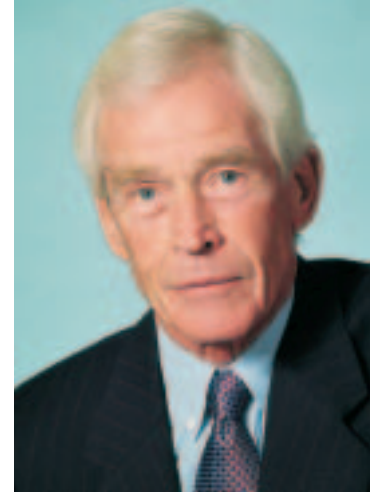


“Halma’s
remarkable
progress over
thirty-year period”

*David Barber,
Chairman*



My normal pattern in these statements, as our long-term shareholders will recognise, has been to focus very specifically on the Group’s financial results in such a way that readers can easily and accurately measure our progress within the year under review. However, this will be my last Statement as Chairman of Halma. With this in mind, I have chosen not to comment on the year’s results or on our immediate prospects. These are all covered in sufficient detail elsewhere within this Annual Report.

My first Statement as Chairman of Halma was written thirty years ago, in 1973, against a political and financial background dramatically different to the one we now see. Halma was then a tiny and unknown company. I trust that shareholders will forgive me if I use this particular Statement to review the whole of that thirty-year span and give one or two examples of what has been achieved by the Group over that period.

I have been privileged throughout my time as Halma Chairman to lead a quite outstanding body of people. This team has changed and developed over the years. Some are now retired. However, the increasing size of the Group means that most are still with us and still have many years of service ahead of them. To all of this team is due the credit and the praise for what has been achieved.

Specific Achievements

Out of many possible examples of Halma’s remarkable progress over this thirty-year period I have selected the following:

- A consistently high rate of return on capital employed. The year-end rate of return has been in excess of 40% throughout the whole of the last twenty years, and, during the year under review, it rose to 54%.
- The compound growth rate in earnings per share over the whole of the thirty

years since 1972/73 now averages 19% per annum. Few, if any, UK companies can match this record.

- Halma's growth has been virtually self-financed. Since August 1972, having adjusted for scrip issues and for issues under the share option schemes, the total number of Halma shares in issue has increased by less than 1.3% per annum.
- Meanwhile, profit before taxation has risen by a compound increase of 20% per annum.
- The Group has a record of unbroken dividend growth since the 1970's. During the whole of a twenty-year period to March 2000, the dividend per share was increased by not less than 20% per annum, possibly the longest such sequence ever recorded by any UK quoted company.
- £10,000 invested in Halma shares at the average share price obtaining during 1974, 1975 or 1976, including gross dividend income, would be worth, as at the end of March 2003, over £4.8 million.
- It is interesting to illustrate this by way of example. Jack Welch, on his retirement from GE, was very proud to claim that during his twenty-year tenure as Chief Executive their share price increased by 2,876%. It would be *folie de grandeur* for me to compare Halma with GE, one of the most successful companies in the world in recent decades. Nonetheless, it is worthy of note that, taking our 1974, 1975 or 1976 share price as a base, the share price of Halma (as at end March 2003) has increased by 37,850%.

All of us, management and investors alike, can surely take quiet pride in such exceptional results, and I know that all my fellow shareholders would wish me to record our appreciation and thanks to everyone in Halma for what has been achieved.

Board Changes

In the interim accounts I reported the resignation of Hamish Ritchie after his distinguished service as a non-executive Director. Then in May 2003 we were shocked and saddened by the sudden death of another non-executive Director, Lord McGowan. Duncan was a quite exceptional individual, a delightful colleague, wise and well-loved. Our deepest sympathies go out to his widow and to his family.

We will very much miss the contribution and companionship of both Duncan and Hamish. I am very pleased, therefore, that Andrew Walker, who has a wealth of relevant Boardroom experience, joined us in May 2003, and we warmly welcome him to the Board. Action is, of course, already in hand to recruit a further additional non-executive Director to bring us back to full strength.

I have left until last the pleasurable task of welcoming Geoff Unwin as my successor as Chairman of the Halma Group. I need hardly comment on the crucial importance of this succession, especially in a Group like Halma which has had a consistent management team over many years. Geoff, of course, joined us after

a brilliant executive career, latterly as the Chief Executive of Cap Gemini, one of the world's largest and most successful Information Technology companies. He has worked very closely with me during the past twelve months, and I have had ample opportunity to observe his skills and his ability.

With this background and with my own, I believe unique, appreciation of the qualities needed for this position, I can assure shareholders that we have a Chairman with exactly the right combination of experience, sensitivity and drive and who I believe can provide us with a future of consistent and substantial growth. I wish him every good fortune.

In conclusion, may I thank everyone in the Halma Group and all of our shareholders for their unfailing support and friendship to me over the years. It has been an exciting and immensely satisfying experience for me, and I trust that, as the song says, the best is yet to come.

A handwritten signature in blue ink that reads "David Barber". The signature is fluid and cursive, with a large initial 'D' and 'B'.

David S Barber

“Provided markets remain stable we expect profit growth”

*Stephen O'Shea,
Chief Executive*



Summary

Results in the second half of the year moved ahead of the first half not only in organic terms but also from the success of the acquisitions of BEA and Radcom. We have produced good results even though improvements in markets did not occur.

Our operations made pre-tax pre-goodwill profit of £46.5 million* (2001/02: £48.3 million) on sales of £267 million (2001/02: £268 million). Our very strong operating cash generation, 110% of operating profit, funded a further dividend growth of 10% at the interim and subject to shareholder approval, a final dividend growth also of 10%.

This cash is generated by our remarkably high return on sales and return on capital employed, which this year reached 54% (2001/02: 41%). This is the highest level ever achieved in the Group. This is a testament to the quality of management in our subsidiaries who have made more effective use of their resources, controlled costs, developed new products and in a number of cases improved their market shares.

For the first time the USA became our largest market, representing 31% of the Group's sales. However, movements in the value of the US dollar reduced the Sterling value of our American earnings. We made our greatest growth in mainland Europe where sales grew by 10%. Sales increased to Africa and the Middle East, and to the Far East and Australasia. There is a trend towards increased manufacturing migration from Europe and the USA towards the Far East and Eastern Europe. Indeed an increasing proportion of components and sub-assemblies used in the Group are sourced from these territories as we continue to keep our product costs low.

I am pleased but not surprised by the success of BEA. This was our largest acquisition so far at £46 million net of cash but including earn-out payments for

* see Consolidated Profit and Loss Account

results to the end of March 2003. In the six months we have owned it, net of interest on the cash we used, BEA delivered £2.1 million to Group profits. Operating profits at £2.9 million reached our target levels. The acquisition was fully funded from cash accumulated from earnings in operating companies so that even after a further small acquisition the Group was cash neutral at the end of the year.

In the year we invested record amounts in product development. This produces growth opportunities and refreshes our offering to customers. Together with the acquisitions we have a stronger set of products to start the new year.

Sectoral Performance

Despite challenging conditions in the markets we serve, three of our six business groups – Fire and Gas, Elevator Electronics and Process Safety – achieved an improved profit performance.

Profits were increased in our FIRE & GAS sector as the mix of products sold was moved towards more profitable products, causing the return on sales to improve. Apollo, our professional smoke detector business, increased sales to almost all territories with particularly impressive sales growth into mainland Europe. R&D has been continuing at a high pace with several new products launched at the beginning of the new financial year. This will lead to a short-term increase in marketing costs, but will allow us to grow market share by providing our customers with a larger range of products and training them in their use. This reinforces customer loyalty which is a strong feature of our fire detection business.

We have been growing sales of gas detectors in the USA and in mainland Europe but experienced reduced volume of sales into the UK. We are concentrating on products with a high ease of use, usually single button operation, that are tough enough to survive the aggressive and hazardous environments where they are used. We also launched new products in May 2003. These include a new range of personal gas monitors for hostile environments. These are potentially life-saving products. Our customers include water, electricity and gas utilities and also telecoms, construction and chemical companies.

Our two strengths in the WATER sector are leak detection and water sterilisation using ultraviolet (UV) light technology. Our leak detection and flow management business is based in the UK and France and is affected by the spending patterns of the water utilities. They have been deferring capital expenditure and the UK water regulator has reduced the emphasis on cutting leakage. Our efforts have therefore increasingly been directed towards the USA where sales are growing, and to other countries where, because of shortages, the wastage of large amounts of clean water through leaks is unacceptable. We are offering technology that is new to some of these territories and we are confident of long-term development even though the start up phase can be relatively slow and resource intensive.

At the end of the financial year we further strengthened our flow measurement activities by the purchase of Radcom which added a strength in measuring flows of dirty water and reporting results by using satellite communications.

In UV sterilisation we take contaminated water and make it fit for use in a variety of applications including for drinking, in swimming pools, as water used for

irrigation, and also to improve the quality and shelf-life of food and drinks. Chlorination of water is not always effective in eliminating parasites and chlorine by-products have been shown to damage both people and buildings. We minimise or eliminate the use of this poisonous gas in many critical applications thereby making a useful contribution to improving the environment. There is growing recognition of the value of this technology and its use is increasing particularly in the USA.

We make a considerable number of products that protect people at work. In our PROCESS SAFETY sector we make pressure relief products and safety systems that ensure machines are safe before people can gain access. We specialise in situations where it is critical that an ordered process is carried out correctly to safely manage the plant, protect the operations and to prevent accidents and emissions.

Growth in profits during the year has been partly driven by some recovery in spending by the petrochemical companies which includes safety spending with us. We are also operating successfully in the USA where safety expectations are rising towards the high levels demanded in Europe. Automotive applications have had a good year as customers have moved, changed, upgraded or made new production lines.

We foresee opportunities to grow our emergency pressure relief operations. We currently have a moderate market share. There are three larger US based competitors, all of whom have a very large installed base, and a big and regular demand for spares. We have a greater dependence on the chemical industry, our largest customer, which has had a slow year for major new process plants. We provide an extraordinarily high level of service and response and thereby are capturing some of our competitors' spares business. We have also been developing products specifically for the food industry, a niche that we can develop into a strong market for us.

As expected, heavy industry in the USA has been slow to improve, such that our RESISTORS sector which is largely based in America, has continued to experience difficult conditions in its biggest market. Accordingly we have moved resource into exports. Sales have grown into the Near, Middle and Far East, and to Africa and Australasia, but this has only partially offset the reductions in US sales. The net effect is a £4 million sales reduction and £1 million profit reduction compared to last year.

Work is continuing on controlling our costs, further increasing exports and managing our working capital. In this sector our assets employed have been reduced by £2 million (22%) in the year and the cash generated used, in part, to purchase BEA. The return on sales reduced from 13% to 11% in our resistors sector, but as a result of good resource management the return on capital employed remained at 36%. In many engineering businesses this return would be considered high even in the best of times.

Because of our range of technologies and broad customer base, we expect to reverse the current trend in resistor sales. However, we will need better export strength or an improvement in American markets to reach previous levels of profit in this particular sector.

Within our OPTICS & SPECIALIST sector we include our ophthalmic diagnosis companies, and a grouping of other subsidiaries along with the national and international holding companies.

Our optics business has held steady in sales and profits, with new products launched last year making useful contributions. There is an increasing level of cross-fertilisation between these companies. The quality of Research & Development, for us mainly development, has been improving and producing a range of new products. Increasingly our customers are becoming more and more careful about cross-contamination of patients, and recently we introduced a number of unique precision aspheric lenses that can be sterilised regularly by high heat levels.

The specialist businesses in this sector have market shares that are lower than elsewhere in the Group. They are more subject to pricing pressures and do not have as much power with suppliers as our market leading companies. To improve profitability we have made a number of changes in the management of several of these companies.

As you travel around the world, automatic doors in elevators and in airports, shops and hotels help to maximise the comfortable and safe flow of people. Our businesses lead the world and hold by far the largest market shares in sensors for automatic doors. We have long held this position for elevator doors. In our ELEVATOR ELECTRONICS sector we also provide controls, displays and emergency communications for elevators and other transit applications.

Active management of costs has been important, particularly because the major US market has remained both dull and steady. By sourcing extrusions, electrical sub-assemblies and mechanical parts in Eastern Europe we have made valuable material cost savings. There is some consolidation of our smaller customers into our larger ones, which changes the pricing mix and offsets our productivity and material cost gains.

In October we purchased BEA. This company is the world market leader in sensors for fixed automatic doors. It is headquartered in Liège, Belgium with a major facility in Pittsburgh USA, an operation in China and offices in Japan and elsewhere. I am very pleased with our managers and BEA's management in the purchase and integration of this operation. My initial targets have been met. BEA brings some new technologies and techniques into the Group and is being effective in transferring their best practice to other companies in the Group. They use a number of innovation techniques that are being reviewed for use elsewhere in the Group.

People

The Group's executive managers would like to associate themselves wholeheartedly with the remarks of David Barber in his Chairman's Statement. We too were greatly saddened by Lord McGowan's death and had a very high regard for Hamish Ritchie. We are very pleased to have attracted Geoff Unwin and Andrew Walker to our Board. I have enjoyed working with Geoff over recent months and I am looking forward to working even more closely with him in the future.

On a personal note, I have learned hugely from David Barber for every one of the last 20 years. He is by any measure a remarkable man, his vision has guided the development of the Group. His enduring contribution includes the assembly and coaching of a management that is committed to exceptional standards. There is a deep seated, results orientated culture in Halma. David provided an outstanding environment for managers to develop and many of us owe much to him.

I would also like to thank executives and managers right the way through the Group, in every country and every company. Most have had to overcome market difficulties, have improved productivity and motivated their staff. Our employees contributed energy, enthusiasm and skill to the companies they work in – many thanks to each of you.

Strategy & Prospects

Our strategy of building high market shares in safety related markets has proved effective and shows in the Group's resilience under the current difficult market conditions. We continue to generate exceptional returns on capital employed, at a record level this year, thereby creating wealth for shareholders. We have again demonstrated the ability to find, complete and integrate related acquisitions successfully. We are creating new products for existing customers and also improving our effectiveness in export markets.

Provided markets remain stable, even at current levels, we expect to achieve sales and profit growth. We are not relying on markets to improve in order to achieve high profits and high returns. We consider the future is in our own hands. Significant new products are being launched at the start of 2003/04. Initially launch costs are incurred but these are high value units so payback is quite rapid.

We are aiming to return to a sequence of record profits.



Stephen R O'Shea

“ . . . entering
the new year
in good shape ”

*Kevin Thompson,
Finance Director*



Financial performance

The full year's turnover of £267 million was held at last year's figure. Profit before taxation and goodwill amortisation was £46.5 million* (2001/02: £48.3 million). Turnover, profit before taxation and return on sales were higher in the second half of the year than the first, without including the benefit of acquisitions. The Group continues to operate at a high rate of profitability with return on sales now exceeding 17% for more than 10 consecutive years.

Relative to Sterling, the weak US dollar and stronger Euro have had an impact on these results. Approximately one-third of turnover and profits are made in US dollars and translating these weaker US dollars into Sterling has reduced turnover and profits by 2.4%, offset a little by the benefit of contributions in stronger Euros.

Looking ahead, I expect some continuation of the increase in insurance costs which we have seen impact the Group in 2002/03, together with higher UK National Insurance and pension costs. In total, I believe these costs will increase overheads by £1.7 million in 2003/04, however a number of initiatives are continuing which will reduce both overhead and material purchase costs and I expect these to mitigate the increases at least in part. We are managing to offset sales price pressures in some markets through improved product design and even better procurement.

Cashflow and Returns

Even by Halma standards, the cash flow performance this year was very good. Free cash flow (the cash left over from our operating activities and interest but after funding capital expenditure, working capital and tax) was £36 million, exceeding the record achieved last year. Excluding currency effects and acquisitions made in the year, stocks were reduced by £3.3 million (9%) following a £5.1 million reduction last year, and working capital in total was pushed down

* see Consolidated Profit and Loss Account

by £8.8 million (13%). We finished the year with net debt of less than £0.1 million after spending £47 million on acquisitions.

Operating cash flow for the year, being cash flow from operating activities less capital expenditure, amounted to £50.9 million. This means that the cash conversion rate (operating cash flow as a percentage of operating profit before goodwill amortisation) was very strong at 110%.

A consistently high return on capital employed has long been a feature of Halma. During the year we converted our cash, which earns a relatively low return, into businesses which earn a much higher return. I am very pleased to report a return on capital employed of 54% this year, the twentieth consecutive year over 40%, and the highest ever year-end figure.

Dividends

Following the 10% increase in the interim dividend, the Directors recommend an increase of 10% in the final dividend per share. If approved, this dividend, amounting to 3.527p per share, will be paid on 18 August 2003 to shareholders on the register at the close of business on 18 July 2003, giving a total dividend for the year of 5.812p. Our excellent cash generation will therefore finance a distribution to shareholders of £21 million for the year.

Tax and Treasury

The effective tax rate on profit before goodwill amortisation has increased from 31.5% to 32.9%, in part due to the increase in income earned in higher tax jurisdictions and in particular that of the BEA companies. I expect an effective tax rate closer to 32% in 2003/04 depending on the exact mix of profits earned around the world.

At 29 March 2003 the Group held currency loans amounting to US dollar 31 million and Euro 10 million. These loans are only for balance sheet hedging purposes, covering the majority of our US dollar and Euro assets.

We do not use complex tax planning schemes nor complex derivative financial instruments. No speculative treasury transactions are undertaken.

Pensions

The triennial valuation of the Group pension schemes was carried out during the year. This showed that the main Group scheme is 69% funded, compared with 97% funding at the 1999 valuation. This reduction arises because of the fall in equity markets and investment returns.

We have increased both employer and employee contributions to the schemes during the year in line with the actuary's recommendations. The charge against profit in 2003/04 will be £1 million higher than this year but there is no need for a further increase in the cash contributions. Under current assumptions the deficit would be eliminated over a 15-year period.

As with many companies, the cost of providing a defined benefit promise to employees has increased significantly in the last few years. The effects of increased longevity, loss of ACT relief and of course the fall in equity valuations more recently have led us to close the defined benefit pension scheme to new members and a defined contribution scheme has now been established.

We have adopted the transitional provisions of FRS 17 (Retirement Benefits) for the year ended 29 March 2003. There is no material difference between the charge to the Group profit and loss account under FRS 17 compared to SSAP 24 (the existing rules). Full adoption of FRS 17 will mean that the net deficit on the Group's defined benefit pension schemes is shown as a liability on the consolidated balance sheet. At 29 March 2003, the deficit, net of deferred tax, was £31 million. This figure reflects the prudent assumptions required under FRS 17 and the significant decline in equity values over the period, and represents a relatively small proportion of Halma's current market capitalisation.

Compliance

High quality finance executives operate within each business, monitoring and assisting progress. In addition to self-certification, each business is subject to regular, comprehensive financial review, carried out by our senior finance staff. The output from these reviews supports the continued improvement in simple, valuable systems and allows us to address any weaknesses found. I am committed to maintaining the strong control in the Group and to increasing the pace of improvement even further.

During the year we carried out a review of our audit services and appointed Deloitte & Touche as our auditors. I am pleased with the quality of service they are able to provide to us.

BEA Acquisition

The BEA group of companies was acquired in October 2002. At the company level, BEA's pre-tax return on its operating assets is in excess of 70%. Its contribution to pre-tax profit in the year, net of the cost of financing the acquisition, was £2.1 million and is of course strongly earnings enhancing. Including deferred consideration earned up to March 2003 but not including the cash we acquired, the purchase price is £46 million and the post-tax return on investment for the period we have owned BEA is 8.3%. We bought BEA for its long-term benefits but this figure still compares well with our cost of capital which has been calculated as falling in the range of 7% to 8.5%. This was a strong acquisition.

Value Creation

We are entering the new year in good shape. Returns and cash flow remain strong and we have minimal net debt. Good financial controls are embedded in the Group. It is against this background that we will push to increase the pace of improvement even further and continue to focus on the creation of value.

