,300)**	(33,700)
Retirement benefit liability recognised in the balance sheet	**(5,800)**	(5,400)
Related deferred tax asset	**1,740**	1,620
Net pension liability	**(4,060)**	(3,780)

The movements in liability recognised in the balance sheet during the year were:

	UK pensions	
	2005	2004
	£000	£000
Defined benefit obligation at beginning of year	**(33,700)**	(32,200)
Current service cost	**(900)**	(900)
Interest cost	**(1,800)**	(1,700)
Change in assumptions on DBO	**(3,700)**	(900)
Actual benefit payments	**1,200**	1,000
Experience gain	**(1,400)**	1,000
Defined benefit obligation at end of year	**(40,300)**	(33,700)

The movements in the fair value of plan assets during the year were:

	UK pensions	
	2005	2004
	£000	£000
Value of assets at beginning of year	**28,300**	25,400
Expected return on assets	**2,100**	1,900
Actuarial gain	**3,100**	800
Contributions paid by employer	**2,200**	1,200
Actual benefit payments	**(1,200)**	(1,000)
Value of assets at end of year	**34,500**	28,300

The expense recognised in the income statement was as follows:

	UK pensions	
	2005	2004
	£000	£000
Current service cost	**(900)**	(900)
Interest on schemes' liabilities	**(1,800)**	(1,700)
Expected return on schemes' assets	**2,100**	1,900
Total expense recognised in income statement	**(600)**	(700)

Statement of recognised income and expense (SORIE)

	UK pensions	
	2005	2004
	£000	£000
Actuarial loss recognised in SORIE	**(1,935)**	919
Deferred tax on actuarial amount recognised in SORIE	**600**	(270)
Cumulative loss recognised in SORIE at beginning of year	**649**	-
Cumulative loss recognised in SORIE at end of year	**(686)**	649

Share-based payments - The Group

Disclosures of the share-based payments offered to employees are set out below. More detail on each scheme is given in the directors' remuneration report on pages 28 to 35. The charge to the income statement in respect of share-based payments is made up as follows.

	2005	2004
	£000	£000
Share Option Scheme	**374**	301
Performance Share Plan	**139**	-
Employee Share Ownership Plan	**525**	502
Total expense recognised in income statement	**1,038**	803

NOTES TO THE ACCOUNTS *(continued)*

29 EMPLOYEE BENEFITS *(continued)*

a) Share Option Scheme

The Group operates equity settled share option schemes for employees. Awards are determined by the Remuneration Committee whose objective is to align the interests of employees with those of shareholders by giving an incentive linked to added shareholder value. Options are subject to performance conditions, which if met make the options exercisable between the third and tenth anniversary of the date of grant. For options granted from 1995 to 2001 the performance condition is an increase in EPS of more than 6% greater than the increase in the UK retail prices index over a consecutive three year period between grant and exercise. From and including the 2002 options the increase in EPS was revised to 9% greater than the increase in the UK retail price index over a three year consecutive period and from 2005 the performance condition needs to be met over the three year period from 1st January prior to the date of the grant. If the condition is not met at the end of the three year period the option will lapse.

Under the transitional requirements of IFRS 2 all awards made after 7th November 2002 need to be subject to the recognition and measurement principles in IFRS 2. Applying IFRS 2 to earlier awards is optional, but we have chosen to adopt IFRS 2 from 1st July 2001 to give greater clarity and comparability between accounting periods. The share options granted during 2005 have been measured by Watson Wyatt LLP, Actuaries and Consultants, using the Present Economic Value ("PEV") valuation methodology. The relevant disclosures in respect of the 2005 share option scheme grants and for the other grants made after 1st July 2001 are set out below.

	2002 Grant	2003 Grant	2004 Grant	**2005 Grant**
Grant date	22nd March	14th March	25th March	**21st April**
Exercise price / share price at grant date	436.0p	394.5p	541.9p	**686.0p**
Number of employees	74	70	74	**66**
Shares under option	363,500	411,000	410,500	**359,600**
Vesting period	3 years	3 years	3 years	**3 years**
Expected volatility	25%	25%	25%	**20%**
Risk-free interest rate	4.2%	4.2%	4.6%	**4.6%**
Expected dividend yield	4.5%	4.5%	4.5%	**4.0%**
Fair value	80.0p	65.0p	88.4p	**121.5p**

The number and weighted average exercise prices of share options are as follows:

Option (exercise price)	Outstanding at start of year	Granted during year	Exercised during year	Lapsed during year	Outstanding at end of year
1996 grant (739p)	241,500		(96,000)	(10,000)	135,500
1997 grant (669p)	225,500		(122,000)		103,500
1998 grant (420p)	211,000		(191,500)		19,500
1999 grant (525p)	242,500		(161,595)		80,905
2000 grant (319.2p)	328,000		(249,050)		78,950
2001 grant (397.7p)	413,500		(316,500)		97,000
2002 grant (436p)	346,000		(235,000)		111,000
2003 grant (394.5p)	411,000		(5,000)	(9,000)	397,000
2004 grant (541.9p)	410,500			(6,000)	404,500
2005 grant (686p)		359,600			359,600
	2,829,500	**359,600**	**(1,376,645)**	**(25,000)**	**1,787,455**
Weighted average exercise price	£4.77	£6.86	£4.56	£5.68	£5.34
Weighted average contractual life remaining					6.54 years

Performance conditions in respect of all exercisable shares have been met.

b) Performance Share Plan

Following shareholder approval of the Performance Share Plan at the annual general meeting on 12th May 2005 awards over shares were made to executive directors.

Awards under the Performance Share Plan take the form of contingent rights to acquire shares, subject to the satisfaction of a performance target. To the extent that they vest, awards may be satisfied in cash or in shares. The performance target in 2005 is based on the Company's total shareholder return ("TSR") relative to the TSR of other companies included in the FTSE All-Share Engineering and Machinery Sector over a three year performance period where awards will vest on a sliding scale. All shares within an award will vest if the Company's TSR is at or above the upper quartile. 25% will vest if the TSR is at the median and the number of shares that will vest will be calculated pro-rata on a straight line basis between 25% and 100% if the Company's TSR falls between the median and the upper quartile. No shares will vest if the Company's TSR is below the median.

Shares awarded under the Performance Share Plan in 2005 have been valued by Towers Perrin using the Monte Carlo simulation valuation methodology. The relevant disclosures in respect of the Performance Share Plan grant in 2005 are set out below.

	2005 Grant
Grant date	**20th May**
Share price at grant date	**708.5p**
Number of employees	**7**
Shares under scheme	**115,168**
Vesting period	**3 years**
Probability of vesting	**51%**
Probability of ceasing employment before vesting	**zero**
Fair value	**361.3p**

c) Employee Share Ownership Plan

UK employees are eligible to participate in the Employee Share Ownership Plan ("ESOP"). The aim of the Plan is to encourage increased shareholding in the Company by all UK employees and so there are no performance conditions. Employees are invited to join the Plan when an offer is made each year. Individuals save for 12 months during the accumulation period and subscribe for shares at the lower of the price at the beginning and the end of the accumulation period under Inland Revenue rules. The Company provides a matching share for each share purchased by the individual.

Shares issued under the Employee Share Ownership Scheme in 2005 have been measured by Watson Wyatt LLP, Actuaries and Consultants, using the Present Economic Value ("PEV") valuation methodology. The relevant disclosures in respect of the 2005 Employee Share Ownership Plan and the other Plans granted since the early adoption of IFRS 2 on 1st July 2001 are set out below.

	2001 ESOP	2002 ESOP	2003 ESOP	2004 ESOP	**2005* ESOP**
Grant date	1st October	1st October	1st October	1st October	**1st October**
Exercise price	320.5p	358.3p	548.2p	599.0p	**785.7p**
Number of employees	783	724	761	810	**869**
Shares under scheme	122,497	119,038	84,993	86,241	**73,169**
Vesting period	3 years	3 years	3 years	3 years	**3 years**
Expected volatility	25.0%	25.0%	25.0%	20.0%	**20.0%**
Risk free interest rate	4.0%	4.0%	4.0%	4.6%	**4.3%**
Expected dividend yield	4.5%	4.5%	4.5%	4.0%	**3.0%**
Fair value	352.0p	391.0p	574.0p	622.0p	**828.0p**

* The accumulation period for the 2005 ESOP ends in September 2006, therefore some figures are projections

29 EMPLOYEE BENEFITS *(continued)*

Share-based payments - Parent Company

Disclosures of the share-based payments offered to employees of the parent company are set out below. The description and operation of each scheme is the same as outlined in the Group disclosure set out above.

a) Share Option Scheme

The equity settled share options issued to employees of the parent company are charged in the parent company's income statement. The relevant disclosures in respect of the 2005 share option scheme grants and for the other grants made after 1st July 2001 are set out below.

	2002 Grant	2003 Grant	2004 Grant	**2005 Grant**
Grant date	22nd March	14th March	25th March	**21st April**
Exercise price / share price at grant date	436.0p	394.5p	541.9p	**686.0p**
Number of employees	7	7	8	**2**
Shares under option	139,000	133,000	137,753	**8,400**
Vesting period	3 years	3 years	3 years	**3 years**
Expected volatility	25%	25%	25%	**20%**
Risk-free interest rate	4.2%	4.2%	4.6%	**4.6%**
Expected dividend yield	4.5%	4.5%	4.5%	**4.0%**
Fair value	80.0p	65.0p	88.4p	**121.5p**

The number and weighted average exercise prices of share options are as follows:

Option (exercise price)	Outstanding at start of year	Granted during year	Exercised during year	Lapsed during year	Outstanding at end of year
1996 grant (739p)	72,500		(42,500)		30,000
1997 grant (669p)	75,000		(45,000)		30,000
1998 grant (420p)	117,500		(117,500)		-
1999 grant (525p)	102,500		(62,500)		40,000
2000 grant (319.2p)	107,500		(82,500)		25,000
2001 grant (397.7p)	143,500		(108,500)		35,000
2002 grant (436p)	121,500		(74,000)		47,500
2003 grant (394.5p)	133,000				133,000
2004 grant (541.9p)	137,753				137,753
2005 grant (686p)		8,400			8,400
	1,010,753	**8,400**	**(532,500)**	**-**	**486,653**
Weighted average exercise price	£4.73	£6.86	£4.61		£4.91
Weighted average contractual life remaining					6.12 years

Performance conditions in respect of all exercisable shares have been met.

b) Performance Share Plan

The relevant disclosures in respect of the Performance Share Plan grant in 2005 are set out below.

	2005 Grant
Grant date	**20th May**
Share price at grant date	**708.5p**
Number of employees	**7**
Shares under scheme	**115,168**
Vesting period	**3 years**
Probability of vesting	**51%**
Probability of ceasing employment before vesting	**zero**
Fair value	**361.3p**

30 ANALYSIS OF CHANGES IN NET CASH

	THE GROUP			
	At 1st January 2005 £000	Cash flow £000	Exchange movement £000	**At 31st December 2005 £000**
Current portion of long term borrowings	(8,183)			**(25,010)**
Non-current portion of long term borrowings	(34,432)			**(7,540)**
Short term borrowings	-			**(1,498)**
Total borrowings	(42,615)			**(34,048)**
Comprising:				
Borrowings	(41,768)	7,728	440	**(33,600)**
Finance Leases	(847)	372	27	**(448)**
	(42,615)	8,100	467	**(34,048)**
Cash and cash equivalents	48,756	7,407	766	**56,929**
Bank overdrafts	(4,842)	1,278	(272)	**(3,836)**
Net cash and cash equivalents	43,914	8,685	494	**53,093**
Net cash	1,299	16,785	961	**19,045**

31 RELATED PARTY TRANSACTIONS

THE GROUP	**2005 £000**	2004 £000
Sales to associated companies	**915**	881
Dividends from associated companies	**351**	71
Amounts due from associated companies at 31st December	**248**	182
PARENT COMPANY		
Dividends received from subsidiaries	**25,309**	23,616
Loans and amounts due from subsidiaries at 31st December	**36,247**	33,665
Amounts due to subsidiaries at 31st December	**955**	941

The transactions above were priced on an arm's length basis.

32 PURCHASE OF BUSINESSES

2005

	Mitech South Africa [1]			EMCO Flow Systems USA [2]			Other including Eirdata [3]	Total
	Book value £000	Fair value adjustments £000	Fair value £000	Book value £000	Fair value adjustments £000	Fair value £000	Fair value £000	Fair value £000
Fixed assets								
Property, plant and equipment	57	-	57	28	-	28	11	96
Intangibles	-	904	904	-	693	693	130	1,727
	57	904	961	28	693	721	141	1,823
Current assets								
Inventories	288	(43)	245	11	-	11	-	256
Trade receivables	820	(41)	779	355	-	355	50	1,184
Other receivables	563	-	563	-	-	-	-	563
Cash	210	-	210	-	-	-	64	274
	1,881	(84)	1,797	366	-	366	114	2,277
Total assets	1,938	820	2,758	394	693	1,087	255	4,100
Deferred tax liabilities	-	271	271	-	-	-	-	271
Current liabilities								
Trade payables	475	-	475	26	-	26	5	506
Tax	322	-	322	-	-	-	2	324
Other payables	-	-	-	109	-	109	12	121
	797	-	797	135	-	135	19	951
Total liabilities	797	271	1,068	135	-	135	19	1,222
Total net assets	1,141	549	1,690	259	693	952	236	2,878
Goodwill			1,175			1,869	195	3,239
Purchase consideration			**2,865**			**2,821**	**431**	**6,117**
Satisfied by Cash paid			2,636			2,616	153	5,405
Deferred consideration			100			-	236	336
Expenses			129			205	42	376
			2,865			**2,821**	**431**	**6,117**

Analysis of net flow of cash and cash equivalents in respect of purchase of subsidiaries	
Cash consideration	5,223
Expenses	182
Cash acquired	(199)
Deferred consideration on Eirdata Environmental Services Ltd acquisition	660
Net cash outflow	**5,866**

1 The acquisition of Mitech, comprising Actuators and Controls (Pty) Limited and Proportional Control Technology (Pty) Limited, in South Africa from their common shareholders was completed on 1st June 2005. The acquisition was accounted for by the acquisition method of accounting. Consideration of £2,636,000 was paid on completion. The book value of intangibles net of tax, inventories and trade receivables has been adjusted to reflect Spirax Sarco's accounting policies in order to arrive at their fair value.

The revenue and profits after tax of the business acquired included in these accounts are £2,481,000 and £223,000 respectively which equate to £4,253,000 and £382,000 respectively on an annualised basis.

2 The acquisition of the assets and business of EMCO Flow Systems of Longmont, Colorado, USA from Advanced Energy Industries, Inc., USA was completed on 24th June 2005. The acquisition was accounted for by the acquisition method of accounting. Consideration of £2,616,000 was paid on completion. The book value of intangibles has been adjusted to reflect Spirax Sarco's accounting policies in order to arrive at their fair value.

The business acquired has been absorbed into the business of Spirax Sarco, Inc. and therefore its results since acquisition are not available.

3 Following the acquisition of 80% of Eirdata Environmental Services Limited in Eire in 2004, the remaining 20% was acquired on 1st October 2005. Consideration of £153,000 was paid on completion. No fair value adjustments are required other than for intangible assets with a fair value of £130,000.

2004

		Eirdata Environmental Services Limited Eire			
		Book value £000	Accounting policy adjustments £000	Fair value adjustments £000	Fair value £000
Fixed assets					
	Property, plant and equipment	49	-	-	49
	Intangibles	-	-	538	538
		49	-	538	587
Current assets	Stock	29	-	-	29
	Trade debtors	212	(11)	-	201
	Other debtors	34	-	-	34
	Cash	208	-	-	208
		483	(11)	-	472
Total assets		532	(11)	538	1,059
Current liabilities	Trade creditors	50	-	-	50
	Tax	22	-	-	22
	Other creditors	68	-	-	68
		140	-	-	140
Total net assets		392	(11)	538	919
Goodwill					639
Purchase consideration					**1,558**
Satisfied by	Cash paid				446
	Deferred consideration				976
	Expenses				136
					1,558

Analysis of net flow of cash and cash equivalents in respect of purchase of subsidiaries	
Cash consideration	446
Expenses	136
Cash acquired	(249)
Deferred consideration on Ampe S.r.l. and M&M International S.r.l. acquisitions	470
Net cash outflow	**803**

The acquisition of 80% of Eirdata Environmental Services Limited in Eire from its shareholders was completed on 1st October 2004. The acquisition was accounted for by the acquisition method of accounting. Consideration of £446,000 was paid on completion. The book value of trade debtors has been adjusted to reflect Spirax Sarco's accounting policies in order to arrive at their fair value.

The total profits after tax of the business acquired for its financial year ended 29th February 2004 was £145,000. The total profits after tax of the business acquired in the seven months in 2004 prior to acquisition on 1st October 2004 was £143,000.

NOTES TO THE ACCOUNTS *(continued)*

33 DERIVATIVES AND OTHER FINANCIAL INSTRUMENTS

The Group does not enter into significant derivative transactions. The Group's principal financial instruments comprise bank loans, guaranteed senior notes, cash and short term deposits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial instruments such as trade debtors and trade creditors, which arise directly from its operations. It is, and has been throughout the period under review, the Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk and foreign currency risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below. These policies have remained fundamentally unchanged since the beginning of 2000.

Interest rate risk

The Group borrows in desired currencies at both fixed and floating rates of interest as appropriate to the purposes of the borrowing depending on which gives best value.

Liquidity risk

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of overdrafts, loans and finance leases as appropriate.

Foreign currency risk

The Group has operations around the world and therefore its balance sheet can be affected significantly by movements in the rate of exchange between sterling and various other currencies particularly the US dollar and euro. The Group seeks to mitigate the effect of this structural currency exposure by borrowing in these currencies where appropriate while maintaining a low cost of debt.

The Group also has transactional currency exposures principally as a result of trading between Group companies. Such exposures arise from sales or purchases by an operating unit in currencies other than the unit's functional currency. Net cash flows between any two currencies of less than £1m per annum would not usually be considered sufficiently material to warrant forward cover. Forward cover is not taken out more than twelve months in advance or for more than 80% of the forecast exposure.

2005

Interest rate risk profile of financial liabilities

The interest rate profile of the financial liabilities of the Group as at 31st December was as follows:

	Total £000	Fixed rate financial liabilities £000	Floating rate financial liabilities £000	Financial liabilities on which no interest is paid £000
Euro	37,593	214	25,525	11,854
US dollar	5,968	2,325	1,837	1,806
Other	21,848	1,888	6,095	13,865
	65,409	**4,427**	**33,457**	**27,525**

In respect of fixed rate financial liabilities the interest rate for euro financial liabilities is 4.4% fixed for 0.5 years. The interest rate for US dollar financial liabilities is 6.7% fixed for 0.1 years.

The benchmark rates for the floating rate financial liabilities are as follows:

Japanese yen, US dollar	LIBOR
Euro	LIBOR/EURIBOR

Interest rate risk profile of financial assets

The interest rate profile of the financial assets of the Group as at 31st December was as follows:

	Total £000	Floating rate financial assets £000	Financial assets on which no interest is earned £000
Sterling	50,797	39,625	11,172
Other	93,113	12,303	80,810
	143,910	**51,928**	**91,982**

Financial assets on which no interest is earned comprise trade and other receivables and cash at bank and in hand.

Floating rate financial assets comprise cash placed on money market deposit mainly at call and three month rates. The average rate of interest received on sterling deposits during the year was 4.7%.

Currency exposures
As explained above, the Group's objectives in managing the currency exposures arising from its net investment overseas (in other words, its structural currency exposures) are to maintain a low cost of debt while partially hedging against currency depreciation. All gains and losses arising from these structural currency exposures are dealt with in the statement of total recognised income and expenditure.

Transactional (or non-structural) exposures give rise to net currency gains and losses that are recognised in the income statement. Such exposures include the monetary assets and monetary liabilities in the Group balance sheet that are not denominated in the operating (or 'functional') currency of the operating unit involved. At 31st December the currency exposures in respect of the euro was a net monetary asset of £206,000 and in respect of the US dollar a net monetary asset of £783,000.

At 31st December the percentage of debt to net assets, excluding debt was 50% for the euro and 19% for the US dollar.

Maturity of financial liabilities
The Group's financial liabilities at 31st December reprice (or mature if earlier) in the following periods:

	Trade and other payables £000	Overdrafts £000	Short term borrowings £000	Finance leases £000	Long term borrowings £000	Total £000
In six months or less, or on demand	27,525	-	-	68	30,621	58,214
In more than six months but no more than twelve	-	3,836	1,498	68	1,481	6,883
In more than one year but no more than two	-	-	-	37	-	37
In more than two years but no more than three	-	-	-	39	-	39
In more than three years but no more than four	-	-	-	39	-	39
In more than four years but no more than five	-	-	-	42	-	42
In more than five years	-	-	-	155	-	155
	27,525	3,836	1,498	448	32,102	65,409

Cash flow hedge
At 31st December the Group had contracts outstanding to purchase £1,050,000 with South Korean Won.

Borrowing Facilities
The Group has various borrowing facilities available to it. The undrawn committed facilities available at 31st December in respect of which all conditions precedent had been met at that date were as follows:

	£000
Expiring in one year or less	**19,241**

Fair values of financial assets and financial liabilities
Fair values of financial assets and liabilities at 31st December are not materially different from book values due to their size or the fact that they were at short term rates of interest. Fair values have been assessed as follows:

Derivatives
Forward exchange contracts are marked to market using year end exchange rates.

Interest-bearing loans and borrowings
Fair value is calculated based on discounted expected future principal and interest cash flows.

Finance lease liabilities
The fair value is estimated as the present value of future cash flows, discounted at market interest rates for homogeneous lease agreements. The estimated fair values reflect change in interest rates.

Trade and other receivables / payables
For receivables / payables with a remaining life of less than one year, the notional amount is deemed to reflect the fair value.

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

At 31st December, it is estimated that a general increase of one percentage point in interest rates in respect of financial assets would increase the Group's profit before tax by approximately £500,000.

Since the year end loans totalling £17,736,000 have been repaid. Consequently, in respect of financial liabilities, the Group is not significantly at risk from increases in interest rates.

It is estimated that a general increase of one percentage point in the value of sterling against other foreign currencies would have decreased the Group's profit before tax by approximately £500,000 for the year ended 31st December. The forward exchange contracts have been included in this calculation.

NOTES TO THE ACCOUNTS *(continued)*

33 DERIVATIVES AND OTHER FINANCIAL INSTRUMENTS *(continued)*
2004
The disclosures below, which are under UK GAAP exclude short term debtors and creditors.

Interest rate risk profile of financial liabilities
The interest rate profile of the financial liabilities of the Group as at 31st December was as follows:

	Total £000	Fixed rate financial liabilities £000	Floating rate financial liabilities £000
Euro	29,420	1,117	28,303
US dollar	5,994	4,162	1,832
Other	12,043	1,750	10,293
	47,457	7,029	40,428

In respect of fixed rate financial liabilities the interest rate for euro financial liabilities is 4.4% fixed for 1.5 years. The interest rate for US dollar financial liabilities is 6.7% fixed for 1.1 years.

The benchmark rates for the floating rate financial liabilities are as follows:

Japanese yen } US dollar }	LIBOR
Euro	LIBOR/EURIBOR

Interest rate risk profile of financial assets
The interest rate profile of the financial assets of the Group as at 31st December was as follows:

	Total £000	Floating rate financial assets £000	Financial assets on which no interest is earned £000
Sterling	28,182	28,042	140
Other	20,574	16,026	4,548
	48,756	44,068	4,688

Financial assets on which no interest is earned comprise cash at bank and in hand.

Floating rate financial assets comprise cash placed on money market deposit mainly at call and three month rates.

Currency exposures
As explained above, the Group's objectives in managing the currency exposures arising from its net investment overseas (in other words, its structural currency exposures) are to maintain a low cost of debt while partially hedging against currency depreciation. All gains and losses arising from these structural currency exposures are dealt with in the statement of total recognised income and expenditure.

Transactional (or non-structural) exposures give rise to net currency gains and losses that are recognised in the income statement. Such exposures include the monetary assets and monetary liabilities in the Group balance sheet that are not denominated in the operating (or 'functional') currency of the operating unit involved. At 31st December the currency exposures in respect of the euro was a net monetary asset of £32,000 and in respect of the US dollar a net monetary asset of £730,000.

At 31st December the percentage of debt to net assets, excluding debt was 50% for the euro and 28% for the US dollar.

Maturity of financial liabilities
The maturity profile of the Group's financial liabilities at 31st December was as follows:

	£000
In one year or less, or on demand	13,025
In more than one year but no more than two	11,511
In more than two years but no more than five	22,631
In more than five years	290
	47,457

Borrowing Facilities
The Group has various borrowing facilities available to it. The undrawn committed facilities available at 31st December in respect of which all conditions precedent had been met at that date were as follows:

	£000
Expiring in one year or less	16,079

Fair values of financial assets and financial liabilities
Fair values of financial assets and liabilities at 31st December are not considered to be materially different from book values due to their size or the fact that they were at short term rates of interest.

34 EXPLANATION OF TRANSITION TO IFRS

The Group

As described in note 1, the 2005 accounts have been prepared in accordance with the recognition and measurement criteria of International Financial Reporting Standards (IFRS). On 12th July 2005, the Group announced a comprehensive restatement of its 2004 results under IFRS. This announcement is available from the Company's web site at www.SpiraxSarcoEngineering.com or copies can be requested from the Company Secretary. Reconciliations of the Group's Income Statement, Balance Sheet and Cash Flow showing the effects of both reformat and restatement between UK GAAP and IFRS for 2004 figures are set out on the following pages. Details of the changes on transition (1st January 2004) are also shown. The principle restatement changes from the transition to IFRS are described below along with the effects on the 2004 figures.

Minorities (IAS 27 Consolidated financial statements)
Reassessing control in minority interests resulting in a change in the treatment of the Group's investments in India and Mexico on consolidation from subsidiary companies to associate companies. More detail on associated companies is given in Note 1 on page 42 and Note 16 on page 52. Although there is a reduction in 2004 sales of £9.8 million and in pre-tax profit of £1.8 million, there is no change in EPS or net assets attributable to shareholders.

Pensions (IAS 19 Employee benefits)
Recognising the deficit on defined benefit pension schemes on the balance sheet and the higher income statement charge for pensions under IAS 19. More detail on defined benefit pension plans is given in Note 1 on page 44 and in Note 29 on pages 57 to 61. For the 2004 year £28.0 million of additional balance sheet net liabilities have been recognised and the income statement charge (before tax) increases by £0.7 million.

Share Schemes (IFRS 2 Share-based payments)
Recording the cost of share-based payments awarded to employees on a fair value basis. More detail on employee share plans and long term incentive plans is given in Note 1 on page 44 and in Note 29 on pages 61 to 63. The 2004 income statement charge (before tax) increases by £0.4 million.

Goodwill (IFRS 3 Business combinations)
Ceasing goodwill amortisation (subject to annual impairment testing). More detail on goodwill and annual impairment testing is given in Note 1 on pages 43 and 44 and in Note 13 on pages 50 and 51. The 2004 income statement reflects the reversal of the £0.7 million charge under UK GAAP.

Dividends (IAS 10 Events after the balance sheet date)
Not accruing a liability for dividends that have not been declared or approved at the balance sheet date. More detail on dividends paid in the year and arising in respect of the year is given in Note 11 on page 49. Shareholders funds increase by £11.4 million at 31st December 2004.

Research and development (IAS 38 Intangible assets)
Capitalisation of the development element of R&D expenditure under certain circumstances. More detail on research and development is given in Note 1 on page 43 and in Note 13 on pages 50 and 51. Net intangible assets increased by £2.5 million (before tax effects) at 31st December 2004. Changes to the income statement are immaterial.

Tax (IAS 12 Income taxes)
Providing deferred tax on property revaluations. More detail on taxation is given in Note 1 on page 45 and in Note 8 on page 48. This results in the creation of a £1.8 million deferred tax liability at 31st December 2004.

Parent company

As described in Note 1, the 2005 accounts have been prepared in accordance with the recognition and measurement criteria of IFRS. Reconciliations of the parent company's Balance Sheet showing the effects of both reformat and restatement between UK GAAP and IFRS for 2004 figures are set out on the following pages. Details of the changes on transition (1st January 2004) are also shown. The principle restatement changes from the transition to IFRS are described below.

Pensions (IAS 19 Employee benefits)
Recognising the deficit for defined benefit pension schemes on the balance sheet and the higher income statement charge for pensions under IAS 19. More detail on defined benefit pension plans is given in Note 1 on page 44 and in Note 29 on pages 59 to 61. For the 2004 year £3.8 million of additional balance sheet net liabilities have been recognised.

Share schemes (IFRS 2 Share-based payments)
Recording the cost of share-based payments awarded to employees on a fair value basis. More detail on employee share plans and long term incentive plans is given in Note 1 on page 44 and in Note 29 on pages 63 and 64.

NOTES TO THE ACCOUNTS *(continued)*

34 EXPLANATION OF TRANSITION TO IFRS *(continued)*

REFORMAT AND RESTATEMENT OF GROUP BALANCE SHEET
As at 1st January 2004

THE GROUP

UK GAAP	UK GAAP as previously reported £000	Reformat £000	Restatement £000	IFRS £000	IFRS
					ASSETS
Fixed assets					**Non-current assets**
Tangible assets	88,089		(6,409)	81,680	Property, plant and equipment
Intangible assets	11,123			11,123	Goodwill
			7,187	7,187	Other intangible assets
			379	379	Prepayments
			2,013	2,013	Investment in associates
		4,099	13,381	17,480	Deferred tax
	99,212	4,099	16,551	119,862	
Current assets					**Current assets**
Stocks	60,695		(1,304)	59,391	Inventories
Debtors	90,515	(19,451)	(1,388)	69,676	Trade receivables
		15,352	(7,470)	7,882	Other current assets
Cash deposits	38,197	(38,197)			
Cash at bank and in hand	4,977	38,197	(1,453)	41,721	Cash and cash equivalents
	194,384	(4,099)	(11,615)	178,670	
			4,936	298,532	**Total assets**
					EQUITY AND LIABILITIES
Creditors due within one year					**Current liabilities**
	86,727	(39,872)	(11,375)	35,480	Trade and other payables
		12,602	(1)	12,601	Bank overdrafts
		20,094	(6)	20,088	Current portion of long term borrowings
		7,176	27	7,203	Current tax payable
	86,727	-	(11,355)	75,372	
Net current assets	107,657	(4,099)	(260)	103,298	**Net current assets**
Creditors due after one year					**Non-current liabilities**
	25,376	(541)	(7)	24,828	Long term borrowings
		6,517	714	7,231	Deferred tax
Provisions for liabilities and charges					
	17,677	(6,965)	35,049	45,761	Post-retirement benefits
		989	-	989	Provisions
	43,053	-	35,756	78,809	
	129,780		24,401	154,181	**Total liabilities**
Net assets	163,816		(19,465)	144,351	**Net assets**
Equity					**Equity**
Share capital	18,690			18,690	Share capital
Share premum account	35,996			35,996	Share premium account
Other reserves	6,182	(4,350)		1,832	Other reserves
Profit and loss account	99,782	4,350	(16,840)	87,292	Retained earnings
	160,650		(16,840)	143,810	
Minority interest	3,166		(2,625)	541	Minority interest
Total equity	163,816		(19,465)	144,351	**Total equity**
			4,936	298,532	**Total equity and liabilities**

REFORMAT AND RESTATEMENT OF GROUP INCOME STATEMENT

For the year ended 31st December 2004

THE GROUP

UK GAAP	UK GAAP as previously reported £000	Reformat £000	Restatement £000	IFRS £000	IFRS
Turnover	325,833		(9,842)	315,991	**Revenue**
Operating costs	(274,733)		6,698	(268,035)	Operating costs
Operating profit	51,100		(3,144)	47,956	**Operating profit**
		(1,848)	(9,072)	(10,920)	Financial expenses
		1,584	9,349	10,933	Financial income
Net interest payable	(264)		277	13	**Net financing income**
			735	735	Share of profit of associates
Profit before taxation	50,836		(2,132)	48,704	**Profit before taxation**
Taxation	(17,154)		892	(16,262)	Taxation
Profit after taxation	33,682		(1,240)	32,442	**Profit for the period**
Minority interests - equity	(1,135)	1,135			
Attributable profit	32,547	(32,547)			
					Attributable to:
		32,547	(233)	32,314	Equity holders of parent
		1,135	(1,007)	128	Minority interest
			(1,240)	32,442	
Basic EPS	43.4p		-0.3p	43.1p	Basic EPS

34 EXPLANATION OF TRANSITION TO IFRS *(continued)*

REFORMAT AND RESTATEMENT OF GROUP BALANCE SHEET

As at 31st December 2004

THE GROUP

UK GAAP	UK GAAP as previously reported £000	Restatement: Reformat £000	Restatement £000	IFRS £000	IFRS
					ASSETS
Fixed assets					**Non-current assets**
Tangible assets	89,094		(5,580)	83,514	Property, plant and equipment
Intangible assets	11,713		149	11,862	Goodwill
			6,988	6,988	Other intangible assets
			345	345	Prepayments
			2,494	2,494	Investment in associates
		5,010	11,605	16,615	Deferred tax
	100,807	5,010	16,001	121,818	
Current assets					**Current assets**
Stocks	59,756		(1,527)	58,229	Inventories
Debtors	100,576	(22,150)	(2,405)	76,021	Trade receivables
		17,140	(8,752)	8,388	Other current assets
Cash deposits	45,500	(45,500)			
Cash at bank and in hand	4,886	45,500	(1,630)	48,756	Cash and cash equivalents
	210,718	(5,010)	(14,314)	191,394	
			1,687	313,212	**Total assets**
					EQUITY AND LIABILITIES
Creditors due within one year					**Current liabilities**
	75,948	(19,964)	(12,555)	43,429	Trade and other payables
		4,871	(29)	4,842	Bank overdrafts
		8,195	(12)	8,183	Current portion of long term borrowings
		6,898	(110)	6,788	Current tax payable
	75,948	-	(12,706)	63,242	
Net current assets	134,770	(5,010)	(1,608)	128,152	**Net current assets**
Creditors due after one year					**Non-current liabilities**
	34,657	(210)	(15)	34,432	Long term borrowings
		14	(14)	-	Tax payable
		7,523	(250)	7,273	Deferred tax
Provisions for liabilities and charges					
	18,907	(7,971)	30,399	41,335	Post-retirement benefits
		644	-	644	Provisions
	53,564	-	30,120	83,684	
			17,414	146,926	**Total liabilities**
Net assets	182,013		(15,727)	166,286	**Net assets**
Equity					**Equity**
Share capital	18,800			18,800	Share capital
Share premum account	38,024			38,024	Share premium account
Other reserves	6,139	(5,440)		699	Other reserves
Profit and loss account	115,078	5,440	(12,561)	107,957	Retained earnings
	178,041		(12,561)	165,480	
Minority interest	3,972		(3,166)	806	Minority interest
Total equity	182,013		(15,727)	166,286	**Total equity**
			1,687	313,212	**Total equity and liabilities**

REFORMAT AND RESTATEMENT OF GROUP CASH FLOW

For the year ended 31st December 2004

THE GROUP

UK GAAP	UK GAAP as previously reported £000	Reformat £000	Restatement £000	IFRS £000	IFRS
					Cash flows from operating activities
Operating profit	51,100	(264)	(2,132)	48,704	Profit before taxation
Depreciation and amortisaton	13,302		(272)	13,030	Depreciation and amortisaton
			(735)	(735)	Share of profit of associates
			357	357	Equity settled share plans
		264	(277)	(13)	Net finance income
			(3,059)	61,343	Operating profit before changes in working capital and provisions
Increase in debtors	(9,094)		2,219	(6,875)	Increase in trade and other receivables
Decrease in stocks	342		277	619	Decrease in inventories
		224	(247)	(23)	Decrease in provisions and post retirement benefits
Increase in creditors and provisions	7,562	(224)	(199)	7,139	Increase in trade and other payables
Cash inflow from operating activities	63,212	-	(1,009)	62,203	Cash generated from operations
Interest received	1,584	(1,584)			
Interest paid	(1,846)		17	(1,829)	Interest paid
Dividends paid to minority interests	(432)	432			
Taxation	(16,780)		709	(16,071)	Income taxes paid
			(283)	44,303	**Net cash from operating activities**
Capital expenditure					**Cash flows from investing activities**
Purchase of tangible fixed assets	(14,787)		392	(14,395)	Purchase of property, plant and equipment
Sales of tangible fixed assets	653		(12)	641	Proceeds of sales of equipment
			(674)	(674)	Developmement expenditure capitalised
Acquisitions and disposals	(803)			(803)	Acquisition of subsidiaries
		1,584	(67)	1,517	Interest received
Equity dividends paid	(15,289)	15,289	71	71	Dividends received
			(290)	(13,643)	**Net cash used in investing activities**
Financing					**Cash flows from financing activities**
Issue of shares	2,138			2,138	Proceeds from issue of share capital
Decrease in debt	(2,677)	347		(2,330)	Repayment of borrowings
		(347)	(13)	(360)	Payment of finance lease liabilities
		(15,721)	399	(15,322)	Dividends paid
			386	(15,874)	**Net cash used in financing activities**
Net increase in cash in the period before investments in liquid resources	14,973	-	(187)	14,786	**Net increase in cash and cash equivalents**
Current asset investments not included in cash	(7,745)				
Increase in cash in the period	7,228				

NOTES TO THE ACCOUNTS *(continued)*

34 EXPLANATION OF TRANSITION TO IFRS *(continued)*

REFORMAT AND RESTATEMENT OF PARENT COMPANY BALANCE SHEET

As at 1st January 2004

PARENT COMPANY

UK GAAP	UK GAAP as previously reported	Restatement Reformat	Restatement	IFRS	IFRS
	£000	£000	£000	£000	
					ASSETS
Fixed assets					**Non-current assets**
Investments	55,698	(10,338)		45,360	Investments in subsidiaries
		10,338		10,338	Loans to subsidiaries
			2,288	2,288	Deferred tax
	55,698	-	2,288	57,986	
Current assets					**Current assets**
Debtors	19,988	(404)		19,584	Due from subsidiaries
		404		404	Other current assets
Cash deposits	20,000	(20,000)			
Cash at bank and in hand	1,060	20,000		21,060	Cash and cash equivalents
	41,048	-	-	41,048	
			2,288	99,034	**Total assets**
					EQUITY AND LIABILITIES
Creditors due within one year					**Current liabilities**
	11,274	(54)	(10,542)	678	Trade and other payables
		54		54	Current tax payable
	11,274	-	(10,542)	732	
Net current assets	29,774		10,542	40,316	**Net current assets**
Creditors due after one year					**Non-current liabilities**
			6,800	6,800	Post-retirement benefits
	941			941	Due to subsidiaries
	941		6,800	7,741	
	12,215		(3,742)	8,473	**Total liabilities**
Net assets	84,531		6,030	90,561	**Net assets**
Equity					**Equity**
Share capital	18,690			18,690	Share capital
Share premum account	35,996			35,996	Share premum account
Other reserves	1,832			1,832	Other reserves
Profit and loss account	28,013		6,030	34,043	Retained earnings
Total equity	84,531		6,030	90,561	**Total equity**
			2,288	99,034	**Total equity and liabilities**

REFORMAT AND RESTATEMENT OF PARENT COMPANY BALANCE SHEET

As at 31st December 2004

PARENT COMPANY

UK GAAP	UK GAAP as previously reported £000	Restatement Reformat £000	Restatement £000	IFRS £000	IFRS
					ASSETS
Fixed assets					**Non-current assets**
Investments	58,083	(11,165)		46,918	Investments in subsidiaries
		11,165		11,165	Loans to subsidiaries
			2,426	2,426	Deferred tax
	58,083	-	2,426	60,509	
Current assets					**Current assets**
Debtors	23,832	(401)	(931)	22,500	Due from subsidiaries
		401		401	Other current assets
Cash deposits	28,042			28,042	Cash and cash equivalents
	51,874	-	(931)	50,943	
			1,495	111,452	**Total assets**
					EQUITY AND LIABILITIES
Creditors due within one year					**Current liabilities**
	15,095	(1,792)	(11,356)	1,947	Trade and other payables
		1,092		1,092	Bank overdrafts
		355		355	Current tax payable
	15,095	(345)	(11,356)	3,394	
Net current assets	36,779	345	10,425	47,549	**Net current assets**
Creditors due after one year					**Non-current liabilities**
			5,400	5,400	Post-retirement benefits
	298	345		643	Due to subsidiaries
	298	345	5,400	6,043	
	15,393		(5,956)	9,437	**Total liabilities**
Net assets	94,564		7,451	102,015	**Net assets**
Equity					**Equity**
Share capital	18,800			18,800	Share capital
Share premum account	38,024			38,024	Share premum account
Other reserves	1,832			1,832	Other reserves
Profit and loss account	35,908		7,451	43,359	Retained earnings
Total equity	94,564		7,451	102,015	**Total equity**
			1,495	111,452	**Total equity and liabilities**

RECONCILIATION OF COMPANY PROFIT AFTER TAXATION

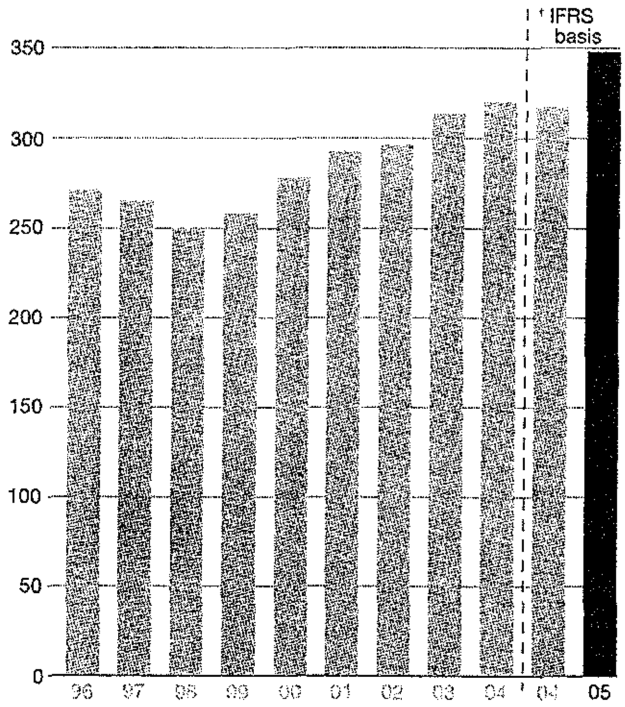
Year ended 31st December 2004		Profit after taxation
UK GAAP as previously reported		23,997
Restatement - Employee benefits:	Pension plans	(314)
	Share based payments	(70)
IFRS		23,613

FINANCIAL SUMMARY 1996 - 2005

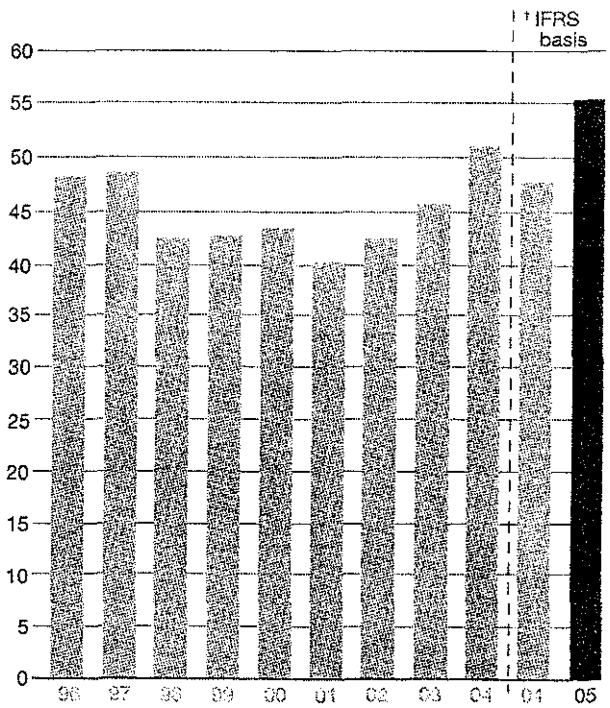
	1996 £000	1997 £000	1998 £000	1999 £000
Revenue	271,980	265,595	249,030	258,942
Operating profit *	48,214	48,574	42,433	42,721
Operating profit margin	17.7%	18.3%	17.0%	16.5%
Profit before taxation *	47,113	47,715	42,270	41,751
Profit before taxation **	47,113	47,715	30,641	41,751
Profit after taxation	30,984	31,229	20,140	29,058
Dividends in respect of the year	11,686	12,535	13,116	13,102
Net assets	119,898	128,772	136,196	128,737
Earnings per share (basic) *	38.0p	38.3p	34.5p	36.1p
Earnings per share (basic) **	38.0p	38.3p	24.1p	36.1p
Dividends in respect of the year (per share)	14.8p	15.8p	16.5p	17.3p
Return on capital employed	37.1%	36.5%	30.3%	28.0%

† The results for 2004 and 2005 have been prepared under International Financial Reporting Standards, prior year figures are shown as originally reported including 2004 for reference.
* before exceptional and non-operating items
** after exceptional and non-operating items
Return on capital employed prior to 2005 is based on operating profit before the exceptional and non-operating items and goodwill amortisation, and average net assets excluding net goodwill and net debt. For 2005 (and the IFRS 2004 comparative) see note 26.

revenue (£m)

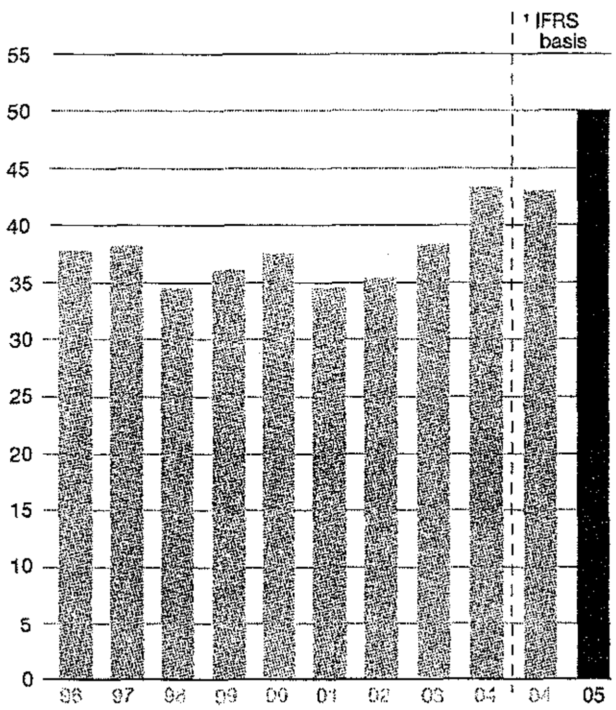


operating profit (£m)
(before exceptional and non-operating items)

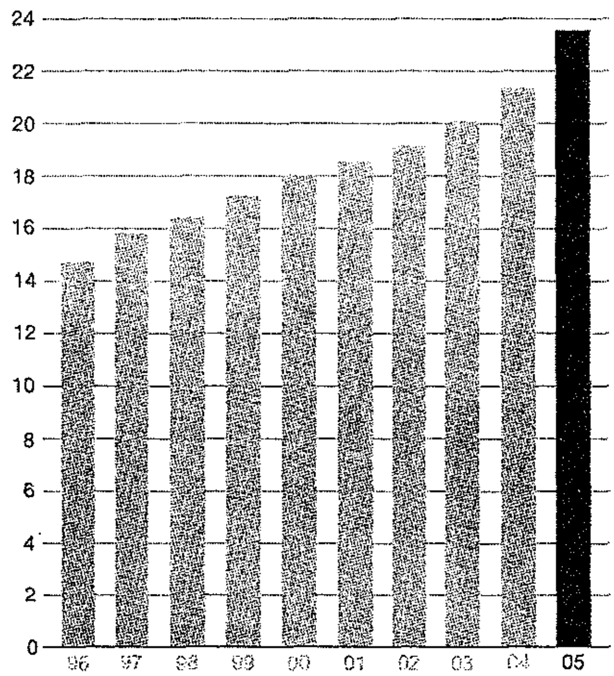


2000	2001	2002	2003	2004	† Prepared under IFRS 2004	2005
£000	£000	£000	£000	£000	£000	**£000**
278,148	291,942	296,363	314,087	325,833	315,991	**349,100**
43,370	40,803	42,674	45,750	51,100	47,956	**55,170**
15.6%	14.0%	14.4%	14.6%	15.7%	15.2%	**15.8%**
41,157	38,025	40,693	44,564	50,836	48,704	**56,959**
40,167	38,641	40,693	44,564	50,836	48,704	**56,959**
27,300	26,625	26,806	29,426	33,682	32,442	**38,187**
13,301	13,752	14,350	15,028	16,102	16,196	**18,318**
138,264	145,115	149,293	163,816	182,013	166,286	**198,246**
37.4p	34.4p	35.3p	38.5p	43.4p	43.1p	**50.0p**
35.4p	35.3p	35.3p	38.5p	43.4p	43.1p	**50.0p**
18.0p	18.6p	19.3p	20.1p	21.4p	21.4p	**23.8p**
26.2%	23.6%	25.6%	28.3%	31.0%	27.2%	**30.4%**

earnings per share (p)
(before exceptional
and non-operating items)



dividends per share (p)



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Allen & Overy

IMPORTANT DATES

Ordinary shares quoted ex-dividend	19th April 2006
Record date for final dividend	21st April 2006
Annual general meeting	10th May 2006
Final dividend payable	22nd May 2006

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Spirax-Sarco Investments Ltd.
Spirax-Sarco Overseas Ltd.
Watson-Marlow Ltd.
Eirdata Environmental Services Ltd.

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Sarco International, Corp.
Watson-Marlow, Inc.

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Spirax Sarco (Thailand) Ltd.

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Brazil
Spirax Sarco Ind. e Com. Ltda.
New Zealand
Spirax Sarco Ltd.
South Africa
Spirax-Sarco South Africa (Pty.) Ltd.
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Actuators and Controls (Pty) Ltd.
Proportional Control Technology (Pty) Ltd.

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Spirax Sarco Equip. Ind. Lda.
Russia
Spirax-Sarco Engineering LLC
Spain
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Spirax-Sarco Engineering S.L.
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