

Chief Executive's Statement



Sir Kevin Smith

Chief Executive

'Against a background of expected improvements in global economies, the Group should make significant progress in 2010. Our balance sheet strength and excellent market positions give the Board confidence in a strong and sustained GKN recovery.'

As we entered our 250th year, the global financial crisis had already severely impacted demand in automotive markets worldwide and expectations were high that aerospace and off-highway end markets would be similarly affected during 2009. Investor concerns had weighed heavily on the Company's share price and all three major debt rating agencies had downgraded GKN's credit to sub-investment grade.

2009 was set to present the severest of challenges for GKN, its management team and employees right across the Group.

The Company has met those challenges head on and I am pleased to report that GKN has emerged from 2009 in excellent shape, already making strong progress in recovery and strategically well positioned in all its major businesses.

Repositioning to perform

Restructuring activities had been launched in 2008 and were extended in 2009 both to protect short term performance and position the Group for a swift return to acceptable levels of profitability as markets recover. The total restructuring programme sadly will have removed around 7,000 jobs and resulted in the closure of 15 facilities worldwide. It will conclude during 2010 at a total cash cost of around £189 million, having lowered the break-even point in the Automotive, Powder Metallurgy and OffHighway businesses by around 20% and repositioned Aerospace for anticipated lower aircraft production volumes.

An intense focus on all elements of cash flow has been a key feature throughout the year, enabling us to deliver very strong operating cash flow. The Group's balance sheet also benefited from the proceeds of the rights issue, and net debt at 31 December 2009 stood at £300 million compared with £708 million at the end of 2008.

Refinancing for success

Having stabilised operating performance during the first quarter and with the Company back to profitability in the second quarter, we moved to address the market uncertainties around the Group's debt financing, in particular the renewal of a £350 million revolving credit facility which is due to expire in July 2010. After extensive discussions with our lending banks, it became clear that the terms available for new debt would constrain the Group's development and we believed acceptance of these terms would not be in the best interests of shareholders.

Consequently, in June we launched a £423 million rights issue, which was strongly supported by shareholders for which we are extremely grateful. The rights issue not only removed any market uncertainties around GKN's financing, but also provided some capacity to pursue new opportunities to develop and grow. In September we also secured £60 million of repayable investment funding from the UK Government for the Airbus A350 XWB programme and in December we agreed an £80 million technology-related loan facility from the European Investment Bank on attractive

terms. In December we were also able to buy back £124 million of our 2012 bond, reducing annual interest costs by around £8 million per year.

GKN left 2009 with a strong balance sheet and a capital structure well able to support the continuing development of the Group.

Building the future

Integration of the Filton aerostructures facility, acquired in January 2009, has gone extremely well and has helped to propel GKN Aerospace forward as Europe's No. 1 aerostructures company and amongst the top three in the world. GKN Aerospace was also successful in winning a number of important additional work packages on the A350 XWB and the Joint Strike Fighter.

GKN's Automotive operations also had much success in winning new business with existing and new technology. Although new programme opportunities were more limited than usual, GKN Driveline secured around 90% of business for which we were invited to bid, including a number of important new programmes. A new driveshaft plant was opened in China through our SDS joint venture with SAIC, ensuring we continue to have capacity to take advantage of growth in the Chinese market. Our latest hybrid rear axle products secured their launch customer in Europe on Peugeot Citroën's HYbrid4 system and will be available on vehicles from 2011.

GKN Sinter Metals also had a successful year in winning new programmes and secured £25 million in annualised sales of business re-sourced by customers from competitors. Technology continues to play an important part in Powder Metallurgy and we were delighted to achieve another breakthrough from our high performance gear programme with the award of a contract to produce the world's first powder-forged differential gears.

Performing to plan

In automotive markets, as the year developed, global vehicle inventories

stabilised and government incentive schemes supported improved vehicle sales and production volumes. Performance in Automotive and Powder Metallurgy also improved steadily as the benefits of restructuring significantly reduced operating costs. First half trading losses of £51 million were more than offset in the second half with profits of £58 million.

OffHighway sales declined sharply in the second quarter as the global recession impacted demand in all market segments. By June volumes were down more than 50% and stayed very weak through the second half.

Aerospace had a record trading year. Growth in sales to the military sector more than offset the slight decline in civil aerospace demand and there was a strong initial contribution from Filton.

Overall, in an extremely challenging market environment, decisive management action delivered a creditable performance. A trading profit before tax of £91 million was delivered in the second half and we finished the year strongly with a trading margin of 6.5% in the fourth quarter.

Enduring values

Although a difficult year, 2009 brought out the best in GKN: the quality of our businesses and the skill, commitment and sheer determination of our people to succeed. That resilience is built on a culture and value set which have developed through generations of GKN employees.

Our drive for excellence continued in 2009. We further improved customer service and product quality, maintained our world class health and safety performance and continued to develop our people under GKN's continuous improvement programme. Our technology development activities progressed as planned, with a sustained drive to develop products and processes for the new low carbon world. And our Hearts of Gold and Evolve community involvement

programmes recognised individuals, teams and partnerships whose achievements were both humbling and inspiring.

Despite the difficulties in our end markets, 2009 was a year in which GKN people across the Group excelled. I am extremely grateful to them and immensely proud of their efforts and contributions. Those efforts and the tough decisions and decisive actions taken in GKN's 250th year have positioned the Company strongly to flourish for many years to come.

Outlook

The outlook for our major markets is mainly positive although some uncertainty remains, particularly around second half demand.

Against this background we expect our Automotive and Powder Metallurgy businesses to make strong progress in 2010, with the improvement in end market demand, healthy order books and improving mix underpinning sales growth. Further incremental benefits from restructuring are expected to support steadily improving trading margins from 2009 second half levels.

Aerospace sales are expected to be broadly flat, assuming there are no further reductions in production schedules in the second half. Although Airbus will receive price downs from Filton in 2010, we expect double digit trading margins to be maintained in Aerospace.

In OffHighway, we expect some increase in sales and a good improvement in trading profits, as the modest recovery in demand is converted to trading profit from a much reduced fixed cost base.

Against a background of expected improvements in global economies, the Group should make significant progress in 2010. Our balance sheet strength and excellent market positions give the Board confidence in a strong and sustained GKN recovery.