

Financial review

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2006 was another challenging year for Archant. The decline in consumer advertising which started in 2005 continued through 2006, although the rate of decline slowed in the second half of the year, and there were steep increases in paper and energy prices for the second year running. Significant effort was focused on improving productivity, resulting in a substantial reduction in underlying costs. The Group continued to invest for the future, with further magazine acquisitions, the refurbishment of Prospect House in Norwich and increased investment in IS, in particular the homes24 and jobs24 on-line classified advertising services.

Revenue at £191.0m (2005: £194.1m) was £2.9m (1.6 per cent) lower than 2005, mainly as a result of lower newspaper advertising sales. Magazine revenue increased by 13.2 per cent to £49.9m (2005: £44.1m). Operating profit before amortisation of intangibles and exceptional costs fell by £2.1m (6.8 per cent) to £29.5m. Year-on-year performance improved during the second half and operating profit before amortisation and exceptional items for the six months to the end of December was up 3.3 per cent on the same period in 2005.

Amortisation of intangibles increased by £6.0m to £8.6m (2005: £2.6m) as a result of magazine acquisitions and the decision to start amortising newspaper intangible assets. Exceptional items at £0.8m (2005: £2.4m) were £1.6m lower than last year.

Interest payable was £0.3m lower than 2005, due to lower average net debt. Other finance charges were also £0.3m lower, as a result of higher long term bond yields.

Profit before tax at £16.4m (2005: £22.4m) was £6.0m (26.6 per cent) lower than last year. The tax charge was £8.7m (2005: £5.8m), resulting in an effective rate of 53.1 per cent (2005: 25.7 per cent). The increase in the tax rate is due to a one-off deferred tax cost of £2.3m resulting from the decision to amortise newspaper intangible assets and changes in tax legislation at the end of 2005. Profit after tax was £8.9m lower at £7.7m (2005: £16.6m). Adjusted earnings per share, which reflect the underlying performance of the business, were down 14.5p (9.8 per cent) at 133.1p. Basic earnings per share decreased

by 63.1p (53.7 per cent) to 54.5p.

Net debt at the end of the year was £54.8m (2005: £59.1m) after acquisitions and capital expenditure of £10.5m.

Summary of divisional operating results

Revenue and operating profit before amortisation and exceptional items were:

	Revenue		Operating profit	
	2006	2005	2006	2005
	£m	£m	£m	£m
Newspapers & printing	141.1	150.0	24.2	27.9
Magazines & contract publishing	49.9	44.1	6.1	5.0
Common costs	-	-	(0.9)	(1.3)
	191.0	194.1	29.4	31.6

Newspapers and printing

Trading conditions for UK regional newspapers were difficult again in 2006, with profits impacted by declining advertising revenue and increases in newsprint and energy prices. The Group has responded to these conditions by accelerating the development of its lifestyle magazines and on-line revenue streams, as well as by implementing productivity improvement and other cost saving projects in most areas of the business. Performance improved in the second half of the year as the rate of revenue decline slowed.

	1st half		2nd half	
	£m	vs 2005	£m	vs 2005
Revenue	72.4	(7.5%)	68.7	(4.3%)
Cost	59.1	(4.1%)	57.8	(4.4%)
Operating profit	13.3	(19.8%)	10.9	(3.7%)

The revenue decline is not expected to continue in 2007 unless there is a material change in the economic outlook. There will be continuing emphasis on controlling costs and, while newsprint and energy price increases are expected to be lower than in 2006, significant pressure is expected on staff costs, which make up 45 per cent of Archant's cost base.

Archant's newspaper and printing revenues decreased by 5.9 per cent to £141.1m (2005: £150.0m) during the year. Advertising revenue declined in all categories other than property, which grew by 6.1 per cent. Classified advertising decline slowed in the second half, while display did not perform as well.

Advertising	Full year	1st half	2nd half
Property	6.1%	5.2%	7.2%
Other classified	(9.3%)	(11.7%)	(6.5%)
Display	(9.8%)	(9.3%)	(10.3%)
Leaflets & other	(3.1%)	(3.0%)	(3.1%)
All advertising	(6.4%)	(7.4%)	(5.2%)

Circulation revenue declined by 3.1 per cent over the year, with a smaller reduction in the second half as a result of price increases in some areas. Other revenue declined by 1.9 per cent in 2006 but improved in the second half.

Operating costs at £116.9m (2005: £122.1m) were down £5.2m (4.3 per cent) as a result of productivity improvements and other cost savings, despite significant increases in newsprint (6.3 per cent) and energy prices. Operating profit decreased by 13.3 per cent to £24.2m (2005: £27.9m) despite the reduction in costs.

Since the end of the year the newspaper business has taken steps to consolidate its presence in Cambridgeshire, with the acquisition of *Agenda*, a lifestyle magazine, and *Property Plus*, a property magazine. We have also reached agreement, conditional on approval from the Office of Fair Trading, to sell our Scottish titles.

Magazines and contract publishing

2006 was another successful year for Archant's magazine and contract publishing businesses, with further acquisitions and a significant increase in operating profit despite the difficult trading conditions. Revenue has now reached £49.9m (2005: £44.1m), an increase of 13.2 per cent, and operating profit increased by £1.2m (23.7 per cent) to £6.1m. Acquisitions made in 2006 contributed £4.8m to the revenue growth and £0.5m of the profit growth.

Archant Life acquired Metropolis, a publisher of free distribution lifestyle magazines in London, during January 2006. This business has been merged with the business acquired from Highbury House in 2005 and, together, they are delivering around 600,000 magazines every month to the most prosperous areas of London. Advent Media, the publisher of six county magazines in the Midlands, was acquired during April 2006, bridging the gap between the Group's county magazines in the north and the south. Archant Life's growth strategy has made further progress since the end of the year with the acquisitions of *Living Edge*, a lifestyle magazine for the southern suburbs of Manchester, and *West Essex Life*, which is focused on the area of north-west Essex just inside the M25.

Amortisation of newspaper intangible assets

All media markets have been subject to accelerating fragmentation during recent years. This means that there are an increasing number of ways for advertisers to reach consumers and for consumers to access news and entertainment. Archant has accelerated the development of its magazine and internet businesses in the last two years in order to capitalise on this trend. One consequence of this fragmentation is that the traditional newspaper titles are unlikely to be able to sustain the same level of profitability indefinitely. The Board has therefore decided that it would be prudent to amortise, over periods not exceeding 20 years, those titles that are currently included on the balance sheet. This brings our policy on newspaper intangible assets into line with our policy on magazine intangible assets.

The decision to amortise newspaper intangible assets will increase the charge to the profit and loss account for amortisation by £5.5m from 2006 in respect of current titles. In addition, there was a one-off £2.3m deferred tax charge in the year, reflecting the difference between the tax and accounting treatment of these assets. There is no impact on cash.

Associated company

During August, the Group made a further £200k investment (2005: £800k) in its associate, a publishing company operating in the UK. Although the associate also suffered from the poor trading conditions during the year, it continued to grow and Archant's share of its losses amounted to £291k (2005: £347k), £56k lower than last year despite the increased share in the company.

Exceptional items

Exceptional items were £1.6m lower in 2006 than 2005 due to lower costs and the profit on the sale of some freehold property. The sale of the office at Campfield Road, St Albans, which was surplus to requirements, generated a profit of £0.5m (2005: £nil). Restructuring costs at £1.3m (2005: £1.8m) were down £0.5m and there was no discretionary pension increase in 2006 (2005: 2.0 per cent), saving £0.6m.

Taxation

The effective rate of taxation for the year was 53.1 per cent (2005: 25.7 per cent). The standard rate of tax was 30.0 per cent (2005: 30.0 per cent). The increase in the effective tax rate was due mainly to the changes in tax legislation at the end of 2005 that were flagged in last year's report (7.3 per cent), the impact of the newspaper intangible amortisation (7.1 per cent) and the one-off deferred tax charge as a result of starting to amortise newspaper intangible assets (13.8 per cent). The 2006 effective rate was higher than the standard rate due mainly to amortisation of intangible assets which was not deductible for tax purposes

(10.3 per cent) and a one-off deferred tax charge in 2006 arising from the decision to start amortising newspaper intangible assets (13.8 per cent).

Earnings per share

Basic earnings per share decreased by 63.1p (53.7 per cent) to 54.5p and adjusted earnings per share decreased by 14.5p (9.8 per cent) to 133.1p. Adjusted earnings per share is intended 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. The major movements during the year are shown in the table below:

	Basic	Adjusted
2005 earnings per share	117.6	147.6
Underlying profit change	(7.0)	(6.1)
Exceptional items	9.2	-
Amortisation of magazine intangibles	(3.6)	-
Change in tax legislation	(8.4)	(8.4)
Sub-total before impact of newspaper amortisation	107.8	133.1
Impact of newspaper intangible asset amortisation		
- Ongoing annual amortisation charge	(37.2)	-
- One-off deferred tax charge in 2006	(16.1)	-
2006 earnings per share	54.5	133.1

Dividends and dividend cover

It is proposed that the dividend for the year be increased to 38.1p. At this level the dividend would be covered 3.5 times (2005: 3.9 times) by adjusted earnings per share and 1.4 times (2005: 3.1 times) by basic earnings per share.

Net debt and cash flow

The Group continues to be cash generative, although operating cash flow at £29.2m (2005: £33.6m) was £4.4m lower than in 2005, mainly due to increased working capital. Profit conversion into cash was again strong at 149 per cent (2005: 126 per cent). The improvement in cash conversion was partly due to the amortisation of newspaper intangible assets in 2006.

Net debt at the end of the year was £54.8m (2005: £59.1m). Movements in net debt are summarised below:

	2006	2005
	£m	£m
Operating cash flow	29.2	33.6
Interest paid	(3.4)	(3.6)
Tax paid	(4.8)	(5.2)
Dividends paid	(5.3)	(5.3)
Other cash flows	0.1	0.0
Cash flow before acquisitions and capital expenditure	15.8	19.5
Capital expenditure	(6.2)	(5.7)
Sale of fixed assets	1.3	0.1
Acquisitions and investment in associate	(5.6)	(15.8)
Issue of new shares and EBT net dealings	(1.1)	0.9
Decrease/(increase) in net debt	4.2	(1.0)

Net debt at the end of the year comprised:

	2006	2005
	£m	£m
Bank and cash balances	2.2	2.6
Bank overdrafts and loans	(55.5)	(59.3)
Loan notes payable	(1.5)	(2.3)
Net debt	(54.8)	(59.0)

The bank overdraft and loans include £2.5m (2005: £0.3m) in relation to the Employee Benefit Trust overdraft which is guaranteed by the Group.

Capital expenditure

Capital expenditure during the year was £6.2m (2005: £5.7m), including £2.9m for the refurbishment of Prospect House in Norwich and £1.5m in respect of information technology.

Pension schemes

The triennial actuarial valuation completed in 2005 indicated that liabilities of the Group's defined benefit pension scheme of £111.6m were underfunded by £6.6m as at 1 January 2005. In 2005 and 2006 the Group made cash contributions to the scheme totalling £1.5m towards the reduction of this deficit. The deficit shown in the balance sheet has been determined using the FRS17 accounting standard which the Group adopted in 2005. Under this standard the defined benefit scheme total cost in the profit and loss account has decreased by £0.1m to £3.1m and the deficit shown on the balance sheet has decreased by £5.3m from £16.8m to £11.5m. As the liabilities of the pension scheme are expected to fall due over a period of more than 50 years and the deficit is less than one year's profit before tax, it is not considered onerous.

New accounting standards and policies

No new accounting standards were adopted during 2006. The decision to start amortising newspaper intangible assets, while material to the Group's results, does not constitute a change of accounting policy.

Treasury management

The Group derives its funding from share capital, retained profits, bank borrowing and the issue of loan notes.

The main risk that the Group faces from its treasury activities is interest rate risk. The Group's activities are primarily in the UK and there is minimal foreign currency risk. The Group's treasury objective is to minimise borrowing costs and maximise returns on funds subject to short term liquidity requirements.

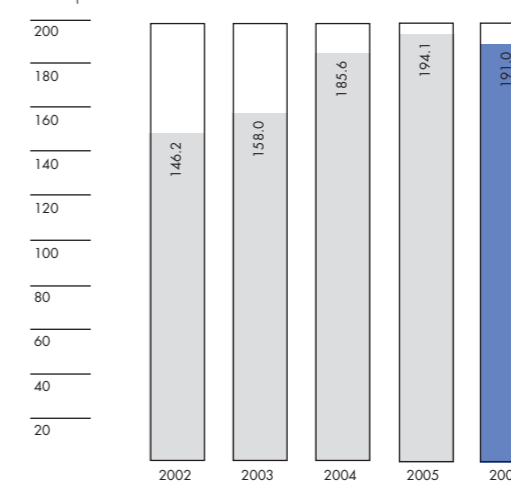
Cash is managed centrally, with surplus balances invested in money market funds. The loan notes payable are £1.5m Archant Lifestyle PLC Loan Notes 2008, which bear interest at 1.0 per cent less than the Barclays Bank base rate plus guarantee costs of 0.45 per cent.

The Group has secured a £105.0m facility from the Royal Bank of Scotland at competitive rates of interest which was used to fund the share buy-back in 2004 and to fund subsequent acquisitions. The Group has a £5.0m overdraft facility from Barclays Bank and acts as guarantor for the Employee Benefit Trust's £3.5m overdraft facility, which is also provided by Barclays Bank.

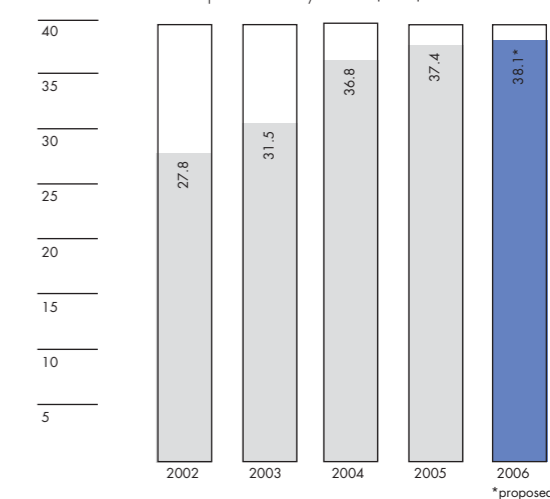
Net assets

Net assets on 1 January 2006 were £103.2m. Retained profit for the year was £7.7m, which was transferred to reserves. Other movements included an increase of £5.7m arising from the FRS17 Retirement Benefits accounting standard and dividend payments of £5.3m. Net assets at the end of the year were £110.2m.

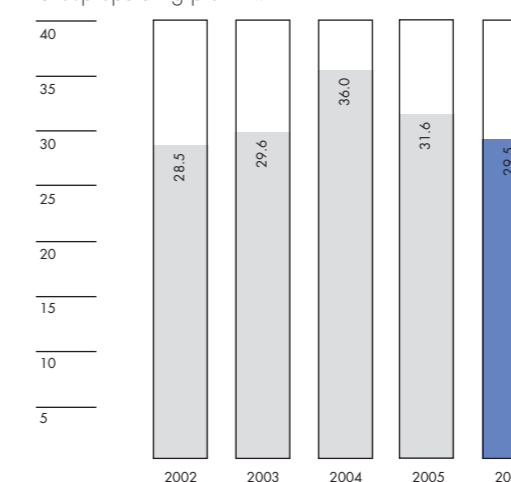
Group turnover £m



Dividend declared per ordinary share pence per share

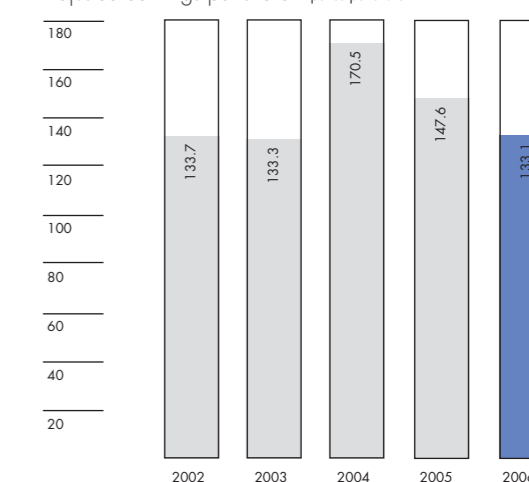


Group operating profit* £m



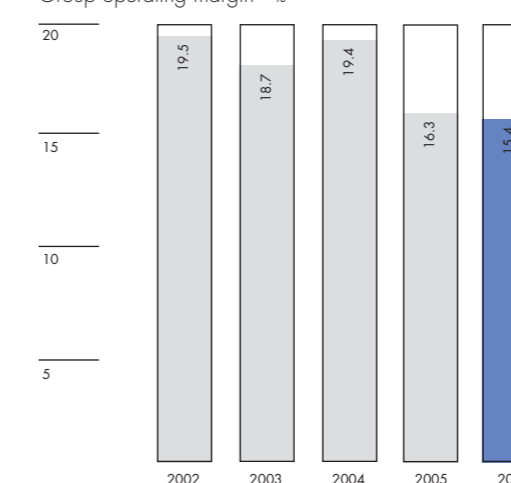
* before amortisation, impairment and exceptional items

Adjusted earnings per share* pence per share



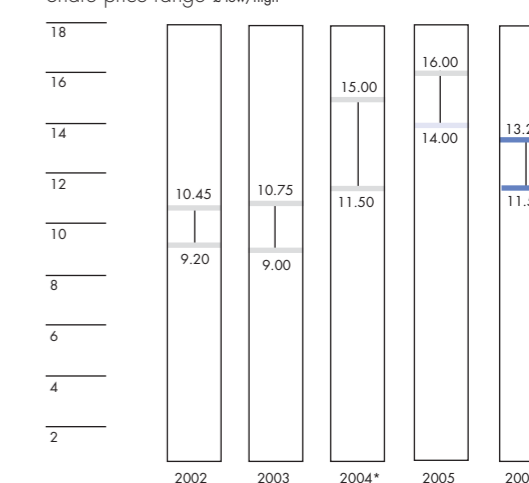
* before amortisation, impairment and exceptional items

Group operating margin* %



* before amortisation, impairment and exceptional items

Share price range £ low/high



* Shares were repurchased under the buy-back at £20.00 per share on 8 December 2004