Chief Executive's Statement

Aerospace

During 2005, the aerospace industry continued its rapid recovery in build rates. Boeing delivered 290 aircraft, up from 285 in 2004, and booked a net 1,002 of new orders. They plan to deliver 395 aircraft in 2006, a 36% increase. Airbus has not yet announced its build plan for 2006, but it delivered 378 aircraft in 2005, an 18% increase over 2004, and booked an unprecedented net 1,055 in new orders during the year.

Together, Boeing and Airbus delivered 668 aircraft in 2005 but took net orders for 2,057 aircraft – a book to bill ratio of 3.1. This was a record year for the industry, both for the large civil aircraft builders and for the engine suppliers, such as Rolls-Royce, GE and Snecma. In the smaller regional jet aircraft sector the two main assemblers fared less well. Bombardier reduced regional jet deliveries by 26%, from 176 aircraft in 2004 to 130 in 2005, and Embraer by 10% from 134 to 120. Bookings were also down with Bombardier, suffering from significant cancellations on its CRJ 200 programme, receiving net orders for only 4 aircraft in 2005 compared to 135 in 2004 and Embraer booking 90, down from 108.

The small business jet sector was very buoyant and the military and defence sector remained at a healthy level.

Senior Aerospace has a good spread of customers in the aerospace industry with about 30% of sales being to the military and defence sector. The industry recovery, however, is being powered by the demand for Boeing and Airbus large civil aircraft that should see build rates at a higher level for a number of years to come.

In addition, there are a variety of new programmes that are helping demand. The very large Airbus A380 flew for the first time in 2005 and is due into service in 2007. Work has commenced on the European military transport aircraft, the A400M, and production of the Eurofighter has been extended into its second tranche of around 250 aircraft. Both Boeing and Airbus have launched new mid-size large civil aircraft – respectively the B787 and A350 – and had received orders of 291 and 87 aircraft for these models by the end of 2005. The new aircraft are planned to cost less to buy and fly compared to the current equivalent aircraft.

Growth in the aerospace industry is not, however, without its challenges. The availability and price of raw materials is a major concern and this could slow the industry efforts to increase build rates. The industry uses a variety of specialist materials in higher volumes than most other industries. One such material is titanium, where by January 2006 the price had risen by over 65% from a year earlier and the delivery lead time for supplies of titanium had stretched to around 72 weeks.

In addition to build rates increasing, and new aircraft being launched, Senior Aerospace now has an additional member company. Sterling Machine was bought from its private owners in January 2006. Located in Connecticut, USA, it is a well run, profitable, growing and well invested business which makes transmission and rotor-head components for military helicopters – primarily for its main customer Sikorsky. The build rate of the Sikorsky Blackhawk is forecast to grow substantially in the near term as a result of a strong order book. In the medium term, the US government has agreed financing to recommence production of the heavy lift Sikorsky Super Stallion. Sterling Machine is a welcome addition to the Group.

Automotive

In both Europe and North America, automotive markets were flat in 2005. Within these markets, diesel engined vehicles in Europe continued to gain market share as common rail diesel technology became available to most engine assemblers. This high pressure fuel technology increases power output, reduces noise and vibration, improves fuel consumption and helps meet emission standards which authorities around the world continue to tighten. In North America, the rise in fuel prices during 2005 precipitated a switch from large sports utility vehicles to smaller regular passenger cars. Fortunately, the Group's products in production today are more likely to be fitted on the latter rather than the former. In addition, the "Big 3" continued to have their market share eroded by the Japanese and Korean assemblers. These two factors resulted in some distress in the industry with General Motors, Ford and Daimler Chrysler announcing rationalisations, cost reductions and plant closures.

In Senior Automotive, material price pressures slackened somewhat in 2005 compared to 2004 when the industry had witnessed dramatic price increases in a variety of metals. Senior almost exclusively uses varieties of stainless steels where price increases of its component metals (nickel, molybdenum, cobalt etc.) had led to the need to negotiate surcharge mechanisms with both raw material suppliers and customers. The supply chain in the industry now has surcharge mechanisms in place that largely address variations in raw material prices.

Investment by the Division over the last three years in new product programmes is now bearing fruit. The diesel engine manufacturers in the USA, who build essentially for heavy truck assemblers, have adopted common rail high pressure fuel systems for their 2007 model year. It is currently the most economic way to meet 2007 emission standards. Today, the Division has little exposure to heavy trucks but, by 2007, sales in this sector will increase substantially and the dependence upon diesel engines, both large in the USA and small in Europe, will increase significantly. This will dilute Senior's exposure to regular passenger vehicles.

Industrial

In 2005, there were conflicting fortunes in the Industrial Division. Trying to complete the Wembley Stadium ducting contract on cost, and on time, proved impossible on a very difficult site where the main contractor, Multiplex, has regularly reported on its own financial and operational difficulties. The contract is near to completion with the adverse financial impact of the contract being recognised in the 2005 results. By contrast oil and gas, in North America, has been a very healthy market and looks set to continue as long as the crude oil price remains high. Together with the cost reductions affected in 2004, this helped the performance of the Industrial Division improve significantly in 2005, particularly at Pathway.

Operational Excellence

Throughout the Group, engineered products are manufactured for large original equipment assemblers. Consequently, demand levels in the Group's factories are a direct function of the success of the Group's customers in selling their own products together with the dynamics of the marketplaces themselves. In order to continue to be a successful and growing business, the Group remains committed to operational improvements, cost reduction and value enhancement through product and process design and development. Operational excellence, impeccable customer service and profitable pricing remain core objectives.

These policies and improving markets leave Senior well placed to grow in the future.