

Consolidated Income Statement

For the year ended 31 December 2008

| | Notes | 2008 £m | 2007 £m |
|---|-------|------------|------------|
| Sales | 2 | 4,376 | 3,869 |
| <i>Trading profit</i> | | 201 | 277 |
| <i>Restructuring and impairment charges</i> | | (153) | (31) |
| <i>Amortisation of non-operating intangible assets arising on business combinations</i> | | (10) | (8) |
| <i>Profits and losses on sale or closures of businesses</i> | | — | (7) |
| <i>Change in value of derivative and other financial instruments</i> | | (124) | (10) |
| Operating profit/(loss) | 3 | (86) | 221 |
| Share of post-tax earnings of joint ventures | 13 | 6 | 24 |
| Interest payable | 4 | (66) | (62) |
| Interest receivable | 4 | 19 | 19 |
| Other net financing charges | 26 | (3) | (3) |
| Net financing costs | | (50) | (46) |
| Profit/(loss) before taxation | | (130) | 199 |
| Taxation | 5 | 10 | (1) |
| Profit/(loss) from continuing operations | | (120) | 198 |
| Profit after taxation from discontinued operations | 6 | 13 | — |
| Profit/(loss) after taxation for the year | | (107) | 198 |
| Profit attributable to minority interests | | 2 | 2 |
| Profit/(loss) attributable to equity shareholders | | (109) | 196 |
| | | (107) | 198 |
| Earnings per share — p | 7 | | |
| Continuing operations — basic | | (17.3) | 27.9 |
| Continuing operations — diluted | | (17.3) | 27.8 |
| Dividends per share — p | 8 | | |
| Interim dividend per share | | 4.5 | 4.3 |
| Final dividend per share | | — | 9.2 |

Consolidated Statement of Recognised Income and Expense

For the year ended 31 December 2008

| | Notes | 2008 £m | 2007 £m |
|---|-------|------------|------------|
| > | | | |
| Currency variations | | 565 | 66 |
| Derivative financial instruments: | | | |
| Net transactional hedging | 19 | (8) | — |
| Translational hedging | 19 | (213) | (28) |
| Actuarial gains and losses on post-employment obligations: | | | |
| Subsidiaries | 26 | (386) | 224 |
| Joint ventures | | — | 1 |
| Tax on items taken directly to equity | 5 | (23) | (92) |
| Net profits/(losses) not recognised in the income statement | | (65) | 171 |
| Profit/(loss) for the year | | (107) | 198 |
| Total recognised income and expense for the year | 23 | (172) | 369 |
| Total recognised income and expense for the year attributable to: | | | |
| Equity shareholders | | (178) | 365 |
| Minority interests | | 6 | 4 |
| | | (172) | 369 |

Consolidated Balance Sheet

At 31 December 2008

| | Notes | 2008 £m | 2007 £m |
|-----------------------------------|-------|----------------|----------------|
| Assets | | | |
| Non-current assets | | | |
| Goodwill | 11 | 367 | 280 |
| Other intangible assets | 11 | 153 | 136 |
| Property, plant and equipment | 12 | 1,797 | 1,462 |
| Investments in joint ventures | 13 | 119 | 100 |
| Other receivables and investments | 14 | 23 | 22 |
| Deferred tax assets | 5 | 52 | 56 |
| | | 2,511 | 2,056 |
| Current assets | | | |
| Inventories | 15 | 718 | 552 |
| Trade and other receivables | 16 | 645 | 571 |
| Current tax assets | 5 | 17 | 2 |
| Derivative financial instruments | 20 | 62 | 25 |
| Cash and cash equivalents | 18 | 114 | 282 |
| | | 1,556 | 1,432 |
| Total assets | | 4,067 | 3,488 |
| Liabilities | | | |
| Current liabilities | | | |
| Borrowings | 18 | (97) | (92) |
| Derivative financial instruments | 20 | (190) | (30) |
| Trade and other payables | 17 | (972) | (837) |
| Current tax liabilities | 5 | (115) | (104) |
| Provisions | 21 | (49) | (45) |
| | | (1,423) | (1,108) |
| Non-current liabilities | | | |
| Borrowings | 18 | (725) | (696) |
| Derivative financial instruments | 20 | (2) | — |
| Deferred tax liabilities | 5 | (63) | (75) |
| Trade and other payables | 17 | (38) | (31) |
| Provisions | 21 | (54) | (51) |
| Post-employment obligations | 26 | (834) | (331) |
| | | (1,716) | (1,184) |
| Total liabilities | | (3,139) | (2,292) |
| Net assets | | 928 | 1,196 |
| Shareholders' equity | | | |
| Ordinary share capital | 22 | 372 | 372 |
| Share premium account | | 29 | 29 |
| Retained earnings | | 290 | 834 |
| Other reserves | | 214 | (58) |
| | | 905 | 1,177 |
| Minority interests — equity | 23 | 23 | 19 |
| Total equity | | 928 | 1,196 |

The financial statements on pages 74 to 118 were approved by the Board of Directors and authorised for issue on 25 February 2009. They were signed on its behalf by:

Sir Kevin Smith, William C Seeger — Directors

Consolidated Cash Flow Statement

For the year ended 31 December 2008

| | Notes | 2008 £m | 2007 £m |
|---|-------|--------------|--------------|
| Cash flows from operating activities | | | |
| Cash generated from operations | 25 | 328 | 299 |
| Interest received | | 18 | 16 |
| Interest paid | | (66) | (60) |
| Tax paid | | (45) | (28) |
| Dividends received from joint ventures | | 24 | 13 |
| | | 259 | 240 |
| Cash flows from investing activities | | | |
| Purchase of property, plant and equipment | | (192) | (172) |
| Purchase of intangible assets | | (13) | (20) |
| Receipts of government capital grants | | 1 | — |
| Proceeds from sale of fixed assets | | 7 | 21 |
| Acquisition of subsidiaries (net of cash acquired) | | (1) | (71) |
| Proceeds from sale of joint venture — discontinued | 6 | 18 | — |
| Investment in joint ventures | | (1) | — |
| Investment loans and capital contributions | | 1 | 7 |
| | | (180) | (235) |
| Cash flows from financing activities | | | |
| Net proceeds from ordinary share capital transactions | 22 | 1 | 5 |
| Net proceeds from borrowing facilities | | 112 | 13 |
| Finance lease payments | | (9) | (1) |
| Repayment of borrowings | | (33) | (5) |
| Settlement of forward foreign currency contracts for net investment hedging | | (230) | (12) |
| Dividends paid to shareholders | 8 | (97) | (91) |
| Dividends paid to minority interests | | (3) | (1) |
| | | (259) | (92) |
| Currency variations on cash and cash equivalents | | 24 | 9 |
| Movement in cash and cash equivalents | | (156) | (78) |
| Cash and cash equivalents at 1 January | | 250 | 328 |
| Cash and cash equivalents at 31 December | 25 | 94 | 250 |

Notes to the Financial Statements

1 Accounting policies and presentation

The Group's key accounting policies are summarised below.

Basis of preparation and consolidation

The consolidated financial statements (the 'statements') have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed and adopted for use by the European Union. These statements have been prepared using all standards and interpretations required for financial periods beginning 1 January 2008. No standards or interpretations have been adopted before the required implementation date.

No new, amended or revised standards were required to be applied to these statements. IFRIC 11 and 14 have been applied to these statements with no impact. IFRIC 12 also became effective but is not relevant.

These statements have been prepared under the historical cost method except where other measurement bases are required to be applied under IFRS as set out below.

Basis of consolidation

The statements incorporate the financial statements of the Company and its subsidiaries (together 'the Group') and the Group's share of the results and equity of its joint ventures.

Subsidiaries are entities over which, either directly or indirectly, the Company has control through the power to govern financial operating policies so as to obtain benefit from their activities. Except as noted below, this power is accompanied by a shareholding of more than 50% of the voting rights. The results of subsidiaries acquired or sold during the year are included in the Group's results from the date of acquisition or up to the date of disposal. All business combinations are accounted for by the purchase method. Assets, liabilities and contingent liabilities acquired in a business combination are measured at fair value.

In a single case the Company indirectly owns 100% of the voting share capital of an entity but is precluded from exercising either control or joint control by a contractual agreement with the United States Department of Defense. In accordance with IAS 27 this entity has been excluded from the consolidation and treated as an investment. Further details are contained in note 14.

Intra-group balances, transactions, income and expenses are eliminated.

Minority interests represent the portion of shareholders' earnings and equity attributable to third party shareholders.

Joint ventures

Joint ventures are entities in which the Group has a long term interest and exercises joint control with its partners over their financial and operating policies. In all cases voting rights are 50% or lower. Investments in joint ventures are accounted for by the equity method. The Group's share of equity includes goodwill arising on acquisition.

The Group's share of profits and losses resulting from transactions between the Group and joint ventures are eliminated.

Foreign currencies

Subsidiaries and joint ventures account in the currency of their primary economic environment of operation, determined having regard to the currency which mainly influences sales revenue and input costs. Transactions are translated at exchange rates approximating to the rate ruling on the date of the transaction except in the case of material transactions where actual spot rate may be used if it more accurately reflects the underlying substance of the transaction. Where practicable, transactions involving foreign currencies are protected by forward contracts. Assets and liabilities in foreign currencies are translated at the exchange rates ruling at the balance sheet date.

Material foreign currency movements arising on the translation of intra-group balances treated as part of the net investment in a subsidiary are recognised through equity. Movements on other intra-group balances are recognised through the income statement.

The Group's presentational currency is sterling. On consolidation, results and cash flows of foreign subsidiaries and joint ventures are translated to sterling at average exchange rates. Assets and liabilities are translated at the exchange rates ruling at the balance sheet date.

Profits and losses on the realisation of currency net investments include the accumulated net exchange differences that have arisen on the retranslation of the currency net investments since 1 January 2004 up to the date of realisation.

Presentation of the income statement

IFRS is not fully prescriptive as to the format of the income statement. Line items and subtotals have been presented on the face of the income statement in addition to those required under IFRS.

Sales shown in the income statement are those of continuing subsidiaries.

Operating profit is profit or loss before discontinued operations, taxation, finance costs and the share of post-tax profit of joint ventures accounted for using the equity method. In order to achieve consistency and comparability between reporting periods, operating profit is analysed to show separately the results of normal trading performance and individually significant charges and credits. Such items arise because of their size or nature and, in 2008, comprise:

- > charges relating to the Group-wide restructuring programmes announced in 2004 and 2008;
- > the impact of the annual goodwill impairment review;
- > asset impairment and restructuring charges which arise from events which are significant to any reportable segment;
- > amortisation of the fair value of non-operating intangible assets arising on business combinations;
- > profits or losses on businesses sold or closed which do not meet the definition of discontinued operations or which the Group views as capital rather than revenue in nature; and
- > changes in the fair value of derivative financial instruments between the opening and closing balance sheets and material currency translation movement arising on intra-group funding transactions.

The Group's post-tax share of joint venture profits is shown as a separate component of profit before tax. Material restructuring and impairment charges are separately identified.

Net finance costs are analysed to show separately interest payable, interest receivable and the net of interest payable on post-employment obligations and the expected return on pension scheme assets.

Revenue recognition

Sales

Revenue from the sale of goods is measured at the fair value of the consideration receivable which generally equates to the invoiced amount, excluding sales taxes and net of allowances for returns, early settlement discounts and rebates.

Invoices for goods are raised when the risks and rewards of ownership have passed which, dependent upon contractual terms, may be at the point of despatch, acceptance by the customer or, in Aerospace, certification by the customer. Revenue from royalties and the rendering of services is not significant.

Certain businesses, principally those in Powder Metallurgy, recognise an element of revenue via a surcharge mechanism. The surcharge invoiced or credited is generally based on prior period movement in raw material price indices applied to current period deliveries. In those instances where recovery of such increases is guaranteed, irrespective of the level of future deliveries, revenue is recognised, or due allowance made, in the same period as the cost movement takes place.

Other income

Interest income is recognised using the effective interest method. Revenue from dividends is not significant.

Sales and other income is recognised in the income statement when it can be reliably measured and its collectability is reasonably assured.

Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and impairment charges.

Cost

Cost comprises the purchase price plus costs directly incurred in bringing the asset into use. Where freehold and long leasehold properties were carried at a valuation at 23 March 2000, these values have been retained as book values and therefore deemed cost at the date of the IFRS transition. Borrowing costs are not capitalised.

Where assets are in the course of construction at the balance sheet date they are classified as capital work in progress. Transfers are made to other asset categories when they are available for use.

Depreciation

Depreciation is not provided on freehold land or capital work in progress. In the case of all other categories of property, plant and equipment, depreciation is provided on a straight line basis over the course of the financial year from the date the asset is available for use.

Depreciation is applied to specific classes of asset so as to reduce them to their residual values over their estimated useful lives, which are reviewed annually.

The range of main rates of depreciation used are:

| | Years |
|---|----------|
| Freehold buildings | Up to 50 |
| Steel powder production plant | 18 |
| General plant, machinery, fixtures and fittings | 6 to 15 |
| Computers | 3 to 5 |
| Commercial vehicles and cars | 4 to 5 |

Notes to the Financial Statements

continued

1 Accounting policies and presentation *continued*

Property, plant and equipment is reviewed at least annually for indications of impairment. Impairments are charged to the income statement. Similarly, where property, plant and equipment has been impaired and subsequent reviews demonstrate the recoverable value is in excess of the impaired value an impairment reversal is recorded. The amount of the reversal cannot exceed the theoretical net book amount at the date of the reversal had the item not been impaired. Impairment reversals are credited to the income statement against the same line item to which the impairment was previously charged.

Costs attributable to leasehold properties are written off to profit by equal annual instalments over the period of the lease or 50 years, whichever is the shorter.

Leased assets

Operating lease rentals are charged to the income statement as incurred over the lease term. Where fixed assets are financed by leasing arrangements which give rights approximating to ownership, the assets are treated as if they had been purchased and the capital element of the leasing commitment is shown as a finance lease liability. The asset and liability are measured at the fair value of the leased asset or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. The rentals payable are apportioned between interest, which is charged to the income statement, and capital which reduces the outstanding obligation. The asset is depreciated or amortised in line with similar owned assets.

Discontinued operations

The profit or loss on discontinued operations comprises the trading results up to the date of disposal or discontinuance and the profit or loss on the disposal or closure where businesses are sold or closed by the date on which the financial statements are approved. A discontinued operation is a business or businesses that have either been disposed of or closed or satisfies the criteria to be classified as held for sale and that represents either a material line of business within the Group or within one of its reported segments or a primary geographical area of operation. Where businesses fall to be treated as discontinued in the current year the comparative data is reclassified to reflect those businesses as discontinued.

Financial assets and liabilities

Borrowings are measured initially at fair value which usually equates to proceeds received and includes transaction costs. Borrowings are subsequently measured at amortised cost.

Cash and cash equivalents comprise cash on hand and demand deposits and overdrafts together with highly liquid investments of less than three months maturity. Unless an enforceable right of set-off exists and there is an intention to net settle, the components of cash and cash equivalents are reflected on a gross basis in the balance sheet.

The carrying value of other financial assets and liabilities, including short term receivables and payables, are stated at amortised cost less any impairment provision unless the impact of the time value of money is considered to be material.

Derivative financial instruments

The Group does not trade in derivative financial instruments. Derivative financial instruments including forward foreign exchange contracts are used by the Group to manage its exposure to (i) risk associated with the variability in cash flows in relation to both recognised assets or liabilities or forecast transactions and (ii) changes in the value of the Group's net investment in overseas operations. All derivative financial instruments are measured at the balance sheet date at their fair value.

Where derivative financial instruments are not designated as or not determined to be effective hedges, any gain or loss on remeasurement is taken to the income statement. Where derivative financial instruments are designated as and are effective as cash flow hedges, any gain or loss on remeasurement is held in equity and recycled through the income statement when the designated item is transacted.

Remeasurement gains and losses on derivative financial instruments held as net investment hedges are recognised in equity via the statement of recognised income and expense to the extent it is effective until the instrument and the underlying hedged investment are sold, when the profit or loss arising is recognised in the income statement.

Gains or losses on derivative financial instruments no longer designated as effective hedges are taken directly to the income statement.

Derivatives embedded in non-derivative host contracts are recognised at their fair value when the nature, characteristics and risks of the derivative are not closely related to the host contract. Gains and losses arising on the remeasurement of these embedded derivatives at each balance sheet date are taken to the income statement.

Goodwill

Goodwill consists of the excess of the fair value of the consideration over the fair value of the identifiable intangible and tangible assets net of the fair value of the liabilities including contingencies of businesses acquired at the date of acquisition.

Goodwill in respect of business combinations of subsidiaries is recognised as an intangible asset. Goodwill arising on the acquisition of a joint venture is included in the carrying value of the investment.

Where negative goodwill arises, following reassessment of fair values, it is credited to the income statement in the period in which the acquisition is made.

Goodwill is not amortised but tested at least annually for impairment. Impairments are charged to the income statement. Goodwill is carried at cost less any recognised impairment losses that arise from the annual assessment of its carrying value. To the extent that the carrying value exceeds the recoverable amount, determined as the higher of estimated discounted future net cash flows or recoverable amount on a fair value less cost to sell basis, goodwill is written down to the recoverable amount and an impairment charge is recognised in the income statement.

Other intangible assets

Other intangible assets are stated at cost less accumulated amortisation and impairment charges.

Computer software

Where computer software is not integral to an item of property, plant or equipment its costs are capitalised and categorised as intangible assets. Cost comprises the purchase price plus costs directly incurred in bringing the asset into use. Amortisation is provided on a straight line basis over its economic useful life which is in the range of 3–5 years.

Development costs

Where development expenditure results in a new or substantially improved product or process and it is probable that this expenditure will be recovered it is capitalised. Amortisation is charged from the date the asset is available for use. In Aerospace, amortisation is charged over the asset's life up to maximum of fifteen years either on a straight line basis or, where sufficient contractual terms exist, a unit of production method is applied. In Automotive, amortisation is charged on a straight line basis over the asset's life up to a maximum of seven years.

Capitalised development costs are subject to annual impairment reviews. Impairments are charged to the income statement.

Research expenditure is written off as incurred.

Assets acquired on business combinations – non-operating intangible assets

Non-operating intangible assets are intangible assets that are acquired as a result of a business combination, which arise from contractual or other legal rights and are not transferable or separable. On initial recognition they are measured at fair value. Amortisation is charged on a straight line basis to the income statement over their expected useful lives which are:

| | Years |
|--|-------------------|
| Marketing related assets — brands and trademarks | 30–50 |
| — agreements not to complete | Life of agreement |
| Customer related assets | 2–15 |
| Technology based assets | 5–10 |

Inventories

Inventories are valued at the lower of cost and estimated net realisable value with due allowance being made for obsolete or slow-moving items. Cost is determined on a first in, first out or weighted average cost basis. Cost includes raw materials, direct labour, other direct costs and the relevant proportion of works overheads assuming normal levels of activity. Net realisable value is the estimated selling price less estimated selling costs and costs to complete.

Taxation

Current and deferred tax are recognised in the income statement unless they relate to items recognised directly in equity when the related tax is also recognised in equity.

Full provision is made for deferred tax on all temporary timing differences resulting from the difference between the carrying value of an asset or liability in the consolidated financial statements and its tax base. The amount of deferred tax reflects the expected manner of realisation or settlement of the carrying amount of the assets and liabilities using tax rates enacted or substantively enacted at the balance sheet date.

Deferred tax assets are reviewed at each balance sheet date and are only recognised to the extent that it is probable that they will be recovered against future taxable profits.

Deferred tax is recognised on the unremitted profits of joint ventures. No deferred tax is recognised on the unremitted profits of overseas branches and subsidiaries except to the extent that it is probable that such earnings will be remitted to the parent in the foreseeable future.

Notes to the Financial Statements

continued

1 Accounting policies and presentation *continued*

Pensions and post-employment benefits

The Group's pension arrangements comprise various defined benefit and defined contribution schemes throughout the world. In the UK and in certain overseas companies pension arrangements are made through externally funded defined benefit schemes, the contributions to which are based on the advice of independent actuaries or in accordance with the rules of the schemes. In other overseas companies funds are retained within the business to provide for retirement obligations.

The Group also operates a number of defined contribution and defined benefit arrangements which provide certain employees with defined post-employment healthcare benefits.

The Group accounts for all post-employment defined benefit schemes through full recognition of the schemes' surpluses or deficits on the balance sheet at the end of each year. Actuarial gains and losses are included in the statement of recognised income and expense. Current and past service costs, curtailments and settlements are recognised within operating profit. Returns on scheme assets and interest on obligations are recognised as a component of other net financing charges.

For defined contribution arrangements the cost charged to the income statement represents the Group's contributions to the relevant schemes in the period in which they fall due.

Share-based payments

Share options granted to employees and share-based arrangements put in place since 7 November 2002 are valued at the date of grant or award using an appropriate option pricing model and are charged to operating profit over the performance or vesting period of the scheme. The annual charge is modified to take account of shares forfeited by employees who leave during the performance or vesting period and, in the case of non-market related performance conditions, where it becomes unlikely the option will vest.

Government grants

Grants receivable from governments or similar bodies are credited to the balance sheet in the period in which the conditions relating to the grant are met. Where they relate to specific assets they are amortised on a straight line basis over the same period as the asset is depreciated. Where they relate to revenue expenditure and/or non-asset criteria they are taken to the income statement to match the period in which the expenditure is incurred and criteria met.

Treasury shares

GKN shares which have been purchased and not cancelled are held as treasury shares and deducted from shareholders' equity.

Dividends

The annual final dividend is not provided for until approved at the annual general meeting whilst interim dividends are charged in the period they are paid.

Standards, revisions and amendments to standards and interpretations issued but not yet applied

The Group does not intend to adopt any standard, revision or amendment before the required implementation date. The following standards and amendments are likely to impact the reporting of the Group's results, assets and liabilities.

IFRS 8 'Operating Segments' was issued in November 2006 and is required to be implemented from 1 January 2009. It requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reviewed by the Chief Operating Decision Maker, as defined in the standard, to allocate resources to the segments and to assess their performance, and supersedes IAS 14 'Segment Reporting'. The effect of this standard on Group disclosures is still to be fully determined.

IAS 23 (Amendments) 'Borrowing Costs' came into effect on 1 January 2009. The Group will apply this standard prospectively. Currently the Group has no borrowings directly attributable to qualifying assets. In relation to an Aerospace investment programme the Group is currently in discussion with third parties on funding options which may result in borrowing costs, directly attributable to qualifying assets, being capitalised. It is not yet possible to quantify the impact of this.

The following is a summary of relevant revisions and amendments to standards and interpretations which are unlikely to have a material impact on the Group's results, assets or liabilities.

IAS 39 (Amendment) and IFRS 7 (Amendment) regarding reclassification of financial assets.

IAS 1 (Revised) and IAS 1 (Amendment) regarding presentation of financial statements.

IAS 39 (Amendment) regarding eligible hedged items.

IFRS 2 (Amendment) regarding vesting conditions.

IAS 27 (Revised) and IFRS 3 (Revised) regarding non-controlling interests and business combinations.

IAS 36 (Amendment) regarding disclosure of calculation of fair value less costs to sell.

IFRS 5 (Amendment) regarding disclosure of assets and liabilities when there is a partial loss of control.

IAS 38 (Amendments) regarding methods of amortisation and recognition of prepaid goods and services.

IAS 19 (Amendment) regarding difference between past service cost and curtailment, definition of return on plan assets and long and short term employee benefits.

IFRIC 16 'Hedges of a net investment in a foreign operation'.

IAS 31 (Amendment) regarding joint ventures accounted for in accordance with IAS 39.

IAS 20 (Amendment) regarding the benefit of a below-market rate government loan.

There are a number of standards, amendments to standards and interpretations that are not relevant to the Group which have therefore not been listed above.

Significant judgements, key assumptions and estimates

The Group's significant accounting policies are set out above. The preparation of financial statements, in conformity with IFRS, requires the use of estimates, subjective judgement and assumptions that may affect the amounts of assets and liabilities at the balance sheet date and reported profit and earnings for the year. The Directors base these estimates, judgements and assumptions on a combination of past experience, professional expert advice and other evidence that is relevant to the particular circumstance.

The accounting policies where the Directors consider the more complex estimates, judgements and assumptions have to be made are those in respect of acquired non-operating intangible assets – business combinations (note 24), post-employment obligations (note 26), derivative and other financial instruments (notes 3e and 20), taxation (note 5) and impairment of non-current assets (notes 11 and 12). The details of the principal estimates, judgements and assumptions made are set out in the related notes as identified.

Notes to the Financial Statements

continued

2 Segmental analysis

The Group is managed by type of business. Segmental information is provided having regard to the nature of the goods and services provided and the markets served.

Primary reporting format — business segments

| 2008 | Automotive | | | | | Corporate and Unallocated £m | Total £m |
|--|-----------------|---------------------------|----------------------------|------------------|-----------------|---------------------------------|----------------|
| | Driveline £m | Other Automotive £m | Powder Metallurgy £m | OffHighway £m | Aerospace £m | | |
| Sales | 2,123 | 84 | 618 | 549 | 1,002 | — | 4,376 |
| EBITDA | 168 | — | 31 | 53 | 136 | (11) | 377 |
| Depreciation and impairment charges | (92) | (4) | (32) | (12) | (25) | (1) | (166) |
| Amortisation of intangible assets | (3) | — | (1) | (1) | (5) | — | (10) |
| Trading profit/(loss) | 73 | (4) | (2) | 40 | 106 | (12) | 201 |
| Restructuring — 2008 plan | (23) | (13) | (106) | (3) | (3) | (1) | (149) |
| — 2004 plan | (4) | — | — | — | — | — | (4) |
| Other impairments | — | — | — | — | — | — | — |
| Amortisation of business combination non-operating intangibles | (2) | — | — | (2) | (6) | — | (10) |
| Profits and losses on sale or closures of businesses | — | — | — | — | — | — | — |
| Change in value of derivative and other financial instruments | (35) | 1 | (4) | (2) | (93) | 9 | (124) |
| Operating profit/(loss) | 9 | (16) | (112) | 33 | 4 | (4) | (86) |
| Share of post-tax earnings of joint ventures before impairment | 13 | 4 | — | — | (1) | — | 16 |
| Impairment — post-tax | (10) | — | — | — | — | — | (10) |
| Share of post-tax earnings of joint ventures | 3 | 4 | — | — | (1) | — | 6 |
| Segment assets | | | | | | | |
| Goodwill | 79 | — | 32 | 51 | 205 | — | 367 |
| Investments in joint ventures | 90 | 27 | — | 2 | — | — | 119 |
| Derivative financial instruments | 1 | — | — | 1 | 60 | — | 62 |
| Operating assets | 1,579 | 50 | 543 | 342 | 816 | 6 | 3,336 |
| Other unallocated assets: | | | | | | | |
| — Cash and cash equivalents | — | — | — | — | — | 114 | 114 |
| — Current tax assets | — | — | — | — | — | 17 | 17 |
| — Deferred tax assets | — | — | — | — | — | 52 | 52 |
| Total assets | 1,749 | 77 | 575 | 396 | 1,081 | 189 | 4,067 |
| Segment liabilities | | | | | | | |
| Derivative financial instruments | (31) | — | (5) | (4) | (152) | — | (192) |
| Operating liabilities: | | | | | | | |
| — Post-employment obligations | (308) | — | (47) | (77) | (111) | (291) | (834) |
| — Other | (474) | (18) | (114) | (150) | (305) | (52) | (1,113) |
| Other unallocated liabilities: | | | | | | | |
| — Borrowings | — | — | — | — | — | (822) | (822) |
| — Current tax liabilities | — | — | — | — | — | (115) | (115) |
| — Deferred tax liabilities | — | — | — | — | — | (63) | (63) |
| Total liabilities | (813) | (18) | (166) | (231) | (568) | (1,343) | (3,139) |
| Other segment items | | | | | | | |
| Capital expenditure | | | | | | | |
| — Property, plant and equipment | 108 | 1 | 33 | 18 | 31 | 1 | 192 |
| — Intangible assets | 3 | — | — | 1 | 9 | — | 13 |
| Other non-cash expenses (share-based payments) | 1 | — | — | — | — | 1 | 2 |

All business segments shown above are continuing. EBITDA is earnings before interest, tax, depreciation and amortisation.

Amounts in respect of discontinued operations in the period, £13 million post-tax, were attributable to the final proceeds on the disposal of the Group's Aerospace joint venture investment in AgustaWestland.

2 Segmental analysis *continued*

Primary reporting format — business segments

| 2007 | Automotive | | Powder Metallurgy £m | OffHighway £m | Aerospace £m | Corporate and Unallocated £m | Total £m |
|--|-----------------|---------------------------|----------------------------|------------------|-----------------|------------------------------------|-------------|
| | Driveline £m | Other Automotive £m | | | | | |
| Sales | 1,922 | 109 | 602 | 416 | 820 | — | 3,869 |
| EBITDA | 227 | 2 | 58 | 39 | 112 | (10) | 428 |
| Depreciation and impairment charges | (75) | (5) | (28) | (10) | (24) | — | (142) |
| Amortisation of intangible assets | (3) | — | (1) | — | (5) | — | (9) |
| Trading profit/(loss) | 149 | (3) | 29 | 29 | 83 | (10) | 277 |
| Restructuring — 2004 plan | (19) | — | (14) | — | — | — | (33) |
| Other impairments | — | 2 | — | — | — | — | 2 |
| Amortisation of business combination non-operating intangibles | (1) | — | — | (2) | (5) | — | (8) |
| Profits and losses on sale or closures of businesses | — | (7) | — | — | — | — | (7) |
| Change in value of derivative and other financial instruments | (1) | (1) | (1) | (2) | (5) | — | (10) |
| Operating profit/(loss) | 128 | (9) | 14 | 25 | 73 | (10) | 221 |
| Share of post-tax earnings of joint ventures | 14 | 10 | — | — | — | — | 24 |
| Segment assets | | | | | | | |
| Goodwill | 65 | — | 24 | 38 | 153 | — | 280 |
| Investments in joint ventures | 71 | 28 | — | 1 | — | — | 100 |
| Derivative financial instruments | 6 | — | — | — | 19 | — | 25 |
| Operating assets | 1,280 | 56 | 531 | 251 | 620 | 5 | 2,743 |
| Other unallocated assets: | | | | | | | |
| — Cash and cash equivalents | — | — | — | — | — | 282 | 282 |
| — Current tax assets | — | — | — | — | — | 2 | 2 |
| — Deferred tax assets | — | — | — | — | — | 56 | 56 |
| Total assets | 1,422 | 84 | 555 | 290 | 792 | 345 | 3,488 |
| Segment liabilities | | | | | | | |
| Derivative financial instruments | (1) | (1) | (1) | (1) | (9) | (17) | (30) |
| Operating liabilities: | | | | | | | |
| — Post-employment obligations | (208) | (7) | (23) | (45) | (32) | (16) | (331) |
| — Other | (446) | (21) | (122) | (115) | (209) | (51) | (964) |
| Other unallocated liabilities: | | | | | | | |
| — Borrowings | — | — | — | — | — | (788) | (788) |
| — Current tax liabilities | — | — | — | — | — | (104) | (104) |
| — Deferred tax liabilities | — | — | — | — | — | (75) | (75) |
| Total liabilities | (655) | (29) | (146) | (161) | (250) | (1,051) | (2,292) |
| Other segment items | | | | | | | |
| Capital expenditure | | | | | | | |
| — Property, plant and equipment | 94 | 2 | 38 | 11 | 28 | 1 | 174 |
| — Intangible assets | 3 | — | — | 1 | 16 | — | 20 |
| Other non-cash expenses (share-based payments) | 2 | — | 1 | — | 1 | 2 | 6 |

All business segments shown above are continuing.

Intra-group sales between segments and regions are not significant. The analyses of operating profit by business includes an allocation, based on their nature, of costs incurred centrally in the United Kingdom, United States of America, China and Germany. Unallocated costs represent corporate expenses. Segment assets and liabilities comprise all non-current and current items as per the balance sheet but exclude taxation, borrowings and cash and cash equivalents. Cash and cash equivalents and borrowings are not allocated to specific segments as these resources are managed centrally and no business in any segment has sufficient autonomy to manage these resources. Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one year.

Notes to the Financial Statements

continued

2 Segmental analysis *continued*

Secondary reporting format — by geographical region

| | Sales by destination | | Segment assets | | Capital expenditure | |
|---------------------------|----------------------|--------------|----------------|--------------|---------------------|------------|
| | 2008 £m | 2007 £m | 2008 £m | 2007 £m | 2008 £m | 2007 £m |
| Continuing operations | | | | | | |
| Europe | 2,018 | 1,773 | 1,709 | 1,411 | 96 | 87 |
| Americas | 1,748 | 1,595 | 1,623 | 1,315 | 78 | 75 |
| Rest of the World | 610 | 501 | 546 | 417 | 31 | 32 |
| Corporate and Unallocated | — | — | 189 | 345 | — | — |
| | 4,376 | 3,869 | 4,067 | 3,488 | 205 | 194 |

3 Operating profit

The analysis of the components of operating profit is shown below:

(a) Trading profit

| | 2008 £m | 2007 £m |
|---|----------------|----------------|
| Sales by subsidiaries | 4,376 | 3,869 |
| Less: UK cylinder liner manufacturing operation | — | (22) |
| | 4,376 | 3,847 |
| Operating costs and other income | | |
| Change in stocks of finished goods and work in progress | 18 | 12 |
| Raw materials and consumables | (1,737) | (1,415) |
| Unwind of fair value inventory adjustments arising on business combinations | — | (1) |
| Staff costs (note 9) | (1,232) | (1,100) |
| Reorganisation costs (note (i)): | | |
| Redundancy and other amounts | (5) | (4) |
| Impairment of plant and equipment | (1) | (1) |
| Depreciation of property, plant and equipment (note (ii)) | (165) | (141) |
| Amortisation of intangible assets | (10) | (9) |
| Operating lease rentals payable: | | |
| Plant and equipment | (12) | (12) |
| Property | (23) | (20) |
| Impairment of trade receivables | (6) | (3) |
| Amortisation of government grants | 2 | 2 |
| Net exchange differences on foreign currency transactions | 3 | (1) |
| Other costs (note (iv)) | (1,007) | (877) |
| | (4,175) | (3,570) |
| Trading profit | 201 | 277 |

- (i) Reorganisation costs shown above reflect ongoing actions in the ordinary course of business to reduce costs, improve productivity and rationalise facilities in continuing operations. Costs incurred include redundancy and related post-employment obligation charges, asset write-downs and impairments and other revenues and expenditure directly attributable to the reorganisation actions. Headcount realignment activity continued at a cost of £3 million (2007 – £3 million). Rationalisation of a UK facility continued at a cost of £2 million (2007 – £2 million including a £1 million plant and equipment impairment charge).
- (ii) Including depreciation charged on assets held under finance leases of £1 million (2007 – £1 million).
- (iii) Research and development expenditure in subsidiaries was £90 million (2007 – £81 million).
- (iv) Other costs include a £5 million credit from the release of an unutilised provision established on acquisition as a result of changed customer contract requirements in an Aerospace business and a £3 million charge in respect of abortive acquisition costs in Driveline. Property surpluses were nil (2007 – £4 million).

3 Operating profit continued**(v) Auditors' remuneration**

The analysis of auditors' remuneration is as follows:

| | 2008 £m | 2007 £m |
|--|--------------|--------------|
| Fees payable to PricewaterhouseCoopers LLP for the Company's annual financial statements | (0.7) | (0.6) |
| Fees payable to PricewaterhouseCoopers LLP and their associates for other services to the Group: | | |
| – Audit of the Company's subsidiaries pursuant to legislation | (3.1) | (2.8) |
| <i>Total audit fees</i> | <i>(3.8)</i> | <i>(3.4)</i> |
| – Other services pursuant to legislation | (0.1) | (0.1) |
| – Tax services | (0.6) | (0.5) |
| – Corporate finance transaction services | – | – |
| – Other services | (0.1) | (0.1) |
| <i>Total non-audit fees</i> | <i>(0.8)</i> | <i>(0.7)</i> |
| Fees payable to PricewaterhouseCoopers LLP and their associates in respect of associated pension schemes | | |
| – Audit | – | – |
| – Other services | – | – |
| <i>Total fees payable to PricewaterhouseCoopers LLP and their associates</i> | <i>(4.6)</i> | <i>(4.1)</i> |

All fees payable to PricewaterhouseCoopers LLP, the Company's auditors, include amounts in respect of expenses. All fees payable to PricewaterhouseCoopers LLP have been charged to the income statement except for those in relation to associated pension schemes, which are borne by the respective schemes.

(b) Restructuring and impairment charges

| | 2008 | | | 2007 | | |
|---|--------------------------|-----------------|-------------|----------------------------------|----------------------------|-------------|
| | Restructuring programmes | | Total £m | Restructuring 2004 plan £m | Other impairments £m | Total £m |
| | 2008 plan £m | 2004 plan £m | | | | |
| Restructuring and impairment charges | | | | | | |
| Goodwill impairment | – | – | – | – | – | – |
| Tangible fixed asset impairments/reversals | (125) | (2) | (127) | 7 | 2 | 9 |
| Other asset write-downs | (4) | – | (4) | (1) | – | (1) |
| | (129) | (2) | (131) | 6 | 2 | 8 |
| Redundancy and employee related costs including | | | | | | |
| post-employment curtailments | (16) | – | (16) | (16) | – | (16) |
| Other reorganisation costs including property surplus | (4) | (2) | (6) | (23) | – | (23) |
| Subsidiaries | (149) | (4) | (153) | (33) | 2 | (31) |
| Impairment of joint ventures | (10) | – | (10) | – | – | – |
| Subsidiaries and joint ventures | (159) | (4) | (163) | (33) | 2 | (31) |

Restructuring

The Group's 2004 restructuring programme concluded in the first half of 2008, with the costs charged relating mainly to reorganisation costs (including incremental costs borne by the Group as a consequence of dedicated restructuring and transition teams) and equipment relocation costs attributable to the transfer of equipment between closing facilities and continuing operations, incremental premium freight and product homologation costs. These costs were incurred in Driveline operations in North America and Europe and were charged in the first half of 2008.

In response to the severe economic downturn in our automotive markets and in anticipation of activity reductions in both off-highway and aerospace markets, the Group commenced further restructuring in the final quarter of 2008. As a result of this planned restructuring, charges amounting to £149 million in subsidiaries and an impairment in respect of joint venture investments, £10 million, have been recognised. Cash based charges amount to £20 million. An analysis by segment and description of the 2008 restructuring plan charges is set out as follows:

Notes to the Financial Statements

continued

3 Operating profit *continued*

| | 2008 Plan | | | Total £m |
|-------------------|-------------------|------------------|----------------------|-------------|
| | Impairments £m | Redundancy £m | Reorganisation £m | |
| Driveline | (25) | (6) | (2) | (33) |
| Other Automotive | (11) | (2) | — | (13) |
| Powder Metallurgy | (100) | (4) | (2) | (106) |
| OffHighway | — | (3) | — | (3) |
| Aerospace | (3) | — | — | (3) |
| Corporate | — | (1) | — | (1) |
| | (139) | (16) | (4) | (159) |
| Subsidiaries | (129) | (16) | (4) | (149) |
| Joint ventures | (10) | — | — | (10) |

The £139 million impairments reflect either planned changes and commercial actions to the structure of how our businesses satisfy customer demand or write-downs as a result of significant curtailment in the future volume expectations of certain businesses. In Powder Metallurgy impairments of £100 million include the impact on the Sinter Metals North American fixed asset base (£81 million) on the back of significant reductions in automotive volume projections and reductions to estimated realisable values of the fixed assets and inventories (£11 million) in Hoeganaes attributable to two businesses that are being exited. In Driveline impairments are attributable to the rationalisation of UK manufacturing capacity (£10 million) and write-offs of dedicated customer programme specific fixed assets arising on the programme cancellation or volume reductions (£5 million). In Aerospace the reduction of engine component production capacity in Europe as a result of transfers to the US, in agreement with specific customers, has resulted in fixed asset write-downs of £3 million. As a consequence of intractable losses, severe volume reductions and forecast cash outflows into the foreseeable future in our UK Other Automotive subsidiary business the entire production fixed asset base has been impaired (£11 million).

The Sinter North America and UK Other Automotive impairment, £81 million and £11 million respectively, were determined on a value in use basis where the pre-tax discount rates used were 10% and 12%.

Impairments recognised in respect of joint ventures reflect a change in how Driveline will satisfy customer supply in selected geographical territories. Consequently, joint venture arrangements are being unwound and the carrying value of the Group's investment therein has been fully impaired.

Non-asset related 2008 plan charges are predominantly employee related and include short-time working costs of £2 million, redundancy charges of £14 million including £1 million attributable pension past service costs and other reorganisation costs of £4 million. Other reorganisation costs include £2 million of charges in respect of an onerous consumables supply lease that arose as a consequence of the curtailment of activity in a Powder Metallurgy site.

Redundancy costs provided represent charges for contractual severance, other employee related exit costs and post-employment augmentation where applicable. These charges have only been recognised where formal communication with the employees or relevant employee bodies had taken place before 31 December 2008. Short-time working represents payments made to employees in the period when they are away from the workplace and not engaged in any productive or non-productive activities in the plants affected, and therefore are not contributing to the business operations.

The 2007 restructuring charges of £33 million relate to the Group's 2004 restructuring programme to facilitate geographical migration of Driveline production capacity, support recovery actions in Powder Metallurgy and the realignment and reduction of production capacity, overhead and infrastructure cost across the Group. Pension past service charges included therein amounted to £4 million in the year. Other reorganisation charges were net of a £2 million property surplus in a Powder Metallurgy business sold post-restructuring closure.

Cash outflow in respect of 2008, 2004 and earlier periods' strategic restructuring actions amounted to £28 million (2007 – £40 million including £4 million property disposal proceeds).

Other impairments

The £2 million impairment reversal recognised in 2007 arose in relation to the Group's UK cylinder liner manufacturing operation. The business disposed of land and buildings and plant and machinery at a value greater than the theoretical net book value of the assets had they not been impaired. Consequently, a proportion of the previously recognised impairment has been reversed.

3 Operating profit *continued***(c) Amortisation of non-operating intangible assets arising on business combinations**

| | 2008 | 2007 |
|-------------------|-------------|------------|
| | £m | £m |
| Marketing related | — | — |
| Customer related | (7) | (5) |
| Technology based | (3) | (3) |
| | (10) | (8) |

(d) Profits and losses on sale or closures of businesses

| | 2008 | 2007 |
|---|------|------|
| | £m | £m |
| Profits and losses on closures of businesses | | |
| Trading losses of the UK cylinder liner manufacturing operation | — | (7) |

(e) Change in value of derivative and other financial instruments

| | 2008 | 2007 |
|--|--------------|-------------|
| | £m | £m |
| Embedded derivatives | 43 | — |
| Forward exchange contracts (not hedge accounted) | (175) | (9) |
| Commodity contracts (not hedge accounted) | (1) | (1) |
| Net gains and losses on intra-group funding | 9 | — |
| | (124) | (10) |

IAS 39 requires derivative financial instruments to be valued at the balance sheet date and any difference between that value and the intrinsic value of the instrument to be reflected in the balance sheet as an asset or liability. Any subsequent change in value is reflected in the income statement unless hedge accounting is achieved. Such movements do not affect cash flow or the economic substance of the underlying transaction. In 2008 and 2007 the Group used transactional hedge accounting in a limited number of instances. As a consequence, and to assist year on year comparison, the change in value continues to be identified as a separate element of operating profit.

4 Interest payable and interest receivable

| | 2008 | 2007 |
|--|-------------|-------------|
| | £m | £m |
| Interest payable and fee expense | | |
| Short term bank and other borrowings | (11) | (7) |
| Loans repayable within five years | (29) | (29) |
| Loans repayable after five years | (26) | (25) |
| Finance leases | — | (1) |
| | (66) | (62) |
| Interest receivable | | |
| Short term investments, loans and deposits | 7 | 9 |
| Net investment hedges | 9 | 10 |
| AgustaWestland escrow receipt | 3 | — |
| | 19 | 19 |
| Net interest payable and receivable | (47) | (43) |

£3 million interest was received in August 2008 relating to the £35 million AgustaWestland deferred consideration when monies held in escrow were released (see note 6).

Notes to the Financial Statements

continued

5 Taxation

(a) Tax expense

| | 2008 | 2007 |
|--|------|------|
| | £m | £m |
| Analysis of charge in year | | |
| Current tax charge/(credit) | | |
| Current year | 33 | 38 |
| Utilisation of previously unrecognised tax losses and other assets | (44) | (9) |
| Adjustments in respect of prior years | 1 | 3 |
| Net movement on provisions for uncertain tax positions | — | 4 |
| | (10) | 36 |
| Deferred tax charge/(credit) | | |
| Origination and reversal of temporary differences (excluding post-employment obligations) | (69) | 12 |
| Tax in respect of post-employment obligations | (5) | (3) |
| Tax on change in value of derivative financial instruments | (2) | — |
| Utilisation of previously unrecognised tax losses and other assets | — | (7) |
| Other changes in unrecognised deferred tax assets | 80 | (28) |
| Changes in tax rates | (2) | (8) |
| Adjustments in respect of prior years | (2) | (1) |
| | — | (35) |
| Total tax charge/(credit) for the year | (10) | 1 |
| Tax in respect of restructuring, impairments and derivative financial instruments included above | | |
| Current tax (credit)/charge | (3) | (7) |
| Deferred tax (credit)/charge | (4) | 2 |
| | (7) | (5) |
| Tax in respect of utilisation of previously unrecognised losses against foreign exchange gains and losses on intra-group funding included above | | |
| Current tax (credit)/charge | (29) | — |

The Group is required to estimate the income tax due in each of the jurisdictions in which it operates. This requires an estimation of the current tax liability together with an assessment of the temporary differences which arise as a consequence of differing accounting and tax treatments. These temporary differences result in deferred tax assets or liabilities which are measured using substantively enacted tax rates expected to apply when the temporary differences reverse. Recognition of deferred tax assets, and hence credits to the income statement, is based on forecast future taxable income and therefore involves judgement regarding the future financial performance of particular legal entities or tax groups in which the deferred tax assets are recognised.

The Group is subject to many different tax jurisdictions and tax rules as a consequence of its geographic spread. It is therefore subject to tax audits and tax reviews which, by their nature, are often complex and can require several years to conclude. The total accrual for income tax in any period is, therefore, based on management judgement, interpretation of country specific tax law and the likelihood of crystallisation and settlement. Tax benefits are not recognised unless it is probable that the tax positions are sustainable. As amounts set aside in any period could differ from actual tax liabilities, adjustments may be required in subsequent periods which may have a material impact on the Group's income statement and/or cash tax payment. Payments in respect of tax liabilities for an accounting period comprise payments on account and payments on the final resolution of open items with tax authorities and, as a result, there can be substantial differences between the charge in the income statement and cash tax payments. Interest on provisions for uncertain tax positions is, where relevant, provided for in the tax charge.

Details of the effective tax rate for the Group and the underlying events and transactions affecting this are given in the business review on pages 14 and 15.

5 Taxation *continued*

| Tax reconciliation | 2008 | | 2007 | |
|---|-------|------|------|------|
| | £m | % | £m | % |
| Profit/(loss) before tax | (130) | | 199 | |
| Less share of post-tax earnings of joint ventures | (6) | | (24) | |
| Profit/(loss) before tax excluding joint ventures | (136) | | 175 | |
| Tax (credit)/charge calculated at 28.5% (2007 – 30.0%) standard UK corporate tax rate | (39) | 29 | 53 | 30 |
| Differences between UK and overseas corporate tax rates | (10) | 7 | 5 | 2 |
| Non-deductible and non-taxable items | 11 | (8) | (8) | (4) |
| Utilisation of previously unrecognised tax losses and other assets | (44) | 32 | (16) | (9) |
| Other changes in unrecognised deferred tax assets | 80 | (59) | (28) | (16) |
| Changes in tax rates | (2) | 1 | (8) | (4) |
| Deferred tax (credit)/charge in respect of post-employment obligations | (5) | 4 | (3) | (1) |
| Current year tax charge/(credit) on ordinary activities | (9) | 6 | (5) | (2) |
| Net movement on provision for uncertain tax positions | — | — | 4 | 2 |
| Adjustments in respect of prior years | (1) | 1 | 2 | 1 |
| Total tax charge/(credit) for the year | (10) | 7 | 1 | 1 |

(b) Tax in equity

| Tax on items included in equity (credit)/charge | 2008 £m | 2007 £m |
|--|------------|------------|
| Deferred tax on post-employment obligations | — | 84 |
| Deferred tax on non-qualifying assets | (3) | 6 |
| Deferred tax on foreign exchange gains and losses on intra-group funding | (3) | 2 |
| Current tax on foreign exchange gains and losses on intra-group funding | 29 | — |
| | 23 | 92 |

(c) Current tax

| | 2008 £m | 2007 £m |
|--------------------|------------|------------|
| Assets | | |
| United Kingdom | — | 2 |
| Overseas | 17 | — |
| | 17 | 2 |
| Liabilities | | |
| Overseas | (115) | (104) |
| | (115) | (104) |

(d) Recognised deferred tax

Deferred tax is calculated in full on temporary differences under the liability method.

| | 2008 £m | 2007 £m |
|--------------------------|------------|------------|
| Deferred tax assets | 52 | 56 |
| Deferred tax liabilities | (63) | (75) |
| | (11) | (19) |

Notes to the Financial Statements

continued

5 Taxation *continued*

The movements in deferred tax assets and liabilities (prior to the offsetting of balances within the same jurisdiction as permitted by IAS 12) during the period are shown below:

| | Assets | | | Liabilities | | Total £m |
|----------------------------------|----------------|------------------|-------------|--------------------|-------------|-------------|
| | Pensions £m | Tax losses £m | Other £m | Fixed assets £m | Other £m | |
| At 1 January 2007 | 102 | 20 | 28 | (94) | (5) | 51 |
| Included in the income statement | 3 | 27 | 45 | (31) | (9) | 35 |
| Included in equity | (84) | — | — | (6) | (2) | (92) |
| Subsidiaries acquired | — | — | — | (2) | (6) | (8) |
| Other movements | — | — | (6) | — | 6 | — |
| Currency variations | — | — | 2 | (7) | — | (5) |
| At 31 December 2007 | 21 | 47 | 69 | (140) | (16) | (19) |
| Other movements | 11 | (11) | — | — | — | — |
| Included in the income statement | 5 | (29) | (19) | 34 | 9 | — |
| Included in equity | — | — | — | 3 | 3 | 6 |
| Currency variations | 7 | 20 | 37 | (63) | 1 | 2 |
| At 31 December 2008 | 44 | 27 | 87 | (166) | (3) | (11) |

Deferred tax assets totalling £14 million (2007 – £35 million) have been recognised relating to territories where tax losses have been incurred in the year. It is anticipated that future profitability arising from restructuring and other actions will result in their realisation.

(e) Unrecognised deferred tax assets

Deferred tax assets have not been recognised in relation to certain taxable losses and other temporary differences on the basis that their future economic benefit is uncertain. The gross and tax values of these unrecognised assets together with any expiry dates where relevant are shown below. The tax value of the assets has been calculated using tax rates enacted or substantively enacted at the balance sheet date.

| | 2008 | | | 2007 | | |
|---|-----------------|--------------|------------------|-----------------|--------------|------------------|
| | Tax value £m | Gross £m | Expiry period | Tax value £m | Gross £m | Expiry period |
| Tax losses — with expiry: national | 300 | 867 | 2019–2028 | 186 | 532 | 2019–2027 |
| Tax losses — with expiry: local | 44 | 532 | 2009–2028 | 40 | 813 | 2008–2027 |
| Tax losses — without expiry | 66 | 202 | | 118 | 402 | |
| Other temporary differences | 71 | 215 | | 32 | 113 | |
| Unrecognised deferred tax assets | 481 | 1,816 | | 376 | 1,860 | |

Included above are tax losses of £756 million with a tax value of £187 million (2007 – £677 million with a tax value of £109 million) that are severely restricted for future use and management, based on the Group's current profile, believes they are unlikely to be utilised in the foreseeable future.

No deferred tax is recognised on the unremitted earnings of overseas subsidiaries except where the distribution of such profits is planned. If the earnings were remitted in full tax of £28 million (2007 – £25 million) would be payable.

(f) Franked Investment Income — Litigation

In September 2003 GKN filed a claim in the High Court of England and Wales ('the High Court') in respect of various Advance Corporation Tax payments made and Corporate Tax paid on certain foreign dividend receipts which, in its view, were levied by HMRC in breach of GKN's EU community law rights. GKN joined a Group Litigation Order ('GLO') with several other claimants and a test case was selected from the members of the GLO to proceed to trial on a representative basis.

At the commencement of that trial in June 2004 the High Court referred the test case to the European Court of Justice ('ECJ') for guidance on the issues raised. In December 2006 the ECJ issued its guidance to the High Court and the test case returned to the High Court for the full trial in July 2008. The High Court issued its judgment on 27 November 2008.

The November High Court judgment held in favour of the claimants on certain key aspects of the claim. Both parties, however, have appealed to the Court of Appeal and depending upon the outcome of this a further reference to the ECJ may be required before the issue is ultimately resolved. Given the importance of the matters at issue it is expected that appeals will ultimately be taken to the House of Lords and that this process may take several more years to complete. Given the complexity of the case and uncertainty over the issues raised it is not possible to predict with any reasonable degree of certainty what the final outcome could be. The range of possible outcomes is so wide that it is potentially misleading to quote any estimates of the possible recoveries at this stage. As a result no contingent asset has been recognised and disclosed in these financial statements.

6 Discontinued operations

In August 2008, the Group reached agreement with Finmeccanica regarding the £35 million deferred consideration placed into escrow in November 2004, the date of disposal of the Group's 50% share of AgustaWestland. Under the agreement the £35 million, together with accrued interest, was shared equally. As a result, £21 million was received, of which £3 million was recognised as interest and £18 million recognised as profit on sale of discontinued operations. The interest represents the cumulative interest on the escrow monies earned during the period from initial disposal to final agreement. Tax of £5 million was charged against the profit on sale.

7 Earnings per share

| | 2008 | | | 2007 | | |
|--------------------------------|----------------|---|--------------------------------|----------------|---|--------------------------------|
| | Earnings £m | Weighted average number of shares m | Earnings per share pence | Earnings £m | Weighted average number of shares m | Earnings per share pence |
| Continuing operations | | | | | | |
| Basic eps | (122) | 704.7 | (17.3) | 196 | 703.4 | 27.9 |
| Dilutive securities | — | 1.1 | — | — | 2.9 | (0.1) |
| Diluted eps | (122) | 705.8 | (17.3) | 196 | 706.3 | 27.8 |
| Discontinued operations | | | | | | |
| Basic eps | 13 | 704.7 | 1.8 | — | — | — |
| Dilutive securities | — | 1.1 | — | — | — | — |
| Diluted eps | 13 | 705.8 | 1.8 | — | — | — |

Adjusted earnings per share — continuing operations

| | 2008 | | 2007 | |
|--|------------|-------------|------------|-------------|
| | £m | pence | £m | pence |
| Adjusted earnings and adjusted basic earnings per share | | | | |
| Profit attributable to equity shareholders — continuing operations | (122) | (17.3) | 196 | 27.9 |
| Adjustments for: | | | | |
| Restructuring and impairment charges | 153 | 21.7 | 31 | 4.4 |
| Amortisation of non-operating intangibles on business combinations | 10 | 1.4 | 8 | 1.1 |
| Profits and losses on sale or closures of businesses | — | — | 7 | 1.0 |
| Change in value of derivative and other financial instruments | 124 | 17.6 | 10 | 1.4 |
| Impairment of joint ventures | 10 | 1.4 | — | — |
| Taxation on adjustments | (7) | (1.0) | (5) | (0.7) |
| Adjusted earnings attributable to equity shareholders — continuing operations | 168 | 23.8 | 247 | 35.1 |

The Directors consider adjusted earnings per share, as calculated above, gives a useful additional indicator of underlying performance.

8 Dividends

| | Paid or proposed in respect of: | | Recognised in: | |
|---|------------------------------------|---------------|----------------|------------|
| | 2008 pence | 2007 pence | 2008 £m | 2007 £m |
| 2006 final year dividend paid (8.7 pence per share) | — | — | — | 61 |
| 2007 interim dividend paid | — | 4.3 | — | 30 |
| 2007 final year dividend paid | — | 9.2 | 65 | — |
| 2008 interim dividend paid | 4.5 | — | 32 | — |
| 2008 final year dividend | — | — | — | — |
| | 4.5 | 13.5 | 97 | 91 |

The Directors have decided not to pay a final dividend in respect of the financial year ended 31 December 2008.

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9 Employees including Directors

| | 2008 £m | 2007 £m |
|-------------------------------------|--------------|--------------|
| Employee benefit expense | | |
| Wages and salaries | 1,031 | 930 |
| Social security costs | 161 | 147 |
| Post-employment costs | 38 | 28 |
| Equity-settled share-based payments | 2 | 6 |
| | 1,232 | 1,111 |

Amounts included in 2007 above relating to the UK cylinder liner manufacturing operation are wages and salaries £9 million, post-employment costs £1 million and social security costs £1 million.

| | 2008 Number | 2007 Number |
|--|----------------|----------------|
| Average monthly number of employees (including executive Directors) | | |
| By business | | |
| Driveline | 17,967 | 18,022 |
| Other Automotive | 1,392 | 1,506 |
| Powder Metallurgy | 6,585 | 6,959 |
| OffHighway | 4,108 | 3,815 |
| Aerospace | 7,887 | 7,241 |
| Central | 208 | 192 |
| Total | 38,147 | 37,735 |

Key management

The key management of the Group comprises GKN plc Board Directors and the members of the Group's Executive Committee during the year and their aggregate compensation is shown below. Details of Directors' remuneration are contained in the Directors' remuneration report on pages 61 to 71.

| | 2008 £m | 2007 £m |
|---|------------|-------------|
| Key management compensation | | |
| Salaries and short term employee benefits | 5.5 | 7.1 |
| Post-employment benefits | 1.2 | 1.2 |
| Termination benefits | — | 0.1 |
| Share-based benefits | 0.8 | 2.5 |
| | 7.5 | 10.9 |

Salaries and short term employee benefits comprises annual salary, benefits in kind and amounts accrued in respect of short term variable remuneration schemes. Details of the Directors' short term variable remuneration schemes are set out in the remuneration report. Other members of key management participate in schemes based on the achievement of profit and cash targets and which are payable in cash. The amount outstanding at 31 December 2008 in respect of annual short term variable remuneration was £1 million (2007 – £3 million). Post-employment benefits represent the charge to trading profit under IAS 19 attributable to key management arising in the year and the attributable cost of post-employment medical benefits. Termination benefits include redundancy, pension augmentations and ex gratia payments arising in connection with loss of office and termination of employment with the Group. Share-based payments represents the annual charge attributable to key management in respect of their participation in the Group's share-based remuneration arrangements; details of the nature of these arrangements are set out in note 10 and in the Directors' remuneration report. Total awards made or shares granted in the year to key management in respect of these arrangements were:

| | 2008 | | 2007 | |
|------------------------------|-------------------------------|--|-------------------------------|--|
| | Number of instruments 000s | Weighted average exercise price pence | Number of instruments 000s | Weighted average exercise price pence |
| Executive Options | — | — | 349 | 380.30 |
| Long Term Incentive Plan | — | — | 499 | — |
| Bonus Co-Investment Plan | — | — | — | — |
| Profit Growth Incentive Plan | — | — | 125 | — |

7,141 options were exercised by key management during the year (2007 – 7,141), whilst 1,287,264 options lapsed (2007 – 2,992,479).

10 Share-based payments

The Group has granted options over shares to employees for a number of years under different schemes. Where grants were made after 7 November 2002 they have been accounted for as required by IFRS 2 'Share-based Payment'. As permitted by the transitional arrangements of that standard, awards made before that date have not been so accounted. All options have been valued at the date of grant by an independent third party using a Monte Carlo model which uses the same principle as a binomial model.

No new awards were made in 2008. Details of awards made since 7 November 2002 are:

(a) Employee Sharesave Scheme

In September 2003 the Company awarded options to UK employees under an approved Sharesave scheme, the terms of which were that the employee entered into regular savings commitment up to a maximum of £250 per month for a three year period. The cumulative savings were then used to acquire options over a number of shares at a 10% discount to market price at the date of grant. There were no performance conditions but, in general, the employee must remain in employment for the three year period. Inputs to the valuation model were: option price 229p, volatility 38%, expected dividend yield 4.3%, risk-free interest rate 4.49% and a term of 3.25 years. There have been no further awards since September 2003.

(b) Executive Share Option Schemes (ESOS)

Awards were made to Directors and certain senior employees in March 2003 under the 2001 scheme and in September 2004, April 2005 and April 2006 under the 2004 scheme. In April 2007 awards were made to Directors under the 2004 scheme. Under both schemes options were granted with a fixed exercise price equal to the market price at the date of grant and subject to meeting performance conditions over a three year period. In the case of the 2001 scheme, the performance condition was based on earnings per share (eps) growth whilst under the 2004 scheme the condition is based on Total Shareholder Return (TSR) compared with that of comparator companies. Under the 2001 scheme only, where the performance condition is not satisfied in full after the first three years, retesting is carried out each year up to six years from the date of grant. Inputs to the valuation model were: option price 163p to 380.3p, volatility 31% to 38%, expected dividend yield 3.3% to 6.2%, risk-free interest rate 4.28% to 5.40% and expected terms of 6.4 years to 6.7 years.

(c) Long Term Incentive Plans (LTIP)

Awards were made to Directors and certain senior employees in March 2003 under the 2001 scheme and in September 2004, April 2006 and April 2007 under the 2004 scheme. In April 2005 awards were made to Directors under the 2004 scheme. Under both schemes, options were granted subject to TSR performance over a three year period compared with a comparator group. There is no retest facility under either scheme. Inputs to the valuation model were: option price nil, volatility 23% to 39%, expected dividend yield 3.3% to 6.2%, risk-free interest rate 4.05% to 5.40% and a term of 3 years to 4 years 9.5 months.

(d) Bonus Co-Investment Plan (BCIP)

Under the Bonus Co-Investment Plan, certain senior employees (excluding Directors) were entitled to use up to 10% of their gross short term annual bonus potential to purchase shares in the Company at market price. Provided they remain in employment for three years and the shares are retained for that period the Company matches those shares. For shares purchased by employees in 2004 the match was on a two for one basis and in 2005 was two and a half for one. In addition, in 2005 there was a further one for one match if certain profit targets are achieved. All shares under the scheme are purchased in the open market. Inputs to the valuation model were: option price nil, volatility, where applicable, 37%, expected dividend yield 4.9% to 5.4%, risk-free interest rate, where applicable, 4.94% and a term of 3 years.

(e) Profit Growth Incentive Plan (PGIP)

Awards were made in April 2007 under the PGIP to certain senior employees (excluding Directors). Any benefit under the PGIP will be deliverable dependent upon the extent to which profit growth targets are satisfied by the Group over a 3 year performance period; the Group's reported profit for the year prior to the year of award forms the baseline for this performance measure. The PGIP is a cash-based incentive plan, however, for certain very senior employees the benefit is deliverable in shares; the number of shares given below will be released following the performance period if the minimum targeted profit growth is achieved. A maximum of twice the amount of shares listed below will be released on achievement of the maximum profit target, with one and a half times the number being released for interim performance. No shares will be released and the awards will lapse if the minimum profit target is not achieved. Release is also conditional upon the satisfaction of a personal shareholding requirement. Any awards deliverable under the PGIP will be satisfied from GKN ordinary shares already in issue.

The expected volatility is based on historical volatility over a period commensurate with the term of the awards. The risk-free interest rate is the rate obtainable from government securities over the expected life of the equity incentive.

Further details of the ESOS, LTIP, BCIP and PGIP schemes are given in the remuneration report on pages 61 to 71.

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10 Share-based payments *continued*

Shares granted under each award were:

| Scheme | Date of grant | Number of shares 000s | Contractual life of options years |
|------------------------------|---------------|--------------------------|--------------------------------------|
| Employee Sharesave | 18/09/2003 | 1,880 | 3 |
| Executive Options | 19/03/2003 | 7,735 | 10 |
| | 16/09/2004 | 5,550 | 10 |
| | 05/04/2005 | 4,203 | 10 |
| | 11/04/2006 | 2,705 | 10 |
| | 02/04/2007 | 349 | 10 |
| Long Term Incentive Plan | 16/09/2004 | 1,133 | 3 |
| | 16/09/2004 | 2,006 | 10 |
| | 05/04/2005 | 613 | 10 |
| | 11/04/2006 | 850 | 3 |
| | 11/04/2006 | 1,883 | 10 |
| Bonus Co-Investment Plan | 10/08/2004 | 675 | 3 |
| | 21/04/2005 | 1,151 | 3 |
| Profit Growth Incentive Plan | 02/04/2007 | 333 | 3 |

A reconciliation of option movements over the year to 31 December 2008 is shown below:

| | 2008 | | 2007 | |
|----------------------------|----------------|---|----------------|---|
| | Number 000s | Weighted average exercise price pence | Number 000s | Weighted average exercise price pence |
| Outstanding at 1 January | 12,113 | 251.53 | 24,378 | 235.35 |
| Granted | — | — | 349 | 380.30 |
| Forfeited | (4,252) | 265.35 | (10,428) | 223.78 |
| Exercised | (480) | 193.37 | (2,186) | 223.99 |
| Outstanding at 31 December | 7,381 | 247.34 | 12,113 | 251.53 |
| Exercisable at 31 December | 3,334 | 189.22 | 213 | 231.45 |

For options outstanding at 31 December the range of exercise prices and weighted average contractual life is shown in the following table:

| Range of exercise price | 2008 | | 2007 | |
|-------------------------|-----------------------------|--|-----------------------------|--|
| | Number of shares 000s | Contractual weighted average remaining life years | Number of shares 000s | Contractual weighted average remaining life years |
| 130p–180p | 3,488 | 4.208 | 3,855 | 5.208 |
| 215p–230p | 413 | 0.867 | 650 | 1.409 |
| 240p–260p | — | — | 3,140 | 7.250 |
| 261p–280p | — | — | 7 | — |
| 300p–385p | 3,480 | 6.297 | 4,461 | 6.745 |

The weighted average share price during the period for options exercised over the year was 221.5p (2007 – 356.2p). The total charge for the year relating to share-based payment plans was £2 million (2007 – £6 million), all of which related to equity-settled share-based payment transactions. After deferred tax, the total charge was £2 million (2007 – £6 million).

Liabilities in respect of share-based payments were not material at either 31 December 2008 or 31 December 2007. There were no vested rights to cash or other assets at either 31 December 2008 or 31 December 2007.

11 Goodwill and other intangible assets

| | 2008 | Restated 2007 |
|---------------------------------------|------------|------------------|
| | £m | £m |
| Goodwill | | |
| Cost | | |
| At 1 January | 407 | 372 |
| Subsidiaries acquired | — | 30 |
| Currency variations | 142 | 5 |
| At 31 December | 549 | 407 |
| Accumulated impairment | | |
| At 1 January | 127 | 127 |
| Currency variations | 55 | — |
| At 31 December | 182 | 127 |
| Net book amount at 31 December | 367 | 280 |

Comparative information regarding cost and accumulated impairment has been re-presented to reclassify amortisation and impairment charges made under UK GAAP as cost. The net book amount is unchanged.

The carrying value of goodwill at 31 December comprised:

| Business segment | Business | Geographical location | 2008 | 2007 |
|---|--------------------|------------------------------|------------|------------|
| | | | £m | £m |
| Driveline | Driveshafts | Americas | 54 | 44 |
| Powder Metallurgy | Hoeganaes | North America | 24 | 17 |
| OffHighway | Wheels | Italy | 23 | 18 |
| Aerospace | Aerostructures | North America | 35 | 25 |
| | Propulsion Systems | North America | 93 | 67 |
| | Propulsion Systems | North America | 42 | 30 |
| | | | 271 | 201 |
| Other businesses not individually significant to the carrying value of goodwill | | | 96 | 79 |
| | | | 367 | 280 |

An impairment test is a comparison of the carrying value of the assets of a business or cash generating unit (CGU) to their recoverable amount. Where the recoverable amount is less than the carrying value, an impairment results. During the year, all goodwill was tested for impairment, with no impairment charges resulting.

For the purposes of carrying out impairment tests, the Group's total goodwill has been allocated to a number of CGUs and each of these CGUs has been separately assessed and tested. The size of a CGU varies but is never larger than a primary or secondary reportable segment. In some cases, the CGU is an individual subsidiary or operation. The allocation of goodwill by business segment is set out in note 2.

All of the recoverable amounts were measured based on value in use. Detailed forecasts for the next five years have been used in the majority of impairment tests except where a longer term more detailed forecast is available and appropriate. These forecasts are based on approved annual budgets and represent a best estimate of future performance.

Key assumptions

In determining the recoverable amount of all CGUs it is necessary to make a series of assumptions to estimate future cash flows. In each case, these key assumptions have been made by management reflecting past experience and are consistent with relevant external sources of information.

Operating cash flows

The main assumptions within forecast operating cash flow include the achievement of future sales prices and volumes (including reference to specific customer relationships, product lines and the use of industry relevant external forecasts of global vehicle production within Driveline businesses and consideration of specific volumes on certain US military and civil programmes within Aerospace), raw material input costs, the cost structure of each CGU and the ability to realise benefits from annual productivity improvements, the impact of foreign exchange rates upon selling price and cost relationships and the levels of ongoing capital expenditure required to support forecast production.

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11 Goodwill and other intangible assets *continued*

Pre-tax risk adjusted discount rates

Pre-tax risk adjusted discount rates are derived from risk-free rates based upon long term government bonds in the territory, or territories, within which each CGU operates. A relative risk adjustment (or 'beta') has been applied to risk-free rates to reflect the risk inherent in each CGU relative to all other sectors on average, determined using an average of the betas of comparable listed companies. Consideration is also given to both the amount and timing of estimated future tax cash flows.

Except for Driveline's operations in South America where rates ranging between 18% and 24% have been factored into impairment models, the range of pre-tax risk adjusted discount rates set out below have been used for impairment testing. The range of rates reflects the mix of geographical territories within CGUs within the segments.

Driveline: 10% (North America)–15% (Eastern European and certain Asia Pacific region countries)

Powder Metallurgy: 10%–12% (North America and Europe)

OffHighway: 10%–13% (North America and Europe)

Aerospace: 10%–11% (North America and Europe)

Long term growth rates

To forecast beyond the five years covered by detailed forecasts, a long term average growth rate has been used. In each case, this is not greater than the published Oxford Economic Forecast average growth rate in gross domestic product for the next five year period in the territory or territories where the CGU is primarily based. This results in a range of nominal growth rates from 0.7% to 7.0% with most countries between 2.0% and 4.0% in both years.

Goodwill sensitivity analysis

Sensitivity analysis to likely and potential changes in key assumptions has been reviewed. At 31 December 2008, the date of the Group's annual impairment test, the estimated recoverable amount of two individual CGUs within the Group's Aerospace (Propulsion Systems) and Powder Metallurgy (Hoeganaes) businesses exceeded their carrying value by £88 million and £74 million respectively. The table below shows the discount and long term growth rate assumptions used in the calculation of value in use and the amount by which each rate must change in isolation in order for the estimated recoverable amount to equal the carrying value.

| | Assumptions used in calculation of value in use | | Change required for the carrying value to exceed the recoverable amount | |
|--|---|-------------------|---|-------------------|
| | Aerospace | Powder Metallurgy | Aerospace | Powder Metallurgy |
| Pre-tax risk adjusted discount rate | 10% | 10% | 3.8% points | 3.7% points |
| Long term growth rate | 3.0% | 3.0% | 5.9% points | 5.4% points |
| Total pre-discounted forecast operating cash flows | £516 million | £423 million | 38% | 39% |

At 31 December 2008, the estimated recoverable amount of the Group's Driveline Driveshafts operations in the Americas and Asia Pacific regions exceeded their carrying value by £15 million and £43 million respectively. The table below shows the discount and long term growth rate assumptions used in the calculation of value in use and the amount by which each rate must change in isolation in order for the estimated recoverable amount to equal the carrying value.

| | Assumptions used in calculation of value in use | | Change required for the carrying value to exceed the recoverable amount | |
|--|---|--------------|---|--------------|
| | Americas | Asia Pacific | Americas | Asia Pacific |
| Pre-tax risk adjusted discount rate | 10%–24% | 10%–15% | 0.3% points | 2.3% points |
| Long term growth rate | 3.0%–7.0% | 0.7%–7.0% | 0.5% points | 4.2% points |
| Total pre-discounted forecast operating cash flows | £793 million | £331 million | 3% | 21% |

Other than as disclosed above, it is not considered that a reasonably possible change in any of the key assumptions would generate a different impairment test outcome to the one included in this annual report.

11 Goodwill and other intangible assets *continued*

| | 2008 | | | | 2007 | | | |
|---------------------------------------|-------------------------|-------------------------|---|-------------|-------------------------|-------------------------|---|-------------|
| | Development costs £m | Computer software £m | Assets arising on business combinations £m | Total £m | Development costs £m | Computer software £m | Assets arising on business combinations £m | Total £m |
| Intangible assets | | | | | | | | |
| Cost | | | | | | | | |
| At 1 January | 102 | 78 | 68 | 248 | 87 | 75 | 48 | 210 |
| Subsidiaries acquired | — | — | — | — | — | — | 21 | 21 |
| Capital expenditure | 7 | 6 | — | 13 | 15 | 5 | — | 20 |
| Disposals | (2) | — | — | (2) | — | (4) | — | (4) |
| Currency variations | 2 | 20 | 29 | 51 | — | 2 | (1) | 1 |
| At 31 December | 109 | 104 | 97 | 310 | 102 | 78 | 68 | 248 |
| Accumulated amortisation | | | | | | | | |
| At 1 January | 39 | 61 | 12 | 112 | 36 | 58 | 4 | 98 |
| Charge for the year | 4 | 6 | 10 | 20 | 3 | 6 | 8 | 17 |
| Disposals | — | — | — | — | — | (4) | — | (4) |
| Currency variations | 1 | 15 | 9 | 25 | — | 1 | — | 1 |
| At 31 December | 44 | 82 | 31 | 157 | 39 | 61 | 12 | 112 |
| Net book amount at 31 December | 65 | 22 | 66 | 153 | 63 | 17 | 56 | 136 |

The net book amount of assets arising on business combinations includes marketing related assets of £6 million (2007 – £4 million), customer related assets of £45 million (2007 – £38 million) and technology based assets of £15 million (2007 – £14 million). Computer software under finance leases amounts to £1 million (2007 – £2 million). In January 2009 development costs in an Aerospace subsidiary amounting to £21 million were realised in cash at a value in excess of the 31 December carrying values.

12 Property, plant and equipment

| | 2008 | | | | 2007 | | | |
|--|--------------------------|-----------------------------|--------------------------------|--------------|--------------------------|-----------------------------|--------------------------------|--------------|
| | Land and buildings £m | Other tangible assets £m | Capital work in progress £m | Total £m | Land and buildings £m | Other tangible assets £m | Capital work in progress £m | Total £m |
| Cost | | | | | | | | |
| At 1 January | 521 | 2,773 | 105 | 3,399 | 505 | 2,567 | 85 | 3,157 |
| Subsidiaries acquired | — | — | — | — | 3 | 16 | — | 19 |
| Capital expenditure | 6 | 117 | 69 | 192 | 6 | 92 | 76 | 174 |
| Disposals | (1) | (100) | — | (101) | (18) | (74) | — | (92) |
| Transfers | 5 | 77 | (82) | — | 5 | 55 | (60) | — |
| Currency variations | 165 | 876 | 31 | 1,072 | 20 | 117 | 4 | 141 |
| At 31 December | 696 | 3,743 | 123 | 4,562 | 521 | 2,773 | 105 | 3,399 |
| Accumulated depreciation and impairment | | | | | | | | |
| At 1 January | 115 | 1,822 | — | 1,937 | 111 | 1,692 | — | 1,803 |
| Charge for the year: | | | | | | | | |
| Charged to trading profit | | | | | | | | |
| Depreciation | 11 | 154 | — | 165 | 11 | 130 | — | 141 |
| Impairments | — | 1 | — | 1 | — | 1 | — | 1 |
| Restructuring and impairment | 14 | 113 | — | 127 | (1) | (8) | — | (9) |
| Disposals | (1) | (96) | — | (97) | (10) | (69) | — | (79) |
| Currency variations | 45 | 587 | — | 632 | 4 | 76 | — | 80 |
| At 31 December | 184 | 2,581 | — | 2,765 | 115 | 1,822 | — | 1,937 |
| Net book amount at 31 December | 512 | 1,162 | 123 | 1,797 | 406 | 951 | 105 | 1,462 |

Included within Other tangible assets at net book amount are plant and equipment £1,134 million (2007 – £928 million), fixtures and fittings £26 million (2007 – £21 million) and motor vehicles £2 million (2007 – £2 million). The net book amount of assets under finance leases is land and buildings £3 million (2007 – £7 million) and plant and equipment £1 million (2007 – £1 million).

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13 Investments in joint ventures

| | 2008 £m | 2007 £m |
|---|------------|------------|
| Group share of net assets | | |
| At 1 January | 100 | 83 |
| Share of post-tax earnings of joint ventures | 16 | 24 |
| Dividends paid | (24) | (13) |
| Actuarial gain on post-employment obligations, including deferred tax | — | 1 |
| Additions | 1 | — |
| Currency variations | 36 | 5 |
| At 31 December | 129 | 100 |
| Accumulated impairment | | |
| Charge for the year | 10 | — |
| At 31 December | 10 | — |
| Net book amount at 31 December | 119 | 100 |
| Group share of net book amount at 31 December | | |
| Non-current assets | 97 | 70 |
| Current assets | 89 | 91 |
| Current liabilities | (54) | (50) |
| Non-current liabilities | (13) | (11) |
| | 119 | 100 |

The joint ventures have no significant contingent liabilities to which the Group is exposed and nor has the Group any significant contingent liabilities in relation to its interest in the joint ventures other than bank guarantees set out in note 27. The share of capital commitments of the joint ventures is shown in note 29.

| | 2008 £m | 2007 £m |
|---|------------|------------|
| Group share of results of joint ventures | | |
| Sales | 241 | 253 |
| Operating costs and other income | (221) | (221) |
| Trading profit | 20 | 32 |
| Net financing costs | — | — |
| Profit before taxation | 20 | 32 |
| Taxation | (4) | (8) |
| Share of post-tax earnings — before impairments | 16 | 24 |
| Impairment, including tax on impairment of nil | (10) | — |
| Share of post-tax earnings | 6 | 24 |

The impairment charge attributable to a provision for diminution in value, which is entirely attributable to Driveline, arises as customer supply logistics are addressed in selected geographical territories and joint venture relationships are unwound.

The segmental analysis of the Group's share of joint venture sales and trading profit is set out below:

| | 2008 | | 2007 | |
|------------------|-------------|-------------------------|-------------|-------------------------|
| | Sales £m | Trading profit £m | Sales £m | Trading profit £m |
| Driveline | 145 | 15 | 130 | 17 |
| Other Automotive | 92 | 6 | 120 | 15 |
| OffHighway | 4 | — | 3 | — |
| Aerospace | — | (1) | — | — |
| | 241 | 20 | 253 | 32 |

14 Other receivables and investments

| | 2008 £m | 2007 £m |
|---|------------|------------|
| Other investments | — | — |
| Indirect taxes and amounts recoverable under employee benefit plans | 19 | 13 |
| Other receivables | 4 | 9 |
| | 23 | 22 |

Other investments mainly comprise the Group's net investment in GKN Aerospace Services Structures Corp. which is an entity in which the Group has, since 2003, had a 100% share in the equity. This corporation operates under a proxy agreement with the United States Department of Defense developing high technology, classified products for the Joint Strike Fighter. The agreement currently places significant restrictions on the Group's management and control of the business for the life of the contract so that, in accordance with IAS 27 it has been excluded from the consolidation and treated as an investment. The investment, which is fully provided, is stated at cost less provision for diminution. At 31 December 2008, under the accounting policies of GKN Aerospace Services Structures Corp., the excluded net liabilities were £8 million (2007 – £5 million) and the operating loss for the year then ended was £1 million (2007 – £1 million). No goods or services were provided to GKN Aerospace Services Structures Corp. by the Group during 2008 and 2007. GKN Aerospace Services Structures Corp. supplied goods to the Group amounting to £1 million during 2008 (2007 – nil). Transactions between the Group and GKN Aerospace Services Structures Corp. are priced on an 'arm's length' basis.

15 Inventories

| | 2008 £m | 2007 £m |
|------------------|------------|------------|
| Raw materials | 315 | 264 |
| Work in progress | 242 | 176 |
| Finished goods | 161 | 112 |
| | 718 | 552 |

Inventories of £64 million (2007 – £51 million) are carried at net realisable value. The amount of any write-down of inventory recognised as an expense in the period was £4 million (2007 – £2 million).

16 Trade and other receivables

| | 2008 £m | 2007 £m |
|---|------------|------------|
| Trade receivables | 550 | 509 |
| Amounts owed by joint ventures | 11 | 10 |
| Other receivables | 39 | 19 |
| Prepayments | 16 | 14 |
| Indirect taxes recoverable | 29 | 19 |
| | 645 | 571 |
| Provisions for doubtful debts against trade receivables | | |
| At 1 January | (6) | (5) |
| Charge for the year: | | |
| Additions | (6) | (3) |
| Unused amounts reversed | 1 | 1 |
| Amounts used | 4 | 1 |
| Currency variations | (2) | — |
| At 31 December | (9) | (6) |
| Ageing analysis of trade receivables and amounts owed by joint ventures past due but not impaired | | |
| Up to 30 days overdue | 47 | 40 |
| 31–60 days overdue | 13 | 11 |
| 61–90 days overdue | 6 | 4 |
| More than 90 days overdue | 11 | 7 |
| Trade receivables subject to provisions for doubtful debts | 15 | 12 |

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17 Trade and other payables

| | 2008 | | 2007 | |
|---|---------------|-------------------|---------------|-------------------|
| | Current £m | Non-current £m | Current £m | Non-current £m |
| Trade and other payables | (685) | (1) | (602) | (1) |
| Amounts owed to joint ventures | (3) | — | (2) | — |
| Accrued interest | (28) | — | (26) | — |
| Payroll taxes, indirect taxes and audit fees | (43) | (1) | (36) | (2) |
| Amounts due to employees and employee benefit plans | (122) | (31) | (119) | (22) |
| Government grants | (1) | (5) | (1) | (5) |
| Customer advances and deferred income | (90) | — | (51) | (1) |
| | (972) | (38) | (837) | (31) |

Non-current trade and other payables fall due within 2 years.

18 Net borrowings

(a) Analysis of net borrowings

| | Notes | Current | Non-current | | | Total £m | Total £m |
|--|-------|--------------------------|---------------------------|----------------------------|-------------------------------|--------------|--------------|
| | | Within one year £m | One to two years £m | Two to five years £m | More than five years £m | | |
| 2008 | | | | | | | |
| Other borrowings | | | | | | | |
| £350 million 6 ³ / ₄ % 2019 unsecured bond | i | — | — | — | (346) | (346) | (346) |
| £325 million 7% 2012 unsecured bond | i | — | — | (325) | — | (325) | (325) |
| Other secured US\$ denominated loan | | (2) | (1) | (4) | (5) | (10) | (12) |
| Other long term borrowings | | (7) | (37) | (3) | — | (40) | (47) |
| Finance lease obligations | iii | (1) | (1) | (2) | (1) | (4) | (5) |
| Bank overdrafts | | (20) | — | — | — | — | (20) |
| Other short term bank borrowings | | (67) | — | — | — | — | (67) |
| Borrowings | | (97) | (39) | (334) | (352) | (725) | (822) |
| Bank balances and cash | | 102 | — | — | — | — | 102 |
| Short term bank deposits | ii | 12 | — | — | — | — | 12 |
| Cash and cash equivalents | iv | 114 | — | — | — | — | 114 |
| Net borrowings | | 17 | (39) | (334) | (352) | (725) | (708) |
| 2007 | | | | | | | |
| Other borrowings | | | | | | | |
| £350 million 6 ³ / ₄ % 2019 unsecured bond | i | — | — | — | (346) | (346) | (346) |
| £325 million 7% 2012 unsecured bond | i | — | — | (325) | — | (325) | (325) |
| £30 million 12 ³ / ₈ % 2008 Westland Group plc debenture | i | (30) | — | — | — | — | (30) |
| Other secured US\$ denominated loan | | (1) | (1) | (6) | (1) | (8) | (9) |
| Other long term borrowings | | (2) | (4) | (2) | — | (6) | (8) |
| Finance lease obligations | iii | (1) | (1) | (2) | (8) | (11) | (12) |
| Bank overdrafts | | (32) | — | — | — | — | (32) |
| Other short term bank borrowings | | (26) | — | — | — | — | (26) |
| Borrowings | | (92) | (6) | (335) | (355) | (696) | (788) |
| Bank balances and cash | | 135 | — | — | — | — | 135 |
| Short term bank deposits | ii | 147 | — | — | — | — | 147 |
| Cash and cash equivalents | iv | 282 | — | — | — | — | 282 |
| Net borrowings | | 190 | (6) | (335) | (355) | (696) | (506) |

18 Net borrowings *continued*

Other borrowings include: Unsecured £350 million (2007 – £350 million) 6³/₄% bond maturing in 2019 less unamortised issue costs of £4 million (2007 – £4 million), unsecured £325 million (2007 – £325 million) 7% bond maturing in 2012 less unamortised issue costs of nil (2007 – nil) and secured term loans of £10 million (2007 – £39 million). These secured term loans include nil (2007 – £30 million) debenture stocks of Westland Group plc, redeemed in the year, which were secured by a floating charge on the undertaking and net assets including financial assets of nil (2007 – £88 million) of that company and certain of its subsidiaries and guaranteed by GKN Holdings plc, and £10 million (2007 – £9 million) secured by way of a fixed and floating charge on certain Aerospace fixed assets.

Notes

- (i) Denotes borrowings at fixed rates of interest until maturity. All other borrowings and cash and cash equivalents are at variable interest rates.
- (ii) The average interest rate on short term bank deposits was 2.22% (2007 – 5.48%). Deposits at 31 December 2008 have no fixed maturity date (2007 – 2 days).
- (iii) Finance lease obligations gross of finance charges fall due as follows: £1 million within one year (2007 – £2 million); £4 million in one to five years (2007 – £8 million) and £2 million in more than five years (2007 – £12 million).
- (iv) £10 million (2007 – £18 million) of the Group's cash and cash equivalents are held by the Group's captive insurance company to maintain solvency requirements and as collateral for Letters of Credit issued to the Group's principal external insurance providers. These funds, therefore, are not circulated within the Group on demand.

(b) Fair values of borrowings and cash and cash equivalents

| | 2008 | | 2007 | |
|--|------------------|------------------|------------------|------------------|
| | Book value £m | Fair value £m | Book value £m | Fair value £m |
| Other borrowings | (730) | (520) | (718) | (736) |
| Finance lease obligations | (5) | (5) | (12) | (12) |
| Bank overdrafts and other short term bank borrowings | (87) | (87) | (58) | (58) |
| Bank balances and cash | 102 | 102 | 135 | 135 |
| Short term bank deposits | 12 | 12 | 147 | 147 |
| | (708) | (498) | (506) | (524) |

The following methods and assumptions were used in estimating fair values for financial instruments:

Unsecured bank overdrafts, other short term bank borrowings, bank balances and cash and short term bank deposits approximate to book value due to their short maturities. For other borrowings and finance lease obligations carrying fixed rates of interest, the repayments which the Group is committed to make have been discounted at the relevant interest rates applicable at 31 December 2008. Bonds included within other borrowings have been valued using quoted closing market values.

Notes to the Financial Statements

continued

19 Financial risk management

The Group's activities give rise to a number of financial risks: market risk, credit risk and liquidity risk. Market risk includes foreign exchange risk, cash flow and fair value interest rate risk and commodity price risk. The Group has in place risk management policies that seek to limit the adverse effects on the financial performance. Derivative financial instruments, mainly forward foreign exchange contracts, are used to hedge risk exposures that arise in the ordinary course of business.

Risk management policies have been set by the Board and are implemented by the central Treasury Department that receives regular reports from all the operating companies to enable prompt identification of financial risks so that appropriate actions may be taken. The Treasury Department has a policy and procedures manual that sets out specific guidelines to manage foreign exchange risks, interest rate risk, financial credit risk and liquidity risk and the use of financial instruments to manage these. These disclosures should be read in conjunction with the financing and risk commentary in the business review on pages 36 to 39.

(a) Foreign exchange risk

The Group has transactional currency exposures arising from sales or purchases by operating subsidiaries in currencies other than the subsidiaries' functional currency. These exposures are forecast on a monthly basis by operating companies and are reported to the central Treasury Department. Under the Group's foreign exchange policy, such exposures are hedged on a reducing percentage basis over a number of forecast time horizons.

The Group has a significant investment in overseas operations. As a result, the sterling value of the Group's balance sheet can be affected by movements in exchange rates. Until December 2008, the Group's policy was to mitigate the effect of these translational currency exposures for major currencies (US dollar, euro and yen) by hedging 70% to 90% of the net investment in overseas operations using forward foreign currency contracts or foreign currency borrowings. Such hedging instruments were in place until maturity in December 2008. The net investment hedging policy was suspended in December 2008 due to concerns about settlement values at a time of exchange rate volatility.

The main impact of foreign exchange risk on the Group's results arises from the translation into sterling of the results of operations outside of the UK. The Group's largest exposures are the euro and the US dollar where a 1% movement in the average rate impacts trading profit of subsidiaries and joint ventures by £1.2 million and £0.8 million respectively.

Regarding financial instruments, a 1% strengthening of sterling against the currency rates indicated below would have the following impact on operating profit:

| | Trading profit | | |
|-----------|--------------------------------|--|---------------------------|
| | Payables and receivables £m | Derivative financial instruments £m | Intra-group funding £m |
| Euro | 0.2 | (0.4) | (1.3) |
| US dollar | (0.3) | 8.3 | (1.0) |

The derivative sensitivity analysis has been prepared by reperforming the calculations used to determine the balance sheet values adjusted for the changes in the individual currency rates indicated with all other cross currency rates remaining constant. The sensitivity is a fair value change relating to derivatives for which the underlying transaction has not occurred at 31 December. The Group intends to hold all such derivatives to maturity. The analysis of other items has been prepared based on an analysis of a currency balance sheet.

Analysis of net borrowings by currency:

| | 2008 | | | 2007 | | |
|-----------|------------------|---------------------------------|-------------|------------------|---------------------------------|-------------|
| | Borrowings £m | Cash and cash equivalents £m | Total £m | Borrowings £m | Cash and cash equivalents £m | Total £m |
| Sterling | (726) | 24 | (702) | (702) | 152 | (550) |
| US dollar | (27) | 15 | (12) | (36) | 10 | (26) |
| Euro | (10) | 35 | 25 | (12) | 41 | 29 |
| Others | (59) | 40 | (19) | (38) | 79 | 41 |
| | (822) | 114 | (708) | (788) | 282 | (506) |

19 Financial risk management *continued*

(b) Interest rate risk

The Group is exposed to fair value interest rate risk on fixed rate borrowings and cash flow interest rate risk on variable rate net borrowings/funds. The Group's policy is to optimise interest cost in reported earnings and reduce volatility in the debt related element of the Group's cost of capital. This policy is achieved by maintaining a target range of fixed and floating rate debt for discrete annual periods, over a defined time horizon. The Group's normal policy is to require interest rates to be fixed for 30% to 70% of the level of underlying borrowings forecast to arise over a 12 month horizon. This policy remains suspended following a Board decision in December 2004 after receipt of the original sale proceeds on the sale of the GKN share in AgustaWestland given the absence of floating rate bank debt. Following repayment of the fixed interest Westland Group plc debenture in September 2008 the Group has operated close to the policy parameters. At 31 December 2008 83% (2007 – 89%) of the Group's gross borrowings were subject to fixed interest rates.

As at 31 December 2008 £12 million (2007 – £147 million) was in bank deposits of which £12 million (2007 – £145 million) was on deposit with UK banks.

A 1% change in interest rates would have a £0.4 million impact on net interest. This sensitivity flexes the interest rate of variable rate borrowings, assuming the level and currency mix at 31 December 2008 remains in place for 12 months.

(c) Credit risk

The Group is exposed to credit-related losses in the event of non-performance by counterparties to financial instruments. In terms of substance, and consistent with the related balance sheet presentation, the Group considers it has two types of credit risk; operational and financial. Operational credit risk relates to non-performance by customers in respect of trade receivables and by suppliers in respect of other receivables. Financial credit risk relates to non-performance by banks and similar institutions in respect of cash and deposits, facilities and financial contracts, including forward foreign currency contracts.

Operational

As tier-one suppliers to automotive, off-highway and aerospace original equipment manufacturers, the Group may have substantial amounts outstanding with a single customer at any one time. The credit profiles of such original equipment manufacturers are available from credit rating agencies. The failure of any such customer to honour its debts could materially impact the Group's results. However, there are many advantages in these relationships. In certain parts of the Group, mainly Industrial Distribution Services within Driveline and OffHighway there are a greater proportion of amounts receivable from small and medium sized customers.

Credit risk and customer relationships are managed at a number of levels within the Group. At a subsidiary level documented credit control reviews are required to be held at least every month. The scope of these reviews includes amounts overdue and credit limits. At a divisional level debtor ratios, overdue accounts and overall performance are reviewed regularly. Provisions for doubtful debts are determined at these levels based upon the customer's ability to pay and other factors in the Group's relationship with the customer.

At 31 December the amount of trade receivables analysed by major segment due from the largest 5 customers as a proportion of total trade receivables is as follows:

| | 2008 % | 2007 % |
|-------------------|-----------|-----------|
| Driveline | 48 | 46 |
| Powder Metallurgy | 20 | 21 |
| OffHighway | 32 | 32 |
| Aerospace | 54 | 45 |

The amount of trade receivables outstanding at the year end does not represent the maximum exposure to operational credit risk due to the normal patterns of supply and payment over the course of a year. Based on management information collected as at month ends the maximum level of trade receivables at any one point during the year was £714 million (2007 – £650 million).

Financial

Credit risk is mitigated by the Group's policy of only selecting counterparties with a strong investment graded long term credit rating, normally at least AA- or equivalent, and assigning financial limits to individual counterparties.

The maximum exposure with a single bank for deposits is £12 million (2007 – £25 million), whilst the maximum mark to market exposure for forward foreign currency contracts at 31 December 2008 to a single bank was nil (2007 – £3 million). The amounts on deposit at year end represent the Group's maximum exposure to financial credit risk with Group indebtedness varying over the course of a year in line with normal financing and trading patterns.

Notes to the Financial Statements

continued

19 Financial risk management *continued*

(d) Capital risk management

The Group's objectives when managing capital are to safeguard the ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain a capital structure which optimises the cost of capital.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce borrowings.

The Group monitors capital on the basis of the ratio of Gross borrowings to EBITDA.

The Group seeks to operate at an EBITDA of subsidiaries to Gross debt ratio of 2.5 times or less and the ratios at 31 December 2008 and 2007 were as follows:

| | 2008 £m | 2007 £m |
|---|------------------|------------------|
| Gross borrowings | 822 | 788 |
| EBITDA | 377 | 428 |
| Gross borrowings to EBITDA ratio | 2.2 times | 1.8 times |

The Group's only external banking covenant requires an EBITDA of subsidiaries to net interest payable and receivable ratio of 3.5 times or more. The ratios at 31 December 2008 were as follows:

| | 2008 £m | 2007 £m |
|--|------------------|-------------------|
| EBITDA | 377 | 428 |
| Net interest payable and receivable | (47) | (43) |
| EBITDA to net interest payable and receivable ratio | 8.0 times | 10.0 times |

(e) Liquidity risk

The Group is exposed to liquidity risk as part of its normal financing and trading cycle at times when peak borrowings are required. Borrowings normally peak in May and September following dividend and bond coupon payments. The Group's policies are to ensure that sufficient liquidity is available to meet obligations when they fall due and to maintain sufficient flexibility in order to fund investment and acquisition objectives. Liquidity needs are assessed through short and long term forecasts. Committed bank facilities of £350 million expire in July 2010 and on which there were drawings at the year end of £34 million (2007 – £350 million expiring in July 2010 and undrawn at the year end). A further £9 million of the facility had been utilised for Letters of Credit on Group borrowings in China. Additional committed facilities were agreed in the year amounting to £55 million, maturing in 2013 and €50 million maturing in 2011. Committed facilities are provided through 12 banks.

Maturity analysis of borrowings and derivative financial instrument liabilities

| | Within one year £m | One to two years £m | Two to five years £m | More than five years £m | Total £m |
|---|--------------------------|---------------------------|----------------------------|-------------------------------|-------------|
| 2008 | | | | | |
| Borrowings (note 18) | (97) | (39) | (334) | (352) | (822) |
| Contractual interest payments and finance lease charges | (50) | (49) | (107) | (144) | (350) |
| Derivative financial instruments liabilities — receipts | 319 | 111 | 220 | 211 | 861 |
| Derivative financial instruments liabilities — payments | (373) | (133) | (269) | (260) | (1,035) |
| | (201) | (110) | (490) | (545) | (1,346) |
| 2007 | | | | | |
| Borrowings (note 18) | (92) | (6) | (335) | (355) | (788) |
| Contractual interest payments and finance lease charges | (50) | (47) | (128) | (169) | (394) |
| Derivative financial instruments liabilities — receipts | 883 | 16 | 23 | 18 | 940 |
| Derivative financial instruments liabilities — payments | (894) | (17) | (23) | (18) | (952) |
| | (153) | (54) | (463) | (524) | (1,194) |

There is no significant difference in the contractual undiscounted value of other financial liabilities from the amounts stated in the balance sheet and balance sheet notes.

19 Financial risk management *continued***(f) Commodity price risk**

The Group is exposed to changes in commodity prices, particularly of metals, which has a significant impact on input costs and the overall financial results. The Group seeks to mitigate this exposure in a variety of ways including medium term price agreements, surcharges and advance purchasing. In rare circumstances and only in respect of certain specified risks, the Group uses derivative commodity hedging instruments. The impact of such financial instruments in respect of the overall commodity price risk is not material.

(g) Categories of financial assets and financial liabilities

| | Loans and receivables £m | Amortised cost £m | Held for trading | | Derivatives used for hedging £m | Total £m |
|-----------------------------------|--------------------------------|-------------------------|---------------------------|--------------------------------|--|-------------|
| | | | Financial assets £m | Financial liabilities £m | | |
| 2008 | | | | | | |
| Other receivables and investments | 4 | — | — | — | — | 4 |
| Trade and other receivables | 600 | — | — | — | — | 600 |
| Derivative financial instruments | — | — | 62 | (184) | (8) | (130) |
| Cash and cash equivalents | 114 | — | — | — | — | 114 |
| Borrowings | — | (822) | — | — | — | (822) |
| Trade and other payables | — | (717) | — | — | — | (717) |
| Provisions | — | (5) | — | — | — | (5) |
| | 718 | (1,544) | 62 | (184) | (8) | (956) |
| 2007 | | | | | | |
| Other receivables and investments | 9 | — | — | — | — | 9 |
| Trade and other receivables | 538 | — | — | — | — | 538 |
| Derivative financial instruments | — | — | 24 | (13) | (16) | (5) |
| Cash and cash equivalents | 282 | — | — | — | — | 282 |
| Borrowings | — | (788) | — | — | — | (788) |
| Trade and other payables | — | (631) | — | — | — | (631) |
| Provisions | — | (1) | — | — | — | (1) |
| | 829 | (1,420) | 24 | (13) | (16) | (596) |

Notes to the Financial Statements

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20 Derivative financial instruments

| | 2008 | | | 2007 | |
|---|--------------|-------------------|-------------------|--------------|-------------------|
| | Current | | Non-current | Current | |
| | Assets £m | Liabilities £m | Liabilities £m | Assets £m | Liabilities £m |
| Forward currency contracts | | | | | |
| not hedge accounted | 13 | (171) | — | 23 | (6) |
| hedge accounted | — | (6) | (2) | 1 | — |
| Commodity contracts — not hedge accounted | — | (2) | — | — | (1) |
| Embedded derivatives | 49 | (11) | — | 1 | (6) |
| Net investment hedges | — | — | — | — | (17) |
| | 62 | (190) | (2) | 25 | (30) |

The amounts in respect of embedded derivatives primarily represent the movement between 1 January 2008 and 31 December 2008 or date of maturity in the value of the embedded derivatives in commercial contracts between European Aerospace subsidiaries and customers and suppliers outside the USA which are denominated in US dollars.

Forward foreign exchange contracts, commodity contracts and embedded derivatives are marked to market using published prices, with forward foreign exchange contracts and commodity contracts being settled on a net basis.

Hedge accounting

Cash flow hedges

The Group manages exposure to foreign currency fluctuations on outstanding purchase and sale agreements using forward foreign currency contracts. The Group has adopted transactional foreign exchange hedge accounting in a limited number of contracts. The value of forward foreign exchange contracts subject to hedge accounting was £8 million liability (2007 – £1 million asset). The net cash flows and profit impact will occur during 2009 to 2012 (2007 – during 2008). A £7 million loss was recognised in equity during the year (2007 – £1 million gain) in respect of contracts outstanding at 31 December. An accumulated gain of £1 million was removed from equity during the year and included in the income statement as a £1 million gain in cost of sales. Cash flow hedging was 100% effective during 2008 and 2007.

Net investment hedging

See note 19. For the purposes of hedge accounting, net investment hedging was 100% effective during 2008 and 2007.

21 Provisions

| | Restructuring £m | Warranty £m | Legal and | Other £m | Total £m |
|----------------------------|---------------------|----------------|---------------------|-------------|--------------|
| | | | environmental £m | | |
| At 1 January 2008 | (28) | (13) | (21) | (34) | (96) |
| Charge for the year: | | | | | |
| Additions | (21) | (7) | (4) | (4) | (36) |
| Unused amounts reversed | — | 1 | — | 7 | 8 |
| Amounts used | 26 | 5 | 3 | 7 | 41 |
| Currency variations | (7) | (4) | (5) | (4) | (20) |
| At 31 December 2008 | (30) | (18) | (27) | (28) | (103) |
| Due within one year | (23) | (10) | (10) | (6) | (49) |
| Due in more than one year | (7) | (8) | (17) | (22) | (54) |
| | (30) | (18) | (27) | (28) | (103) |

21 Provisions *continued*

Restructuring

Restructuring provisions outstanding at 31 December 2008 relate primarily to the estimated future cash outflows in respect of redundancies and onerous contracts (predominantly leases) arising from Group strategic restructuring programmes, details of the charges in respect of which are included in note 3. Amounts are only set aside when irrevocable commitments exist at the balance sheet date and these invariably reflect actual or constructive contractual arrangements which indicate the amount and most likely timing of flows. Cash outflows that are expected to arise beyond 12 months in part relate to lease contracts where the average remaining maturity is 5 years from 31 December as well as phased retirement scheme payments in European Driveline and OffHighway businesses which have between 3 and 5 years to run.

Warranty

Provisions set aside for warranty exposures either relate to amounts provided systematically based on historical experience under contractual warranty obligations attaching to the supply of goods or specific provisions created in respect of individual customer issues undergoing commercial resolution and negotiation. In the event of a claim, settlement will be negotiated with the customer based on supply of replacement products and compensation for the customer's associated costs. Amounts set aside represent management's best estimate of the likely settlement and the timing of any resolution with the relevant customer.

Legal and environmental

Legal provisions amounting to £9 million (2007 – £5 million) relate to management estimates of amounts required to settle or remove litigation actions that have arisen in the normal course of business. Further details are not provided to avoid the potential of seriously prejudicing the Group's stance in law. Amounts unused and reversed only arise when the matter is formally settled or when a material change in the litigation action occurs where legal advice confirms lower amounts need to be retained to cover the exposure.

As a consequence of primarily legacy activities a small number of sites in the Group are subject to environmental remediation actions, which in all cases are either agreed formally with relevant local and national authorities and agencies or represent management's view of the likely outcome having taken appropriate expert advice and following consultation with appropriate authorities and agencies. Amounts charged and carried reflect the current best estimates of the likely cost of remediation and inherent timings.

Other

Other provisions include claims provisions held within the Group's captive insurance company £10 million (2007 – £8 million), provisions held in respect of onerous loss making contracts £6 million (2007 – £11 million), and long service non-pension and other employee related obligations arising primarily in the Group's continental European subsidiaries £12 million (2007 – £15 million). Claims provisions and charges are established in accordance with external insurance and actuarial advice. The onerous loss making contract provisions relate to specific non-cancellable contractual commitments where it is anticipated that unavoidable net operating losses will arise.

Vacant leasehold property provisions included in Restructuring and Other provisions above amount to £5 million (2007 – £1 million).

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22 Share capital

| | Authorised | | Allotted, called up and fully paid | |
|--|----------------|----------------|------------------------------------|----------------|
| | 2008 £m | 2007 £m | 2008 £m | 2007 £m |
| Ordinary shares of 50p each | 450 | 450 | 372 | 372 |
| | Number 000s | Number 000s | Number 000s | Number 000s |
| Ordinary shares of 50p each | | | | |
| At 1 January | 900,000 | 900,000 | 743,699 | 741,513 |
| Shares issued under the share option schemes | — | — | 205 | 2,186 |
| At 31 December | 900,000 | 900,000 | 743,904 | 743,699 |

At the last Annual General Meeting, shareholder authority was obtained for the Company to purchase up to a maximum of 70.5 million of its own ordinary shares (representing 10% of the issued share capital of the Company on 31 December 2007) for a period ending on the earlier of the next Annual General Meeting or 1 August 2009, provided that certain conditions (relating to the purchase price) are met. The Notice of Annual General Meeting proposes that shareholders approve a resolution updating and renewing this authority. Shares in the Company may also be purchased by the GKN Employee's Share Ownership Plan (ESOP) Trust.

At 31 December 2008 there were 38,384,253 ordinary shares of 50p each (nominal value £19.2 million (2007 – £19.3 million)) held as treasury shares. No shares were purchased in the open market during 2008 or 2007. A total of 274,889 shares were transferred out of treasury during 2008 to satisfy the exercise of options by former employees under share option schemes.

The remaining treasury shares, which represented 5.2% (2007 – 5.2%) of the called up share capital at the end of the year, have not been cancelled but are held as treasury shares and represent a deduction from shareholders' equity.

During the year shares issued under the share option schemes generated less than £1 million (2007 – £5 million).

23 Changes in equity

| | Share capital £m | Share premium £m | Retained earnings £m | Other reserves | | | Shareholders' equity £m | Minority interests – equity £m | Total equity £m |
|--|---------------------|---------------------|-------------------------|------------------------|-----------------------|----------------------|----------------------------|-----------------------------------|--------------------|
| | | | | Exchange reserve £m | Hedging reserve £m | Other reserves £m | | | |
| At 1 January 2007 | 371 | 25 | 589 | (98) | 45 | (40) | 892 | 16 | 908 |
| Total recognised income and expense for the year | — | — | 329 | 64 | (28) | — | 365 | 4 | 369 |
| Share issues | 1 | 4 | — | — | — | — | 5 | — | 5 |
| Share-based payments | — | — | 6 | — | — | — | 6 | — | 6 |
| Transfers | — | — | 1 | — | — | (1) | — | — | — |
| Dividends | — | — | (91) | — | — | — | (91) | (1) | (92) |
| At 31 December 2007 | 372 | 29 | 834 | (34) | 17 | (41) | 1,177 | 19 | 1,196 |
| Total recognised income and expense for the year | — | — | (492) | 535 | (221) | — | (178) | 6 | (172) |
| Sale of treasury shares | — | — | 1 | — | — | — | 1 | — | 1 |
| Share-based payments | — | — | 2 | — | — | — | 2 | — | 2 |
| Minority investment | — | — | — | — | — | — | — | 1 | 1 |
| Transfers | — | — | 42 | (2) | — | (40) | — | — | — |
| Dividends | — | — | (97) | — | — | — | (97) | (3) | (100) |
| At 31 December 2008 | 372 | 29 | 290 | 499 | (204) | (81) | 905 | 23 | 928 |

Retained earnings include £99 million (2007 – £100 million) of the Company's shares held in treasury. Other reserves include accumulated reserves where distribution has been restricted due to legal or fiscal requirements and accumulated adjustments in respect of piecemeal acquisitions. The accumulated debit balance includes the impact of the demerger transaction of Industrial Services in 2001.

24 Acquisitions

There were no acquisitions in 2008.

Finalisation of fair value adjustments in respect of the 2007 acquisition of Teleflex Aerospace Manufacturing Group of Teleflex Inc on 29 June 2007 were finalised in the first half of 2008. There have been no amendments to the provisional fair values disclosed in the consolidated financial statements for the year ended 31 December 2007.

Post balance sheet acquisition

On 5 January 2009, the Group acquired the wing component and sub-assembly operation of Airbus UK which is located on the Airbus Filton site in the UK. The acquisition of the Filton facility delivers considerable benefits as the Group becomes a leading global player in critical wing structures and composites and establishes a strategic supplier relationship with Airbus.

The contractual consideration of £176 million after allowing for pension funding and other employee related matters will result in an aggregate cash payment of up to £136 million to Airbus. This amount comprises an initial cash payment of £96 million paid on completion with a subsequent amount payable following finalisation of acquisition date inventory adjustments and £36 million payable in annual instalments over the six years 2010–2015 contingent on revenue metrics. Professional fees and other costs directly attributed to the acquisition are expected to amount to £6 million. The cash spend in 2008 on this acquisition was £1 million.

The fair value exercise is at an early stage and due to its proximity to the year end it is impracticable to determine appropriate fair values. Provisional book and fair values will be disclosed in the Group's 2009 Half Year Report. Initial unaudited book values at the date of acquisition recorded in 2009 management accounts reflect fixed assets of £48 million and inventory of £41 million.

As previously included in announcements to the Stock Exchange it is expected that the Filton operation will generate sales in 2009 of approximately £375 million and will be earnings accretive and cash generative. 2009 trading margin is estimated at 6% before the impact of fair value adjustments, particularly to inventory and property, plant and equipment, which will be determined during the fair value exercise.

On completion of the acquisition the Group secured additional borrowing facilities amounting to £180 million.

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25 Cash flow reconciliations

| | 2008 £m | 2007 £m |
|--|--------------|--------------|
| Cash generated from operations | | |
| Operating profit/(loss) | (86) | 221 |
| Adjustments for: | | |
| Depreciation, impairment and amortisation of fixed assets | | |
| Charged to trading profit | | |
| Depreciation | 165 | 141 |
| Impairment | 1 | 1 |
| Amortisation | 10 | 9 |
| Amortisation of non-operating intangible assets arising on business combinations | 10 | 8 |
| Restructuring and impairment charges | 127 | (9) |
| Changes in fair value of derivative financial instruments | 133 | 10 |
| Amortisation of capital grants | (2) | (2) |
| Net profits on sale of fixed assets | (1) | (8) |
| Charge for share-based payments | 2 | 6 |
| Movement in post-employment obligations | (26) | (29) |
| Change in inventories | 7 | (51) |
| Change in receivables | 93 | (14) |
| Change in payables and provisions | (105) | 16 |
| | 328 | 299 |
| Movement in net debt | | |
| Net movement in cash and cash equivalents | (156) | (78) |
| Net movement in borrowings | (79) | (8) |
| Currency variations | 24 | 5 |
| Finance leases | 9 | 1 |
| Subsidiaries acquired and sold | — | — |
| Movement in year | (202) | (80) |
| Net debt at beginning of year | (506) | (426) |
| Net debt at end of year | (708) | (506) |
| Reconciliation of cash and cash equivalents | | |
| Cash and cash equivalents per balance sheet | 114 | 282 |
| Bank overdrafts included within current liabilities — borrowings | (20) | (32) |
| Cash and cash equivalents per cash flow | 94 | 250 |

26 Post-employment obligations

| Post-employment obligations as at the year end comprise: | | 2008 | 2007 |
|---|------------|--------------|--------------|
| | | £m | £m |
| Pensions | — funded | (417) | (24) |
| | — unfunded | (348) | (260) |
| Medical | — funded | (18) | (9) |
| | — unfunded | (51) | (38) |
| | | (834) | (331) |

Pensions and medical — funded

The Group's pension arrangements comprise various defined benefit and defined contribution schemes throughout the world. A number of retirement plans are operated which provide certain employees with post-employment medical benefits.

Pensions

In the UK, pension arrangements are made through an externally funded defined benefit scheme. In the USA and the Rest of the World there are a number of externally funded defined benefit schemes while in certain companies in Europe funds are retained within the business to provide for post-employment obligations.

(a) Defined benefit schemes — measurement and assumptions

Independent actuarial valuations of all major defined benefit scheme assets and liabilities were carried out at 31 December 2008. The present value of the defined benefit obligation, the related current service cost and the past service cost were measured using the projected unit credit method.

Key assumptions were:

| | UK | Americas | Europe | ROW |
|---|---------|----------|--------|-----|
| | % | % | % | % |
| 2008 | | | | |
| Rate of increase in pensionable salaries | 3.9 | 3.5 | 2.50 | 3.5 |
| Rate of increase in payment and deferred pensions | 3.0 | 2.0 | 1.75 | n/a |
| Discount rate | 6.5 | 5.8 | 6.00 | 2.0 |
| Inflation assumption | 2.9 | 2.5 | 1.75 | 1.0 |
| Rate of increases in medical costs: | | | | |
| initial/long term | 6.6/4.5 | 9.0/5.0 | n/a | n/a |
| 2007 | | | | |
| Rate of increase in pensionable salaries | 4.3 | 3.5 | 2.50 | 2.0 |
| Rate of increase in payment and deferred pensions | 3.4 | 2.0 | 1.75 | n/a |
| Discount rate | 5.9 | 6.4 | 5.60 | 2.3 |
| Inflation assumption | 3.3 | 2.5 | 1.75 | 1.0 |
| Rate of increases in medical costs: | | | | |
| initial/long term | 8.0/4.5 | 9.0/5.0 | n/a | n/a |

Discount rates in the table above for the UK and Europe were referenced against specific iBoxx indices, whilst the Citigroup liability index was the reference point for the USA discount rate. The reference for the UK discount rate was the yield as at 31 December on the iBoxx Corporate rated AA bonds with a maturity of 15 years plus, which was 6.7%. Allowing for movements in the rate immediately after the end of the year a discount rate of 6.5% was selected. The equivalent reference rate for Europe is the iBoxx Corporate rated AA bonds with a maturity of 10 years plus. The constituents of this index also changed on 2 January and the selected 6% discount rate reflects a 30 bps reduction in the yield from the reported 31 December 2008 yield. For the USA, the discount rate matched the Citigroup liability index as at end 2008 of 5.8%.

Notes to the Financial Statements

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26 Post-employment obligations *continued*

The underlying mortality assumptions for the major schemes are as follows:

United Kingdom

Such is the size and profile of the UK scheme that data on the scheme's mortality experience is collected and reviewed annually. The key current year mortality assumptions for the scheme use PA92 (Year of Birth) tables with a plus 2.5 year age adjustment to reflect actual mortality experience for the scheme together with medium cohort projected improvement in longevity. Using these assumptions a male aged 65 lives for a further 19.8 years, whilst a male aged 40 is expected to live a further 21 years after retiring at 65. The prior period valuations used the same mortality assumptions.

Overseas

In the USA, CL2007 tables which were first adopted in 2007 have been used whilst in Germany the RT2005-G tables have again been used. In the USA the longevity assumption for a male aged 65 is that he lives a further 18.8 years whilst in Germany for a further 17.7 years. The longevity assumption for a USA male currently aged 40 is that he also lives for a further 18.8 years once attaining 65 years, with the German equivalent assumption being 17.7 years. These assumptions are based solely on the prescribed tables not on actual GKN experience.

Assumption sensitivity analysis

The impact of a one percentage point movement in the primary assumptions as at 31 December 2008 is set out below:

| | UK | | Americas | | Europe | | ROW | |
|---------------------------------------|-------------------|---------------------------|-------------------|---------------------------|-------------------|---------------------------|-------------------|---------------------------|
| | Liabilities £m | Income statement £m | Liabilities £m | Income statement £m | Liabilities £m | Income statement £m | Liabilities £m | Income statement £m |
| Discount rate +1% | 230 | — | 44 | 1 | 45 | 1 | 6 | — |
| Discount rate -1% | (279) | — | (55) | (1) | (48) | (1) | (6) | — |
| Rate of inflation +1% | (233) | — | — | — | (29) | — | — | — |
| Rate of inflation -1% | 195 | — | — | — | 32 | — | — | — |
| Rate of increase in medical costs +1% | — | — | (1) | — | — | — | — | — |
| Rate of increase in medical costs -1% | — | — | 1 | — | — | — | — | — |

(b) Defined benefit schemes — reporting

The amounts recognised in the income statement are:

| | 2008 | | | 2007 | |
|--|--------------------------------------|--|---|-------------|-------------|
| | Employee benefit expense £m | Redundancy and other employment amounts £m | Restructuring and impairment charges £m | Total £m | Total £m |
| Included within operating profit | | | | | |
| Current service cost | (35) | — | — | (35) | (32) |
| Past service cost | (1) | (1) | (1) | (3) | 7 |
| Settlement/curtailments | 12 | — | — | 12 | 2 |
| | (24) | (1) | (1) | (26) | (23) |
| Included within net financing costs | | | | | |
| Expected return on pension scheme assets | | | | 163 | 146 |
| Interest on post-employment obligations | | | | (166) | (149) |
| | | | | (3) | (3) |

The 2008 past service cost charge relates to augmentations arising in the UK on redundancy programmes and additional charges in respect of a continental European subsidiary. The 2007 past service credit of £7 million included a £12 million credit from the impact of changes to retiree medical benefits in the USA, partly offset by a past service charge of £5 million, £4 million of which is within Restructuring and impairment charges primarily from further downsizing of a UK business in the Automotive portfolio.

The 2008 settlement/curtailment credit arises from changes to freeze pension benefit entitlements in Driveline and Powder Metallurgy businesses in the USA. The 2007 settlement/curtailments credit arises from changes in pension regulations in Italy.

26 Post-employment obligations *continued*

The amounts recognised in respect of funded obligations in the balance sheet are:

| | 2008 | | | | Total £m | 2007 £m |
|--|----------|----------------|--------------|-----------|-------------|------------|
| | UK £m | Americas £m | Europe £m | ROW £m | | |
| Present value of funded obligations | (2,031) | (354) | (20) | (39) | (2,444) | (2,528) |
| Fair value of plan assets | 1,759 | 202 | 29 | 19 | 2,009 | 2,495 |
| Net obligation recognised in the balance sheet | (272) | (152) | 9 | (20) | (435) | (33) |

The contributions expected to be paid by the Group during 2009 to the UK scheme are £29 million and to overseas schemes are £30 million.

Cumulative actuarial gains and losses recognised in equity are as follows:

| | 2008 £m | 2007 £m |
|-----------------------------|------------|------------|
| At 1 January | 242 | 17 |
| Net actuarial gains in year | (386) | 225 |
| At 31 December | (144) | 242 |

Movement in schemes' obligations (funded and unfunded) during the year

| | UK £m | Americas £m | Europe £m | ROW £m | Total £m |
|-------------------------------|----------|----------------|--------------|-----------|-------------|
| At 1 January 2008 | (2,264) | (270) | (268) | (24) | (2,826) |
| Current service cost | (20) | (7) | (5) | (3) | (35) |
| Interest | (131) | (18) | (16) | (1) | (166) |
| Contributions by participants | (7) | — | — | — | (7) |
| Actuarial gains and losses | 258 | (22) | 10 | (2) | 244 |
| Benefits paid | 123 | 12 | 15 | 2 | 152 |
| Past service cost | (2) | 1 | (2) | — | (3) |
| Curtailments | — | 12 | — | — | 12 |
| Currency variations | — | (109) | (87) | (18) | (214) |
| At 31 December 2008 | (2,043) | (401) | (353) | (46) | (2,843) |
| At 1 January 2007 | (2,375) | (301) | (277) | (23) | (2,976) |
| Subsidiaries acquired | — | — | — | — | — |
| Current service cost | (16) | (8) | (6) | (2) | (32) |
| Interest | (119) | (17) | (13) | — | (149) |
| Contributions by participants | (11) | — | — | — | (11) |
| Actuarial gains and losses | 141 | 28 | 36 | — | 205 |
| Benefits paid | 121 | 13 | 13 | 2 | 149 |
| Past service cost | (5) | 12 | — | — | 7 |
| Curtailments | — | — | 2 | — | 2 |
| Currency variations | — | 3 | (23) | (1) | (21) |
| At 31 December 2007 | (2,264) | (270) | (268) | (24) | (2,826) |

Notes to the Financial Statements

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26 Post-employment obligations *continued*

Movement in schemes' assets during the year

| | UK £m | Americas £m | Europe £m | ROW £m | Total £m |
|-------------------------------|--------------|----------------|--------------|-----------|--------------|
| At 1 January 2008 | 2,248 | 212 | 21 | 14 | 2,495 |
| Expected return on assets | 144 | 17 | 1 | 1 | 163 |
| Actuarial gains and losses | (539) | (87) | — | (4) | (630) |
| Contributions by Group | 22 | 12 | 1 | 2 | 37 |
| Contributions by participants | 7 | — | — | — | 7 |
| Benefits paid | (123) | (11) | (1) | (2) | (137) |
| Currency variations | — | 59 | 7 | 8 | 74 |
| At 31 December 2008 | 1,759 | 202 | 29 | 19 | 2,009 |
| At 1 January 2007 | 2,187 | 196 | 19 | 13 | 2,415 |
| Subsidiaries acquired | — | — | — | — | — |
| Expected return on assets | 131 | 14 | 1 | — | 146 |
| Actuarial gains and losses | 21 | — | (1) | (1) | 19 |
| Contributions by Group | 19 | 15 | 1 | 2 | 37 |
| Contributions by participants | 11 | — | — | — | 11 |
| Benefits paid | (121) | (11) | (1) | (1) | (134) |
| Currency variations | — | (2) | 2 | 1 | 1 |
| At 31 December 2007 | 2,248 | 212 | 21 | 14 | 2,495 |

The defined benefit obligation is analysed between funded and unfunded schemes as follows:

| | 2008 | | | | | 2007 £m |
|----------|----------|----------------|--------------|-----------|-------------|------------|
| | UK £m | Americas £m | Europe £m | ROW £m | Total £m | |
| Funded | (2,031) | (354) | (20) | (39) | (2,444) | (2,528) |
| Unfunded | (12) | (47) | (333) | (7) | (399) | (298) |
| | (2,043) | (401) | (353) | (46) | (2,843) | (2,826) |

The fair value of the assets in the schemes and the expected rates of return were:

| | UK | | Americas | | Europe | | ROW | |
|-----------------------------|--|-------|--|-------|--|-------|--|-------|
| | Long term rate of return expected | Value | Long term rate of return expected | Value | Long term rate of return expected | Value | Long term rate of return expected | Value |
| | % | £m | % | £m | % | £m | % | £m |
| At 31 December 2008 | | | | | | | | |
| Equities (inc. hedge funds) | 8.0 | 667 | 8.5 | 125 | — | — | 5.6 | 7 |
| Bonds | 5.3 | 912 | 5.5 | 70 | — | — | 1.6 | 8 |
| Property | 6.8 | 80 | — | — | — | — | — | — |
| Cash/short term mandate | 2.0 | 74 | 4.4 | 7 | — | — | 1.1 | 2 |
| Other assets | 6.5 | 26 | — | — | 5.6 | 29 | 0.9 | 2 |
| | | 1,759 | | 202 | | 29 | | 19 |
| At 31 December 2007 | | | | | | | | |
| Equities (inc. hedge funds) | 8.0 | 1,114 | 8.5 | 142 | — | — | 6.2 | 8 |
| Bonds | 5.1 | 810 | 5.5 | 57 | — | — | 1.3 | 4 |
| Property | 6.7 | 102 | — | — | — | — | — | — |
| Cash/short term mandate | 5.7 | 190 | 4.7 | 13 | — | — | 1.0 | 1 |
| Other assets | 5.8 | 32 | — | — | 5.1 | 21 | 0.9 | 1 |
| | | 2,248 | | 212 | | 21 | | 14 |

The expected return on plan assets is a blended average of projected long term returns for the various asset classes. Equity returns are developed based on the selection of the equity risk premium above the risk-free rate which is measured in accordance with the yield on government bonds. Bond returns are selected by reference to the yields on government and corporate debt, as appropriate to the plan's holdings of these instruments, all other asset classes returns are determined by reference to current experience.

The actual return on plan assets was negative £467 million (2007 – £165 million positive).

26 Post-employment obligations *continued*

History of experience gains and losses

| | UK | Americas | Europe | ROW |
|---|---------|----------|--------|---------|
| 2008 | | | | |
| Experience adjustments arising on scheme assets: | | | | |
| Amount — £m | (539) | (86) | — | (4) |
| Percentage of scheme assets | (30.6%) | (43.1%) | 0.0% | (21.0%) |
| Experience gains and losses on scheme liabilities: | | | | |
| Amount — £m | 7 | 2 | (5) | — |
| Percentage of the present value of scheme liabilities | 0.3% | 0.5% | (1.4%) | 0.0% |
| Present value of scheme liabilities — £m | (2,043) | (401) | (353) | (46) |
| Fair value of scheme assets — £m | 1,759 | 202 | 29 | 19 |
| Deficit — £m | (284) | (199) | (324) | (27) |
| 2007 | | | | |
| Experience adjustments arising on scheme assets: | | | | |
| Amount — £m | 21 | — | (1) | (1) |
| Percentage of scheme assets | 0.9% | — | (4.8%) | (7.1%) |
| Experience gains and losses on scheme liabilities: | | | | |
| Amount — £m | (7) | 4 | (3) | — |
| Percentage of the present value of scheme liabilities | (0.3%) | 1.6% | (1.4%) | 0.0% |
| Present value of scheme liabilities — £m | (2,264) | (270) | (268) | (24) |
| Fair value of scheme assets — £m | 2,248 | 212 | 21 | 14 |
| Deficit — £m | (16) | (58) | (247) | (10) |
| 2006 | | | | |
| Experience adjustments arising on scheme assets: | | | | |
| Amount — £m | 35 | 15 | (1) | — |
| Percentage of scheme assets | 1.6% | 7.6% | (4.5%) | — |
| Experience gains and losses on scheme liabilities: | | | | |
| Amount — £m | 15 | — | — | (1) |
| Percentage of the present value of scheme liabilities | 0.6% | 0.0% | 0.0% | (6.7%) |
| Present value of scheme liabilities — £m | (2,375) | (301) | (277) | (23) |
| Fair value of scheme assets — £m | 2,187 | 196 | 19 | 13 |
| Deficit — £m | (188) | (105) | (258) | (10) |
| 2005 | | | | |
| Experience adjustments arising on scheme assets: | | | | |
| Amount — £m | 187 | (1) | 1 | 2 |
| Percentage of scheme assets | 9.7% | (0.7%) | 5.0% | 14.7% |
| Experience gains and losses on scheme liabilities: | | | | |
| Amount — £m | (22) | 3 | (5) | (1) |
| Percentage of the present value of scheme liabilities | (0.9%) | 0.9% | (1.8%) | (3.0%) |
| Present value of scheme liabilities — £m | (2,381) | (316) | (284) | (23) |
| Fair value of scheme assets — £m | 1,915 | 170 | 20 | 14 |
| Deficit — £m | (466) | (146) | (264) | (9) |
| 2004 | | | | |
| Experience adjustments arising on scheme assets: | | | | |
| Amount — £m | 68 | 4 | (1) | (3) |
| Percentage of scheme assets | 4.0% | 3.1% | (7.3%) | (17.6%) |
| Experience gains and losses on scheme liabilities: | | | | |
| Amount — £m | (8) | 1 | — | 1 |
| Percentage of the present value of scheme liabilities | (0.4%) | (0.4%) | 0.0% | 1.2% |
| Present value of scheme liabilities — £m | (2,152) | (262) | (260) | (41) |
| Fair value of scheme assets — £m | 1,697 | 128 | 19 | 17 |
| Deficit — £m | (455) | (134) | (241) | (24) |

(c) Defined contribution schemes

The Group operates a number of defined contribution schemes outside the United Kingdom. The charge to the income statement in the year was £14 million (2007 – £10 million).

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27 Contingent assets and liabilities

Aside from the unrecognised contingent asset referred to in note 5 in respect of Franked Investment Income, there were no other material contingent assets at 31 December 2008.

At 31 December 2008 the Group had contingent liabilities in respect of bank and other guarantees amounting to £13 million (2007 – £7 million). In the case of certain businesses performance bonds and customer finance obligations have been entered into in the normal course of business.

28 Operating lease commitments — minimum lease payments

The minimum lease payments which the Group is committed to make at 31 December are:

| | 2008 | | 2007 | |
|--|----------------|--|----------------|--|
| | Property £m | Vehicles, plant and equipment £m | Property £m | Vehicles, plant and equipment £m |
| Payments under non-cancellable operating leases | | | | |
| Within one year | 27 | 12 | 19 | 11 |
| Later than one year and less than five years | 69 | 23 | 50 | 19 |
| After five years | 55 | 3 | 43 | 1 |
| | 151 | 38 | 112 | 31 |

29 Capital expenditure

Contracts placed against capital expenditure sanctioned at 31 December 2008 so far as not provided by subsidiaries amounted to £84 million (2007 – £47 million) and the Group's share not provided by joint ventures amounted to £1 million (2007 – £1 million).

30 Related party transactions

In the ordinary course of business, sales and purchases of goods take place between subsidiaries and joint venture companies priced on an 'arm's length' basis. Sales of product by subsidiaries to joint ventures in 2008 totalled £74 million (2007 – £70 million). The amount due at the year end in respect of such sales was £11 million (2007 – £8 million) (see note 16). Purchases by subsidiaries from joint ventures in 2008 totalled £11 million (2007 – £10 million). The amount due at the year end in respect of such purchases was £3 million (2007 – £2 million) (see note 17).

At 31 December 2008 a Group subsidiary had nil receivable (2007 – £2 million receivable) from a joint venture in respect of a short term financing facility bearing interest at LIBOR plus 1% (see note 16).

31 Post-balance sheet events

On 5 January 2009 the Group completed the acquisition of the wing component and sub-assembly operation of Airbus UK at Filton (see note 24).

In January 2009 the Group concluded the realisation in cash of Aerospace non-current and current assets amounting to £35 million with a customer at an amount in excess of their 31 December 2008 carrying value.