Finance Director's review

Turnover and profitability

The results for this year reflect the general European downturn in IT spending, which resulted in Group turnover reducing by 8.0% to £1.9 billion. However unlike 2001, where there was a significant downturn in the second half of the year in comparison to the first half, both halves of 2002 were relatively similar in revenue terms (see table 1).

Pre-exceptional pre-tax profits increased by 6.1%, whereas post-exceptional pre-tax profits increased by 57.8%.

In 2001, the Group took two exceptional items. These related to the closure of the iGroup, which resulted in a non-operating exceptional charge of £3.1 million, and to the sale of our sub-scale German business to GE CompuNet, which resulted in a charge of £13.1 million. The structure of the German deal involved selling the operating business and customer contracts, with the Group being responsible for such items as collection of debtors and payment of creditors. We have been more successful than anticipated in recovery of these assets, resulting in a non-operating exceptional credit in 2002 of £0.9 million.

In recognition of the continued weak state of the product sales market, particularly in the UK, the Group has taken actions to reduce its overhead cost structure. This has made an important contribution to the overall resilience of the pre-tax profit. It is worthy of note that these cost reductions were achieved without resorting to exceptional charges in 2002.

Operating profits

Group operating profit increased by 2.0% to £56.2 million. However, including the share of the operating loss in Biomni, total Group operating profit increased by 3.9% to £54.9 million. Two notable points are:

- the Group share of the Biomni joint venture loss reduced from £2.2 million to £1.3 million and;

- the operating profit includes a charge of £4.7 million, which comprises £2.9 million goodwill impairment in our BeLux operations and £1.8 million impairment to the carrying value of listed investments to current market value. Excluding the goodwill and market value adjustment, the underlying Group operating profit on continuing businesses increased by 2.2% from £59.6 million to £60.9 million.

In 2002, the UK represented amost 83% of Group revenues. H2 2002 revenue in the UK declined by 7.3% on H1. This reduction includes a fall in product sales of over 12% which, as last year, was mitigated by services revenue growth. It is particularly pleasing to note the continued services growth in 2002, with professional services and managed services revenues increasing by 13.0% and 16.4% respectively over the previous year. Lower product sales but increased service sales led to more consistent revenue from one half to the next, with operating profit margins in the UK increasing from 3.1% in H1 to 4.2% in H2.

In France, a revenue growth of 20.7% was encouraging, although this included the results of the acquired business of GE Capital IT Solutions SA (GECITS). We estimate that approximately half of this growth was organic. Operating profit was disappointing, reducing from £6.4 million in 2001 to £2.4 million, although this included, as anticipated, integration costs arising from the acquisition. The integration costs recorded were £3.2 million and losses were incurred on business transferred from the GECITS acquisition. Whilst it was possible to identify these losses in H1, which amounted to £0.8 million, in H2 the GE business was fully integrated into the core French operations. Consequently it was not possible to identify the loss on the business transferred from the GECITS acquisition for the year as a whole. As this business was loss making on acquisition, the Group received a payment from the vendor to assist in the financing and development of the business. This has resulted in a release of negative goodwill in 2002 of £3.7m.

Clearly, as the French market has reduced over 2001, the growth of Computacenter France implies we have taken significant share and we expect this consolidation to continue.

The BeLux region performance, although not material at a Group level, remains disappointing, with revenue decreasing by 11.9% to £12.6 million and operating losses increasing from £1.2 million to £3.9 million. However, having reviewed the carrying value of the goodwill, we have taken the decision to write-off all of the goodwill in our BeLux business, which resulted in a charge of £2.9 million included in the BeLux operating profit. Excluding this write-off, the BeLux operating loss improved from £1.2 million to £1.0 million.

Earnings per share and dividend

Diluted earnings per share increased by 100% to 19.8p. However, excluding the impact of non-operating exceptional items, the increase in the diluted EPS was 7.8%, increasing from 17.9p to 19.3p. It is our intention to recommend an increased dividend of 5.8p per share. The dividend will be payable on 30 May 2003 to registered shareholders as at 2 May 2003.

Cash flow and working capital

The main elements of working capital are as shown below:

	Dec 2001	Dec 2002	Change
Stock days	21	24	3
Debtor days	42	43	1
Creditor days	36	33	(3)

Whilst stock levels remained almost static, the reduction in Group turnover resulted in an increase of stock days from 21 to 24. Excluding the 2003 acquisitions, we expect stock days to remain at levels similar to those at the end of December 2002.

Creditor days reduced from 36 to 33, partly due to a mix change of vendors and also due to the HP payment terms change. All HP invoices, for pre-merger Compaq products, dated from 1 December onwards, were on 14 days payment terms, with a settlement discount, as opposed to previous terms of in excess of 30 days. This has impacted the 2002 year-end cash position by circa £6 million and the full impact is approximately £20 million, depending on the absolute level of HP purchases and the position relative to other vendors.

Table 1: Group revenues, H1 2000 to H2 2002
£million

	Half 1	Half 2	Total
2000	926.7	1,061.7	**1,988.4**
2001	1,173.6	919.8	**2,093.4**
2002	975.0	951.7	**1,926.7**
% change*	**(16.9)**	**3.5**	**(8.0)**

*2002/2001

Table 2: Group pre-exceptional pre-tax profit, H1 2000 to H2 2002
£million

	Half 1	% return	Half 2	% return	Total	% return
2000	19.2	2.1	36.4	3.4	55.6	2.8
2001	32.6	2.8	18.5	2.0	51.1	2.4
2002	24.4	2.5	29.8	3.1	54.2	2.8
% change*	**(25.2)**		**61.1**		**6.1**	

*2002/2001

The cash inflow from operating activities relative to Group operating profit was 107.9%, which compares to 157.2% in 2001. In 2001 the level of cash generation was exceptional as it was driven by the significant slowdown experienced in H2 2001, with a consequent reduction in the level of working capital required. As revenues in H2 2002 were broadly similar to revenues in H2 2001, this effect was not repeated.

Cash generation from operations of £60.6 million contributed to the improvement in the Group's net cash position to £83.4 million. Capital expenditure reduced from £15.8 million to £10.8 million.

In November 2002 the Group repaid £38.3 million that was outstanding on bonds raised in 1995. These bonds carried an interest rate of 10% and the net effect of their repayment, given current interest rates, will save the Group approximately £2.4 million per annum.

Taxation

The effective tax rate for the Group was 32.8% compared to 45.3% in the previous year. The major reason for the high effective tax rate in 2001 was the impact of the unrelieved operating losses in Germany and, in particular, the loss incurred on the disposal of the German operations. This accounted for a 15.3% differential in the tax rate from the standard 30%.

The effective tax rate for 2002 at 32.8% was 2.8% ahead of the UK standard rate of 30%. The main reasons are analysed below:

	£m charge	% impact
Expenses not deductible for tax purposes	0.5	0.9
Losses of overseas undertakings not available for relief	1.2	2.2
Write down of investment	0.6	1.0
Goodwill amortised	(1.0)	(1.8)
Impairment of goodwill	0.9	1.6
Deferred tax movements	0.5	0.8
Adjustment to prior year provisions (current & deferred tax)	(1.1)	(1.9)
Total	**1.6**	**2.8**

Financial instruments

The Group's financial instruments comprise borrowings, cash and liquid resources, and various items that arise directly from its operations. The Group occasionally enters into hedging transactions, principally forward exchange contracts or currency swaps. The purpose of these transactions is to manage currency risks arising from the Group's operations and its sources of finance. The Group's policy remains that no trading in financial instruments shall be undertaken, other than as required for the business operations.

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk and foreign currency risk. Our policies for managing each of these risks are set out below.

Interest rate risk

The Group finances its operations through a mixture of retained profits, bank borrowings and, in France, invoice factoring. The Group's bank borrowings, other facilities and deposits are at floating rates. No interest rate derivative contracts have been entered into. We will continue to monitor this position to ensure that the interest rate profile is appropriate for the Group. When long-term borrowings are utilised the Group's policy is to maintain these borrowings at fixed rates to manage the Group's exposure to interest rate fluctuations.

Liquidity risk

The Group's policy is to ensure that we have sufficient funding and committed bank facilities in place to meet any foreseeable peak in borrowing requirements. At 31 December 2002 we had £77.4 million of committed bank facilities with maturities for up to 1 year, of which 10.0% were drawn down.

The Group's net cash position at the year-end of £83.4 million, in combination with the above facilities and the ability to access approximately £50 million of funds through sale and lease back of fixed assets, provides a generous cushion for financing working capital movements.

Whilst the Group's net cash position reduced by £36.5 million on 2 January 2003, due to the payment of the initial consideration for the acquisition of GE CompuNet and GECITS Austria, the overall net cash and working capital facilities outlined above leave us in a strong position for financing the ongoing requirements of the business.

Foreign currency risks

The Group operates in the UK, France, Belgium, Luxembourg and, since the beginning of 2003, in Germany and Austria. The Group uses local borrowings to fund its operations in each of these countries, where principal receipts and payments are denominated in local currency. In each country a small proportion of the sales are made to customers outside those countries. For those countries within the Euro zone the level of non-Euro denominated sales is very small and, if material, the Group's policy is to eliminate currency exposure through forward currency contracts. For the UK, the vast majority of sales and purchases are denominated in sterling and any material exposures are eliminated through forward currency contracts.

In certain circumstances the Group uses forward exchange contracts to hedge foreign currency exposures arising on forecast receipts and payments.

Anthony Conophy

Tony Conophy
Finance Director

Table 3: Revenues by country, H1 2001 to H2 2002
£million

	2001 Half 1	2001 Half 2	**2002 Half 1**	**2002 Half 2**
UK	1,001.0	753.0	**828.9**	**768.4**
France	117.1	145.4	**140.1**	**176.7**
BeLux	8.5	5.8	**6.0**	**6.6**
Germany	47.0	15.6	**–**	**–**
TOTALS	1,173.6	919.8	**975.0**	**951.7**

Table 4: Operating profit, H1 2001 to H2 2002
£million

	2001 Half 1	2001 % return	2001 Half 2	2001 % return	**2002 Half 1**	**2002 % return**	**2002 Half 2**	**2002 % return**
UK continuing	37.8	3.8	16.6	2.2	**25.7**	**3.1**	**31.9**	**4.2**
UK discontinued	(3.4)		0.3		**–**		**–**	
France	2.1	1.8	4.2	2.9	**0.2**	**0.1**	**2.2**	**1.2**
BeLux	(0.5)	(5.8)	(0.6)	(10.3)	**(0.5)**	**(8.3)**	**(3.3)***	**(50.0)**
Germany	(0.6)	(1.3)	(0.8)	(5.1)	**–**		**–**	
TOTALS	35.4		19.6		**25.4**		**30.8**	

* This includes a goodwill write-off of £2.9 million; excluding this charge the operating margin loss is 6.1%