Chairman's statement

Thirty years of dividend growth of 5% or more per annum

Geoff Unwin
Chairman

Introduction

This financial year marks an historic milestone for Halma. Subject to shareholders approving the final recommended dividend of 4.78p per share, an increase of 5% for the year, this will be the thirtieth consecutive year of dividend increases of 5% p.a. or more, which we believe is a record for our sector.

I thought it might be useful to reflect on some of the important principles which have contributed to that performance over the three decades.

- Firstly, we invest in companies with robust market drivers, making products which target non-discretionary spend where it is difficult for competitors to get into the market and where value far exceeds costs thereby helping to drive strong margins.
- Secondly, our management philosophy is to devolve responsibility for all aspects of performance to the individual companies themselves. This keeps them close to their markets, understanding customer needs and driving strong innovation where it counts – in the market.
- Thirdly, we standardise reporting and risk assessment across all companies.
- Fourthly, as a result, we produce good returns on total invested capital (this year 13.1%) and generate cash which we use to finance dividends, and the balance we reinvest in the businesses themselves or invest in acquiring more companies which meet these business criteria.

Reading this, you might think that all sounds rather obvious – why don't more companies do it? Some do. The difference perhaps is that we stick to it, because we believe it works. Take one example: surely we do not need so many managing directors, finance directors and so on; why not consolidate dramatically and save swathes of cost? The answer is that we could do and occasionally we will consolidate two or more companies. However, in the process of consolidation, typically what happens is that everyone becomes internally focused, attention on the market reduces, innovation falters and ground is lost (often permanently) all for a transient one-off cost saving.

Having said that, we are not frozen in time, we continually question the basics and change where needed. Some examples of this over the last few years are:

Geographic markets

We have seen recently the strong emergence of the developing economies. However, if like many of our companies you had little or no experience of operating there, where would you start? Our response was to set up hubs in China and more recently India, to help our individual companies enter the market. In effect, making the water slightly warmer for them. As a result, for example, we started with three and now have nineteen companies operating in China and last year our sales there increased by 25%.

Innovation

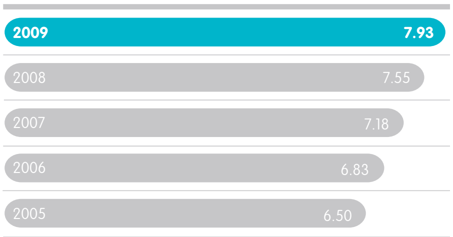
The pace of change gets faster by the day and advances in technology are there to be seized. Within the Group we have strong pockets of deep expertise in many domains and recognise that certain technologies and techniques have applications across the Group in more than just the originating company. So this year we hosted an innovation event to encourage the cross-fertilisation of ideas, which in turn we believe will increase the speed and effectiveness of innovation across the Group.

2009 CORPORATE RESPONSIBILITY ACHIEVEMENTS

What we said	What we've achieved
1. Measurement and reporting of our carbon footprint	Halma's carbon policy was approved by the Board in 2007 and calls for a 10% reduction in the carbon footprint by 2010. To date our consumption has reduced by 7%.
2. Establishment of non-financial KPI in respect of the workplace	Halma conducts an annual survey of our employees to assess how well our espoused values are present in our organisation. This year's survey showed continuing good alignments.
3. Continuing development of our people	The Halma Executive Development Programme and the Management Development Programme, aimed at middle-managers, continue whilst further training is taking place at lower levels within subsidiary companies.
4. Emphasis on business ethics	Since 2007, the Group has formally adopted Group-wide policies on human rights and business practices to reinforce the strong ethical culture already prevalent throughout the Group.
5. Maintenance of the composition and balance of the Board	The Board appointed an internal successor for a retiring executive Director bringing a new US perspective and additional expertise of our Health and Analysis sector.

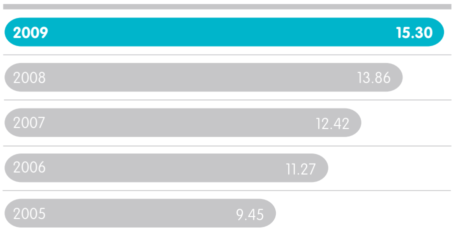
DIVIDENDS PER SHARE (PAID & PROPOSED)
pence

7.93p +5%



ADJUSTED EARNINGS PER SHARE[1]
pence

15.30p +10%



People development
Our results are a function of the dedication, capability and quality of our people. Over the last few years we have significantly increased our investment in training, running tailor-made programmes for our key people. Increasingly, we have been looking to promote from within, which in turn improves the career prospects for all.

In summary, the Group has very strong, sound foundations which we continuously seek to improve without eroding them. It is these values which have driven our performance consistently over three decades.

Halma: what we do and our strategy
Our business is to make products which protect lives and improve the quality of life for people worldwide. We do this through continuous innovation in market-leading products which meet the increasing demands for improvements to health, safety and the environment. We build strong positions in niche markets where the demand is global. Our businesses are autonomous and highly entrepreneurial.

Strategically we aim to grow profit and revenue in excess of 5% p.a. organically, to have Return on sales in the region of 18% or above and generate post-tax Return on total invested capital of more than 12%. As a result we are highly cash generative and reinvest in our businesses through people, product and market development, continue to acquire more companies with like characteristics, and strive to give annual dividend growth of 5% or more to our shareholders.

Results
Unsurprisingly, the second half saw a weakening in our order intake (the detail is provided in Andrew Williams' report) and action was taken, where necessary, across the Group to bring costs in line with new levels of demand. Nevertheless, full year revenue from continuing operations increased 15.4% to £455.9m (2008: £395.1m) underlying organic revenue growth[1] was 10.7% with currency having a net impact of 8.2%, i.e. 2.5% organic growth at constant currency. Profit before tax and amortisation of acquired intangibles on continuing operations was £79.1m (2008: £72.8m), an increase of 8.7% and organic profit growth[1] was 5.1%, at constant currency a decline of 3.3%. Statutory profit before tax increased 7.0% to £72.8m. The Board is recommending[2] a final dividend of 4.78p per share, an increase of 5%. Our dividend cover[2] has increased to 1.93 times (2008: 1.83 times). Return on total invested capital was 13.1% (2008: 14.1%).

Acquisitions and disposals
During the year we acquired Fiberguide Industries, which manufactures optical fibre cables and assemblies, for an initial cash payment of $14m. We also purchased the business and assets of Oerlikon Optics USA Inc.'s operation located in Golden, Colorado, USA for $6m in cash, a business which designs and manufactures optical coatings and optomechanical assemblies and which will operate as part of the newly created Ocean Thin Films, Inc. These two new businesses form part of our Photonics sub-sector within the Health and Analysis sector. There were two very small disposals in the year. Details are included in the Chief Executive's review and Financial review.

Governance
Other than Adam Meyers' appointment to the Board at the beginning of the year and Keith Roy's retirement at the 2008 AGM, there have been no changes at Board level during the year.

People
The second half in particular has been testing for all of us for the economic reasons which saturate our news channels daily. In these uncertain times, people across the Group have reacted to adjust to the circumstances they find in the markets. Often this has been difficult and trying. I give my sincere appreciation and thanks to them all.

Outlook
Visibility in most of our markets is still limited. Different countries, sectors and products are at differing places in the economic cycle. Therefore, we are encouraging all our management teams to react to their markets as they see fit, keeping costs in line with order intake, but not cutting back on vital product investment. When we see improving demand, our operational gearing should show through strongly. In the meantime, we will concentrate on delivering the high level of returns and cash generation that have been the cornerstone of our resilience over 30 years.

Geoff Unwin
Chairman

1 See Financial highlights
2 Subject to the approval of this year's recommended dividend increase at the AGM on 30 July 2009

Chief Executive's review

Our balanced approach of maintaining short-term returns and protecting medium-term growth will continue through the coming year

Andrew Williams
Chief Executive

Revenue and profit growth

Revenue for the full year increased by 15% to a record £455.9m (2008: £395.1m) with underlying organic revenue growth of 11% (after excluding acquisitions). Profit[1] for the full year grew by 9% to a record £79.1m (2008: £72.8m) with underlying organic profit growth[1] of 5% (after excluding acquisitions). Our revenue and profit performance both benefited from an 8% positive contribution from currency movements.

In the second half, organic revenue growth was 8%, benefiting from a 12% positive impact from currency. Order intake during the same period was 3% lower than revenue.

We operate in diverse markets and macro-economic factors affected each of our markets differently in terms of the scale and timing of their impact. Whilst some of our businesses continued to grow revenues, others were affected by lower demand – for example, due to customers reducing inventory or delaying investment decisions. However, the overall impact of lower revenues in the second half was reduced profitability which required action to reduce costs in those businesses affected. The cost of these actions was £1.2m in 2008/09.

In anticipation of current trading trends continuing, we are taking further steps to reduce costs in early 2009/10. We expect the costs of these further actions to be approximately £2.5m. In combination with the action already taken in 2008/09, we anticipate that we will achieve annualised fixed-cost savings in excess of £15m relative to our overhead base during the second half of 2008/09. These savings are in addition to our continuing activities aimed at product cost reductions through value engineering.

Sector review

Our three reporting sectors all achieved double-digit revenue growth.

Infrastructure Sensors increased revenue by 11% and profit by 16% with underlying organic growth in both revenue and profit at constant currency. There was organic profit growth in all four sub-sectors – Fire Detection, Security Sensors, Automatic Door Sensors and Elevator Safety – although there were differences in the revenue growth levels achieved across geographic regions. For example, our Fire Detection business grew revenue strongly in the UK whilst our Security Sensor business continued to experience soft market conditions there. The majority of our Infrastructure Sensors products are fitted to existing commercial and public buildings to comply with safety regulations. During the year, the impact of the slowdown in new commercial/public building construction was mitigated somewhat by increasing sales into existing buildings – particularly where major customers also refocused their efforts on selling more into existing installations.

Revenue in Health and Analysis grew by 23% whilst profits increased by 3%. Fluid Technology and Health Optics achieved revenue and profit growth. Our Photonics business was adversely affected by high overhead costs and delayed new products (now launched) whilst our Water business suffered a major reduction in UK demand. As expected, UK water utilities reduced capital expenditure in year four of their five-year investment cycle but a number also delayed investment due to concerns over constraints within their business. As highlighted in our February Interim Management Statement, significant action was taken in both Photonics and Water to improve profitability. These actions included senior management changes, organisational restructuring and headcount reduction. We anticipate seeing the benefits of these actions come through most strongly in the second half of 2009/10.

Our Industrial Safety businesses delivered a good performance with revenue up 12% and profit up 14%. There was underlying organic growth in both revenue and profit at constant currency. There were particularly strong returns from Gas Detection and Safety Interlocks. Our Bursting Disk businesses grew market share and implemented common manufacturing and sales processes which improved their competitiveness. Following good growth in recent years, Asset Monitoring experienced weaker demand for subsea survey products in the North Sea due to some customers delaying major survey projects.

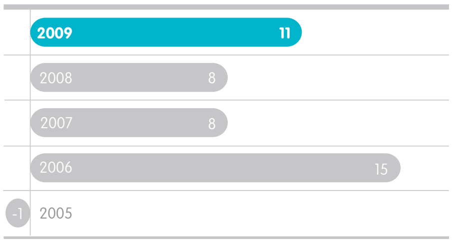
Growing revenue in export markets

Double-digit revenue growth was achieved in all major geographic regions except the UK where revenue fell by 4% mainly due to weakness in our Water, Security Sensor and Asset Monitoring businesses. It was encouraging that we were able to mitigate the impact of this reduction in UK revenue with continued growth in international markets. Revenue outside our traditional operating bases of the USA, UK and Mainland Europe increased by 31% and now represents 22% of Group revenue (2008: 19%). International expansion remains one of our key strategic objectives.

It was pleasing to see revenue from China grow by a further 25% this year to £12m, building on the success of the Halma hubs established there in 2006 (at which time our annualised revenue was £6m). Our new manufacturing hub in Shanghai is operational and an additional three companies are starting to build their products in the region for the first time.

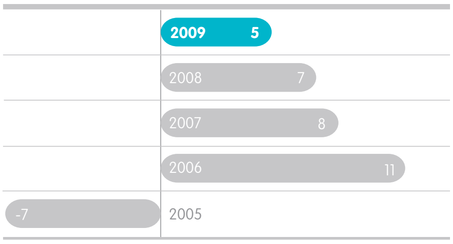
2009 ORGANIC REVENUE GROWTH[1]
%

11%



2009 ORGANIC PROFIT GROWTH[1]
%

5%



In September 2008, we launched a new Halma hub in Mumbai, India where we are recruiting commercial and technical staff for Group companies in all three sectors. We remain committed to increasing our revenues from developing markets. In the coming year, we will continue to make modest investments towards achieving this goal.

Acquisitions and disposals

We made two acquisitions and two small disposals during the year.

Our two acquisitions added new technology and products to our Photonics business. In September 2008 we acquired Fiberguide Industries, a manufacturer of specialist fibre optic components, for $14m. In November 2008 we acquired the Colorado operating assets of Oerlikon Optics USA for $6m, adding new optical coating capabilities and capacity to our existing Ocean Thin Films business. Fiberguide is based in New Jersey, USA and Oerlikon in Colorado, USA. Since acquisition, both businesses have required some reorganisation which is now substantially complete and both are expected to be earnings enhancing in 2009/10.

In January 2009, we sold the assets of the South African based portion of our Security business, Texecom, to local management at book value. This significantly simplified our continuing security business whilst maintaining strong distribution channels in an important territory.

In February 2009, we sold our remaining high-power resistor business, Fortress Systems Pty based in Melbourne, Australia, to Telema SpA based in Milan, Italy for Aus$2.6m. Prior to this disposal, Fortress Systems also distributed our Safety Interlock products and we have merged this retained activity under the management of Fortress Interlocks, UK.

A strong balance sheet

We ended the year with a strong balance sheet and net debt of £51m (2008: £44m). Our bank facilities are in place until 2013. This gives us plenty of headroom within our core borrowing facilities of £165m to invest in existing businesses and in acquisitions. Our cash generation throughout the year was satisfactory, although the effect of currency exchange rate changes increased the value of our loans by £17m. Almost all of our borrowings are in Euro and US Dollars and financed the recent acquisitions in Europe and the USA.

Capital expenditure in existing operations increased by 7% to £16.8m (2008: £15.7m) as our companies continued to invest in their business to maintain high returns. The average return on capital employed in our operating companies was 56%.

Innovation maintains high returns

Halma's resilience over the years is reflected in our ability to maintain high returns. Key to this is our investment in value engineering existing products and developing new products. It is pleasing to report that, despite tougher market conditions this year, our product margins were robust. In Halma, product pricing is determined within each operating company and is typically based on the 'value' to customers. Looking ahead, we are not complacent and our efforts to maintain healthy returns continue apace. This year our expenditure on R&D increased by 23% to £22.9m, equivalent to 5% of revenue (2008: 4.7%).

Encouraging more collaboration inside Halma

Following the period end, in May 2009 we held our first Innovation and Technology Exposition. For the first time, the senior managers from all Halma companies were brought together in one location to identify new collaboration opportunities by sharing their expertise in technology, manufacturing, finance, sales and marketing. In recent years, we have been encouraging more interaction between Halma companies and this event showed that we have benefited from this already but still have a lot of new opportunities. Further details are included on pages 39 to 41 of this report and, in future, I hope to highlight a number of successful new products or significant process improvements which were first initiated at this inaugural event.

Corporate responsibility and sustainability

Halma's commitment to the environment, safety and improving the quality of life for individuals continues to be reflected in both the way we do business and the products we create for our customers.

Our 'operational' commitment is shown in greater detail in the Corporate responsibility review including the clear objectives we set ourselves in areas ranging from carbon policy to the safety of our employees. We set objectives because they make good business sense. These are regularly reviewed and, where necessary, acted upon by the Board.

The positive impact that our products have on society and the environment is significant and is a source of satisfaction for employees.

Chief Executive's review (continued)

Benefiting from investment in people development

We have continued to benefit from our efforts to develop the quality and depth of management talent throughout the Group. We are committed to maintaining this investment since it not only equips people to lead our businesses through the current market uncertainty but also ensures we have effective succession planning and renewed momentum when markets improve.

The Halma Executive Development Programme (HEDP) is our flagship training programme and has had a major influence on the careers of many of our senior managers since it was launched three years ago. I would like to take this opportunity to record our thanks to Nigel Young, the Executive Board member who successfully led the creation of HEDP, who retired in March 2009. Nigel worked in Halma for many years as a Managing Director and Divisional Chief Executive, and we wish him a long and happy retirement.

Delivering consistently high returns requires not just talented people but leaders who set demanding goals and build strong teams with the commitment and innovation to achieve them. The efforts of all Halma employees to achieve such high standards so consistently is appreciated and I thank all of them for their contributions during the past year.

Outlook

We aim to deliver value to shareholders by growing market share, continuing to deliver high returns, maintaining a strong balance sheet and generating cash. This supports our progressive dividend policy and enables ongoing investment in our existing businesses. We will also continue to invest in selected acquisitions as and when suitable, value-adding opportunities present themselves.

One of Halma's strengths is that we operate in diverse niche markets, which have robust long-term demand drivers and where we build strong global market positions. In the past year, there have been some unexpected and sometimes conflicting market trends. However, this variation in market characteristics also contributes to our resilience since whilst some might be in decline, others continue to trade well or are in the process of recovery.

Currently, we are managing the business on the basis that many of our end markets are unlikely to support organic revenue growth in the coming year. We believe we can grow market share and have a flexible manufacturing base which can cope if revenue grows faster than anticipated. In order to maintain returns and absolute earnings, individual businesses have taken action to reduce direct and indirect costs and the benefits are expected to show through in the second half of the year.

We will continue to invest in innovation, people development and growth in developing markets. Although short-term market demand remains difficult to predict, our balanced approach of maintaining returns by responding quickly to market changes and protecting medium-term growth through disciplined investment will continue through the coming year. Despite the current market conditions, this underpins our confidence in continuing to deliver a resilient performance.

Andrew Williams
Chief Executive

[1] See Financial highlights

PERFORMING AGAINST OUR STRATEGY

WHAT WE SAID	WHAT WE HAVE ACHIEVED
Organic growth to exceed 5% p.a.	11% organic revenue growth and 5% organic profit growth driving record results.
Targeted acquisitions	$20m spent acquiring Fiberguide Industries and Oerlikon Optics USA Inc to add further technology and product strength to our Photonics business within Health and Analysis.
Expand business in Asia	Additional subsidiaries using Halma Shanghai hub and four establishing manufacturing in China for the first time. New hub opened in Mumbai, India. Revenues to Asia Pacific and Australasia grew by 26%.
Continued management development	Two more Halma Executive Development Programmes and four Halma Management Development Programmes completed. New Head of Halma People Development appointed.
Maintain high rate of innovation	Investment in R&D increased by 23% to £22.9m. First ever Halma Innovation and Technology event held in May 2009 to accelerate collaboration between subsidiaries.

WE ADD VALUE THROUGH

Entrepreneurial LEADERSHIP

At Halma's annual Innovation Awards, the Gold Award of £20,000 was presented by Geoff Unwin (Chairman, right) to BEA SA for the company's new Laser Scanner automatic door sensor.

BEA's strategy is to diversify and grow sales in new markets and make their business less reliant on the commercial construction sector. Designed to safeguard industrial automatic doors, the unique Laser Scanners' performance exceeds that of competitors' sensors giving them a clear competitive advantage.

"Autonomy in Halma means the freedom to act decisively and take risks. Halma backed our strategy to disrupt the industrial automatic door sensors market and quickly capture a significant share by funding R&D investment in a unique, class-leading laser door sensor."

Philippe Van Genechten,
Managing Director, BEA SA