

Tuesday 10 March 2009

## **Preliminary Results for the Year Ended 31 December 2008**

### ***Strong performance in the face of adverse economic conditions***

Zotefoams plc (“Zotefoams”, or “the Group” or “the Company”), which manufactures and sells high-performance foams, today announces its preliminary results for the 12 months ended 31 December 2008.

#### **HIGHLIGHTS**

- Profit before tax increased 17% to £3.93 million ( 2007: £3.37 million)
- Operating margin improved to 11.6% from 11.0% in 2007
- Strong balance sheet with low gearing at 4% (2007: 6%)
- £5.77 million of cash generated from operations (2007: £4.78 million)
- Proposed final dividend of 3.0p per share making a total for 2008 of 4.5p (2007: 4.5p)
- Invested US\$3 million for a 30% shareholding in MuCell Extrusion LLC with a future option to purchase 100% and a technology licence

#### **Commenting on the results, Nigel Howard, Chairman, said:**

*“In what were difficult trading conditions, particularly towards the latter part of the year, Zotefoams demonstrated good resilience to record a robust set of financial results. Trading for the first two months of 2009 is at lower levels of volumes than anticipated and we are taking appropriate measures to control costs to reflect this lower activity level. Furthermore, the current economic conditions and lack of forward order visibility makes the outlook more uncertain than it has been for many years. However, notwithstanding the likelihood that 2009 will be a challenging year, the Board remains positive about the longer term prospects for the business.”*

#### **Enquiries:**

##### **Zotefoams plc**

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## CHAIRMAN'S STATEMENT

### STRATEGY

Zotefoams' strategy is to grow our existing business in polyolefin foams while developing a portfolio of high-performance polymers. We will seek to grow profitably through a combination of organic growth in both our polyolefin and high-performance polymers businesses and through partnerships or acquisitions in related technologies, products or markets.

### OBJECTIVES

We intend to grow sales in our core polyolefin business in excess of the rate of inflation in Europe and achieve double digit percentage growth in North America and Asia. Our sales growth in America has been supported by our factory in Kentucky since its opening in mid-2001. In Asia, we will consider a similar operation, either under a licence or as a joint venture, as sales increase to a level where such an investment becomes financially attractive. We are also committed to developing a portfolio of unique foam products from high-performance materials which will enjoy significant advantages over competitive materials. This will allow higher margins for Zotefoams and confirm our position as a global leader in foam technology. We intend to achieve this growth while continuing to improve our operating margins and our return on capital employed.

### EMPLOYEES

Our business relies on our employees and on behalf of the Board I would like to thank all of our employees whose talents, efforts and dedication combined to make 2008 a successful year.

### OVERVIEW OF RESULTS

During 2008 we grew profit before tax by 17% to £3.93m (2007: £3.37m) and sales increased by 10% to £34.78m (2007: £31.61m). Gross margins increased to 29.1% (2007: 27.1%) and Group operating margins improved from 11.0% to 11.6% of sales.

In July we invested US\$3 million to acquire a 30% shareholding in a joint venture to exploit and further develop through commercial licensing a unique microcellular foam technology for extrusion. Zotefoams is licensed to use this technology in our own business and we plan to commence manufacture under this licence in 2009.

We generated £5.77m cash from operations, an increase of 21% over 2007 (£4.78m), and ended the year with net debt of £1.15m.

### DIVIDEND

We are proposing to maintain a final dividend of 3.0p per ordinary share which, if approved, would make a total of 4.5p per ordinary share for the year (2007: 4.5p). The dividend is 1.8 times covered by after tax profits.

### OUTLOOK

Over recent years Zotefoams has developed an exciting portfolio of growth options outside our core polyolefin business and the recent investment in MuCell® technology and successes in T-Tubes® insulation add to the opportunities offered by our unique fluoropolymer and nylon foams. Our business has low gearing and strong cash generation and we continue to invest to support these future opportunities.

We are benefiting from favourable exchange rates and prices of our major raw materials are currently lower than in 2008. However, trading for the first two months of 2009 is at lower levels of volumes than anticipated and we are taking appropriate measures to control costs to reflect this lower activity level. Furthermore, the current economic conditions and lack of forward order visibility makes the outlook more uncertain than it has been for many years. However, notwithstanding the likelihood that 2009 will be a challenging year, the Board remains positive about the longer term prospects for the business.

### **NIGEL HOWARD**

Chairman  
9 March 2009

## MANAGING DIRECTOR'S REVIEW

Zotefoams is the world's leading manufacturer of cross-linked block foams. Its products are used in a wide range of markets including sports and leisure, packaging, transport, healthcare, construction, marine and the military. Through a unique production process the Company produces foams which have controlled properties and are of a strength, consistency, quality and purity superior to foams produced by other methods.

## BUSINESS OVERVIEW

Zotefoams considers its business to fall into two distinct categories: polyolefin foams and high-performance polymers. Both businesses rely on our unique production process which uses nitrogen gas at high temperature and pressure to foam solid plastics. Polyolefin foams are mainly made from polyethylene which, when foamed, produces a versatile material used in a wide variety of applications. Typically our products are sold to foam converters who process the foam by a variety of techniques such as cutting, welding, moulding and routing into finished or semi-finished parts based on end-user requirements. The benefits of Zotefoams' products are evident at both foam processors and end-users and include purity, consistency of processing, good performance to weight ratio and aesthetics. Key to growing our business successfully is developing and maintaining close relationships with the converters, combined with business development activities at end-users to highlight the benefits of our materials and track industry trends for future development.

Our main business is in the manufacture and sales of polyolefin foams and sales in this business segment grew to £33.98m (2007: £30.87m) due to favourable foreign exchange rates. This business was affected in the latter part of the year by unfavourable economic conditions which saw a considerable slowdown in key end market segments, particularly in automotive and construction. Other segments were affected to varying degrees although the diversity of our business across market segments limits the risk of a significant segment-specific downturn. In the face of these trading conditions, the Company was able to maintain sales volume levels at similar levels to 2007. In these uncertain times, customers more than ever require shorter lead-times to mitigate inventory exposure. Our ability to anticipate and react to our customers' needs provides us with a real competitive advantage in this environment.

High-performance polymers ("HPP") use the processing technology developed for polyolefin foams and applies it to other materials. This is an emerging business which offers an improved return on capital in new business segments. We have developed, patented and launched world leading products made from fluoropolymer and nylon which are branded "ZOTEK®" - our high-performance foams' trademark. These foams are targeted at highly technical and demanding applications in markets such as aerospace, pharmaceutical, semi-conductor, chemical processing and automotive, where market development lead times are long. The timing of revenue generation is therefore difficult to predict. This segment of our product range is relatively immature and thus far commercial successes are mainly in the aviation market where our ZOTEK® F fluoropolymer foams are gaining acceptance, particularly in North America. During 2008 sales to the aviation market experienced delays in adoption of specified programs. Further delays, along with temporary de-stocking in our supply chain, were caused by industrial action at Boeing late in the year. Despite this, HPP sales were £800,000, an increase of 9% over the previous year with growth from favourable exchange rates and in segments outside aviation offsetting the de-stocking in the aviation market. Progress in penetrating the market for advanced insulation in clean rooms with the T-Tubes® branded product made from ZOTEK® F foams is good with smaller, typically trial basis, installations on biotech and pharmaceutical sites in Europe and Asia and we have added a second direct salesperson in response to the opportunities in this sector.

In July 2008 Zotefoams invested US\$3m for a 30% shareholding in MuCell Extrusion LLC ("ME LLC"), a newly created company set up to develop extrusion-based microcellular foaming using supercritical nitrogen and CO<sub>2</sub> and a licence to use the MuCell® technology. The business model is to license this technology, which is patent protected, across a wide variety of industries where foaming of polymer can reduce material content and costs for the licensee or can provide the benefits such as insulation, light-weight, buoyancy etc associated with lighter density foams. The process has the added benefits of being environmentally friendly and does not use chemical foaming agents, the residues of which are unwanted in many applications. The Company has acquired a license to use the MuCell® technology and is in the process of developing products and investing in process machinery to manufacture thin, low-density roll foams which are widely used in high-performance sealing, automotive, tape and medical markets worldwide. ME LLC has made good progress in developing the technology and licensing third parties for applications across a variety of

markets and materials in rolls, tubes and profiles. Zotefoams has an option to acquire the remaining balance of 70% of the shares of ME LLC from July 2010.

## STRATEGY AND OBJECTIVES

Zotefoams' strategy is to grow our existing business in polyolefin foams while developing a portfolio of high-performance polymers.

Our stated objectives are to:

1. Grow sales in our polyolefin business in excess of the rate of inflation in Europe and achieve double digit percentage growth in North America and Asia.
2. Develop a high-performance polymers portfolio to deliver enhanced margins.
3. Improve our operating margins.
4. Improve our return on capital employed.

Performance in 2008 against these objectives was as follows:

1. Sales:
  - a. Sales in the UK and Europe fell by 1% in constant currency. Having grown by 6% in constant currency in the first half of 2008 performance in the second half was adversely affected by very difficult economic conditions, the impact of which was magnified by significant de-stocking in some segments of our markets;
  - b. Polyolefin sales in North America grew by 1% in constant currency. Our North American business is relatively more exposed to the automotive and construction segments than our European business and these segments were first to feel the impact of the economic downturn; and
  - c. Polyolefin sales in Asia grew by 17% in constant currency. Our presence in Asia is limited to niche, higher added-value products and this is where we are focusing our resources.
2. Sales of high-performance polymers grew by 9%. Delays in two major aviation programs in North America led to significantly reduced sales to this segment offsetting the benefits of a more favourable currency and the growth experienced in other areas.
3. Group operating margins improved from 11.0% to 11.6% of sales revenue.
4. Pre-tax return on capital employed, pre-exceptional items, increased from 13% to 14%.

## FINANCIAL RESULTS

The 10% increase in Group sales was due to favourable exchange rates. Gross margin increased by 2% to 29.1% from 27.1% with the benefit of these favourable exchange rates more than offsetting the increased sterling cost of our currency denominated raw materials.

Our major raw materials are commodity polymers and these have been subject to large price movements during 2008. The price of low density polyethylene, by far our largest raw material cost, started the year at around €1,300 per tonne and then increased in the third quarter to a peak of nearly €1,500 per tonne before falling to just over €700 per tonne in the fourth quarter.

Energy costs have a significant impact on our business with energy costs amounting to 5% of Group sales. In March 2007 we renewed our UK energy contract fixing prices for two years from 1 December 2007 to 30 November 2009 allowing certainty of input prices on which to base our relationship with customers.

Distribution costs (which include selling expenses) rose by 20% as we continued to increase our commercial resources in both polyolefins and high-performance polymers. Administrative expenses include a foreign exchange loss of £0.19m (2007: profit of £0.23m) which represents the profit/loss on forward exchange contracts used to hedge our currency exposure and the foreign exchange translation profit/loss.

We purchased a 30% share of MuCell Extrusion LLC at the beginning of July 2008 and the business broke even, before amortisation costs, in the second half of 2008. After amortisation we have recorded a loss of £27,000 for MuCell Extrusion LLC. After this, Group profit before tax increased by 17% to £3.93m (2007: £3.37).

The overall effective tax rate is 24%, below the UK corporation tax rate of 28.5% for the year. This is principally due to the lower tax charge incurred in our US subsidiary where we have brought forward tax losses. In 2007 our effective tax rate was 13% due to a £0.20m reduction in the Group's deferred tax liability following a change in the rate at which the Group's future corporation tax liabilities are provided for and a

£0.23m favourable adjustment to the tax charge in respect of prior periods. Excluding these two items, our effective tax rate for 2007 was 26%.

#### Earnings Per Share and Dividend

Group earnings per share were 8.3p (2007: 8.0p). In 2008 we grew profit before tax by 17% and profit after tax by 3% due to the impact of one-off tax credits in 2007. The Directors are recommending that the final dividend is maintained at 3.0p per share, and, subject to shareholder approval, payable on 21 May 2009 to shareholders on the Company register at 24 April 2009. This would bring the total dividend to 4.5p per ordinary share for the year (2007: 4.5p).

#### Cash Flow

Cash generated from operations was £5.77m (2007: £4.78m). This paid for capital expenditure of £1.42m which was lower than in previous years (2007: £2.69m) reflecting the phasing of projects. It also paid for our acquisition of a 30% share in MuCell Extrusion LLC and the MuCell® technology licence (£1.56m). We are pleased to report that, after these items and the dividend payment of £1.64m, there was a £0.53m reduction in net debt (2007: net debt increase of £0.26m).

At 31 December 2008 the Group's banking facilities consisted of £0.30m outstanding on a £2.00m loan taken out in 2004, which is repayable by August 2009 and a £5.00m overdraft facility renewable in May 2009. Based on discussions with our bankers the Board expect the overdraft facility to be renewed and since the year end the Group has increased its facilities by taking out a further £3.30m loan. This loan is repayable over five years, has no operating covenants and is secured against certain items of plant and equipment.

At 31 December 2008 net debt was £1.15m (2007: £1.68m) and gearing remained low at 4% (2007: 6%).

#### DAVID STIRLING

Managing Director  
9 March 2009

ZOTEK® and Azote® are registered trademarks of Zotefoams plc

T-Tubes® is a registered trademark of UFP Technologies Inc. See [www.t-tubes.com](http://www.t-tubes.com)

MuCell® is a registered trademark of Trexel Inc.

### Consolidated income statement for the year ended 31 December 2008

		2008	2007
	Note	£000	£000
<b>Revenue</b>	2	<b>34,781</b>	31,606
Cost of sales		(24,658)	(23,035)
<b>Gross profit</b>		<b>10,123</b>	8,571
Distribution costs		(2,820)	(2,344)
Administrative expenses		(3,273)	(2,766)
<b>Operating profit</b>		<b>4,030</b>	3,461
Financial income	4	1,150	1,063
Finance costs	4	(1,222)	(1,152)
<b>Share of loss from associate</b>		<b>(27)</b>	-
<b>Profit before tax</b>		<b>3,931</b>	3,372
Taxation	5	(925)	(454)
<b>Profit for the year</b>	3	<b>3,006</b>	2,918
Attributable to:			
Equity holders of the parent		3,006	2,918
<b>Earnings per share Basic (p)</b>	6	<b>8.3</b>	8.0
<b>Diluted (p)</b>	6	<b>8.1</b>	7.9

### Consolidated statement of recognised income and expense for the year ended 31 December 2008

2008

2007

	£000	£000
Foreign exchange translation differences on investment in foreign subsidiary/associate	3,043	(117)
Effective portion of changes in fair value of cash flow hedges net of recycling	(1,079)	(269)
Actuarial (losses)/gains on defined benefit schemes	(1,658)	1,141
Tax on items taken directly to equity	766	(271)
<b>Net income recognised directly in equity</b>	<b>1,072</b>	<b>484</b>
Profit for the year	3,006	2,918
<b>Total recognised income and expense for the year</b>	<b>4,078</b>	<b>3,402</b>
Attributable to equity holders of the parent	4,078	3,402

## Consolidated balance sheet as at 31 December 2008

	Note	2008 £000	2007 £000
<b>Non-current assets</b>			
Property, plant and equipment		26,775	26,436
Intangible assets		121	-
Investment in associate	7	1,912	-
Deferred tax assets		239	138
<b>Total non-current assets</b>		<b>29,047</b>	<b>26,574</b>
<b>Current assets</b>			
Inventories		4,335	4,280
Trade and other receivables		8,408	7,351
Cash and cash equivalents		429	258
<b>Total current assets</b>		<b>13,172</b>	<b>11,889</b>
<b>Total assets</b>		<b>42,219</b>	<b>38,463</b>
<b>Non-current liabilities</b>			
Interest-bearing loans and borrowings		-	(300)
Employee benefits	9	(3,527)	(2,465)
Deferred tax liabilities		(1,969)	(2,699)
<b>Total non-current liabilities</b>		<b>(5,496)</b>	<b>(5,464)</b>
<b>Current liabilities</b>			
Interest-bearing loans and borrowings		(300)	(400)
Bank overdraft		(1,281)	(1,242)
Tax payable		(937)	(561)
Trade and other payables		(4,984)	(4,130)
<b>Total current liabilities</b>		<b>(7,502)</b>	<b>(6,333)</b>
<b>Total liabilities</b>		<b>(12,998)</b>	<b>(11,797)</b>
<b>Total net assets</b>		<b>29,221</b>	<b>26,666</b>
<b>Equity</b>			
Issued share capital		1,889	1,820
Own shares held		(69)	-
Share premium		13,941	13,941
Capital redemption reserve		15	15
Translation reserve		2,291	(752)
Hedging reserve		(1,264)	(185)
Retained earnings		12,418	11,827
<b>Total equity attributable to the equity holders of the Company</b>		<b>29,221</b>	<b>26,666</b>

## Consolidated cash flow statement for the year ended 31 December 2008

	2008 £000	2007 £000
<b>Cash flows from operating activities</b>		
Profit for the year	3,006	2,918
Adjustments for:		
Depreciation, amortisation and impairment	2,931	3,129
Gain on sale of plant and equipment	-	(9)
Financial income	(1,150)	(1,063)
Financial expense	1,222	1,152
Share of loss from associate	27	-
Equity-settled share-based payments	165	91
Taxation	925	454
<b>Operating profit before changes in working capital and provisions</b>	<b>7,126</b>	<b>6,672</b>
Increase in trade and other receivables	(596)	(1,287)
Decrease/(increase) in inventories	227	(504)
(Decrease)/Increase in trade and other payables	(387)	498
Decrease in provisions and employee benefits	(600)	(600)
<b>Cash generated from the operations</b>	<b>5,770</b>	<b>4,779</b>
Interest paid	(68)	(138)
Tax paid	(698)	(564)
<b>Net cash from operating activities</b>	<b>5,004</b>	<b>4,077</b>

Proceeds on disposal of property, plant and equipment	-	22
Interest received	14	17
Acquisition of property, plant and equipment	(1,420)	(2,692)
Acquisition of licence	(150)	-
Investment in associate	(1,410)	-
Distribution from associate	15	-
<b>Net cash used in investing activities</b>	<b>(2,951)</b>	<b>(2,653)</b>
Proceeds from the issue of share capital	-	202
Repurchase of own shares	-	(242)
Repayment of borrowings	(400)	(400)
Dividends paid	(1,638)	(1,637)
<b>Net cash used in financing activities</b>	<b>(2,038)</b>	<b>(2,077)</b>
Net increase/(decrease) in cash and cash equivalents	15	(653)
<b>Cash and cash equivalents at 1 January</b>	<b>(984)</b>	<b>(329)</b>
Effect of exchange rate fluctuations on cash held	117	(2)
<b>Cash and cash equivalents at 31 December</b>	<b>(852)</b>	<b>(984)</b>

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

## 1. Accounting policies

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

The Group financial statements consolidate those of the Company and its subsidiaries (together referred to as the 'Group').

The Group financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ("Adopted IFRS").

The financial information does not constitute the Company's statutory accounts for the year ended 31 December 2008 or 2007 but is derived from those accounts. Statutory accounts for 2007 have been delivered to the Registrar of Companies, and those for 2008 will be delivered following the Company's Annual General Meeting. The auditors have reported on those accounts; their reports were unqualified and did not contain statements under Section 237 (2) of the Companies Act.

## 2. Segment reporting

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

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

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

	Note	Polyolefins		HPP	
		2008 £000	2007 £000	2008 £000	2007 £000
Revenue		33,981	30,872	800	734
Operating profit/(loss)		4,567	4,001	(537)	(540)
Net financing costs					
Loss from associate					
Taxation					
Profit for the year		39,929	36,434	2,051	1,891
Segment assets					
Unallocated assets		—	—	—	—
Total assets					
Segment liabilities		(10,088)	(8,370)	(5)	(167)
Unallocated liabilities		—	—	—	—
Total liabilities					
Depreciation		2,850	3,093	52	36
Capital expenditure		1,394	2,600	26	92

Table continued...

	Note	Consolidated	
		2008 £000	2007 £000
Revenue		34,781	31,606
Operating profit/(loss)		4,030	3,461
Net financing costs		(72)	(89)
Loss from associate		(27)	-
Taxation		(925)	(454)
Profit for the year		3,006	2,918
Segment assets		41,980	38,325
Unallocated assets		239	138
Total assets		42,219	38,463

Segment liabilities	(10,093)	(8,537)
Unallocated liabilities	(2,905)	(3,260)
Total liabilities	(12,998)	(11,797)
Depreciation	2,902	3,129
Capital expenditure	1,420	2,692

### Geographical segments

	UK and Eire £000	Europe £000	North America £000	Rest of the world £000	Total
For the year ended 31 December 2008					
Revenue from external customers	8,369	17,374	7,659	1,379	34,781
Segment assets	30,812	—	11,407	—	42,219
Capital expenditure	1,400	—	20	—	1,420
For the year ended 31 December 2007					
Revenue from external customers	8,180	15,249	7,131	1,046	31,606
Segment assets	30,881	—	7,582	—	38,463
Capital expenditure	2,622	—	70	—	2,692

### 3. Expenses and auditors' remuneration

	2008 £000	2007 £000
Included in profit for the year are:		
Research and development costs expensed	731	803
Net exchange losses/(gains)	185	(227)
Auditors' remuneration:		
Group	95	84
– audit of these financial statements		
– fees receivable by the auditors and their associates in respect of other services:		
– other services pursuant with legislation	24	18
– other services relating to taxation	13	11
– other services relating to acquisition of associate	20	-
	152	113

### 4. Finance income and costs

#### Financial income

	2008 £000	2007 £000
Interest on bank deposits	12	17
Expected return on assets of defined benefit pension fund	1,138	1,046
	1,150	1,063

#### Finance costs

	2008 £000	2007 £000
On bank loans and overdrafts	80	140
Interest on defined benefit pension obligation	1,142	1,012
	1,222	1,152

### 5. Taxation

	2008 £000	2007 £000
UK corporation tax	1,135	904
Overseas taxation	2	(5)
Adjustment to prior year UK tax charge	(66)	(81)
Current taxation	1,071	818
Deferred taxation	(146)	(364)
Total tax charge	925	454

#### Factors affecting the tax charge

The tax charge for the period is lower (2007: lower) than the standard rate of corporation tax in the UK of 28 ½ % (2007: 30%). The differences are explained below:

	2008 £000	2007 £000
Tax reconciliation		
Profit before tax	3,931	3,372
Tax at 28 ½ % (2007: 30%)	1,120	1,011
Effects of:		
Research and development tax credits less expenses not deductible for tax purposes	(7)	(39)
Deferred tax rate change from 30% to 28%	-	(204)
Partial recognition of US tax losses	(60)	(32)

Lower tax rates on overseas earnings	(62)	(51)
Adjustments to UK corporation tax charge in respect of previous periods	(66)	(81)
Adjustments to deferred tax charge in respect of previous periods	-	(150)
<b>Total tax charge</b>	<b>925</b>	<b>454</b>

A reduction in the UK tax rate from 30% to 28%, was effective from 1 April 2008 and in accordance with IAS12 Income Taxes, the deferred tax liabilities and assets have been calculated using a rate of 28%

## 6. Dividends and earnings per share

	<b>2008</b>	2007
	<b>£000</b>	£000
Final dividend prior year of 3.0p (2006: 3.0p) net per 5.0p ordinary share	<b>1,091</b>	1,090
Interim dividend of 1.5p (2007: 1.5p) net per 5.0p ordinary share	<b>547</b>	547
<b>Dividends paid during the year</b>	<b>1,638</b>	1,637

The proposed final dividend for the year ended 31 December 2008 of 3.0p per share (2007: 3.0p) is subject to approval by shareholders at the AGM and has not been included as a liability in these financial statements.

### Earnings per ordinary share

Earnings per ordinary share is calculated by dividing profit after tax of £3,006,000 (2007: £2,918,000) by the weighted average number of shares in issue during the year excluding own shares held by employee trusts which are administered by independent trustees. The number of shares held in the trust at 31 December 2008 was 1,378,098 (2007: nil). Distribution of shares from the trust is at the discretion of the trustees. Diluted earnings per ordinary share adjusts for the potential dilutive effect of share option schemes in accordance with IAS 33.

	<b>2008</b>	2007
	<b>£000</b>	£000
Average number of ordinary shares issued	<b>36,402,608</b>	36,375,270
Deemed issued for no consideration	<b>559,791</b>	692,568
<b>Diluted</b>	<b>36,962,399</b>	37,067,838

Shares deemed issued for no consideration have been calculated based on the potential dilutive effect of the Executive Share Option Scheme, options granted under the HMRC Approved Share Option Scheme, Long Term Incentive Plans and the Deferred Bonus Plan:

Date from which exercisable	Exercise price	Number of shares under option	
		2008	2007
7 April 2007	72.5p	<b>152,834</b>	152,834
22 December 2008	77.0p	<b>684,213</b>	1,026,320
10 May 2010	nil	<b>306,959</b>	306,959
20 March 2011	nil	<b>233,283</b>	-
12 August 2011	106.7p	<b>267,911</b>	-
		<b>1,645,200</b>	1,486,113

The average fair value of one ordinary share during the year was considered to be 78.0p (2007: 113.6p).

## 7. Investments in associates

On 8 July 2008 Zotefoams Inc. acquired a 30% shareholding in MuCell Extrusion LLC. Zotefoams has an option to increase its shareholding to 100%. The earliest this option can be exercised is July 2010 but, depending on certain conditions it may be exercised as late as June 2011.

Net assets acquired were as follows:

	Book value	Fair value adjustment	<b>Fair value</b>
	£000	£000	<b>£000</b>
Brand	-	552	<b>552</b>
Intellectual property	-	1,430	<b>1,430</b>
Property, plant and equipment	17	-	<b>17</b>
Cash and cash equivalents	251	-	<b>251</b>
Net identifiable assets	268	1,982	<b>2,250</b>
Goodwill on acquisition			<b>2,270</b>
100% share			<b>4,520</b>
30% share			<b>1,356</b>
Total purchase price comprising consideration of £1,356,000 and legal fees of £54,000			<b>1,410</b>
Licence to use MuCell® technology			<b>150</b>
<b>Net cash outflow on acquisition</b>			<b>1,560</b>

The intellectual property assets of the business are the patents of the Company. The brand assets are the MuCell® trademark and in particular the formulas, recipes and technological expertise which form the marketing assets of the Company. Other than intellectual property and the brand there were no significant intangible assets acquired as part of the transaction and therefore the differences between the consideration and the fair value of the identifiable assets acquired has been designated goodwill.

Summary aggregated financial information on associates – 100 per cent:

At 31 December:

**2008**                      2007

	£000	£000
Goodwill	3,159	-
Intangible assets	2,642	-
Tangible assets	27	-
Current assets	243	-
Cash	173	-
Total assets	6,244	-
Total liabilities	(127)	-
Net assets	6,117	-

For the period ended 31 December:	2008 £000	2007 £000
Revenue	315	-
Loss after amortisation	(90)	-

MuCell Extrusion LLC was created on 1 July 2008 and therefore the above results reflect six months trading from 1 July 2008 to 31 December 2008. The loss for the period is after amortisation of £90,000 on intangible assets.

The reporting date for MuCell Extrusion LLP is 30 June. The financial information included within these financial statements is based on management information as at 31 December 2008.

Reconciliation of movement in MuCell valuation:

	2008 £000	2007 £000
Initial Cost of investment including expenses	1,410	-
Share of result for period	(27)	-
Distribution received	(15)	-
Effect of movement in foreign exchange	544	-
Investment in associate as at 31 December 2008	1,912	-

## 8. Financial instruments

### Policy

The Group's principal financial instruments include bank loans, cash and short-term deposits the main purpose of which is to raise finance for the Group's operations. Foreign exchange derivatives are used to help manage the Group's currency exposure. It is and has been throughout the period under review, the Group's policy that no trading in financial instruments shall be undertaken.

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

### Credit risk

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. The Group does not require collateral in respect of financial assets. In 2008 and 2007, the Group had credit insurance to mitigate this risk. However, the uninsured exposure as at 31 December 2008 is £1,377,000 (2007: £1,360,000) so elements of risk remain.

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

Trade receivables can be analysed as follows:

	Group 2008 £000	Group 2007 £000
Amounts neither past due or impaired	6,625	5,614
Amounts past due but not impaired		
Less than 60 days	1,459	1,501
More than 60 days	-	-
Total past due but not impaired	1,459	1,501
Amounts impaired	126	97
Impairment allowance	(126)	(97)
Carrying amount of impaired receivables	-	-
Trade Receivables net of allowances	8,084	7,115

### Interest rate risk

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

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

	2008				2007			
	Effective interest rate	Fixed rates £000	Variable rates £000	Total £000	Effective interest rate	Fixed rates £000	Variable rates £000	Total £000
Sterling	4%	—	1,581	1,581	6%	—	1,942	1,942
		—	1,581	1,581		—	1,942	1,942

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

### Liquidity risk

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

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

This facility expires at the end of May 2009 and is utilised by Zotefoams plc and its subsidiary undertakings under a cross-guarantee structure.

In August 2004 Zotefoams plc borrowed £2.0m under a five year mortgage, repayable in equal quarterly instalments. This facility is secured over specific plant assets. At 31 December 2008 £0.3m of this mortgage was outstanding and £1.7m had been repaid. In January 2009 Zotefoams plc borrowed £3.3m under a five year mortgage, repayable in equal quarterly instalments. This facility is secured over specific plant assets.

Cash flow forecasts are produced to monitor the expected cash flow requirements of the Group against the available facilities.

### Foreign currency risk

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

The euro and US dollar rates used in preparing the accounts are as follows:

	2008		2007	
	Average	Closing	Average	Closing
Euro/sterling	1.25	1.03	1.46	1.36
US dollar/sterling	1.84	1.44	2.00	1.99

The Group hedges a proportion of its estimated cash exposure in respect of trade and other receivables, trade and other payables and forecast sales receipts and purchase payments for the next nine months. The Group uses forward exchange contracts to hedge its foreign currency risk. As at 31 December 2008 these forward currency contracts covered approximately two-thirds of the estimated net cash foreign exchange exposure for the next nine months. Further details are shown below in the paragraph on sensitivity analysis.

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

### Forecasted transactions

The Group classifies its forward exchange contracts hedging forecasted transactions as cash flow hedges and states them at fair value. The net fair value of forward exchange contracts used as hedges of forecasted transactions at 31 December 2008 was a net liability of £1,264,000 (2007: net liability of £185,000) comprising assets of £nil (2007: £8,000) and liabilities of £1,264,000 (2007: £193,000) that were recognised in fair value derivatives in 2008.

### Recognised assets and liabilities

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

The maturity profile of the forward contracts as at 31 December is as follows:

	Group 2008			Group 2007		
	Foreign Currency '000	Contract Value £000	Fair Value £000	Foreign Currency '000	Contract Value £000	Fair Value £000
Sell EUR	4,700	3,835	4,492	5,100	3,590	3,761
Sell USD	5,100	2,893	3,500	5,700	2,843	2,857

### Sensitivity analysis

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

Short-term fluctuations in interest rates are not hedged as the Group, at present, does not consider them material. At 31 December 2008 it is estimated that a general increase of one percentage point in interest rates would decrease the Group's profit before tax by approximately £16,000 (2007: £19,000).

At 31 December 2008 it is estimated that an increase of one percentage point in the value of sterling against the euro and US dollar would decrease the Group's profit before tax by approximately £106,000 (2007: £67,000) before forward exchange contracts and £60,000 (2007: £33,000) after forward exchange contracts are included for the euro and £69,000 (2007: £52,000) for the US dollar before forward exchange contracts and £33,000 (2007: £24,000) after forward exchange contracts are included.

The Group has significant undertakings in the USA whose revenue and expenses are denominated in US dollars. It also makes a significant proportion of its sales to European customers and these revenues are predominantly in euros. It was the Group's policy in 2008 to hedge the foreign currency cash flows of invoiced sales net of expected foreign expenditure. Hedging is achieved by the use of foreign currency contracts expiring in the month of expected cash flow.

### Fair values

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

	2008		2007	
	Carrying amount £000	Fair value £000	Carrying amount £000	Fair value £000
Trade and other receivables	8,408	8,408	7,343	7,343
Cash and cash equivalents	(852)	(852)	(984)	(984)
Forward exchange contracts				
– assets	-	-	8	8
– liabilities	(1,264)	(1,264)	(193)	(193)
Secured bank loans	(300)	(300)	(700)	(700)
Trade and other payables	(3,720)	(3,720)	(3,937)	(3,937)

### Estimation of fair values

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

### Derivatives

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

### Interest-bearing loans and borrowings and trade and other receivables/payables

Carrying amounts equals the fair value.

## 9. Employee benefits

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

From 31 December 2005 future accrual of benefits for existing members of the scheme ceased.

Contributions to the plan for the year from the Company were £50,000 per month. Following the triennial review in April 2008 the Company agreed with the Trustees to increase these contributions to £55,000 per month from January 2009 to June 2016.

The Company has opted to recognise all actuarial gains and losses immediately via the Statement of Recognised Income and Expenditure (SORIE). An actuarial valuation of the scheme was carried out as at 5 April 2008 and the results have been updated to 31 December 2008 by a qualified independent actuary. The major assumptions used by the actuary were (in nominal terms) as follows:

	As at 31 December 2008	As at 31 December 2007	As at 31 December 2006
Discount rate	6.30%	5.90%	5.10%
Expected return on plan assets	5.76%	6.62%	6.58%
Rate of salary increase	n/a	n/a	n/a
Rate of increase to pensions in payment	3.00%	3.30%	3.00%
Rate of inflation	3.10%	3.40%	3.10%
Mortality assumption	PCA00 MC	PA92 MC	90% of PA92 MC
Life expectancy from age 65 of current male pensioners:	21.6 years	22.5 years	20.7 years
Commutation assumption	75% of members take maximum cash	No allowance	No allowance

The mortality tables used above are those published by the Institute and Faculty of Actuaries, with allowance for improvements in member longevity in line with "Medium Cohort" projections, based on members' year of birth. These adjusted rates suggest that a man aged 65 retiring at 31 December 2008 could expect to live, on average, until age 87. A 5% change in life expectancy would increase/decrease the pension scheme's IAS 19 liability by approximately £0.6m (£0.4m after deferred tax), all other things being equal.

In 2008 an allowance has been made for commutation to be consistent with the assumption used for the triennial actuarial valuation in April 2008.

The overall expected return on assets assumption of 5.76% as at 31 December 2008 has been derived by calculating the weighted average of the expected rate of return for each asset class. The following approach has been used to determine the expected rate of return for each asset class:

- Equities - allowance for an additional return of 3.25% above that available on UK government securities;
- Bonds – current market yields
- Cash - based on the Bank of England base rate.

	Year ended 31 December 2008		Year ended 31 December 2007		Year ended 31 December 2006	
Present value of scheme assets	Long term rate of return expected	Market value £000	Long term rate of return expected	Market value £000	Long term rate or return expected	Market value £000
Equities	7.0%	9,298	7.1%	13,458	7.1%	12,402
Bonds	3.8%	3,154	4.6%	2,431	4.6%	2,437
Other	2.0%	1,417	5.5%	1,353	5.0%	1,022
		<b>13,869</b>		<b>17,242</b>		<b>15,861</b>

Present value of defined obligation:	
Funded plans	17,396
Total	<b>17,396</b>
Deficit in the scheme	<b>(3,527)</b>
Related deferred tax asset	988
Net pension liability	<b>(2,539)</b>

Reconciliation of opening and closing balances of the present value of the defined benefit obligation:	
Benefit obligation at beginning of year	19,707
Service cost	—
Interest cost	1,142
Actuarial gains	(2,752)
Benefits paid	(701)
Past service costs	—
Benefit obligation at end of year	<b>17,396</b>

Reconciliation of opening and closing balances of the fair value of plan assets:	
Fair value of plan assets at beginning of year	17,242
Expected return on plan assets	1,138
Actuarial (losses)/gain	(4,410)
Contributions by employers	600
Benefits paid	(701)
Fair value of plan assets at end of year	<b>13,869</b>

The amounts recognised in the Income Statement are:	
Interest on obligation	1,142
Expected return on plan assets	(1,138)
Past service cost	—
Total expense/(gain)	<b>4</b>

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

	Group and Company	
	2008	2007
	£000	£000
Cost of sales	—	—
Financial income	(1,138)	(1,046)
Finance costs	1,142	1,012
	<b>4</b>	<b>(34)</b>

Actuarial (losses)/gains shown in SORIE since 1 January 2004:					
	2008	2007	2006	2005	2004
	£000	£000	£000	£000	£000
Balance as at 1 January	1,789	648	222	264	—
Actuarial (losses)/gains	(1,658)	1,141	426	(42)	264
Balance as at 31 December	<b>131</b>	<b>1,789</b>	<b>648</b>	<b>222</b>	<b>264</b>

History of scheme assets, obligations and experience adjustments					
	As at 31 December 2008	As at 31 December 2007	As at 31 December 2006	As at 31 December 2005	As at 31 December 2004
Present value of defined benefit obligation	17,396	19,707	20,101	19,479	18,721
Fair value of scheme assets	13,869	17,242	15,861	14,259	11,529
Deficit in the scheme	(3,527)	(2,465)	(4,240)	(5,220)	(7,192)
Experience adjustments arising on scheme liabilities	(2,752)	(875)	233	1,621	93
Experience item as a percentage of scheme liabilities	(16)%	(4)%	1%	8%	0%
Experience adjustments arising on scheme assets	(4,410)	266	659	1,579	299

Experience item as a percentage of scheme assets	(32)%	2%	4%	11%	3%
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***Other pension schemes***

On 1 January 2006 a separate stakeholder scheme was set up for those employees who were originally in the closed defined benefit scheme. The contributions paid by the Company in 2008 were £505,000 (2007: £527,000).

In addition to this scheme, Zotefoams plc operates a stakeholder scheme which is open to employees who joined after 1 October 2001. The contributions paid by the Company in 2008 were £51,000 (2007: £27,000).

For US based employees Zotefoams Inc. operates a 401(k) plan. The contributions paid by Zotefoams Inc. in 2008 were \$80,000 (2007: \$76,000).