

an early indicator of market trends. For example, in some of the European Textiles businesses, a general decline in the “as used” portion of garment contracts (i.e. the actual number of garments we process for customers) is a reflection of the shift in manufacturing jobs to lower cost countries. For non-portfolio businesses such as City Link, the equivalent KPIs are numbers of consignments handled and Revenue Per Consignment (“RPC”).

Other business and divisional KPIs include growth in total and organic revenue and net margin, as a way to judge the success of performance and productivity and improvement initiatives; improving efficiency in a sustained way is fundamental to first stabilising and then expanding margin. Our business and divisional profit KPI is operating profit (before amortisation of intangible assets). In 2008, we reported operating profit both before and after one-off items, referring to the latter as adjusted operating profit. We believe that to look at underlying trends we need to strip out these items, as they principally relate to one time restructuring/rationalisation projects.

Our activities have the capacity to generate significant cash flow, although growth in revenues is likely to be to the detriment of working capital performance and spend on capital equipment for rental to customers. We therefore monitor divisional operating cash flow and days sales outstanding (which measures the amount of working capital tied up in trade receivables). For the overall group we look at all these KPIs plus some which are only relevant to the group as a whole – free cash flow (which measures our ability to invest in our businesses and to pay dividends) and profit before income tax and amortisation of intangible assets (PBTA). As with operating profit in 2008 we have used adjusted profit before income tax (adjusted PBTA), which also excludes one-off items.

Divisional performance

Initial Textiles and Washroom Services

Market conditions

The textiles and washrooms market in Europe developed consistently in 2008 through to the summer. Market conditions worsened in the second half, particularly in the auto and heavy industrial sectors. While customer terminations have not risen significantly, existing customers have put reduced volumes through the business. We have only small exposure to these sectors.

Key performance indicators

	£m	Change vs 2007
Revenue	612.3	+1.1%
Organic revenue growth		+0.2%
Operating profit	86.0	-19.2%
Adjusted operating profit	85.9	-20.8%
Net adjusted margin	14.0%	-3.9%
Contract portfolio gain	22.1	+10.0%
New business wins	57.1	+4.2%
Net additions/reductions	19.6	+32.4%
Acquisitions/disposals	(0.8)	-
Terminations	(53.8)	+6.3%
Retention rate	90.7%	+0.7%

2008 review

2008 has been a mixed year for the Textiles and Washroom Services division, with marked differences between the performances of the UK and continental European businesses. Overall revenue for 2008 rose by 1.1% (0.2% organic) but adjusted operating profit of £85.9 million was down 20.8% on prior year. Across Europe revenue grew 4.1% on prior year (2.0% organic) with all major markets demonstrating growth with the exception of Spain, where falling hotel occupancy rates have created a difficult market for flat linen laundering services. European adjusted operating profit declined 8.4%. Revenue in the UK declined 17.9% reflecting in part the exit from the wipers business in 2007. The UK Washroom business produced a loss of £5.2 million after adding a further £6 million to its bad debt provisions in Q3. As in 2007 obtaining price increases has again proved challenging in most markets in 2008, with cost inflation leading to an erosion of margins in 2008.

Continental Europe

Excluding the UK the division saw strong organic development of its contract portfolio, which grew 5.3% over the 2007 closing contract portfolio. New business sales were up 9.0%, representing good performances in all markets except for the Netherlands and Austria.

Excellent growth was recorded in France and Germany. A consistent trend of month-on-month improvement in customer retention to the end of Q3 was marred by a dip in the last quarter and as a result the annual retention rate remained at 92.0% for the year. Similarly, for the year as a whole the net of customers' uptrades and downtrades remained steady at a positive 4.1% of opening portfolio, although this dipped slightly in Q4.

Approximately 75% of the division's revenue is generated in France, Germany and Benelux. 2008 revenue from these territories grew by over 4.3% year-on-year as a result of strong new business wins in France and Germany, price indexation in Belgium and excellent retention rates in France (93.9%) and the Netherlands (87.7%). However, higher service expenses in the French and Belgian textiles operations relating to rising labour costs, a back-dated property tax assessment and higher energy costs have impacted financial performance for the year.

In France the industrial textiles portfolio grew strongly from key contract wins secured towards the end of 2007 and further strengthening of the contract portfolio during 2008; the business exited the year having secured significant contracts with SNCF, Sodexho and Rhodia. However cost pressures, in particular those relating to fuel and energy costs in H1, together with competitive price pressures, have offset any benefit from increased revenue, the full benefits of which will not be felt until 2009. In the washrooms business investment in infrastructure to increase the rate of market expansion has enabled the business to grow profits. Customer retention rates across both businesses were excellent and have shown improvements on the prior year. The pressures outlined above, coupled with a back-dated property tax charge and some production inefficiencies during the early summer, have resulted in a year-on-year profit decline.

In Benelux, while the Netherlands struggled to grow the top line, Belgium, assisted by index driven pricing benefits, grew respectably in both revenue and profit for the year. In the Netherlands the sales team put in place in 2006 struggled to maintain the same levels of key account development as those achieved in 2007. Retention, however, was much improved on prior year. Overall the region grew revenue by 2.9% but profit declined as a result of an inability to pass on cost increases to customers.

Our German Washrooms and Textiles business performed well during 2008, growing portfolio by 7.8%, the result of a 15.5% improvement in new business sales and a half-point improvement in retention. Following the sale in Q4 2007 of the loss-making hospitals business, management was able to focus on the profitable businesses, achieving sales growth of 1.6% and good profit growth.

While the Spanish business achieved good growth in its washrooms and garments activities, revenue was flat from linen services which were heavily impacted by

a slowdown in hotel and restaurant linen usage, caused by difficult market conditions in the Spanish hospitality industry.

All of the division's smaller continental European businesses recorded higher revenue in 2008 than in 2007. However, for the majority of these businesses, the full year cost impact of increased sales investment implemented during the course of the year offset any growth in profit. The full benefits of the growth in contract portfolio will not be fully reflected until 2009.

A number of capital investment programmes continued in continental Europe during 2008. A new plant for Prague in the Czech Republic opened on schedule and to budget in November 2008 and a new laundry for our garment textile rental services opened at the beginning of the year in Lokeren in Belgium. The total investment associated with these projects is estimated to be £15 million, of which £2.8 million was spent in 2008 with a further £1 million to follow in 2009.

UK Washrooms

As the UK business strives to overcome legacy operational issues, performance during 2008 has been impacted by terminations and unacceptably high levels of credits arising from poor service levels delivered from H2 2007 through H1 2008. Revenue fell 17.9% to £67.6 million, of which 7.0% related to the closure of the wipers business in 2007 and 2.6% to credits. A new management team put in place during the first half of 2008 has made significant progress in improving customer service levels (consistently reaching 95% for the last three months of the year) and the rate of contract terminations has fallen from its Q2 peak.

However, because of the extent of service issues, accounts receivable has been a major problem for the business and an additional £6.0 million was provided in Q3 2008. Although we believe this will deal with the legacy issues, it has resulted in the business posting a loss of £5.2 million for the year.

The new management team has restructured the business, focusing on service and assigning responsibilities back to local service centres. Cost reduction initiatives are in place alongside efficiency initiatives which are expected to turn the business around during 2009 and restore it to profitability.

2009 preview

In continental Europe we anticipate improvements in productivity and capital efficiency. However revenue progression is uncertain given the very challenging economic circumstances we are likely to face later in the year. In the UK the washrooms business is expected to show improved profitability in 2009 due to the avoidance of one-off costs and productivity improvements. However revenue growth is likely to be challenging.