Financial review

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BRIAN MCCARTHY, FINANCE DIRECTOR

	2009	2008	Change
	£m	£m	£m
Group revenue	142.0	175.1	(33.1)
Operating costs			
Labour	56.9	67.2	(10.3)
Other costs	70.0	85.8	(15.8)
Total operating costs[1]	126.9	153.0	(26.1)
Operating profit[1]	15.1	22.1	(7.0)
Amortisation and impairment	(17.3)	(40.6)	23.3
Net exceptional items	5.4	(4.0)	9.4
Operating profit/(loss)	3.2	(22.5)	25.7
Share of operating results in associate	(0.2)	(0.1)	(0.1)
Impairment of goodwill in associate	-	(0.5)	0.5
Income from investments	0.2	-	0.2
Interest payable	(0.6)	(2.2)	1.6
Other finance expense/income	(1.9)	0.1	(2.0)
Profit/(loss) before tax	0.7	(25.2)	25.9

[1]Excluding exceptional items, amortisation and impairment

Revenue at £142.0M (2008: £175.1m) was £33.1m (18.9%) lower than 2008. Operating profit before amortisation and impairment of intangible assets and exceptional items fell by £7.0m (31.8%) to £15.1m (2008: £22.1m). Total cost savings in the business were £26.1m, a saving of 17.1% over 2008.

The two halves of 2009 produced markedly different results. The rate of revenue decline almost halved from 24.4% to 12.7% between the first and second halves of the year, with July to December revenues 0.7% higher than the six months to the end of June. The cost saving decisions in the first half of the year meant that second half operating profits in 2009 were 11.2% better than the previous year, compared to an operating profit decline of 61.6% in the first half of the year. At £10.1m, operating profit in the second half of the year was double that of the first half.

The decline in operating results, the paucity of merger and acquisition activity in the sector, and the continuing negative view of stock markets on the value of media businesses have had a negative effect on the valuation of businesses that were acquired in the past. The resulting impairment charge of £12.4m (2008: £33.6m) has no cash impact.

Exceptional items increased profit by £5.4m (2008: loss £4.0m). This profit arose principally from the changes to the defined benefit pension scheme, resulting in a one-off credit of £10.0m, off-setting £4.0m of restructuring costs and other one-off costs of £0.6m.

Interest payable at £0.6m was £1.6m lower than 2008 due to lower interest rates and a fall in average net debt. A £1.9m charge (2008: £0.1m credit) is shown as other finance expense in the profit and loss account. This arises from the expected return on pension scheme assets relative to the interest charge on scheme liabilities under the FRS 17 accounting standard.

The corporation tax charge before impairment of intangible assets was £5.0m (2008: £4.1m) resulting in an effective tax rate of 38.6% (2008: 48.3%). The loss after charging impairment and tax was £3.2m (2008: loss £24.1m). Adjusted earnings per share, which reflect the underlying performance of the business, were down 40.4p (38.4%) at 64.7p whilst basic loss per share improved by 149.7p from (172.5p) to (22.8p).

In December 2009, the Group completed a refinancing of its bank facilities through to April 2013 following the expiry of its previous five year facility. In a challenging banking market, the Group secured a £50.0m facility which gives the Group a secure cash position and it retains sufficient headroom for development opportunities.

Net debt at the end of the year was £27.5m (2008: £34.6m) after capital expenditure of £2.6m.

Summary of divisional operating results

The revenue and operating profit before amortisation, impairment and exceptional items were:

	Turnover 2009	Turnover 2008	Operating profit 2009	Operating profit 2008
	£m	£m	£m	£m
Newspapers & printing	98.4	121.6	10.7	16.2
Magazines & contract publishing	43.6	53.5	5.2	5.8
Common costs	-	-	(0.8)	0.1
	142.0	175.1	15.1	22.1

Key performance indicators (KPIs)

The key financial and non-financial performance indicators for the Group include revenue, operating profit, operating margin, advertising volumes, circulation volumes and unique users on-line. The Group seeks to target performance in line with or ahead of competitors.

Details of the Group's performance against the relevant KPIs for each division are included in the respective sections below.

Newspapers and printing

Trading conditions in UK regional newspapers had their low point in the first quarter of 2009, with each subsequent quarter showing relatively lower rates of decline.

During the year like-for-like newspaper and printing revenues fell by £23.3m (19.1%) to £98.4m (2008: £121.6m).

All categories of advertising had their best performance in the fourth quarter of the year. Percentage declines were in double digits in recruitment only, while display advertising achieved growth in the same period. Property revenues improved steadily over the year. Digital revenue continued to grow strongly, with improvements particularly in family announcements, display and on-line classified advertising, where the digital performance on jobs was relatively better than the results in print.

The month of December was ahead overall, a trend which has continued into January.

Advertising year-on-year

	Full year	1st half	2nd half
Recruitment	(44.1%)	(49.4%)	(36.0%)
Property	(35.8%)	(47.3%)	(16.5%)
Motors	(23.0%)	(29.8%)	(14.3%)
Classified	(4.0%)	(2.0%)	(6.0%)
Display	(10.4%)	(15.6%)	(4.9%)
Other	(17.7%)	(25.5%)	(8.8%)
All advertising	(22.4%)	(29.5%)	(13.6%)

Like-for-like circulation volumes for paid-for newspapers declined by 5.3% over the year; evening titles have continued to struggle to retain their position in the face of changing lifestyles, and changes in paid-for distribution models in London have reduced our paid-for sales in the capital. Whilst recognising the brand capital in our paid-for titles, Archant's overall audience is not solely comprised of paid-for titles and we have exploited strong brand relationships in the digital audiences for both our paid-for and free newspaper titles – with unique visitors growing by 39.0% in the year. Circulation revenue from newspapers was down by 5.5% on 2008.

Operating costs at £87.7m (2008: £105.4m) were down £17.7m (16.8%), following concerted actions to reduce all costs in the face of falling revenues. All cost categories showed year-on-year reductions, even with an average newsprint increase of 14.6%. The savings in employment costs were driven by a reduction in full time equivalent staff numbers of 18.1%. Further savings were made as a result of lower paginations as advertising fell, reductions in ink prices and property exits.

Like-for-like operating profit was down 34.3% at £10.7m (2008: £16.2m).

Magazines and contract publishing

Revenues were £43.6m (2008: £53.5m) down £9.9m (18.5%) and operating profit lower by just £0.6m (10.7%) at £5.2m.

The effects of recession brought pressure to bear on all magazine revenues, however it was pleasing to note that Archant Life's subscription revenues increased by 20.2% in the year well in excess of market trends. Advertising revenue fell in all categories over the full year, however trends both in display and property improved over the course of the year, with fourth quarter performance, and December in particular, showing strong like-for-like growth.

Archant Life's revenues declined 19.8% on a like-for-like basis in 2009, with overall circulation revenues down 6.2%, and advertising 22.3% lower. Costs were reduced by 18.1% principally on costs for printing and paper, employment and premises.

Archant Specialist revenues were down 14.4% on a like-for-like basis, with continuing challenges in the French property market. Circulation revenues fell by 5.5%, with advertising revenues excluding the France titles down 15.6%. Costs on a like-for-like basis were reduced by 17.3%, again principally on costs for printing and paper, employment and premises.

Archant Dialogue revenues fell 7.2% offset by cost reductions of 2.6%.

Digital activity

Despite the challenges faced in the recruitment marketplace, revenue from on-line activities increased by 25.2% to £4.7m (2008: £3.8m), mainly driven by revenue from *jobs24*, on-line family announcements and display advertising sales. The key non-financial measures of on-line activity – unique visitors and page impressions – increased by 36.6% and 19.2% respectively. More than 2.4 million people on average visit Archant websites every month.

Impairment of newspaper and magazine intangible assets

The Group is required to review the carrying value of all its intangible assets annually, to determine whether either events or changes in circumstances indicate that the carrying value may not be recoverable. The carrying value is assessed by a number of measures – principally forecast cash flows – which are discounted in line with the Group's cost of capital.

Archant newspaper intangible assets had a pre-impairment carrying value at 31 December 2009 of £32.3m, of which £24.2m relates to titles in London. These titles were acquired from HCN in 1998, INM in 2003 and Highbury House in 2005. The carrying value for the London newspaper titles is no longer supported by their underlying profit performance. In addition, the carrying value of elements of the Herts portfolio, which also formed

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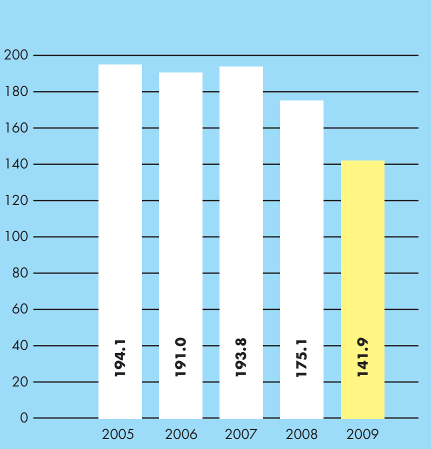
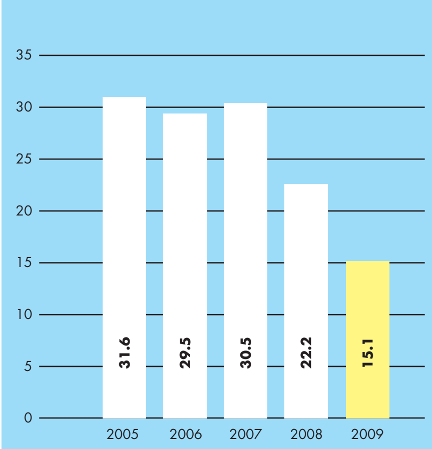
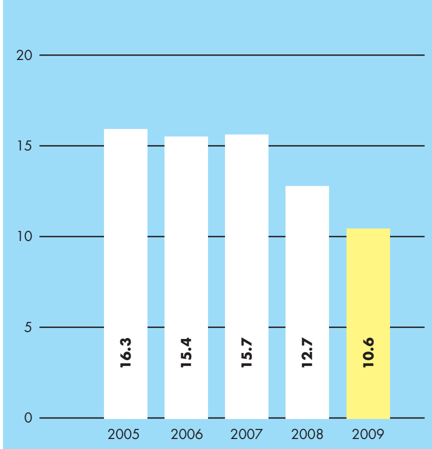


Group turnover £m



Group operating profit £m

* before amortisation, impairment and exceptional items



Group operating margin %

* before amortisation, impairment and exceptional items

part of the HCN acquisition in 1998, have underperformed in the year and an impairment charge has also been applied to these titles. Total newspaper impairment charges of £10.1m have therefore been made during the year. A further charge of £2.3m has been made in respect of certain magazines as detailed in Note 12 to the financial statements.

The impairment charge has no cash impact, but reduces distributable reserves which were £55.0m at the end of 2009 before the impairment charge. The Group's annual dividend payment at its current level is more than adequately covered by the profits generated from normal trading, and distributable reserves after the impairment charge are £43.8m.

Associated companies

During the year the Group made a further £300,000 investment (2008: £215,000) in its associate, KoS Media (Holdings) Ltd, publisher of a number of newspaper and digital titles in Kent, including Kent on Sunday. Archant's share of the associate's losses grew from £158,000 to £196,000 owing to the shortfall in advertising revenues, with the second half of the year an improvement on the first.

Exceptional items

Exceptional costs (excluding impairment) were £4.0m (2008: £4.0m) in respect of the costs of reducing the size of the business – principally redundancy and office closure costs, together with £0.2m of one-off costs relating to the refinancing and £0.3m in respect of the costs of restructuring the defined benefit pension scheme to reduce the rate of growth in future liabilities and reduce the provision in the valuation for inflationary increases on accrued benefits. The restructuring of the pension scheme has resulted in a one-off exceptional credit of £10.0m included in the profit and loss account. The pension changes have no immediate cash flow impact, other than through reduced pension contributions in future years, are not subject to current taxes and reduce the overall pension deficit.

Taxation

The financial statements include a tax charge of £3.8m (2008: credit £1.1m). The pre-impairment effective rate of taxation for the year was 38.6% (2008: 48.3%), and the effective standard rate of tax was 28.0% (2008: 28.5%). The 2009 pre-impairment effective rate was higher than the standard rate due primarily to amortisation of intangible assets that is not deductible for tax purposes, offset by the deferred tax credit on the pension benefit changes outlined above.

Earnings per share

Basic loss per share fell by 87% from last year's 172.5p to 22.8p. Adjusted earnings per share fell by 40.4p (38.4%) to 64.7p. Adjusted earnings per share are considered to be a better indicator of the underlying performance of the business and the difference between basic and adjusted earnings per share is explained in more detail in Note 11 to the financial statements.

Dividends and dividend cover

No final dividend is proposed for 2009. In its place, a first interim dividend for 2010 will be paid on 18 March 2010 at the rate of 13.7p per share. If this dividend was treated as being in respect of 2009, the total dividend for the year would be 20.1p (2008: 26.4p). At this level the dividend would be covered 3.2 times (2008: 4.0 times) by adjusted earnings per share.

Net debt and cash flow

The Group continues to be cash generative and operating cash flow at £14.3m (2008: £26.4m) was £12.1m lower than in 2008 mainly due to a reduction of £7.0m in pre-impairment operating profit. Conversion of profit (before impairment and one-off pension credit) into cash at 257% was again strong (2008: 237%). Net debt at the end of the year was £27.5m (2008: £34.6m). Movements in net debt are summarised below:

	2009	2008
	£m	£m
Operating cash flow	14.3	26.4
Net interest paid	(0.4)	(2.1)
Tax paid	(0.9)	(5.4)
Dividends paid	(2.8)	(5.6)
Cash flow before acquisitions and capital expenditure	10.2	13.3
Capital expenditure	(2.6)	(7.8)
Sale of fixed assets	0.0	0.2
Acquisitions and investment in associate	(0.3)	(2.4)
Share transactions	(0.1)	(1.0)
Other	(0.1)	-
Decrease in net debt	7.1	2.3

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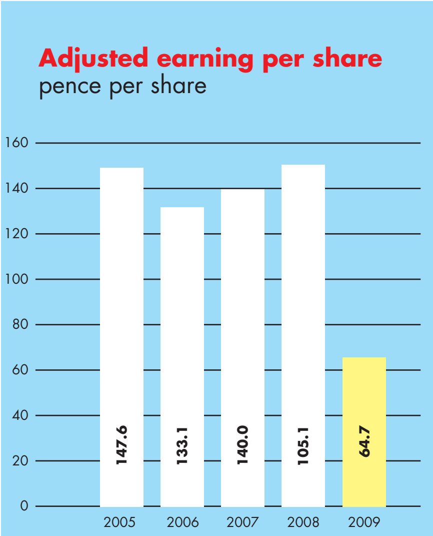
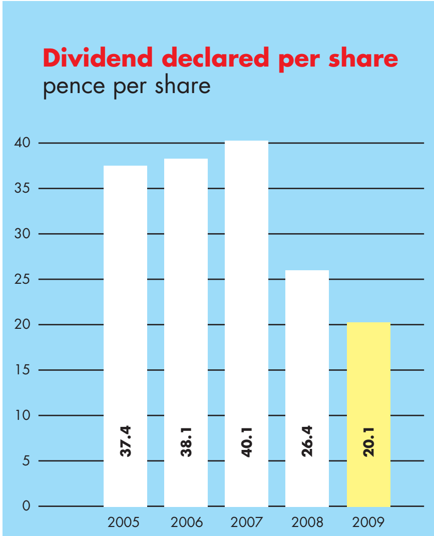
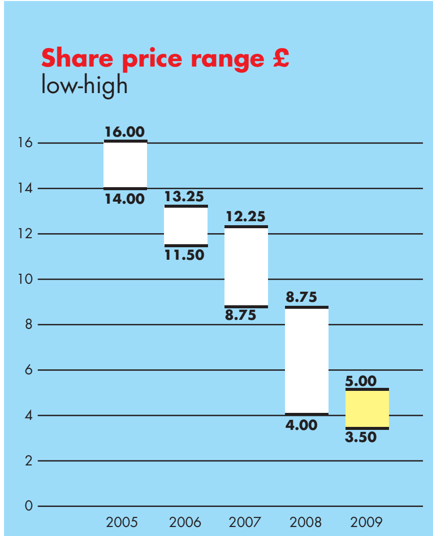


* before amortisation, impairment and exceptional items



* 2009 includes 1st Interim for 2010 for comparative purposes.



Capital expenditure

Capital expenditure during the year was £2.6m (2008: £7.8m) substantially all of which related to investment in IT hardware and software development costs which will improve operating efficiency and system resilience in future years. The expansion to the print plant at Thorpe and the closure of the Ipswich print plant were completed during the year in line with the planned budget and timetable.

Pension scheme

The triennial actuarial valuation completed in 2008 indicated that liabilities of the Group's pension scheme of £148.6m were under-funded by £8.0m as at 1 January 2008. The Group made cash contributions totalling £1.45m towards the reduction of this deficit in 2009 (2008: £0.75m). The deficit shown in the balance sheet was determined using the FRS 17 accounting standard, which the Group adopted in 2005. Under this standard, the defined benefit scheme service cost in the profit and loss account has decreased by £0.4m to £1.7m and the deficit shown on the balance sheet has fallen by £11.1m, from £25.9m to £14.7m.The fall in the deficit is a result of a combination of a recovery in investment markets and increased gilt yields, which have reduced the valuation of liabilities. In addition, liabilities have been reduced by £10.0m (before deferred taxation) relating to the change in future benefits attributable to members of the final salary schemes. As the liabilities of the pension scheme are expected to fall due over a period of more than 50 years and the deficit is close to one year's current operating profit before amortisation, the deficit is not considered onerous.

Treasury management, associated risks and uncertainties

The Group currently derives its funding from share capital, retained profits and bank borrowing. Cash is managed centrally, and the Group's treasury objective is to minimise borrowing costs and maximise returns on funds subject to short-term liquidity requirements.

The main risks that the Group faces from its treasury activities are liquidity risk and interest rate risk. The Group's activities are primarily in the UK and there is minimal foreign currency risk.

Our liquidity risk arises from timing differences between cash inflows and outflows. These risks are managed through unutilised committed and uncommitted credit facilities. Our policy is to ensure continuity of funding and flexibility and to maintain sufficient cash balances and committed facilities to meet anticipated funding requirements. Our resources and the expected future cash flows are regarded as sufficient to meet the anticipated funding requirements of the Group for at least the next 12 months.

The Group successfully refinanced its debt in December 2009, following the expiry of its previous debt facility. A total facility of £50.0m was raised in a challenging banking environment. The Group secured a £45.0m revolving advances facility which expires in April 2013 through RBS and Bank of Ireland and a £5.0m overdraft facility from RBS at competitive rates of interest. The maximum amount of the revolving credit facility will be reduced to £36.0m by 1 January 2013, by equal annual reductions on 1 January in each of years 2011 to 2013. During the year the Company, which had acted as guarantor for the Employee Benefit Trust's overdraft facility, replaced that overdraft with a loan from the Company to the Employee Benefit Trust. In January 2010 the company entered into interest rate swap arrangements covering £15.0m of its debt obligations, expiring in December 2011, to limit the company's exposure to interest rate risk.

Net assets

Net assets on 1 January 2009 were £55.0m. The loss for the year was £3.2m, which was transferred to reserves. Other movements included an increase of £4.2m arising from the FRS 17 Retirement Benefits accounting standard and dividend payments of £2.8m. Net assets at the end of the year were £53.1m.