ZOTEFOAMS

High performance foam solutions for specialist markets worldwide

Zotefoams plc Annual Report 2012

Foam is our world

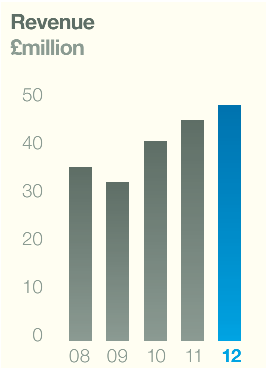
Zotefoams is a world leader in cellular materials technology.

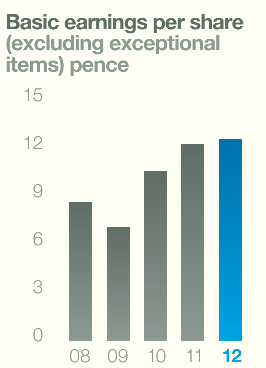
Using a unique manufacturing process with environmentally friendly nitrogen gas expansion, Zotefoams produces lightweight foams in Croydon, UK and Kentucky, USA which it then sells through its global sales force to diverse markets worldwide. Zotefoams also owns and licenses patented MuCell® microcellular foams technology from a base in Massachusetts, USA to customers worldwide and sells T-Tubes® advanced insulation systems made from its patented ZOTEK® fluoropolymer foams.

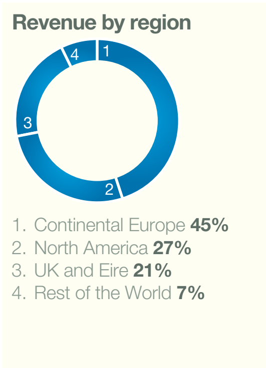
For more information visit:
www.zotefoams.com

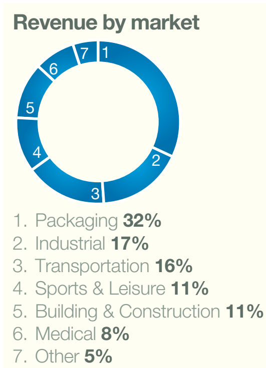
Company Overview
Highlights

- **Record sales up 7% to £47.19m** (2011: £44.21m)
- **High-Performance Products ('HPP') sales up 51% to £3.60m** (2011: £2.38m)
- **Profit before tax up 8% to £5.93m**
- **Strong balance sheet with gearing under 2%**
- **6% increase in proposed final dividend to 3.5p per ordinary 5p share** (2011: 3.3p)









Company Overview

Our Business Model

Our business model is designed to harness our unique manufacturing technologies and intellectual property to produce added value products that meet or anticipate market requirements.

Create

- **Defensible technology leadership**
- **Market position**
- **Unique attributes**

By investing in our technology, usually as an extension of our existing knowledge, we can differentiate from our competitors. Our market position is based around the uniqueness of our product attributes and the advantages that brings to our customers. We are active in many markets, both geographical and across industries, and are well positioned to indentify and deliver these benefits for users of Zotefoams' products and technology. This is particularly important for MuCell Extrusion LLC who license our patents and know-how.

Invest

- **People**
- **Products**
- **Processes**

We ensure Zotefoams' investment is balanced across people, products and business processes ('PPP'). Investment, or the lack of it, in plant and equipment is easy to see, while our PPP investment is less visible. Profitable and sustainable growth relies on the number and quality of our people, the range and differential advantage of our products and the robustness of our processes.

Forward-looking statements

This document contains statements that are not historical facts, but forward-looking statements that involve risks and uncertainties, including the timing and results of technical trials, product development and commercialisation risks, the risks of satisfying the regulatory approval process in a timely manner and the need for and the availability of additional capital. A discussion of principal risks and uncertainties is contained in the section entitled 'Principal Risks and Uncertainties'. These forward-looking statements are based on knowledge and information available to the Directors at the date the Directors' Report was prepared, and are believed to be reasonable at the time of preparation of the Directors' Report, though they are inherently uncertain and difficult to predict. Actual results or experience could differ materially from the forward-looking statements.

Deliver

- Customer value
- Sustainable margin
- Accelerated growth

The delivery of customer value is at the heart of our business. Creating this value and charging the right price gives us sustainable margin. Over 90% of our business is with customers we were supplying five years ago and these customers are the bedrock of our success. Accelerated growth comes from continuing to deliver value on core products augmented by success in new and innovative areas.

Red Bull®

Riding 50ft waves the HydroZOTE™ way

Ian Walsh is a world-renowned big-wave surfer and Red Bull® sponsored athlete. It is not uncommon for Walsh to be chasing massive ocean swells around the world as he rides waves in excess of 50 feet. Surfing waves the size of five-storey buildings creates its own set of challenges, and the need for a supreme floatation vest is a must.

Walsh has been working with a product development company called TECNIQ on various improvements to his surfing gear for quite some time now.

TECNIQ approached Zotefoams about the prospect of an improved floatation foam in 2011. After a year of testing various densities of foam, the team set upon a new grade of foam called HydroZOTE™ LTE. The foam is a remarkable departure from existing PE and PVC floatation foams in that it is approximately 30% lighter in weight and 10% more buoyant. Additionally, HydroZOTE™ absorbs nearly zero water when submerged, compared to 10–15% water absorption from the competition.

Walsh and his fellow big-wave elite have come to rely on HydroZOTE™ in all of their life vests and floatation wetsuits. As Walsh put it: “Maximum floatation is critical to me, it could literally save my life”.

Rob Falken
TECNIQ

Company Overview

Our Strategy and Objectives

Zotefoams' strategy is to expand through a combination of profitable organic growth of our Polyolefin and High-Performance Polymers ('HPP') foams businesses, new customers for our MuCell Extrusion LLC ('MEL') technology licensing business, and through partnerships or acquisitions in related technologies, products or markets.

Key Objectives

Zotefoams measures its development and performance on four key objectives that represent the core elements of our strategy. We intend to:

Grow

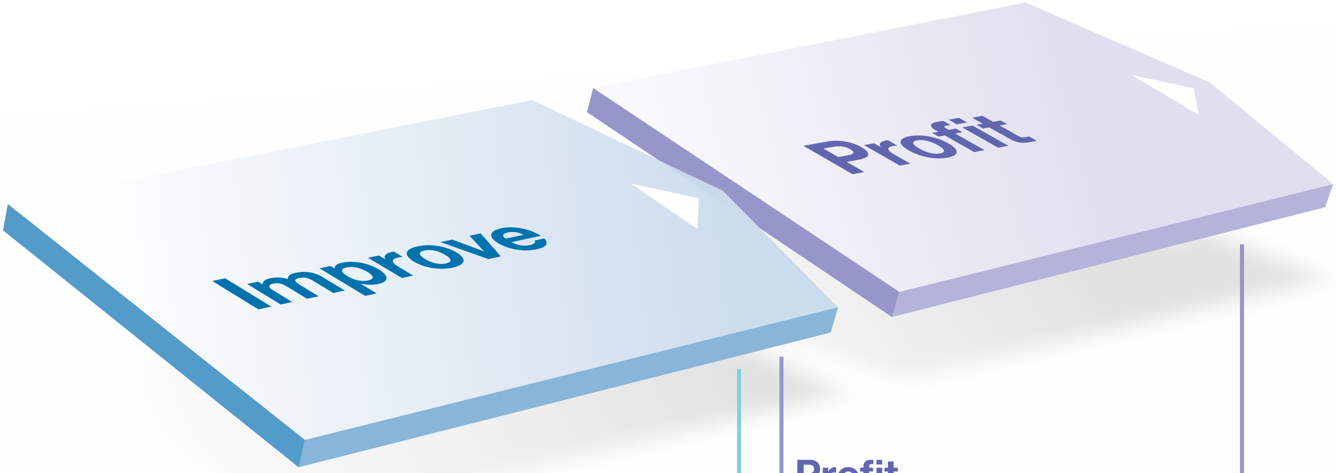
Grow sales in our polyolefin business

Our objective is to grow sales in excess of twice GDP growth and in 2012 sales of our polyolefin products were a record £42.30m (2011: £40.53m), a growth rate of 4.4%. In constant currency the growth rate was 8% with all major regions contributing to this growth. We seek growth through our own product innovation and support for our customers in new applications as well as expanding our business geographically.

Develop

Develop a HPP portfolio and MEL customer base to deliver enhanced margins

HPP sales grew by 51% to £3.60m (2011: £2.38m) and the four main products in this business accounted for 8% of Group sales. MEL sales of £1.33m were at similar levels to 2011, and we see 2012 as a year of transition with good progress in commercialising this technology in our target markets. Within this portfolio we see potential for enhanced margins, with individual HPP products and MEL contracts being highly profitable. These are high growth opportunities that require further investment in products, markets and technology with the potential to be transformational to the Zotefoams Group over time.



Improve
Improve our return on capital employed

In 2012 our return on average pre-tax capital employed ('ROCE') was 20.8% (excluding intangible assets and their amortisation costs). Zotefoams is a capital intensive business and additional capacity is often added in single large investments. With long lead times to commissioning and in large increments of capacity it can take years to 'fill' a new vessel, although the operational benefits are usually realised immediately. We understand that, while year-on-year a large investment may result in a lower ROCE, in the longer term shareholders expect a return above their risk adjusted cost of capital. ROCE is therefore an appropriate benchmark for us.

Profit
Increase our operating margins

Overall Group operating profit margin grew to 12.8% of sales (2011: 12.6%). Margins improved in our Polyolefin foams and HPP business while the increased investment in MEL resulted in a loss in this business in the year. It is pleasing to report a third consecutive increase in operating margin and that this has been achieved while increasing the investment in Zotefoams' business for its long-term health.

MuCell®
MuCell® in flexible packaging

Mondi Consumer Packaging Technologies GmbH was the first packaging company to successfully implement the MuCell® technology in flexible packaging. Mondi's innovative Nor®Cell is a lightweight film using a patented foaming process from MEL to significantly reduce the weight of flexible packaging without decreasing the film thickness. These lightweight films weigh 15–40% less than conventional films and use less material.

Therefore, they are a sustainable solution especially suitable for applications in the food, pet food and hygiene industries. The Nor®Cell film is a winner of the prestigious German Packaging Award in 2012 and the Worldstar Packaging Award in 2013.

Matthias Perick
Nor®Cell Project Manager

Company Overview

Partnering with Foam Converters

Zotefoams' success is based on the business model where we closely co-operate with our partners, the distributors and converters.

In 2012 over 90% of our business was with customers we were supplying five years ago.

The distributor and converter play a big part in the supply chain, from distribution of semi-finished materials to creation of parts that can then be integrated into different end products.

It is a vibrant role that relies on close co-operation as market requirements change constantly.

We are proud to present three distributors/ converters on this page who are representative of the many long-lasting partnerships that have moved our business forward and will remain a cornerstone of our strategy in the future.

ZOTEK® F PVDF Foam

Taking flight

Technifab is a leader in converting engineered closed-cell foams into product solutions that meet and exceed our customers' design and performance requirements.

Having built a strong relationship with Zotefoams, our supplier, we are able to match the right materials to the application. Through our multiple conversion processes, Technifab's innovative engineering and manufacturing teams transform these materials into performance product solutions.

Technifab was founded in 1994 and is a wholly owned subsidiary of Forest City Technologies, Inc.

Technifab's quality system is approved to AS9100 Rev. C and ISO 9001:2008, validating the company's systems and resources within this market segment.

"Taking flight with the aerospace market... foams that are lightweight, flame retardant and moldable, coupled with the right combination of engineering and conversion processes have enabled Technifab to deliver product solutions that are unique, functional, and innovative in aerospace applications."

Jack DeRuyter, VP Business Development, Technifab

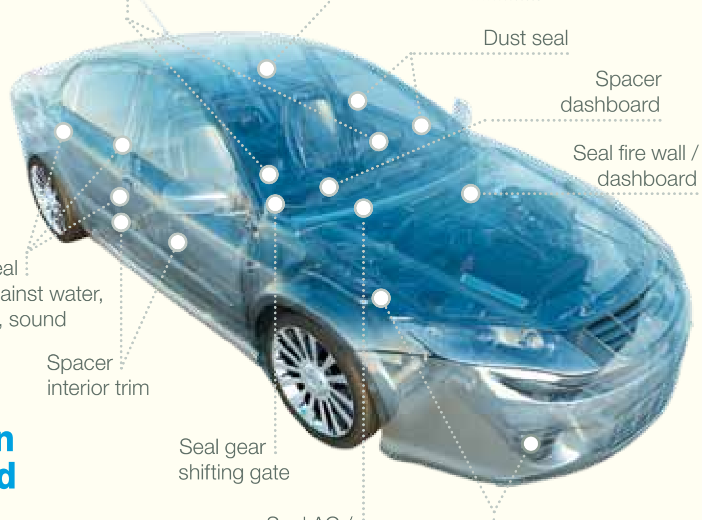
Company Overview

Köpp
Innovation and tradition

In the years since 1968 the relationship between Köpp and Zotefoams has grown into a fully operational partnership.

This led, amongst others, to the introduction of Zotefoams products into the automotive industry worldwide where users such as Mercedes, BMW, GM and Toyota are long-lasting clients that are served throughout the globe with the versatile Zotefoams portfolio.

Reasons for this are the purity of the foam that accounts for very low fogging figures and the isotropic behaviour making it possible to have high performant materials with a very low density (low weight).



"Tradition, experience and innovation will continue to provide the foundation for the successful partnership between Wilhelm Köpp Zellkautschuk GmbH and Zotefoams plc into the 21st century."

Oliver Köpp, Managing Director, Köpp

Ramfoam
Two decades of quality and service

Ramfoam is one of Europe's pre-eminent Polyethylene foam converters, supplying slit and laminated sheets through to complex CNC machined packaging inserts and composite foam structures.

Our leading global clientele base combined with our world class suppliers gives us a robust and exciting platform for business.

"Zotefoams is our partner of choice and has maintained its premier supplier status to us for nearly two decades. With their range of Azote® and HPP grades of foams it allows us the day-to-day security of quality and service whilst allowing us to develop some of the world's finest foam solutions for the future."

Phil Johnson, Managing Director, Ramfoam

Company Overview

Managing Director's Q&A

David Stirling
Managing Director

> **"We believe our long-standing relationships will continue to benefit both Zotefoams and our customers."**

Q How would you describe Zotefoams?
A Zotefoams is a speciality material and technology company. We describe ourselves as a "world leader in cellular material technology", and make foams for the most demanding applications within the markets in which we operate. Many of our products are highly differentiated based on our proprietary technology, and some of our newer foams are truly unique. In addition, MuCell Extrusion LLC ('MEL'), our technology licensing business, has a powerful combination of patents and know-how around the creation of microcellular plastic foams. MEL licensees extrude plastic articles with microcellular (very small) bubbles using an environmentally friendly gas, typically creating foams which reduce raw material usage by approximately 15%.

Q Can you describe the advantages of your Azote® (polyolefin) and HPP products?
A These foams are typically manufactured in 'blocks' which are usually up to 50mm thick and two metres long and have as little as 1.5% plastic content by volume. The products are 'closed cell' which means that there are no breaks in the bubble walls, ideal for impact (sports and packaging) and buoyancy applications. We use a variety of polymers, the most common being low density polyethylene ('LDPE'), which is a versatile and relatively inexpensive plastic. We make ZOTEK® HPP foams from flouropolymer and nylon, which have excellent fire resistance and temperature stability respectively, and offer a high energy-return foam (Pebaxfoam®) aimed mainly at the sports industry. Our foams are very consistent, ideal for high tolerance manufacturing such as in aviation and automotive, offer best in class strength to weight ratio and have no chemical residues. This purity is valued in many demanding applications such as semiconductor manufacturing, pharmaceutical clean rooms and within the medical market.

Q Who are the customers for your foams?
A Most of our sales are to long-standing customers who are foam converters, making parts for industrial, and occasionally consumer, markets. We actively seek new customers, in geographies and application markets where our existing network does not operate, and we work closely with end-users to educate ourselves on their needs and to introduce our unique materials. We believe these long-standing relationships will continue to benefit both Zotefoams and our customers and we seek to be the supplier of choice in the markets in which we operate.

Q Where do you see opportunities for growth?

A Most of our growth is linked to key market trends: energy and material saving delivered by weight reduction; regulation and consumers requiring higher standards of care, for example in fire-retardant materials or purity; and advances in manufacturing technology benefiting from increased consistency of material inputs. We anticipate higher percentage growth rates in Asia as our market penetration is small, in HPP foams which are designed to deliver specific attributes to the market, and in MEL where our technology can deliver significant material cost savings.

Q What is Zotefoams' next stage of growth?

A We plan to invest in a foam expansion factory in Asia to serve the market there, possibly with a local partner. Foam is bulky and transport costs are high unless manufacturing is close to the point of use. Foam expansion in Asia, supplied by intermediate product from UK, overcomes much of this transport disadvantage and we have built our business in North America using the same business model. During 2012 we developed some new products in our Azote® range specifically designed for segments of the market in Europe and North America where we are underrepresented and these will be launched early in 2013. In 2012 we doubled the premises leased by MEL in anticipation of growth in this business and our internally measured pipeline of forward potential is running at record rates.

Q What challenges do you face in implementation of your plans?

A With MEL and HPP it is difficult to be precise about the timing of revenues, as we are selling into technically demanding applications which take time to validate new technologies. However, we are confident in the potential for these businesses. We are expanding our Croydon, UK site to support future growth in Polyolefin and HPP foams and have secured finance to meet these capital commitments. To build a facility in Asia will take about two years from approval to commissioning and we have a dedicated Azote® sales team in Asia, supported by our experience in Europe and North America, focused on increasing our sales in this region to a level which supports this investment.

Company Overview

Chairman's Statement

Nigel Howard
Chairman

"We are continuing our investment in new capacity in Croydon, in people and the longer term development of MEL, and product and market development in our HPP business."

Results

I am pleased to report our 2012 profit before tax increased by 8% to £5.93m (2011: £5.47m) with Basic Earnings per Share up to 12.1p (2011: 11.8p). Revenue of £47.19m was 7% ahead of the previous year (2011: £44.21m) and, in constant currency, all major regions contributed to this growth. Particularly pleasing was the growth from our High-Performance Products ('HPP') segment where sales increased by 51% to £3.60m (2011: £2.38m).

Strategy

Zotefoams' strategy is to expand through a combination of profitable organic growth of our Polyolefin and HPP businesses, new customers for our MuCell Extrusion technology licensing business, and through partnerships or acquisitions in related technologies, products or markets.

Objectives

We target sales growth in our core polyolefin business in excess of twice the average rate of increase in GDP. Our largest markets are EU and North America, although we sell to many countries outside these markets and intend further to expand our sales in these underrepresented and growing markets. Our polyolefin business currently has its main factory in Croydon, UK while customers in America are supplied from our factory in Kentucky, USA, which opened in mid-2001 and has facilities for foam expansion supported by supply from the UK. In order to support our growing sales in Asia we are in the final stages of evaluating a facility similar to Kentucky, either directly or as a joint venture with a local partner, as sales increase to a level where such an investment becomes financially attractive. We are also committed to developing a portfolio of unique foam products from high-performance materials with significant competitive advantages over rival materials. This will allow us to command higher margins and affirm our position as a leading foam technology company. We intend to achieve this growth while continuing to improve our operating margins and our return on capital employed.

Corporate Governance

At Zotefoams, we recognise the importance of being a well managed business, not only for the interests of our shareholders, but for our other stakeholders as well. The Board and I are committed to the highest standards of corporate governance and regularly monitor our compliance with the UK Corporate Governance Code.

People

Our business relies on the skills and dedication of our people and on behalf of the Board I would like to thank all of them, as it is their contribution which made 2012 a successful year for the business.

Dividend

In 2010 the Board adopted a progressive dividend policy subject to profit growth, investment requirements and the other needs of the business. I am pleased to say we intend to retain this policy and the Board therefore proposes to increase its final dividend to 3.5p per ordinary share (2011: 3.3p) which, if approved by the shareholders, would make a total of 5.2p per ordinary share for the year (2011: 4.9p), an increase of 6%. At this level the dividend would be covered more than by two times post-tax earnings. If approved, the dividend will be paid on 23 May 2013 to shareholders on the register on 26 April 2013.

Outlook

Against a strong comparative sales performance at the start of 2012, so far in 2013 we have seen a relatively subdued level of sales. However, levels of order intake are more encouraging and we believe that caution in the supply chain regarding uncertain economic conditions, coupled with our improved lead-time performance, are being reflected in part in a reduction in inventory levels in the market after the strong demand seen in the final quarter of 2012. Raw material prices have risen slightly compared to the second half of 2012 while exchange rates, with sterling relatively weaker against other major currencies, have moved favourably for us since the beginning of January. The multi-market and international scope of Zotefoams' activities mean we are influenced by global economic conditions while the timing of sales from new products and markets, where higher growth rates are anticipated, is more uncertain than in the more established businesses. We are continuing our investment in new capacity in Croydon, in people and the longer term development of MuCell Extrusion LLC, and product and market development in our HPP business. Zotefoams enters 2013 with a strong balance sheet and a wide variety of options for future growth. While being mindful of near-term economic conditions, the Board expects further progress in 2013 and remains confident about the long-term prospects for our business.

Nigel Howard
Chairman
4 March 2013

Company Overview

Business Review

Clifford Hurst
Finance Director

David Stirling
Managing Director

"Zotefoams delivered record sales of £47.19m in 2012 and profit before tax increased by 8% to £5.93m."

Zotefoams is the world leader in cellular materials technology. Using a unique manufacturing process with environmentally friendly nitrogen gas expansion, Zotefoams produces lightweight foams in Croydon, UK and Kentucky, USA which it then sells through its global sales force to diverse markets worldwide. Zotefoams also owns and licenses patented MuCell® microcellular foams technology from a base in Massachusetts, USA to customers worldwide and sells T-Tubes® advanced insulation systems made from its patented ZOTEK® fluoropolymer foams.

Business overview

Zotefoams' business is based around unique cellular materials technologies. We create small and consistent bubbles in plastic, mainly to produce high-quality foams for a wide variety of uses, and also to reduce the materials content of plastic parts. Using inert gases such as nitrogen (N_2) and carbon dioxide (CO_2) makes our foams pure, creates an even distribution of plastic which enhances performance and allows us to foam materials which cannot normally be foamed by other means.

We are active in markets across the globe. Zotefoams' main products are speciality materials and most of our customers are converting foam for industrial and, to a lesser extent, consumer markets. Development and marketing at end users, often alongside our foam converter customers, are also important to us. We produce and sell foams to a number of diverse industries, including: packaging, aviation, automotive, marine, sports, construction and medical. This gives us a unique perspective on the uses of, and requirements for, foams. Investment in sales and marketing resource, approximately 12% of our total workforce, and technical development across our product range, underpins this commitment to growth.

Zotefoams is well-placed to respond to the global concerns about the use of plastics. Recycling is often top of the environmental agenda, however if a product is produced using less plastic in the first place then this considerably lessens the environmental impact of the product. Most of our sales are from foams with less than 4% plastic by volume. Additionally the user benefits of lightweight foam in many applications are obvious: Zotefoams' products make aircraft and cars lighter and hence more fuel efficient, medical products more hygienic, sports and leisure equipment safer and packaging longer lasting.

Our business is organised in three main segments: Polyolefin foams (marketed under the Azote® brand), HPP foams and MuCell Extrusion. They share a common principle of using high-pressure inert gas to foam polymers. Both Azote® polyolefin foams and HPP foams are manufactured at our Croydon facility where we operate autoclave technology to saturate polymer sheets. These 'gas-filled' sheets can then be expanded into foams with as little as 1.5% polymer by volume. This final expansion process is most economically done close to our customers so, in addition to capacity in Croydon, Zotefoams operates a foam expansion facility in Kentucky, USA to serve the North American market. MuCell Extrusion, based in Massachusetts, USA, owns and licenses technology for high-pressure foaming of extruded plastic parts. The main benefit of the MuCell® technology is the reduction of polymer content of these parts, giving cost and environmental benefits to the users.

Overall Zotefoams delivered record sales of £47.19m in 2012 (2011: £44.21m) despite a relatively subdued economic climate and adverse foreign exchange rates. The price of low density polyethylene ('LDPE'), our main raw material, was slightly lower than in 2011 although other material costs were higher as was energy which is a significant cost to our business. Overall for the year gross margins increased to 29.0% (2011: 28.5%) and profit before tax increased by 8%, from £5.47m to £5.93m.

Foreign exchange rates and prices for LDPE can be volatile and often impact our business in the short term. Approximately 80% of our sales are in currencies other than sterling and we estimate that, at constant 2011 exchange rates, sales would have increased by 10%. Our exposure to exchange rate movements is partially offset by our operations in USA and raw material purchases in euros, with the residual transaction exposure managed by hedging a proportion of expected net cash flows with forward foreign currency contracts. The unhedged portion remains a risk to our business and we estimate that movements in exchange rates during 2012 reduced reported profits by approximately £0.6m. In 2012 the average euro price of LDPE was approximately 2% lower than in 2011, but 8% higher than in 2010. From January 2010 to December 2012 the peak monthly euro price was approximately 44% higher than the lowest price and we have experienced monthly movements as large as 22%. Managing this short-term volatility by constantly changing prices to our customers is incompatible with building a specified brand across industrial and consumer markets. Zotefoams therefore manages its sales prices relative to longer term trends in polymer pricing as well as other input costs.

In our Polyolefin foams business sales grew by 4.4% to £42.30m (2011: £40.53m) with volumes 2.9% ahead of last year and price/mix favourable by 1.5%. Polyolefin foams account for 90% of Group sales and profit from this segment increased 13% to £6.43m (2011: £5.68m). In the UK, sales volumes increased by 4%, while in North America and in Continental Europe sales volumes were only marginally higher than in 2011. Outside these established markets, which account for 93% of sales volumes, our business increased by 30% in volume and 31% in value. There were no significant changes in sales mix or end-user markets from the previous year, although in the latter part of the year there was evidence of some inventory increases in the market. As foam is bulky, inventory build usually only happens where there is variability in the supply chain. Zotefoams' longer lead times during the year were a factor in this inventory increase and to improve our service we have invested in additional machinery to remove the bottlenecks in our processes as well as taking actions that have improved efficiency and capacity in other areas. A new foam expansion autoclave, LP42, was operational late in 2012 and a further sheet extruder will be commissioned mid-2013.

In our HPP business we entered 2012 with a record order book and added significantly to this as the year progressed. Overall sales increased 51% to £3.60m (2011: £2.38m). During the year we continued to invest in both R&D and sales and marketing in HPP products and therefore this segment reported a reduced loss of £0.08m (2011: loss of £0.18m). Our patented fluoropolmer ZOTEK® F foams together with T-Tubes® advanced insulation represent 95% of HPP sales and are both profitable. Pebaxfoam® and ZOTEK® N nylon foams are at earlier stages of commercialisation and, although both showed progress throughout the year, revenues are not yet sufficient to carry their marketing and development costs. The strategy for this segment of our business is to develop new products with unique attributes that are valued by end users. Our range of ZOTEK® F fluoropolymer foams has excellent fire retardancy properties as well as being lightweight and thermoformable into a variety of shapes. The main markets for these foams are currently in aviation and, in T-Tubes® branded insulation, in clean room environments. Nylon foams exhibit excellent high temperature performance, insulation and impact resistance. These materials are being trialled in automotive, construction and composites markets with promising results. Pebaxfoam® is made from a very resilient polymer which is known for its energy management properties. The foam is lightweight and provides excellent rebound performance and has been used in insoles and midsoles for high-performance sports shoes. Commercialising some of these materials, particularly those like nylon foams which are aimed at high-end industrial applications, can take years of testing and design. However the value of these opportunities, many in specified applications which can have long life times, is potentially transformational for Zotefoams and we are optimistic about the long-term future of this portfolio of products.

Company Overview

Business Review continued

MuCell Extrusion LLC ('MEL'), the third segment of our business, licenses technology for continuous foaming. We acquired 100% of this business in 2011 after having been a 30% minority shareholder since 2008. MEL technology injects high-pressure inert gas such as carbon dioxide or nitrogen into plastic extruders. The output is microcellular foam, reducing the plastic content, and the cost, of the extruded part. MEL receives royalties, usually based on the savings made by the licensee, and sells enabling equipment for machinery conversion and gas injection. We have invested in MEL and refocused its activities towards a more limited number of segments with high potential and are addressing other markets through channel partners. As well as developing our MuCell Extrusion technology internally we secured exclusive rights to patents from The Dow Chemical Company and Styron in plastic film and sheet in mid-2012. Our existing licensee base is in a variety of segments across the globe although our current focus is in thin films and in extrusion blow moulding bottles, both for packaging, and in plastic sheets which have a variety of uses. In 2012 MEL reported sales of £1.33m (2011: £1.33m) and earnings before interest, tax, depreciation and amortisation (EBITDA) of £0.01m (2011: £0.45m) reflecting the focus on development into the three key markets and our increased investment in people and technology. For MEL to be successful requires our technology to be implemented by plastic parts producers and for their end customers to accept and adopt the benefits of reduced material content. MEL is making good progress on these external requirements and we are confident that our technology is a robust offering for parts producers and will add value to end users.

In 2012 Group capital expenditure was £3.68m (2011: £2.74m), the majority of which was at our Croydon site in relation to our Azote® polyolefin foams business. During the year a new foam expansion autoclave became operational and we purchased a new polyolefin extruder which will be commissioned in mid-2013. We also obtained planning permission to extend one of our factory buildings. The planning approval process for this factory extension took longer than anticipated, delaying most of the expenditure on this project to 2013 and we therefore expect a higher level of capital expenditure in 2013 than in 2012. This investment will give us the building capacity to meet future growth expectations, including the ability to support our plans for foam expansion production capacity in Asia.

Strategy and objectives

Zotefoams' strategy is to expand through a combination of profitable organic growth of our Polyolefin and HPP foams businesses, new customers for our MuCell Extrusion technology licensing business, and through partnerships or acquisitions in related technologies, products or markets. In 2012 we had a record sales year and grew operating profit by 8% while continuing to invest in areas which we believe will further increase the long-term future prospects of our business. Our specifically stated objectives are:

- Sales growth in our polyolefin business to exceed twice the average rate of GDP growth.
- Develop a HPP portfolio to deliver enhanced margins.
- Improve our operating margins.
- Improve our return on capital employed.

Performance against these objectives was as follows:

- Sales of polyolefin foams grew by 8% in constant currency.
- HPP sales grew by 51%.
- Group operating margins increased to 12.8% (2011: 12.6%).
- Pre-tax return on average capital employed, excluding intangible assets and their amortisation costs, increased to 20.8% (2011: 19.5%).

In 2013 we intend to focus on the same four key objectives in our business, although return on capital employed will be impacted by the high levels of capital expenditure planned.

Financial results

Turnover increased by 7%, from £44.21m in 2011 to £47.19m. Gross margins increased to 29.0% (2011: 28.5%) primarily due to the operational gearing benefit of the higher sales and cost reductions, which more than offset higher energy prices and the effect of a weaker euro. The average euro/sterling exchange rate moved from €1.15 in 2011 to €1.23 in 2012. Not only did this impact gross profit but within administrative expenses we recorded a £0.36m loss (2011: £0.05m profit) on the translation of foreign currency balances net of profits on forward exchange hedges. Excluding this distribution and administrative expenses increased by 3% from £7.05m to £7.28m. Profit before tax increased by 8%, from £5.47m to £5.93m.

The effective tax charge is 20% (2011: 17%), which is less than the UK corporation tax rate for the period of 24.5%. This is due to a lower tax charge incurred in our USA operations where we have brought forward tax losses (£0.08m), lower future UK corporation tax rates reducing future deferred tax liabilities by £0.09m and a favourable £0.09m adjustment to the tax charge in respect of prior periods.

Earnings per share and dividend

Group basic earnings per share were 12.1p (2011: 11.8p). The Directors are recommending an increased final dividend of 3.5p per share, and, subject to shareholder approval, payable on 23 May 2013 to shareholders on the Company register at 26 April 2013. This would bring the total dividend to 5.2p per ordinary share for the year (2011: 4.9p).

Cash flow and funding

Operating profit increased to £6.03m from £5.59m in 2011 and EBITDA grew to £9.34m (2011: £8.80m). Cash generated from operations was £6.29m (2011: £6.08m) with an increase in working capital reflecting the 2012 sales growth and a planned increase in inventory. Capital expenditure was £3.68m (2011: £2.74m). Tax payments of £0.99m (2011: £1.05m) and dividend payments of £1.96m (2011: £1.84m) were similar to last year while the £2.23m payment of the final installments of the MEL deferred consideration left a net debt of £0.62m at the end of the year compared to net funds of £1.92m at the end of 2011.

In December 2012 the Group took out a £3.50m mortgage, repayable over five years in equal quarterly installments. This is in addition to its £4.90m multi-currency overdraft facility and the £0.82m remaining at 31 December 2012 on a £3.30m mortgage taken out in 2009. Together with the cash generated by the business, this gives the Group the funding facilities to support its currently approved capital investment plans.

Pensions

There was a £2.23m increase in the gross IAS19 deficit on the Company's Defined Benefit Pension Scheme (the 'Scheme') to £7.17m (2011: £4.94m). This was due to lower bond yields reducing the discount rate used to value the Scheme's liabilities and higher expectations of inflation increasing pre-retirement liabilities, which were only partially offset by the Company contributions to the Scheme and higher than expected investment growth.

At the April 2011 triennial actuarial valuation the Scheme's deficit, calculated on a Statutory Funding Objective basis, was £1.17m. As a result of this the Company has agreed with the Trustees to make contributions to the Scheme of £42,000 per month until 30 September 2013 to eliminate the deficit calculated in April 2011 and in addition paying the ongoing Scheme expenses at £13,000 per month. This will be reviewed following the next triennial actuarial valuation which is scheduled for April 2014.

David Stirling
Managing Director

Clifford Hurst
Finance Director

4 March 2013

Company Overview

Principal Risks and Uncertainties

The Board of Directors believes that the principal risks and uncertainties that the Company currently faces are as stated below. Regular risk reviews are undertaken to ensure that the major risks in the business, that could affect the Company's operations and financial performance, have been identified and that, where possible, mitigating actions and controls are put in place.

Significant risks are reviewed by the Board and the Audit Committee. It is not possible to identify every risk that could affect the Company's business and the mitigating actions and controls that have been put in place may not provide absolute assurance that the risk will neither occur nor materially affect the Company's operations or financial performance.

Risk and potential impact	Description
Operational	As the Company's operations are mainly on one site, a significant operational disruption could impact the ability to manufacture and supply products.
Supply chain	Certain of the Company's raw materials are sourced from single suppliers. Disruption in those supplies, either on a temporary or more permanent basis, could affect production and supplies to the Company's customers.
Technology	The Company's processes for the manufacture of its products are substantially unique to the Company. Whilst the principles behind the processes are not confidential, the precise know-how is. A competitor could match or improve upon the properties and economics of the Company's processes and produce comparable (or better) products at lower prices. Key to the success of the business of MuCell Extrusion LLC ('MEL') is the strength of its intellectual property and, on the back of that, its ability to grant commercial licences. The risks to MEL are that its intellectual property becomes dated or its patents are successfully challenged and hence have no commercial value for being licensed.
Pension	The Company has a Defined Benefit Pension Scheme ('the Scheme') and any inability of the Scheme to meet its liabilities to its members could, ultimately, be the responsibility of the Company.
Foreign exchange	The Company has significant exposure to foreign exchange fluctuations. The Company's operations are substantially based in the UK and, therefore, most of its manufacturing assets and costs are sterling denominated. The Company's customers are normally invoiced in their local currencies. In 2012, approximately 80% of the Company's revenue was in currencies other than sterling. The Company, therefore, generates surpluses in US dollars and euros, which are converted into sterling.
Macro economics	Most of our markets are exposed to general economic conditions. The Company is operationally geared and a fall in demand for its products could adversely impact the Company.
Financing	The Company needs to have sufficient cash, or be able to draw on loan facilities, to finance its operations and growth.

Mitigation actions

The Company has extensive Safety, Health and Environment ('SHE') policies and procedures in place, which are in line with best practice. The Company is certified to accredited standards OHSAS 18001 on Health and Safety and ISO 14001, the International Standard for Environment Management Systems. Regular training is provided on SHE matters to the staff. Pressure equipment used is operated under the Pressure Systems Safety Regulations 2000 and is subject to systematic internal and frequent external inspections in accordance with the Safety Assessment Federation.	The Company and Zotefoams Inc have extensive fire prevention systems in place. A programme is underway to improve further the systems in place on the Croydon site. Reporting of incidents, including 'near misses' and damage to plant or equipment not resulting in personal injury, is mandatory in order to track issues and to prevent reoccurrences. Insurance is in place to cover capital restatement and loss of profits in the event of operational disruption caused by certain events.
Wherever possible, supplies are sourced from more than one supplier or location. However, this is not always possible, due to the special nature of the raw materials used.	The Company continually monitors suppliers and undertakes research of alternative suppliers that could be used and the resulting products that could be offered to the Company's customers as substitutes.
There are high barriers of entry to replicate our processes. Significant capital investment is required for the autoclaves as well as long lead times for their manufacture. The Company has a constant flow of product variants to keep its product offering diversified. The development of High-Performance Products ('HPP') and MEL, where the product offerings are unique and protected by both patents and process capability, opens up new markets for the Company with potential significant and lasting differential advantages.	MEL actively maintains and updates its intellectual property portfolio to ensure it is current. This is done by undertaking research and development to add new patents to the portfolio and obtaining licences of key third party patents, which are complementary to the existing portfolio. The portfolio is not dependent on any particular patent or licence, therefore if a patent is successfully challenged, MEL is still able to license its technology.
To minimise the risk to the Company of meeting the obligations under the Scheme, the Company closed the Scheme to new members in 2001 and closed it to future accrual of benefits in 2005.	The Company has committed to paying £42k monthly to the Scheme to September 2013 to eliminate the deficit based on the actuarial valuation in April 2011. This will be reviewed following the next triennial actuarial valuation which is scheduled for April 2014.
The Company tries to reduce its foreign exposure by making its purchases either in euros or US dollars. For example, there are US dollar costs associated with the Company's operations in Kentucky USA and with MEL. In addition, the majority of the Company's raw materials are purchased in euros. The Company hedges a proportion of its anticipated net exposure to foreign exchange for the next nine months by using forward exchange contracts.	The Company, like most public companies, does not hedge for translating its foreign subsidiaries' assets or liabilities in the consolidation of its Group accounts.
The Company's markets are spread geographically and across a number of markets. The Company's experience is that in these circumstances operational labour costs can be reduced (the Company has implemented an annualised hours system to give some flexibility on this), polymer prices fall with reduced economic demand giving a cost benefit and cash can be generated from reducing working capital	and slowing capital expenditure projects to help offset the effects of a downturn. The Company has always maintained a low financial gearing to give it operational flexibility in a downturn. Going forward the growth of the Company's HPP and MEL businesses should take the Company into less cyclical markets.
The Company has strong cash generation from its operations. The Company has: • a £4.9m overdraft facility (payable on demand); • a £3.3m loan facility taken out in January 2009 (£2.5m had been repaid at 31 December 2012); and • a £3.5m loan facility taken out in December 2012.	Both loan facilities are repayable over five years and have no major financial operating covenants, but are secured against certain items of plant and equipment.

Corporate Information
Board of Directors

David Stirling
Managing Director

Appointed: September 1997 (Finance Director) and May 2000 (Managing Director)

Skills and experience:
David started his career with KPMG in Scotland where he qualified as a Chartered Accountant. He has worked for Price Waterhouse in USA and Poland and with BICC plc. David is a graduate of Glasgow University and has an MBA from Warwick University and an MSc in finance from London Business School.

External appointment:
Non-Executive Director of Bac2 Limited

Nigel Howard
Non-Executive Chairman
Chair of the Nominations Committee and member of the Remuneration Committee

Appointed: January 2006 (Board) and January 2007 (Chairman)

Skills and experience:
Nigel was a Director of Morgan Crucible plc, where he worked for over 36 years in a number of roles including Interim Chief Executive. Nigel is a graduate of Harvard Business School ISMP Program.

External appointment:
Non-Executive Director of Alliance One International Inc (NYSE: AOI)

Clifford Hurst
Finance Director

Appointed: October 2000

Skills and experience:
Clifford trained with Ernst & Young. He then worked for ICI plc and Caradon plc. Before joining Zotefoams plc, Clifford was the Finance Director and then became the Commercial Director of Thermos Limited. Clifford is a Fellow of the Institute of Chartered Accountants in England and Wales and a member of the Association of Corporate Treasurers.

Marie-Louise Clayton
Non-Executive Director
Chair of the Audit Committee and member of the Nominations and Remuneration Committees

Appointed: July 2011

Skills and experience:
Marie-Louise was the Group Finance Director of Venture Production plc, a FTSE 250 company in the oil and gas sector and has held senior positions in Alstom and GEC. She was a Non-Executive Director and Chair of the Audit Committee of Forth Ports plc. Marie-Louise is a Fellow of the Association of Chartered Certified Accountants.

External appointment:
Non-Executive Director of Geoffrey Osborne Ltd and Diploma plc

Richard Clowes
Senior Independent Non-Executive Director
Chair of the Remuneration Committee and member of the Audit and Nominations Committees

Appointed: July 2007

Skills and experience:
Richard has worked for GKN plc and TI Group plc. He was a main Board Director from 2001 to 2005 for GKN plc and has extensive operational and general management experience. At GKN plc, Richard was a Divisional Managing Director for their Powder Metallurgy, Offhighway and Autocomponents Divisions.

Alex Walker
Non-Executive Director
Member of the Audit, Nominations and Remuneration Committees

Appointed: July 2011

Skills and experience:
Alex spent most of his career at Yule Catto & Co plc, where he was Chief Executive for the South East Asia operations before becoming the Group Chief Executive. Alex has also been a Non-Executive Director of Rotork plc and chaired its Remuneration Committee.

External appointment:
Non-Executive Chairman of Spirent Communications plc

Corporate Information

Directors' Report

The Directors present their Annual Report and audited financial statements for the year ended 31 December 2012.

Principal activity

The Group's principal activity is the manufacture and sale of cross-linked block foams.

Business review

The Company is required by the Companies Act 2006 to set out in this report a fair review of the business of the Group during the financial year ended 31 December 2012 and of the position of the Group at the end of the year and a description of the principal risks and uncertainties facing the Group. The information that fulfils these requirements can be found in the sections entitled 'Business Review' and 'Principal Risks and Uncertainties'.

Details of subsidiaries and branches are given in note 11 on page 57.

Results and dividends

Profit attributable to shareholders for the year amounted to £4.73m (2011: £4.50m). An interim dividend of 1.7p (2011: 1.6p) per share was paid on 11 October 2012. The Directors recommend that a final dividend of 3.5p (2011: 3.3p) per share be paid on 23 May 2013 to shareholders who are on the Company's register at the close of business on 26 April 2013. This makes a total dividend of 5.2p per share for the year (2011: 4.9p).

Directors

The appointment, replacement and powers of the Directors are governed by the Company's Articles of Association, the UK Corporate Governance Code, the Companies Act 2006, prevailing legislation and resolutions passed at the Annual General Meeting ('AGM') or other general meeting of the Company.

All of the current Directors named on pages 18 to 19 served throughout the year. In addition, R H Lawson also served as a Director until he retired from the Board on 31 March 2012. The Company's Articles of Association (the 'Articles') give the Directors power to appoint and replace Directors. Under the terms of reference of the Nominations Committee, any appointment must be recommended by the Nominations Committee for approval by the Board of Directors. The Articles also require Directors to retire and, if they so wish, submit themselves for election at the first AGM following their appointment and normally every three years thereafter. As was the case for the 2012 AGM, the Board has decided to follow best practice and all Directors will stand for annual re-election at this year's AGM, notwithstanding that this specific requirement in the UK Corporate Governance Code is for FTSE350 companies.

D B Stirling and C G Hurst, the Executive Directors, have service contracts which are terminable on 12 months' written notice. All the other Directors have service contracts which are terminable on six months' written notice.

The Company has issued Deeds of Indemnity in favour of all of the Directors. These Deeds were in force throughout the year ended 31 December 2012 and remain in force as at the date of this report. These Deeds, as well as the service contracts and the Company's Articles of Association are available for inspection during normal business hours at the Company's registered office and will be available at the AGM and 15 minutes before the meeting.

Conflicts of interest

All Directors submit details to the Company Secretary of any new situations, or changes to existing ones, which may give rise to an actual or potential conflict of interest with those of the Company. On an annual basis, the Company Secretary seeks confirmation from the Directors of their interests, which are reviewed by the Nominations Committee and the Board and, where considered appropriate, approved by the Board.

Where an actual, or potential, conflict is approved by the Board, the Board will normally authorise the situation on the condition that the Director concerned abstains from participating in any discussion or decision affected by the conflicted matter. Authorisation of a conflict is only given by Directors who are not interested in the matter.

Amendment to the Articles of Association

The Company's Articles of Association may only be amended by a special resolution of the shareholders passed in general meeting.

Corporate Governance

The Corporate Governance Report on pages 32 to 34 should be read as forming part of the Directors' Report.

Employees

To ensure employee welfare, the Group has documented, and well publicised, policies on occupational health and safety, the environment and training. The Group operates an equal opportunities, single status employment policy, together with an open management style. The Company operates to a number of recognised industry standards including Quality (ISO 9001), Environmental (ISO 14001) and Occupational Health and Safety (OHSAS 18001) approvals.

Further details of the Group's employment policies, including its policy regarding the employment of disabled people, are set out in the Corporate Social Responsibility Report on page 31.

Substantial shareholdings

As at 4 March 2013, the Company had received notice of the following material interests of 3% or more in the issued ordinary share capital:

	Ordinary share of 5.0p	Percentage of issued share capital
BlackRock Inc.	5,365,824	13.5%
Schroder Investment Management	5,193,352	13.0%
Henderson Global Investors	3,907,575	9.8%
Sekisui Alveo AG	3,814,762	9.6%
Marc and Claire Downes	1,600,000	4.0%
Nicholas Adrian Beaumont-Dark	1,418,000	3.6%

The holding held by BlackRock Inc. includes notified holdings on behalf of BlackRock Emerging Companies Hedge Fund (2,740,941 shares, 6.9%) and BlackRock UK Smaller Companies Fund (1,919,285 shares, 4.8%).

Directors' shareholdings are shown in the Directors' Remuneration Report.

Research and development

The amount spent by the Group on R&D in the year was £869,000 (2011: £897,000). This included work on nylon and microZOTE® as well as potential longer-term products in the development pipeline. In the opinion of the Directors none of this expenditure met the requirements for capitalisation in IAS38 and it was consequently all expensed in the Consolidated Income Statement.

Creditor payment policy

It is not Group policy to follow any standard or code of payment practice. Payment terms are agreed with suppliers when negotiating contracts or transactions. The Group aims to ensure that subject to any necessary variations which may result from supplier-related problems, the agreed payment terms are adhered to. At 31 December 2012, trade creditors of the Company represented 23 days of purchases (2011: 24 days).

Share capital and reserves

The Company has one class of ordinary shares which has no right to fixed income. Each share carries the right, on a poll, to one vote at general meetings of the Company. There are no specific restrictions on the size of a holding nor on the transfer of shares, which are both governed by the general provisions of the Articles of Association and prevailing legislation. The Directors are not aware of any agreements between holders of the Company's shares that may result in restrictions on the transfer of securities or on voting rights. No person has any special rights of control over the Company's share capital and all issued shares are fully paid.

At 31 December 2012, the Zotefoams Employee Benefit Trust (EBT) held 719,262 shares (approximately 1.8% of the issued share capital) (2011: 1,160,954 shares, approximately 2.9% of the issued share capital at 31 December 2011) to satisfy share plans as described in the Directors' Remuneration Report. In accordance with best practice, the voting rights on the shares held in the EBT are not exercised and the right to receive dividends has been waived. During the year the EBT issued 441,692 shares in respect of these share plans and no shares were bought to satisfy future share awards.

At the AGM held on 10 May 2012, authority was given to the Directors to allot unissued shares in the Company up to a maximum amount equivalent of approximately two thirds of the issued share capital of the Company. In addition, a special resolution was passed that granted authority to the Directors to allot equity securities in the Company for cash, without regard to the pre-emption provisions of the Companies Act 2006. Both these authorities, which at the date of this Report had not been used, expire at the AGM to be held on 15 May 2013 and the Directors propose to renew them for a further year.

At the AGM held on 10 May 2012, the Company was given authority to purchase up to 3,983,131 of its ordinary shares. This authority will expire at the 2013 AGM and, at the date of this Report, had not been used. In accordance with normal practice for listed companies, a special resolution will be proposed at this year's AGM to renew this authority to make market purchases up to a maximum of 10% of the issued share capital of the Company.

Treasury and financial instruments

Information in respect of the Group's policies on financial risk management objectives, including policies for hedging, as well as an indication of exposure to financial risk, is given on page 16 and in note 19 to the financial statements.

Pension scheme

The Company closed its Defined Benefit Pension Scheme to future accrual of benefit in December 2005. Employees are offered membership of a Defined Contribution Pension Scheme.

Charitable and political donations

The Group made charitable contributions of £1,238 (2011: £300) and no political contributions (2011: £nil) in the year.

Corporate Information

Directors' Report

Disclosure of information to Auditor

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's Auditor is unaware; and each Director has taken all the steps that they ought to have taken as a Director to make themselves aware of any relevant audit information and to establish that the Company's Auditor is aware of that information.

Auditor

In May 2012, upon the recommendation of the Audit Committee, the Board decided to put the Company's audit to competitive tender, as KPMG Audit plc ('KPMG') had been the Company's auditor since the Company listed in 1995. A formal tender process was initiated in May 2012 and following proposals and presentations from three firms (including KPMG), PricewaterhouseCoopers LLP was successful in the process. As a consequence, KPMG resigned as the Company's Auditor and the Board appointed PricewaterhouseCoopers LLP to fill the casual vacancy.

A resolution to appoint PricewaterhouseCoopers LLP as the Company's Auditor will be proposed at the forthcoming AGM.

By order of the Board

J W Kindell
Company Secretary
4 March 2013

Corporate Information

Directors' Remuneration Report

This report has been prepared in accordance with the Companies Act 2006 (the 'Act'). The report also meets the relevant requirements of the Listing Rules of the Financial Services Authority and describes how the Board has applied the principles relating to Directors' remuneration. As required by the Act, a resolution to approve this report will be proposed at the AGM of the Company at which the approval of the financial statements will be proposed.

The Act requires the Auditor to report to the Company's members on certain parts of the Directors' Remuneration Report and to state whether in their opinion those parts of the report have been properly prepared in accordance with the Act. The report has therefore been divided into separate sections for audited and unaudited information.

Information not subject to audit

Remuneration Committee

The Company has established a Remuneration Committee which is constituted in accordance with the recommendations of the UK Corporate Governance Code. R J Clowes, M-L Clayton, N G Howard and A Walker were members of the Committee throughout 2012 to the date of this report. R H Lawson served on the Committee until 31 March 2012, when he retired from the Board. The Committee would like to thank Mr Lawson for the valued contribution that he made to the Committee. All the members are independent Non-Executive Directors, with the exception of N G Howard, who was independent on appointment as Chairman of the Company. The Committee was chaired throughout 2012 by R J Clowes.

None of the Committee members has any personal financial interest (other than as shareholders) in the Company, nor do they have any interests that may conflict with those of the Company, such as cross directorships. None of the Committee members is involved in the day-to-day management of the business. The Committee makes recommendations to the Board on remuneration matters. No Director is involved in any decision about his or her own remuneration.

In 2012, the Committee met five times and considered the following matters:
- its evaluation and reviewed its terms of reference;
- the Directors' Remuneration Report for 2011 and relevant matters;
- the annual bonuses for the Executive Team and the employees;
- the grant of HMRC Approved Share Options;
- the grant of Long-Term Incentive Plans ('LTIPs') and the vesting of 2009 awards;
- the salary review of the Executive Team; and
- the remuneration of the Chairman.

In determining the remuneration policy and aspects of its work for the year, the Committee consulted D B Stirling (Managing Director) about its proposals.

Remuneration policy for the Executive Directors

The executive remuneration packages have been prudently designed to attract, motivate and retain Directors of the highest calibre to maintain the Group as a market leader of foam technology and to reward them for enhancing value to shareholders.

The Committee is responsible for setting the performance criteria for the Executive Directors and key members of senior management and determining their annual remuneration package.

The remuneration package for Executive Directors and senior management comprises:
- basic annual salary;
- benefits (such as private medical insurance and car allowance);
- annual bonus plan;
- long-term incentive schemes; and
- pension arrangements.

In order to incentivise the Executive Directors to deliver against the Group's strategy of growing the Group and increasing value to the shareholders, the Committee believes that a substantial proportion of the remuneration of the Executive Directors should be performance related. As described further below, Executive Directors may receive an annual bonus incentive, which is capped as a percentage of basic salary, together with long-term incentive arrangements.

Basic annual salary

The Committee reviews each Executive Director's basic annual salary in the first quarter of each year and also when an individual changes position or responsibility. The Committee considers the remuneration of the Executive Team as a whole when determining the appropriate level of remuneration, as well as an individual's performance. The Committee will also consider independent surveys of directors' remuneration to ensure that the proposed level of remuneration is appropriate. Periodically, the Committee will engage the services of a remuneration consultant to provide specific advice on remuneration of its Executive Directors. The Committee has adopted the policy to set the basic annual salary at a level below what it believes is the average market rate for the individual concerned, but to set the incentive potential at a higher rate. Basic annual salaries were last reviewed on 1 April 2012 and were increased by approximately 3% which was consistent with the salary increases of the other employees in the Company.

The Company operates a salary sacrifice scheme under which employees are able to vary their contract of employment to have a reduction in salary in exchange for additional Company contributions to the employees' pension schemes. However, where such sacrifices have been made bonuses and other incentive arrangements are calculated on salary before such reductions are made ('bonusable salary'). Both D B Stirling and C G Hurst have elected to receive a 7% reduced salary for increased contributions to their pension schemes. Further details of the contributions made by the Company into the Defined Contribution Pension Scheme for these individuals are shown in this report within the Information Subject to Audit.

Corporate Information

Directors' Remuneration Report continued

Benefits
The benefits that D B Stirling and C G Hurst both received in the year were a car allowance and private medical insurance cover for them and their respective families.

Annual bonus
Each year, the Committee sets the performance criteria for the annual bonuses of the Executive Team, including the Executive Directors. In setting appropriate performance criteria, the Committee refers to independent surveys of directors' remuneration. The Committee believes that any incentive compensation awarded should be tied to the interests of the Company's shareholders and that the principal measure of those interests is profit before taxation excluding exceptional items. The bonus award for the Executive Directors is normally capped at 100% of bonusable salary. Any element of the bonus payment over 40% of bonusable salary is paid in restricted shares (deferred bonus shares) which will normally only be capable of release if the executive is still in the employment of the Company three years later.

Long-term incentives and share options
The Company currently operates the following long-term incentive schemes:

Since 2007, the LTIP has been the Company's principal long-term incentive scheme for the Executive Directors and senior management. LTIP awards are made by the Committee subject to performance conditions on Total Shareholder Return and EPS (excluding exceptional items) over a three-year period. The Committee believes that these performance criteria best align this incentive with the interests of the shareholders.

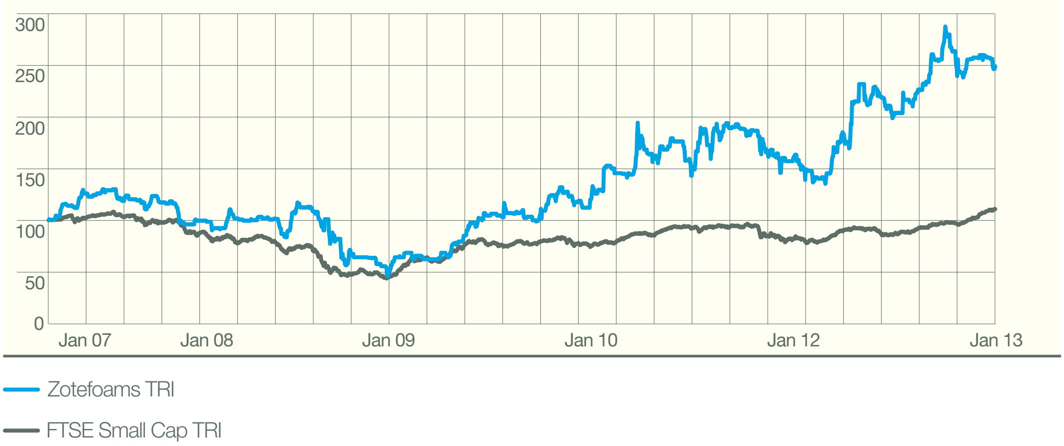
UK-based Executive Directors and senior management have also been granted share options under a Her Majesty's Revenue and Customs Approved Share Option Scheme. These options are only exercisable after a three year vesting period, if the Group's earnings per share, excluding exceptional items and with a normalised tax charge, increases by at least three percentage points per annum in excess of the increase in the Retail Price Index over the same period. The exercise price of the options granted under this Scheme is equal to the market value of the Company's share price at the time when the options are granted. The Executive Directors are entitled to participate provided they meet the eligibility requirements of the scheme.

The Company also has an Executive Share Option Scheme. This was replaced as the main long-term incentive scheme in 2007 by the LTIP and no awards under this Scheme have therefore been made since then, although C G Hurst still holds outstanding options under this Scheme.

Pension arrangements
The Executive Directors are members of the Zotefoams Defined Contribution Alternative Pension Plan. Prior to 31 December 2005 the Executive Directors were active members of the Zotefoams Defined Benefit Pension Scheme (the 'Scheme'). However, this Scheme closed to future accrual of benefit on 31 December 2005 and after this date the Executive Directors became deferred members of this Scheme.

Performance graph
The following graph charts the total cumulative shareholder return (share price movements plus dividends reinvested) of the Company since January 2007. It is compared to the FTSE Small Cap Index which the Committee believes is the most relevant comparison for a company of Zotefoams' size.

Zotefoams and FTSE Small Cap Total Return Index ('TRI') re-based to 100
(January 2007 to December 2012).



Service contracts
The Executive Directors have service contracts with the Company which are terminable on 12 months' written notice from the Company or the respective Director.

The Non-Executive Directors and the Chairman have three-year contracts which can be terminated by the Director or the Company on six months' written notice.

A summary of the service contacts is as follows:

Director	Commencement date	Date of termination	Unexpired period	Notice period
M-L Clayton	1 July 2011	1 July 2014	15 months	6 months
R J Clowes	23 July 2010	22 July 2013	4 months	6 months
N G Howard	3 December 2011	31 December 2014	21 months	6 months
C G Hurst	1 October 2000	Not Applicable	Not Applicable	12 months
D B Stirling	1 September 1997	Not Applicable	Not Applicable	12 months
A Walker	1 July 2011	1 July 2014	15 months	6 months

The service agreements between each of the Directors and the Company do not entitle the respective Director to payment of compensation on termination other than statutory compensation. None of the Directors' or employees' service contracts contain provisions providing for compensation for loss of office or employment that occurs because of a takeover.

Non-Executive Directors
All independent Non-Executive Directors and the Chairman have specific terms of engagement and their remuneration is determined by the Board within the limits set by the Articles of Association and based on independent surveys of fees paid to non-executive directors of similar companies. Independent Non-Executive Directors and the Chairman cannot participate in any of the Company's share options schemes and are not eligible to join the Company's pension scheme.

Information subject to audit
Directors' emoluments

Remuneration in £	Basic salary/fees	Operational bonus	Car allowance	Other benefits[1]	Company pension contributions[2]	**Total 2012**	Total 2011
M-L Clayton	28,563	—	—	—	—	**28,563**	14,000
R J Clowes	28,563	—	—	—	—	**28,563**	27,615
N G Howard	54,125	—	—	—	—	**54,125**	52,125
C G Hurst	123,145	82,367	10,561	1,235	27,470	**244,778**	200,695
R H Lawson	7,000	—	—	—	—	**7,000**	27,500
D B Stirling	176,795	118,596	11,640	1,155	38,709	**346,895**	283,724
A Walker	26,563	—	—	—	—	**26,563**	13,000
	444,754	200,963	22,201	2,390	66,179	**736,487**	618,659

1 Other benefits are calculated in terms of taxable values in the UK.
2 The Company operates a Defined Contribution ('DC') Pension Plan. Individuals can opt to change their contract of employment under a salary sacrifice arrangement, under which their salary is reduced and the Company makes a corresponding contribution into their DC Pension Plan. Both the Executive Directors have opted for the salary sacrifice scheme and the total contributions made by the Company to each individual's pension plan are shown above. None of the Executive Directors made any employee contributions to the DC Pension Plan.

Directors' shareholdings
The beneficial and non-beneficial interests of the Directors (including persons connected with them within the meaning of Section 252 of the Companies Act 2006) in the ordinary shares of the Company are set out below:

Number of ordinary 5.0p shares	**31 December 2012**	31 December 2011
M-L Clayton	**10,000**	10,000
R J Clowes	**47,250**	47,250
N G Howard	**63,000**	63,000
C G Hurst	**220,910**	163,974
D B Stirling	**268,431**	186,935
A Walker	**5,000**	5,000
	614,591	476,159

There have been no changes to Directors' interests between the end of the financial year and the date of this report.

Corporate Information

Directors' Remuneration Report continued

Share options and awards

Options over ordinary shares granted:

	Scheme	As at 31 December 2011	Date of exercise or release	Granted	Exercised or released	Lapsed, forfeited or cancelled	**As at 31 December 2012**	Exercise price	Exercisable	Expiry date
C G Hurst	Executive SOS	59,631	–	–	–	–	**59,631**	72.5p	07.04.2007	06.04.2014
	Executive SOS	115,909	–	–	–	–	**115,909**	77.0p	22.12.2008	21.12.2015
	HMRC SOS	28,116	–	–	–	–	**28,116**	106.7p	12.08.2011	11.08.2018
	LTIP (2009)	103,258	12.04.2012	–	(103,258)	–	**–**	nil	16.03.2012	n/a
	2009 DB	6,408	–	–	–	–	**6,408**	nil	11.03.2013	n/a
	LTIP (2010)	54,090	–	–	–	(8,654)	**45,436**	nil	19.03.2013	n/a
	LTIP (2011)	40,717	–	–	–	–	**40,717**	nil	31.03.2014	n/a
	2010 DB	4,967	–	–	–	–	**4,967**	nil	31.03.2014	n/a
	LTIP (2012)	–	–	34,584	–	–	**34,584**	nil	04.04.2015	n/a
D B Stirling	HMRC SOS	28,116	–	–	–	–	**28,116**	106.7p	12.08.2011	11.08.2018
	LTIP (2009)	147,801	12.04.2012	–	(147,801)	–	**–**	nil	16.03.2012	n/a
	2009 DB	9,173	–	–	–	–	**9,173**	nil	11.03.2013	n/a
	LTIP (2010)	77,424	–	–	–	(12,388)	**65,036**	nil	19.03.2013	n/a
	LTIP (2011)	58,632	–	–	–	–	**58,632**	nil	31.03.2014	n/a
	2010 DB	7,153	–	–	–	–	**7,153**	nil	31.03.2014	n/a
	LTIP (2012)	–	–	49,866	–	–	**49,866**	nil	04.04.2015	n/a

Executive Share Option Scheme ('Executive SOS')

These options were granted under the Zotefoams Executive Share Option Scheme. Whilst there are still existing awards outstanding, the scheme was replaced by LTIP awards in 2007. No awards under the scheme have been made since 2007 and there have been no changes in options granted between the end of the year and the date of this report.

The middle market quoted share price at 31 December 2012 was 201.5p and the high and low prices during the year were 225.0p and 109.0p respectively.

Long-Term Incentive Plans ('LTIPs')

The LTIP awards made are subject to performance and service conditions. 50% of the award is subject to growth in Total Shareholder Return (TSR) and 50% subject to EPS growth. Performance is measured over a three-year period and a proportion of the restricted shares will be released to the participant, to the extent to which TSR and EPS targets over the period have been met, together with additional shares that represent the dividends that would have been paid during the performance period on the restricted shares that have been released.

The table below summarises the performance criteria for the awards that remain outstanding. The awards were made based on 50% of the Executive Directors' bonusable salary.

			Threshold		Maximum	
Award year	Performance period		Performance target	% of award vesting	Performance target	% of award vesting
2010	2010-2012	TSR goal	10% pa growth	12.5	25% pa growth	50
	2012	EPS goal	9.2p	12.5	14.3p	50
2011	2011-2013	TSR goal	10% pa growth	12.5	20% pa growth	50
	2013	EPS goal	10.0p	12.5	15.0p	50
2012	2012-2014	TSR goal	10% pa growth	12.5	20% pa growth	50
	2014	EPS goal	11.0p	12.5	16.0p	50

The total award vesting is the sum of the awards for TSR and EPS. If the performance is below the EPS threshold then no part of the EPS award vests. If performance is below the TSR threshold then no part of the TSR award vests. Between the threshold and the maximum, the award vests on a sliding scale basis.

Normally, the TSR growth target is set from the average share price of the final quarter of the preceding year to the year in which the awards are made. However, in the final quarter of 2011, the Committee felt that the Company's share price did not reflect the true value of the Company and decided that it would be more appropriate to set the TSR growth target for the 2012 award from the average share price in the final quarter of 2010 increased by 10% to produce a baseline that was more meaningful.

On 12 April 2012, the LTIP awards made in March 2009 vested. The market price was 170p. The level of vesting of these awards was 88.7%, which was then increased to reflect the dividends paid during the performance period.

The market value of the 2012 LTIP shares granted was 186.5p on the date of the grant (4 April 2012).

For the LTIP awards made in March 2010, based on the performance of the Company as at 31 December 2012 and the average share price in the final quarter of 2012, 84% of the shares will vest under this award.

HMRC Approved Share Option Scheme ('HMRC SOS')
These options have been granted under a HMRC Approved Share Option Scheme. These options are not exercisable unless EPS increases over a three-year period by at least three percentage points per annum in excess of the increase in the Retail Price Index over the same period. This performance criterion has been met for the awards held by C G Hurst and D B Stirling.

Annual Bonus Deferred Payments – Deferred Bonus Shares ('DB')
Bonus awards over 40% of bonusable salary are in restricted shares (deferred bonus shares) which, once awarded, are held in trust and are not subject to any further performance conditions. In normal circumstances, the deferred bonus shares are only capable of being released if the executive is still employed by the Company three years after the date of the award. On release, additional shares are also released to the executive which represent the dividends that would have been paid on the deferred bonus shares during the restricted period.

The number of deferred bonus shares to be awarded is calculated by dividing the proportion of the bonus above 40% of bonusable salary by the average of the Company's mid market share price for the five immediately preceding dealing days (but not the day of award itself) to the award date.

In 2012 the bonus award under the executive bonus scheme was 62% of bonusable salary. Therefore, 40% of the bonusable salary will be paid in cash and the remaining, 22% of the bonusable salary will be awarded in deferred bonus shares (in 2011, as the bonus was 33% of bonusable salary, the bonus was all paid in cash). Profit before tax increased by 8% in 2012.

Directors' pension entitlements
The Zotefoams Defined Benefit Pension Scheme was closed to future accrual of benefits from 31 December 2005. At this time, all active members left the Scheme and were granted preserved pensions payable from their normal retirement age (or immediately, if the member had reached normal retirement age).

The following serving Directors were members of the Zotefoams Defined Benefit Pension Scheme during the year.

	Accrued pension in scheme at year end[1] £	Gross increase in pension £	Increase in accrued pension net of CPI inflation £	Value of accrued pension at year end[2] £	Value of accrued pension at start of year[3] £
C G Hurst	9,138	193	–	96,447	123,557
D B Stirling	17,954	378	–	159,860	220,520

1 The pension entitlement shown is that which would be paid annually on retirement at normal retirement age (or immediately upon late retirement where applicable), based on service to 31 December 2005 (the date the scheme was closed to future accrual) and excluding any future increases under the Rules of the Scheme.
2 Transfer values have been calculated in accordance with Section 93A of the Pension Schemes Act 1993 and have been calculated in accordance with the Occupational Pension Schemes (Transfer Value) Regulations 1996 on the basis agreed with the Trustees of the Scheme.
3 The change in the transfer value over the year includes the effect of fluctuations in the transfer value due to factors beyond the control of the Company and Directors, such as changes in financial conditions. The transfer value basis was amended as from 1 February 2012 as a result of changes to the statutory measure of inflation for indexation to pensions and as part of a general review of the suitability of the basis.

The following is additional information relating to Directors' pensions from the Scheme:
a) Before the Scheme closed, members of the Scheme had the option of paying Additional Voluntary Contributions (AVCs). The value of these AVCs has been excluded from the above figures.
b) Normal retirement age is 65.
c) On death before retirement, a spouse's pension is payable of one half of the member's preserved pension at leaving, revalued from leaving date to the date of death.
d) On death in retirement, a spouse's pension is payable of one half of the member's pension at death, without reduction for any part of the member's pension surrendered for cash at retirement.
e) Members' Guaranteed Minimum Pensions increase at statutory rates. Other pensions increase at 5% per annum or the increase in the Retail Price Index if less.
f) From 1 January 2006, active employees were able to pay contributions to a defined contribution scheme set up by the Company in order to receive retirement benefits. The Company also contributes to this arrangement. Details of this arrangement and the value of any contributions paid to this arrangement are not included in the above disclosures.

The Executive Directors are members of the Zotefoams Defined Contribution Alternative Pension Plan. Under a salary sacrifice agreement all contributions to this pension plan are paid by the Company and the contributions made by the Company in 2012 are shown in the table of Directors' Emoluments.

Approval
The report was approved by the Board of Directors on 4 March 2013 and signed on its behalf by:

R J Clowes
Senior Independent Non-Executive Director and Chair of the Remuneration Committee
Company number: 2714645

Corporate Information

Audit Committee Report

Summary of the role of the Audit Committee

The Audit Committee is appointed by the Board from the independent Non-Executive Directors of the Company. The Audit Committee's terms of reference, which are available on the Company's website, include all matters indicated by the Disclosure and Transparency Rule 7.1 and the UK Corporate Governance Code. The terms of reference are reviewed regularly by the Audit Committee and, if amended, are then referred to the Board for approval. The terms of reference were reviewed in February 2012 and updated to include a responsibility to review arrangements to prevent bribery.

The Audit Committee is responsible for:

- monitoring the integrity of the financial statements of the Group and any formal announcements relating to the Group's financial performance and reviewing significant financial reporting judgements contained therein;
- reviewing the External Auditor's management letter and management responses;
- reviewing the Group's internal controls and risk management systems;
- reviewing the arrangements by which staff may, in confidence, raise concerns about possible improprieties ('the whistleblowing policy');
- reviewing the arrangements put in place by the Group to prevent bribery and to receive reports of non-compliance;
- annually assessing the need for an internal audit function and monitoring and reviewing the effectiveness of the application of internal audit to the Group;
- making recommendations to the Board, for a resolution to be put to the shareholders for their approval in general meeting, in relation to the appointment of the External Auditor and the approval of the remuneration and terms of engagement of the External Auditor;
- reviewing and monitoring the External Auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements; and
- developing and implementing a policy on the engagement of the External Auditor to supply non-audit services, taking into account relevant guidance regarding the provision of non-audit services by the external audit firm.

The Audit Committee is required to report its findings to the Board, identifying any matters in respect of which it considers that action or improvement is needed, and make recommendations as to the steps to be taken.

Composition of the Audit Committee

Throughout 2012, the members of the Audit Committee were the independent Non-Executive Directors of the Company (M-L Clayton, R J Clowes and A Walker). R H Lawson, who was the Chair of the Committee until 6 December 2011, also served as a member of the Committee until he retired from the Board on 31 March 2012. The Audit Committee wishes to thank him for his contribution and support over the previous nine years. M-L Clayton has been the Chair of the Committee throughout 2012. She is a Fellow of the Association of Chartered Certified Accountants and, in the opinion of the Board, has significant, recent and relevant financial experience to fulfil the requirements of Disclosure and Transparency Rule 7.1 and the UK Corporate Governance Code. All Audit Committee members are expected to be financially literate and, where necessary, the Company provides further training if required.

The Committee normally comprises three members, with a minimum of two members at any time. Two members constitute a quorum.

Meetings

The Audit Committee has a planned calendar linked to events in the Company's financial calendar, where it normally meets three times in the year. Each meeting agenda is predominantly based around these events and is approved by the Audit Committee Chair on behalf of the other members, although other members have the right to require reports on matters of interest in addition to standard agenda items. Due to the audit tender process, the Audit Committee met five times in 2012.

The Company Secretary acts as secretary to the Audit Committee. The Company Chairman, Managing Director, Finance Director, Financial Controller and senior representatives of the External and Internal Auditors are invited to attend relevant meetings of the Committee, although the Committee reserves the right to request any of these individuals to withdraw. At each meeting, the External Auditor is given the opportunity to raise matters without the management being present. Other senior management may be invited to present such reports as are required for the Committee to discharge its duties. During the year, on an informal basis, the Audit Committee Chair meets senior representatives of both the External Auditor and Internal Auditor to discuss matters ahead of the formal Committee meetings.

Overview of the actions taken by the Audit Committee to discharge its duties

Since the beginning of 2012 the Audit Committee has:

- reviewed the financial statements in the 2011 and 2012 report and accounts and the interim report issued in August 2012. As part of this review the Committee received reports from the External Auditor on the audit of the Annual Reports and accounts and the review of the interim report;
- recommended to the Board to put the external audit to tender, oversaw the tender process and recommended to the Board to appoint PricewaterhouseCoopers LLP;
- reviewed the Group's policies on ethics, anti-bribery and corruption, fraud, whistleblowing and employee share trading;
- considered the output from the Group-wide process used to identify, evaluate and mitigate high-level business risks, including reviewing the Group's recently developed high-level business risk matrix;
- agreed a programme of work for 2012 to be performed by the Internal Auditor, and received the Internal Auditor's reports on the work undertaken and management's responses to the proposals made in the reports;
- reviewed the effectiveness of the Group's internal controls (including, but not limited to, financial controls) to ensure that they remain appropriate and adequate as the Group grows;
- reviewed and agreed the scope of the audit work to be undertaken by the External Auditor;
- considered the views of both the External Auditor and Internal Auditor on the effectiveness of the Group's internal financial controls;
- agreed the fees to be paid to the External Auditor for their audit and work on the accounts and interim report;
- undertaken an evaluation of the independence and effectiveness of the External Auditor, including reviewing the Group's policy on non-audit services provided by the External Auditor; and
- reviewed its own effectiveness and terms of reference.

External auditor

As part of good practice, the Audit Committee recommended to the Board that the Group's audit be put to competitive tender, as KPMG Audit plc ('KPMG') had been the Group's auditor since the Company listed in 1995. The tender process commenced in May 2012 and a selection panel was appointed, which included the Audit Committee Chair. The panel considered the proposals submitted and the presentations given by the three invited firms (including KPMG). The selection panel then submitted its proposal to the Audit Committee, which then considered the matter and recommended to the Board that PricewaterhouseCoopers LLP be selected as the External Auditor.

At the conclusion of the external audit, the Audit Committee assesses the effectiveness of the External Auditor in relation to their fulfilment of the agreed audit plan, the robustness and perceptiveness of the Auditor in handling key accounting and audit judgements and the thoroughness of the External Auditor's review of internal financial controls. The Audit Committee, following such a review of these activities, concluded that the External Auditor has performed satisfactorily and has recommended to the Board that a resolution be put to the shareholders at the 2013 AGM to re-appoint the External Auditor.

The Audit Committee is responsible for the development, implementation and monitoring of the Group's policy on external audit. Although the External Auditor is permitted to provide non-audit services, the Committee has agreed a policy that sets a cap on the amount of non-audit work provided. The Committee regularly reviews the amount of non-audit work provided in order to ensure that the Auditor's objectivity and independence are not compromised.

Internal audit function

Each year the Audit Committee reviews the need for an internal audit function and given the size of the Group continues to be of the opinion that the internal audit function is best performed by an external audit firm. Mazars LLP continues to provide such services to the Group, which complement the services provided by the External Auditor. In 2012, the Audit Committee agreed the scope for the internal audits, reviewed the reports received and discussed the proposals made with management. Mazars LLP performs no other work for the Group and the Audit Committee considers them to remain independent.

Overview

As a result of its work during the year and having undertaken a review of its performance, the Audit Committee has concluded that it has acted in accordance with its terms of reference and has ensured the independence and objectivity of the External Auditor. The Chair of the Audit Committee will be available at the AGM to answer any questions about the work of the Committee.

Approval

This report was approved by the Audit Committee and signed on its behalf by:

M-L Clayton
Non-Executive Director and Chair of the Audit Committee
4 March 2013

Corporate Information

Corporate Social Responsibility Report

Zotefoams considers that the management of safety, health, environmental, social and ethical matters forms a key element of effective corporate governance. These areas are covered by the internal control systems and procedures outlined in the Corporate Governance Report on page 34.

Safety, Health and Environment ('SHE')

The Board has in place separate policies relating to Safety, Health and Environment. The Company is certified to accredited standards OHSAS 18001 on Health and Safety and ISO 14001, the International Standard for Environmental Management Systems, and is regularly audited by those bodies to ensure that the Company complies with those standards.

The Board has ultimate responsibility for SHE policy and performance and receives quarterly reports on SHE issues. Annual performance objectives are agreed by the Board and performance against these objectives is monitored as part of its quarterly reporting programme.

The Managing Director is directly responsible to the Board for Safety, Health and Environmental performance. Site Committees on SHE meet once a quarter or more frequently to consider all SHE matters, which are overseen by Steering Committees, chaired by the Managing Director (or appropriate responsible person in subsidiary companies). The Steering Committees meet quarterly to consider overall performance and the impact of current and impending legislation. The Company has both a Health and Safety Adviser and an Environmental Adviser who support these groups.

On joining the Group, all employees receive training on SHE matters, including the Group's policies. All employees are made aware that every employee has a part to play to ensure the safety of themselves and their colleagues at work. Employees are encouraged to report to their managers any unsafe, or potentially unsafe, conditions. Senior managers are responsible for ensuring that SHE policies are implemented in their areas, that their teams are informed of the departmental SHE requirements and that the employees receive training on environmental issues and safe working practices. Regular audits are conducted to ensure policy and procedure implementation is appropriate.

The Company takes the reporting of all SHE incidents very seriously. In 2012, the Company has actively encouraged the employees to report any 'near misses' as well as damage to plant or equipment which has not resulted in personal injury. This has been illustrated by a marked increase in the reporting of 'near miss' incidents in 2012 compared to 2011. The Company also runs initiatives to standardise and maintain working practices to reduce the risk of SHE incidents occurring.

All SHE events are investigated by appropriate levels of management to ascertain the root cause of the event and, wherever possible, working practices and procedures are improved to prevent re-occurrence. In 2012, there were no prosecutions, fines or enforcement actions taken as a result of non-compliance with safety, health or environmental legislation (2011: none).

Health and safety performance

Few controlled substances are used in the manufacture of our foams, but where they are, the Company has established procedures, which the relevant employees are trained on, to ensure the storage and handling of such substances are not only done safely but in accordance with the regulatory requirements. The manufacturing process does involve manual handling and processing of materials. Whenever new or altered equipment or materials are introduced, and at regular periods thereafter, the risks to the processes are assessed and, wherever possible, improvements are made, such as the design of the equipment, to reduce or eliminate the risks identified. The Company's most recent low pressure vessel, which was brought into operation in 2012, was specifically designed to reduce the need for manual handling.

The most strictly controlled parts of the Group's sites are where high pressure gas is used. The high pressure operating vessels are subject to the Pressure Systems Safety Regulations 2000 in the UK and OSHA in the US. Tightly defined procedures and operational controls are in place to manage the safety of these pressure systems. Fail-safe mechanisms known as Pressure Relief Valves ('PRVs') and bursting disks (which act like fuses in an electrical system) are included in the design of the pressure systems, which when triggered allow depressurisation of sections of the system preventing any further risks. Operation of these fail-safe mechanisms release harmless nitrogen gas into the atmosphere.

In 2012 there were five reportable lost time injuries in the Group, which were all manual handling related. All incidents have been fully investigated and appropriate corrective actions have been taken.

Year	**2012**	2011	2010
Reportable lost time injuries	**5**	8	5

Environmental performance

The process used by Zotefoams to manufacture foam is one of the most environmentally friendly methods to manufacture cross-linked polymer foams. Nitrogen gas, which is a harmless gas and comprises 78% of the earth's atmosphere, is used to expand the foams. The common peroxide cross-linking agent, which strengthens the foam's properties, is completely utilised during the manufacturing process. No other chemical additives are used in the Company's basic foam products and, therefore, the basic foam products have no toxic or volatile chemicals (such as solid chemical residues, CFC, HCFC or volatile hydrocarbons). Such substances may be found in foams expanded chemically by the Company's competitors.

In 2012 the Group had 14 internally recorded environmental incidents (2011: 13).

Eight of these were noise or other complaints (2011: 6) due to the close proximity of the Croydon site to residential areas. All complaints were investigated and actions taken.

Four incidents were minor chemical or oil spills (2011: 4) which were dealt with appropriately and had no significant environmental impact. Two were releases of nitrogen gas into the air from bursting disks (2011: 3). While Zotefoams records this as an environmental incident, principally on the grounds of loss of production and noise, the bursting disks are an essential part of the statutory safety regime for the high pressure equipment and are evidence that the safety systems of the plant are functioning as intended.

The vast majority of the waste produced by Zotefoams plc is either solid or foamed polyolefin. Unfortunately, neither of these is easily recyclable by being melt processed (the process used to recycle most plastics) due to the essential cross-linking step used on the polymers to manufacture the foams.

In 2012, 638 tonnes of waste was sent to landfill from the main site in Croydon. This represents a significant reduction from 757 tonnes in 2011, despite higher production volumes, and demonstrates the initiatives taken to improve waste management.

In 2012, water consumption increased to 49,000m³ from 38,000m³ in 2011. A new monitoring programme has been introduced and actions are being taken to reduce this consumption.

The Group regularly monitors its energy consumption, not only to reduce its carbon footprint, but with increasing energy costs, to keep the margins on its products to acceptable levels. In 2012, efforts across the site continued to improve energy efficiency. Energy consumed per kg of material produced in 2012 improved by 1% compared to 2011. In October 2009 Zotefoams entered into a Climate Change Levy (CCL) agreement, which involves the Company meeting specific targets to reduce its energy consumption. Providing Zotefoams meets the requirements of the CCL agreement it receives a rebate on its electricity bills and is also exempt from the Carbon Reduction Commitment Scheme.

Croydon site: Year	**2012**	2011	2010
Internally recorded environmental incidents	**14**	13	15
Waste sent to landfill (tonnes)	**638**	757	687
Water consumption (000s m³)	**49**	38	48
Energy consumption (Kwhr/Kg)	**11.6**	11.7	12.5

People

The people at Zotefoams are a key part of the success of the business. Zotefoams operates an equal opportunities policy, as well as a dignity at work policy and believes diversity (ethnicity, age, gender, language, sexual orientation, religion, socio-economic status, personality and ability) of the employees promotes a better working environment which in turn leads to innovation and business success. Applications for employment by disabled persons are always fully considered and in the event of an employee becoming disabled, every effort is made to ensure that their employment with the Group continues and that appropriate training is provided where necessary. It is the policy of the Group that the training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

Zotefoams places considerable value on the involvement of its people and continues to keep them informed on matters affecting them as employees and on the various factors affecting the performance of the Group. This is achieved through formal and informal meetings. The Company operates a Joint Consultative Committee (JCC), which comprises an employee representative covering each department. The JCC meets regularly and considers a wide range of matters affecting the employees' current and future interests.

Business ethics

Zotefoams is committed to high standards of business conduct and seeks to maintain these standards across all of its operations throughout the world. In 2012, the Company developed a formal ethics policy and updated its policies on anti-bribery and corruption, anti-fraud, employee share trading and whilstleblowing. The ethics policy is available on the Company's website. It is also included with the other policies in the employee handbook. Employees are made aware of the policies on joining Zotefoams and for those employees, such as the sales staff, who work in areas that are considered to carry a greater risk, regular training is provided on anti-bribery and anti non-competitive trading practices.

Corporate Information

Corporate Governance

The Company is committed to the principles of corporate governance contained in the UK Corporate Governance Code (the 'Code') for which the Board is accountable to shareholders. The Code is available from the Financial Reporting Council's website (www.frc.org.uk).

Statement of compliance with the UK Corporate Governance Code

The Company complied with all of the Code's provisions for the year ended 31 December 2012.

Statement about applying the principles of the Code

The Company has applied the principles set out in the Code, including both the main principles and the supporting principles, by complying with the Code as reported above. Further explanation of how the principles and supporting principles have been applied is set out below and in the Directors' Remuneration Report and the Audit Committee Report.

Board effectiveness

The Board's role is to provide the entrepreneurial leadership of the Company within a framework of prudent and effective controls which enable risk to be assessed and managed. The Board sets the strategic aims of the Company, ensures that the necessary resources are in place to achieve the Company's objectives and reviews management performance. The Board's role is to act as representative of the shareholders, who are the Company's owners, and focuses on the governance of the Company. Management is delegated to the Executive Directors and the senior executive management of the Group.

All Directors must take decisions objectively in the interests of the Company.

As part of their role as members of a unitary Board, Non-Executive Directors constructively challenge and help develop proposals on strategy. Non-Executive Directors scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance. They satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible. They are responsible for determining appropriate levels of remuneration of Executive Directors and have a prime role in appointing, and where necessary removing, Executive Directors, and in succession planning.

The Board has three major committees which report into it and function within defined terms of reference. These are the Audit Committee, the Remuneration Committee and the Nominations Committee. The terms of reference for these Committees are available on the Company's website www.zotefoams.com and in paper form, on request to the Company Secretary. In 2012, the terms of reference for all the Committees were reviewed and updated, to ensure that they reflected best practice.

The Board has put in place a schedule of matters that are reserved for its determination or which need to be reported to the Board. This schedule is reviewed regularly and was last updated in February 2013.

Attendance details for 2012 by the Directors for meetings of the Board and these Committees are shown below:

	Formal Board meetings		Audit Committee meetings		Remuneration Committee meetings		Nominations Committee meetings	
Attendance at meetings	Eligible	Attended	Eligible	Attended	Eligible	Attended	Eligible	Attended
M-L Clayton	7	7	5	4	5	5	2	2
R J Clowes	7	7	5	5	5	5	2	2
N G Howard	7	7	n/a	n/a	5	5	2	2
C G Hurst	7	7	n/a	n/a	n/a	n/a	n/a	n/a
R H Lawson	2	2	2	2	2	2	1	1
D B Stirling	7	7	n/a	n/a	n/a	n/a	n/a	n/a
A Walker	7	7	5	5	5	5	2	2

Chairman and Managing Director

The Chairman is responsible for leadership of the Board, ensuring its effectiveness on all aspects of its role and setting its agenda. The Chairman is also responsible for ensuring that the Directors receive accurate, timely and clear information. The Chairman facilitates the effective contribution of the Non-Executive Directors in particular and ensures constructive relations between Executive and Non-Executive Directors.

The Board considers that N G Howard has sufficient time to devote to his role as being the Chairman of the Company. Mr Howard only has one other significant commitment, which is being a non-executive director of Alliance One International Inc. (listed on the New York Stock Exchange).

The Managing Director is responsible for the running of the Company's business. He is supported by the other Executive Director and senior management team members in the Group.

Board balance and independence

Since R H Lawson retired from office on 31 March 2012, the Board structure has comprised two Executive Directors, three independent Non-Executive Directors and a Non-Executive Chairman. R J Clowes replaced R H Lawson as the Senior Independent Director on 5 March 2012.

The Chairman, N G Howard, is also Chair of the Nominations Committee and a member of the Remuneration Committee. Only the respective Committee Chairs and members are entitled to be present at meetings of the Remuneration, Audit and Nominations Committees, but others may attend at the invitation of the Committees. During the year the Chairman met with the Non-Executive Directors without the Executive Directors present and the Non-Executive Directors met without the Chairman being present.

Appointments to the Board and the Nominations Committee
Appointments to the Board are proposed by the Nominations Committee and approved by the Board.

The Nominations Committee comprises the Chairman, N G Howard (who is Chair of the Nominations Committee), and the three independent Non-Executive Directors. N G Howard was independent on his appointment as Chairman. The Committee operates within a defined set of terms of reference from the Board and is responsible for putting in place succession plans for the Board (in particular the Chairman and the Managing Director), reviewing the continuation in office of the Directors, managing the recruitment of new Board members within a specification set by the Board and annually reviewing conflicts of interest authorisations granted to any Board members. The Committee met twice in 2012 to perform its duties as set out in its terms of reference.

The Board acknowledges the benefits of diversity, including that of gender, but when considering appointments to the Board, appointments are made purely on merit and against objective criteria. Search consultants are briefed of these criteria and are encouraged to cast their search sufficiently wide to identify the best candidates. Care is taken to ensure that appointees, as well as the existing Directors, have sufficient time to devote to their roles. With two independent Non-Executive Directors only being recently appointed in 2011, it was not considered necessary to make any further appointments in 2012.

Information and professional development
Each month all Directors receive management reports and briefing papers in relation to Board matters. New appointments to the Board receive an induction and, if appropriate, training. Training is made available in order to fulfil the requirements of being a Director of a listed company. The Directors have access to the Company Secretary and independent professional advisers, at the Company's expense, if required for the furtherance of their duties.

Board evaluation
A formal review of the performance of the Board and Committee performance is carried out each year. The Chairman's performance is reviewed by the other Non-Executive Directors in consultation with the Executive Directors. The other Non-Executive Directors' performance is evaluated by the Chairman in consultation with the Executive Directors. The Executive Teams' performance is evaluated by the Remuneration Committee in conjunction with the Managing Director (except in the case of the Managing Director, when the Managing Director is not present).

The evaluation of the Board takes the form of a questionnaire, prepared by the Chairman, and the results are compiled and discussed, with actions agreed. Each Committee undertakes its own evaluation, led by the relevant Chair in consultation with the Company Secretary. These take the form of a questionnaire and a discussion reviewing the work undertaken during the year and actions agreed. Due to the Company's size, the Board feels, at this stage, it is not appropriate to use the services of an external facilitator for its annual evaluation, but will keep the matter under review. From the 2012 evaluation, the Board had identified the benefits of switching to using one of the commercially available electronic packages for the secure and prompt distribution, access and storage of Board information for its meetings. All the evaluations were completed satisfactorily.

Re-election
Re-election of Board members is required by the Articles at the first AGM following appointment and normally once every three years thereafter. However the Code requires all directors of FTSE350 companies to stand for annual re-election. Although the Company is not within the FTSE350, the majority of Premium Listed companies have now adopted the practice for all their directors to stand for annual re-election. The Board has decided that all of the Directors will stand for annual re-election at the 2013 AGM, as they did at the 2012 AGM.

Remuneration
The principles and details of remuneration policy are set out in the Directors' Remuneration Report.

Financial reporting
The Directors' responsibilities for preparing the financial statements are set out in the Statement of Directors' Responsibilities.

Audit Committee and Auditor
A separate Audit Committee Report provides details of the role and activities of the Committee and its relationship with the External Auditor.

Going concern
The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business Review on pages 12 to 15 and the section entitled 'Principal Risks and Uncertainties' on page 16. This also describes the financial position of the Company, its cash flows and liquidity position. In addition, note 19 to the financial statements includes the Company's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities, borrowing facilities, and its exposure to credit risk and liquidity risk. As a consequence, the Directors believe that the Company is well placed to manage its business risks.

The Directors therefore have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Relations with shareholders
The Company is always willing, where practicable, to discuss with its shareholders its objectives to promote a mutual understanding. Meetings with institutional shareholders are held twice a year following the announcements of the Group's interim and final results. Other meetings are held at institutional shareholders' request. To ensure that the Board, particularly the Non-Executive Directors, understands the views of the shareholders, the Company's corporate brokers provide summary feedback from the investor meetings

Corporate Information

Corporate Governance continued

that they arrange, in particular the meetings held following the interim and final results announcements. The Chairman and R J Clowes (the Senior Independent Non-Executive Director) are available to meet institutional shareholders, as well as the other Non-Executive Directors, if requested.

The Board considers the Annual Report and financial statements and the AGM to be the primary vehicles for communication with private investors. The Chairs of the Audit and Remuneration Committees will normally be present to speak at the AGM. The Chairman, being also the Chair of the Nominations Committee, will normally be present as well. The corporate website www.zotefoams.com contains further information on the Company.

Internal control

The Board has applied the Code by establishing a continuous process for identifying, evaluating and managing the significant risks the Group faces. The Board regularly reviews the process, which has been in place from the start of the year to the date of approval of this report and which is in accordance with the revised guidance on internal control published in October 2005 (the Turnbull Guidance). The Board is responsible for the Group's system of internal control and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss.

In compliance with the Code, the Board regularly reviews the effectiveness of the Group's system of internal control, as well as how it is reported to the Board. The Board's monitoring covers all controls, including financial, operational and compliance controls and risk management. It is based principally on reviewing reports from management to consider whether significant risks are identified, evaluated, managed and controlled and whether any significant weaknesses are promptly remedied and indicate a need for more extensive monitoring. The Board has also performed a specific assessment for the purpose of this Annual Report. This assessment considered all the significant aspects of internal control arising during the period covered by the report. The Audit Committee assists the Board in discharging its review responsibilities.

During the course of its review of the system of internal control, the Board had not identified nor been advised of any failings or weaknesses which it has determined to be significant. Therefore a confirmation in respect of necessary actions has not been considered appropriate.

Key elements of the Group's system of internal controls are as follows:

Control environment

The Group has an appropriate organisational structure for planning, executing, controlling and monitoring business operations in order to achieve Group objectives. Overall business objectives are set by the Board and communicated through the organisation. Lines of responsibility and delegations of authority are documented.

Risk identification

Group management is responsible for the identification and evaluation of key risks applicable to its areas of business. These risks are assessed on a continual basis and may be associated with a variety of internal or external sources including control breakdowns, disruption in information systems or the Company's commercial supply chain, competition, natural catastrophe and regulatory requirements.

Information and communication

Annual budgets are a key part of the planning process and performance against plan is actively monitored at Board level supported by quarterly forecasts. Statistics and commentary on actual operating performance are made available to all Directors monthly.

Through these mechanisms, Group performance is continually monitored, risks identified in a timely manner, their financial implications assessed, control procedures re-evaluated and corrective actions agreed and implemented.

Control procedures

The Group has implemented control procedures designed to ensure complete and accurate accounting for financial transactions and to limit the potential exposure to loss of assets or fraud. Measures taken include physical controls, segregation of duties, reviews by management, internal audit and external audit to the extent necessary to arrive at their audit opinion.

A process of control self-assessment and hierarchical reporting has been established which provides for a documented and auditable trail of accountability. These procedures are relevant across Group operations and provide for successive assurances to be given at increasingly higher levels of management and finally, to the Board. Planned corrective actions are independently monitored for timely completion.

Monitoring and corrective action

There are clear and consistent procedures in place for monitoring the system of internal financial and non-financial controls. The Audit Committee normally meets three times a year and, within its remit, reviews the effectiveness of the Group's system of internal financial controls. The Committee receives reports from External Auditors, Internal Auditors and management.

Non-financial controls are reviewed regularly by executive management who report any issues and corrective actions taken directly to the Board.

Statement of Directors' Responsibilities in Respect of the Annual Report

The Directors are responsible for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Group and Parent Company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Company and of the profit or loss of the Company and Group for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the Directors, whose names and functions are listed on pages 18 to 19 of the Annual Report confirms that, to the best of their knowledge:

- the Group financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group; and
- the Directors' Report beginning on page 20 of the Annual Report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

By order of the Board

C G Hurst
Finance Director

Financial Statements

Independent Auditor's Report
to the members of Zotefoams plc

We have audited the financial statements of Zotefoams plc for the year ended 31 December 2012 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated and Parent Company Statements of Financial Position, the Consolidated and Parent Company Cash Flow Statements, the Consolidated and Parent Company Statements of Changes in Equity and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the Parent Company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

Respective responsibilities of Directors and Auditor
As explained more fully in the Statement of Directors' Responsibilities set out on page 35, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the financial statements
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's and the parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements
In our opinion:
- the financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2012 and of the Group's profit and Group's and Parent Company's cash flows for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Companies Act 2006
In our opinion:
- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006;
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the information given in the Corporate Governance Statement set out on pages 32 to 34 with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements.

Matters on which we are required to report by exception
We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:
- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit; or
- a corporate governance statement has not been prepared by the Parent Company.

Under the Listing Rules we are required to review:
- the Directors' statement, set out on page 35, in relation to going concern;
- the parts of the Corporate Governance Statement relating to the Company's compliance with the nine provisions of the UK Corporate Governance Code specified for our review; and
- certain elements of the report to shareholders by the Board on directors' remuneration.

Stephen Wootten (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Gatwick
4 March 2013

Financial Statements

Consolidated Income Statement

for the year ended 31 December 2012

	Note	2012 £000	2011 £000
Revenue	2	**47,188**	44,208
Cost of sales		**(33,521)**	(31,624)
Gross profit		**13,667**	12,584
Distribution costs		**(3,308)**	(3,114)
Administrative expenses		**(4,329)**	(3,880)
Operating profit		**6,030**	5,590
Financial income	5	**1,029**	1,135
Finance costs	5	**(1,133)**	(1,260)
Profit before tax		**5,926**	5,465
Taxation	6	**(1,198)**	(911)
Profit for the year		**4,728**	4,554
Attributable to:			
Equity holders of the Parent		**4,728**	4,497
Non-controlling interest		**–**	57
		4,728	4,554
Earnings per share Basic (p)	7	**12.1**	11.8
Diluted (p)	7	**11.9**	11.5

Notes on pages 46 to 70 form part of these financial statements.

Financial Statements

Consolidated Statement of Comprehensive Income

for the year ended 31 December 2012

	2012 £000	2011 £000
Profit for the year	**4,728**	4,554
Other comprehensive income		
Foreign exchange translation differences on investment in foreign subsidiaries	**(445)**	(10)
Effective portion of changes in fair value of cash flow hedges net of recycling	**13**	18
Actuarial losses on defined benefit schemes	**(2,814)**	(1,705)
Effect of revaluation of defined benefit scheme under CPI	**–**	1,140
Tax relating to effective portion of changes in fair value of cash flow hedges net of recycling	**(4)**	(4)
Tax relating to actuarial losses on defined benefit schemes	**648**	426
Tax relating to effect of revaluation of defined benefit scheme under CPI	**–**	(285)
Other comprehensive expenditure for the period, net of tax	**(2,602)**	(420)
Total comprehensive income for the year	**2,126**	4,134
Attributable to:		
Equity holders of the Parent	**2,126**	4,018
Non-controlling interest	**–**	116
Total comprehensive income for the year	**2,126**	4,134

Notes on pages 46 to 70 form part of these financial statements.

Financial Statements

Consolidated Statement of Financial Position

as at 31 December 2012

	Note	2012 £000	2011 £000
Non-current assets			
Property, plant and equipment	9	**25,869**	25,433
Intangible assets	10	**5,248**	5,729
Deferred tax assets	17	**460**	490
Total non-current assets		**31,577**	31,652
Current assets			
Inventories	12	**6,640**	5,927
Trade and other receivables	13	**11,612**	10,533
Cash and cash equivalents	14	**3,698**	3,403
Total current assets		**21,950**	19,863
Total assets		**53,527**	51,515
Current liabilities			
Interest-bearing loans and borrowings	16	**(1,360)**	(660)
Tax payable		**(801)**	(787)
Trade and other payables	15	**(4,921)**	(7,887)
Total current liabilities		**(7,082)**	(9,334)
Non-current liabilities			
Interest-bearing loans and borrowings	16	**(2,962)**	(820)
Employee benefits	21	**(7,172)**	(4,944)
Deferred tax liabilities	17	**(621)**	(1,165)
Total non-current liabilities		**(10,755)**	(6,929)
Total liabilities		**(17,837)**	(16,263)
Total net assets		**35,690**	35,252
Equity			
Issued share capital	18	**1,992**	1,992
Own shares held		**(36)**	(58)
Share premium		**16,090**	16,090
Capital redemption reserve		**15**	15
Translation reserve		**345**	790
Hedging reserve		**(38)**	(51)
Retained earnings		**17,322**	16,474
Total equity attributable to the equity holders of the Parent		**35,690**	35,252
Non-controlling interest		**–**	–
Total equity		**35,690**	35,252

Notes on pages 46 to 70 form part of these financial statements.

These financial statements were approved by the Board of Directors on 4 March 2013 and signed on its behalf by:

C G Hurst
Finance Director

Company number: 2714645

Financial Statements

Company Statement of Financial Position
as at 31 December 2012

	Note	2012 £000	2011 £000
Non-current assets			
Property, plant and equipment	9	**22,227**	21,098
Intangible assets	10	**–**	–
Investment in subsidiaries	11	**6,352**	6,352
Total non-current assets		**28,579**	27,450
Current assets			
Inventories	12	**5,447**	4,713
Trade and other receivables	13	**12,061**	11,479
Cash and cash equivalents	14	**3,178**	1,611
Total current assets		**20,686**	17,803
Total assets		**49,265**	45,253
Current liabilities			
Interest-bearing loans and borrowings	16	**(1,360)**	(982)
Tax payable		**(801)**	(782)
Trade and other payables	15	**(4,434)**	(5,141)
Total current liabilities		**(6,595)**	(6,905)
Non-current liabilities			
Interest-bearing loans and borrowings	16	**(2,962)**	(820)
Employee benefits	21	**(7,172)**	(4,944)
Deferred tax liabilities	17	**(621)**	(1,165)
Total non-current liabilities		**(10,755)**	(6,929)
Total liabilities		**(17,350)**	(13,834)
Total net assets		**31,915**	31,419
Equity			
Issued share capital	18	**1,992**	1,992
Own shares held		**(36)**	(58)
Share premium		**16,090**	16,090
Capital redemption reserve		**15**	15
Hedging reserve		**(38)**	(51)
Retained earnings		**13,892**	13,431
Total equity attributable to the equity holders of the Company		**31,915**	31,419

Notes on pages 46 to 70 form part of these financial statements.

These financial statements were approved by the Board of Directors on 4 March 2013 and signed on its behalf by:

C G Hurst
Finance Director

Company number: 2714645

Financial Statements

Consolidated Statement of Cash Flows
for the year ended 31 December 2012

	Note	2012 £000	2011 £000
Cash flows from operating activities			
Profit for the year		**4,728**	4,554
Adjustments for:			
Depreciation, amortisation and impairment		**3,312**	3,213
Financial income		**(1,029)**	(1,135)
Finance costs		**1,133**	1,260
Equity-settled share-based payments		**161**	125
Taxation		**1,198**	911
Operating profit before changes in working capital and provisions		**9,503**	8,928
Increase in trade and other receivables		**(1,165)**	(1,040)
Increase in inventories		**(746)**	(1,778)
(Decrease)/increase in trade and other payables		**(644)**	634
Employee benefit contributions		**(660)**	(660)
Cash generated from operations		**6,288**	6,084
Interest paid		**(38)**	(52)
Tax paid		**(992)**	(1,053)
Net cash from operating activities		**5,258**	4,979
Interest received		**2**	5
Acquisition of MuCell		**(2,231)**	(2,179)
Acquisition of intangible assets		**(63)**	(311)
Acquisition of property, plant and equipment		**(3,683)**	(2,744)
Net cash used in investing activities		**(5,975)**	(5,229)
Proceeds from issue of share capital		**46**	2,376
Repurchase of own shares		**–**	(114)
Repayment of borrowings		**(660)**	(660)
New loans taken out		**3,500**	–
Distribution by subsidiary to non-controlling interest		**–**	(25)
Dividends paid		**(1,956)**	(1,835)
Net cash generated/(used) in financing activities		**930**	(258)
Net increase/(decrease) in cash and cash equivalents		**213**	(508)
Cash and cash equivalents at 1 January		**3,403**	4,005
Effect of exchange rate fluctuations on cash held		**82**	(94)
Cash and cash equivalents at 31 December	14	**3,698**	3,403

Cash and cash equivalents comprise cash at bank and short-term highly liquid investments with a maturity date of less than three months.

Notes on pages 46 to 70 form part of these financial statements.

Financial Statements

Company Statement of Cash Flows
for the year ended 31 December 2012

	Note	2012 £000	2011 £000
Cash flows from operating activities			
Profit for the year		**4,341**	3,885
Adjustments for:			
Depreciation, amortisation and impairment		**2,425**	2,482
Foreign exchange losses		**–**	105
Loss on disposal of plant and equipment		**66**	–
Financial income		**(1,028)**	(1,163)
Finance costs		**1,133**	1,285
Equity-settled share-based payments		**161**	125
Taxation		**1,180**	1,012
Operating profit before changes in working capital and provisions		**8,278**	7,731
Increase in trade and other receivables		**(575)**	(2,480)
Increase in inventories		**(734)**	(1,541)
(Decrease)/increase in trade and other payables		**(660)**	562
Employee benefit contributions		**(660)**	(660)
Cash generated from operations		**5,649**	3,612
Interest paid		**(38)**	(77)
Tax paid		**(1,000)**	(1,008)
Net cash flow from operating activities		**4,611**	2,527
Interest received		**2**	33
Investment in subsidiary		**–**	(2,489)
Repayment of intercompany loan		**–**	4,058
Acquisition of property, plant and equipment		**(3,656)**	(2,524)
Net cash used in investing activities		**(3,654)**	(922)
Proceeds from issue of share capital		**46**	2,376
Purchase of own shares		**–**	(114)
Intercompany loan paid		**(322)**	(3,291)
Intercompany loan received		**–**	322
Repayment of borrowings		**(660)**	(660)
New loans taken out		**3,500**	–
Dividends paid		**(1,956)**	(1,835)
Net cash generated/(used) in financing activities		**608**	(3,202)
Net increase/(decrease) in cash and cash equivalents		**1,565**	(1,597)
Cash and cash equivalents at 1 January		**1,611**	3,287
Effect of exchange fluctuations on cash held		**2**	(79)
Cash and cash equivalents at 31 December	14	**3,178**	1,611

Notes on pages 46 to 70 form part of these financial statements.

Financial Statements

Consolidated Statement of Changes in Equity

for the year ended 31 December 2012

	Note	Share capital £000	Own shares held £000	Share premium £000	Capital redemption reserve £000	Translation reserve £000	Hedging reserve £000	Retained earnings £000	Attributable to owners of the Parent £000	Non-controlling interest £000	Total equity £000
Balance at 1 January 2011		1,915	(69)	13,941	15	859	(69)	14,155	30,747	4,267	35,014
Profit for year		–	–	–	–	–	–	4,497	4,497	57	4,554
Other comprehensive income:											
Foreign exchange translation differences on investment in foreign subsidiaries		–	–	–	–	(69)	–	–	(69)	59	(10)
Effective portion of changes in fair value of cash flow hedges net of recycling		–	–	–	–	–	18	–	18	–	18
Actuarial losses on defined benefit scheme		–	–	–	–	–	–	(1,705)	(1,705)	–	(1,705)
Effect of revaluation of defined benefit scheme under CPI		–	–	–	–	–	–	1,140	1,140	–	1,140
Tax relating to effective portion of changes in fair value of cash flow hedges net of recycling		–	–	–	–	–	–	(4)	(4)	–	(4)
Tax relating to actuarial losses on defined benefit scheme		–	–	–	–	–	–	426	426	–	426
Tax relating to effect of revaluation of defined benefit scheme under CPI		–	–	–	–	–	–	(285)	(285)	–	(285)
Total other comprehensive (expenditure)/ income		–	–	–	–	(69)	18	(428)	(479)	59	(420)
Total comprehensive (expenditure)/income for the year		–	–	–	–	(69)	18	4,069	4,018	116	4,134
Transactions with owners of the Parent:											
Shares issued/options exercised		77	15	2,149	–	–	–	135	2,376	–	2,376
Shares acquired		–	(4)	–	–	–	–	(110)	(114)	–	(114)
Equity-settled share-based payment transactions net of tax		–	–	–	–	–	–	60	60	–	60
Acquisition of non-controlling interest		–	–	–	–	–	–	–	–	(4,358)	(4,358)
Dividends	7	–	–	–	–	–	–	(1,835)	(1,835)	(25)	(1,860)
Total transactions with owners of the Parent		77	11	2,149	–	–	–	(1,750)	487	(4,383)	(3,896)
Balance at 31 December 2011 and 1 January 2012		1,992	(58)	16,090	15	790	(51)	16,474	35,252	–	35,252
Profit for year		–	–	–	–	–	–	4,728	4,728	–	4,728

Financial Statements

Consolidated Statement of Changes in Equity continued

for the year ended 31 December 2012

	Note	Share capital £000	Own shares held £000	Share premium £000	Capital redemption reserve £000	Translation reserve £000	Hedging reserve £000	Retained earnings £000	Attributable to owners of the Parent £000	Non-controlling interest £000	Total equity £000
Other comprehensive income:											
Foreign exchange translation differences on investment in foreign subsidiaries		–	–	–	–	(445)	–	–	(445)	–	(445)
Effective portion of changes in fair value of cash flow hedges net of recycling		–	–	–	–	–	13	–	13	–	13
Actuarial losses on defined benefit scheme		–	–	–	–	–	–	(2,814)	(2,814)	–	(2,814)
Tax relating to effective portion of changes in fair value of cash flow hedges net of recycling		–	–	–	–	–	–	(4)	(4)	–	(4)
Tax relating to actuarial losses on defined benefit scheme		–	–	–	–	–	–	648	648	–	648
Total other comprehensive (expenditure)/ income		–	–	–	–	(445)	13	(2,170)	(2,602)	–	(2,602)
Total comprehensive (expenditure)/ income for the year		–	–	–	–	(445)	13	2,558	2,126	–	2,126
Transactions with owners of the Parent:											
Shares issued/options exercised		–	22	–	–	–	–	24	46	–	46
Equity-settled share-based payment transactions net of tax		–	–	–	–	–	–	222	222	–	222
Dividends	7	–	–	–	–	–	–	(1,956)	(1,956)	–	(1,956)
Total transactions with owners of the Parent		–	22	–	–	–	–	(1,710)	(1,688)	–	(1,688)
Balance at 31 December 2012		**1,992**	**(36)**	**16,090**	**15**	**345**	**(38)**	**17,322**	**35,690**	**–**	**35,690**

The aggregate current and deferred tax relating to items that are credited to equity is £705,000 (2011: a credit of £70,000).

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Company Statement of Changes in Equity

for the year ended 31 December 2012

	Note	Share capital £000	Own shares held £000	Share premium £000	Capital redemption reserve £000	Hedging reserve £000	Retained earnings £000	Total equity £000
Balance at 1 January 2011		1,915	(69)	13,941	15	(69)	11,724	27,457
Profit for year		–	–	–	–	–	3,885	3,885
Other comprehensive income:								
Effective portion of changes in fair value of cash flow hedges net of recycling		–	–	–	–	18	–	18
Actuarial losses on defined benefit scheme		–	–	–	–	–	(1,705)	(1,705)
Effect of revaluation of defined benefit scheme under CPI		–	–	–	–	–	1,140	1,140
Tax relating to effective portion of changes in fair value of cash flow hedges net of recycling		–	–	–	–	–	(4)	(4)
Tax relating to actuarial losses on defined benefit scheme		–	–	–	–	–	426	426
Tax relating to effect of revaluation of defined benefit scheme under CPI		–	–	–	–	–	(285)	(285)
Total other comprehensive income/(expenditure)		–	–	–	–	18	(428)	(410)
Total comprehensive income/(expenditure) for the year		–	–	–	–	18	3,457	3,475
Transactions with owners of the Parent:								
Shares issued/options exercised		77	15	2,149	–	–	135	2,376
Shares acquired		–	(4)	–	–	–	(110)	(114)
Equity-settled share-based payment transactions net of tax		–	–	–	–	–	60	60
Dividends	7	–	–	–	–	–	(1,835)	(1,835)
Total transactions with owners of the Parent		77	11	2,149	–	–	(1,750)	487
Balance at 31 December 2011 and 1 January 2012		1,992	(58)	16,090	15	(51)	13,431	31,419
Profit for year		–	–	–	–	–	4,341	4,341
Other comprehensive income:								
Effective portion of changes in fair value of cash flow hedges net of recycling		–	–	–	–	13	–	13
Actuarial losses on defined benefit scheme		–	–	–	–	–	(2,814)	(2,814)
Tax relating to effective portion of changes in fair value of cash flow hedges net of recycling		–	–	–	–	–	(4)	(4)
Tax relating to actuarial losses on defined benefit scheme		–	–	–	–	–	648	648
Total other comprehensive income/(expenditure)		–	–	–	–	13	(2,170)	(2,157)
Total comprehensive income/(expenditure) for the year		–	–	–	–	13	2,171	2,184
Transactions with owners of the Parent:								
Shares issued/options exercised		–	22	–	–	–	24	46
Equity-settled share-based payment transactions net of tax		–	–	–	–	–	222	222
Dividends	7	–	–	–	–	–	(1,956)	(1,956)
Total transactions with owners of the Parent		–	22	–	–	–	(1,710)	(1,688)
Balance at 31 December 2012		**1,992**	**(36)**	**16,090**	**15**	**(38)**	**13,892**	**31,915**

The aggregate current and deferred tax relating to items that are credited to equity is £705,000 (2011: a credit of £70,000).

Financial Statements
Notes

1. Accounting policies
Zotefoams plc (the 'Company') is a Company incorporated in Great Britain.

The Group financial statements consolidate those of the Company and its subsidiaries (together referred to as the 'Group'). The Parent Company financial statements present information about the Company as a separate entity and not about its Group.

Both Parent Company financial statements and the Group financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ('Adopted IFRS'). On publishing the Parent Company financial statements here together with the Group financial statements the Company is taking advantage of the exemption in Section 408 of the Companies Act 2006 not to present its individual Income Statement and related notes that form part of these approved financial statements.

These financial statements were approved by the Board on 4 March 2013.

Judgements made by the Directors, in the application of these accounting policies that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year, are discussed in note 24.

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business Review on pages 12 to 15 and the section entitled Principal Risks and Uncertainties on page 16. This also describes the financial position of the Company, its cash flows and liquidity position. In addition, note 19 to the financial statements includes the Company's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities, borrowing facilities, and its exposure to credit risk and liquidity risk. As a consequence, the Directors believe that the Company is well placed to manage its business risks.

The Directors therefore have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

The principal accounting policies adopted in the preparation of the Group's consolidated financial statements and the Company's individual financial statements are set out below. The policies have been consistently applied to all of the statements presented.

a) Measurement convention
The financial statements are prepared on the historical cost basis with the following exceptions:
- derivative financial instruments are stated at their fair value

b) Basis of consolidation
i) Subsidiaries
Subsidiaries are entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

ii) Transactions eliminated on consolidation
Intra-group balances and transactions, including any unrealised gains and losses or income and expenses arising from such transactions, are eliminated in preparing the financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

iii) Accounting for business combinations
Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the Group takes into consideration potential voting rights that currently are exercisable.

For acquisitions on or after 1 January 2010, the Group measures goodwill at the acquisition date as:
- the fair value of the consideration transferred; plus
- the recognised amount of any non-controlling interests in the acquiree; plus
- if the business combination is achieved in stages, the fair value remeasured at acquisition date of the existing equity interest in the acquiree; less
- the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

When the excess is negative, a bargain purchase gain is recognised immediately in profit or loss. The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss. Costs related to the acquisition, other than those associated with the issue of debt or equity securities, that the Group incurs in connection with a business combination are expensed as incurred.

Any contingent consideration payable is recognised at fair value at the acquisition date. If the contingent consideration is classified as equity, it is not re-measured and settlement is accounted for within equity. Otherwise, subsequent changes to the fair value of the contingent consideration are recognised in profit or loss.

1. Accounting policies continued

When share-based payment awards (replacement awards) are required to be exchanged for awards held by the acquiree employees (acquiree awards) and relate to past services, then all or a portion of the amount of the acquirer replacement awards are included in measuring the consideration transferred in the business combination. This determination is based on the market-based value of the replacement awards compared with the market-based value of the acquiree awards and the extent to which the replacement awards relate to past and/or future service.

Acquisitions and disposals of non-controlling interests

Acquisitions and disposals of non-controlling interests that do not result in a change of control are accounted for as transactions with owners in their capacity as owners and therefore no goodwill is recognised as a result of such transactions. The adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary. Any difference between the price paid or received and the amount by which non-controlling interests are adjusted is recognised directly in equity and attributed to the owners of the Parent.

Prior to the adoption of IAS27 (2008), goodwill was recognised on the acquisition of non-controlling interests in a subsidiary, which represented the excess of the cost of the additional investment over the carrying amount of the interest in the net assets acquired at the date of the transaction.

c) Foreign currency

i) Foreign currency transactions

Transactions in foreign currencies are translated at the foreign exchange rate prevailing at the time of the transaction.

Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to sterling at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the Income Statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

ii) Financial statements of foreign operations

The assets and liabilities of foreign operations, including fair value adjustments arising on consolidation, are translated to sterling at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated to sterling at the average rate of exchange ruling during the year where this rate approximates to the foreign exchange rates ruling at the dates of the transactions.

Exchange differences arising from this translation of foreign operations since 1 January 2004 are taken directly to translation reserve. They are released into the Income Statement upon disposal.

d) Derivative financial instruments

The Group uses derivative financial instruments to hedge its exposure to foreign exchange risks arising from operational, financing and investment activities. In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, derivative financial instruments are stated at fair value. The gain or loss on re-measurement is recognised immediately in the Income Statement. Where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged (see accounting policy (e)).

The fair value of forward exchange contracts is their quoted market price at the balance sheet date, being the present value of the quoted forward price.

e) Cash flow hedging

When a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or of a highly probable forecasted transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in equity. If a hedge of a forecasted transaction subsequently results in the recognition of a financial asset or a financial liability, then the associated gains or losses that were recognised directly in equity are reclassified into the Income Statement in the same period or periods during which the asset acquired or liability assumed affects the Income Statement.

The ineffective part of any gain or loss is recognised immediately in the Income Statement.

When a hedging instrument expires or is sold, terminated or exercised, or the entity revokes designation of the hedge relationship but the hedged forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, then the cumulative unrealised gain or loss recognised in equity is recognised immediately in the Income Statement.

f) Investments in subsidiaries

Investments in subsidiaries are stated at cost less provision for impairment.

Financial Statements

Notes continued

1. Accounting policies continued

g) Property, plant and equipment

i) Owned assets
Items of property, plant and equipment are stated at cost or deemed cost less accumulated depreciation and impairment losses (see accounting policy (l)).

When parts of an item of property, plant and equipment have different useful lives, those components are accounted for as separate items of property, plant and equipment.

The cost of assets under construction includes the cost of materials and direct labour, and any other costs directly attributable to bringing the asset to a working condition for its intended use.

ii) Leased assets
Leases in terms of which the Group assumes substantially all of the risks and rewards of ownership are classified as finance leases. Lease payments are accounted for as described in accounting policy (r).

iii) Depreciation
Depreciation is charged to the Income Statement on a straight line basis over the estimated useful lives of each part of the item of property, plant and equipment. Land is not depreciated. The estimated useful lives are as follows:

Buildings	20 years
Plant and equipment	5–15 years
Fixtures and fittings	3–5 years

Assets under construction are not depreciated until after the end of the quarter that the asset is in the location and condition necessary for its intended use.

h) Intangible assets

i) Research and development
Expenditure on research activities undertaken with the prospect of gaining new scientific or technical knowledge and understanding is recognised in the Income Statement as an expense as incurred. Expenditure on development activities, whereby research findings are applied to a plan or design for the production of new or substantially improved products and processes, is capitalised if the product or process is technically and commercially feasible and the Group has sufficient resources to complete development. No research and development expenditure has been capitalised to date.

ii) Goodwill
Goodwill represents the excess of the cost of acquisition over the fair value of the Group's interest in the identifiable assets, liabilities and contingent liabilities acquired in a business combination. Goodwill is stated at the amount recognised on acquisition date less any accumulated impairment losses.

iii) Other intangible assets
Intangible assets acquired from a business combination are capitalised at fair value as at the date of acquisition and amortised over their estimated useful economic life. Their carrying value is the fair value at acquisition less cumulative amortisation and any impairment. An intangible asset acquired as part of a business combination is recognised outside goodwill if the asset is separable or arises from contractual or other legal rights and its fair value can be measured reliably. The estimated useful lives of the intangible assets are as follows:

Marketing related	5–15 years
Customer related	2–10 years
Technology related	5–20 years

Amortisation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

Other intangible assets including patents that are purchased by the Group and have finite useful lives are measured at cost less accumulated amortisation and accumulated impairment losses. The cost is the purchase price of the asset. Amortisation is charged to the Income Statement on a straight line basis over the estimated useful lives of the assets. Expenditure on internally generated goodwill and brands is recognised in the Income Statement as an expense as incurred.

i) Trade and other receivables

Trade and other receivables are stated at their nominal amounts less impairment losses (see accounting policy (l)).

j) Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

In determining the cost of raw materials, consumables and goods purchased for resale, the weighted average purchase price is used. For work in progress and finished goods manufactured by the Group, cost is taken as production cost, which includes an appropriate proportion of attributable overheads.

1. Accounting policies continued

k) Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits with an original maturity of three months or less. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purposes of the Statement of Cash Flows.

l) Impairment

The carrying amounts of the Group's assets, other than inventories (see accounting policy (j)), employee benefits (see accounting policy (o)) and deferred tax assets (see accounting policy (s)), are reviewed at each balance sheet date where there is an indication that the asset may be impaired. If any such indication exists, the asset's recoverable amount is estimated (see below).

For goodwill, and intangible assets that have indefinite useful lives or that are not yet available for use, the recoverable amount is estimated each year at the same time. An impairment loss is recognised if the carrying amount of an asset or its related cash-generating unit (CGU) exceeds its estimated recoverable amount.

i) Calculation of recoverable amount

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGUs. Subject to an operating segment ceiling test, for the purposes of goodwill impairment testing, CGUs to which goodwill has been allocated are aggregated so that the level at which impairment testing is performed reflects the lowest level at which goodwill is monitored for internal reporting purposes. Goodwill acquired in a business combination is allocated to groups of CGUs that are expected to benefit from the synergies of the combination.

The Group's corporate assets do not generate separate cash inflows and are utilised by more than one CGU. Corporate assets are allocated to CGUs on a reasonable and consistent basis and tested for impairment as part of the testing of the CGU to which the corporate asset is allocated.

ii) Impairment losses

Impairment losses are recognised in the Income Statement. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU (group of CGUs), and then to reduce the carrying amounts of the other assets in the CGU (group of CGUs) on a pro rata basis.

iii) Reversals of impairment

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

m) Dividends

Final dividends are recognised as a liability in the period in which they are approved. Interim dividends are recognised when they are paid.

n) Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any differences between cost and redemption values being recognised in the Income Statement over the period of the borrowings on an effective interest basis where material.

o) Employee benefits

i) Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in the Income Statement as incurred.

ii) Defined benefits plans

The Group's net obligation in respect of defined benefit post employment plans, including pension plans, is calculated separately for each plan by estimating the amount of future benefit that the employees have earned in return for their service in the current and prior periods. That benefit is discounted to determine its present value, and the fair value of any plan assets is deducted. The discount rate is the yield at the balance sheet date on AA credit rated bonds that have maturity dates approximating the terms of the Group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method.

The Group recognises all actuarial gains and losses that arise through the Statement of Comprehensive Income.

iii) Share-based payment transactions

The share option programme allows Group employees to acquire shares of the Company. The fair value of options granted is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employee becomes unconditionally entitled to the options. The fair value of the options granted before 2006 were measured using a Monte Carlo simulation method. Options granted since 1 January 2006 are valued using a Black-Scholes model. Fair value measurements take into account the terms and conditions upon which the options were granted.

Financial Statements

Notes continued

1. Accounting policies continued

iv) Own shares held by Employee Benefit Trust
Transactions of the Company-sponsored EBT are treated as being those of the Company and are therefore reflected in the Parent Company and Group financial statements. In particular, the trust's purchases and sales of shares in the Company are debited and credited directly to equity.

p) Trade and other payables
Trade and other payables are stated at cost.

q) Revenue
Revenue from the sale of goods is recognised in the Income Statement at the point of despatch when significant risks and rewards of ownership are deemed to have been transferred to the buyer. MuCell Extrusion LLC recognises licence revenue upon transfer of the MuCell® technology provided that no significant Company obligations remain, the licence amount is determinable, and the collection of the related receivable is probable. Royalty income is based on the terms of the licence agreements and is recorded when amounts are determinable and collection of the related receivable is probable. Revenue from equipment sales is recognised upon either shipment or delivery as specified in the contract terms. Revenue from consulting services is recognised either as the services are performed or upon the achievement of a specific milestone. Payments received under these arrangements prior to the completion of the related work are recorded as deferred income.

r) Expenses
i) Operating lease payments
Payments made under operating leases are recognised in the Income Statement on a straight line basis over the term of the lease. Lease incentives received are recognised in the Income Statement as an integral part of the total lease expenses.

ii) Finance lease payments
The finance charge, where material, is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

s) Taxation
Tax on the Income Statement for the periods presented comprises current and deferred tax. Tax is recognised in the Income Statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year and any adjustments to the tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

The following temporary differences are not provided for: the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is more likely than not that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Additional tax that arises from the distribution of dividends is recognised at the same time as the liability to pay the related dividend.

t) New and amended standards adopted by the Group
There are no IFRSs or IFRIC interpretations that are effective for the first time for the financial year beginning on or after 1 January 2012 that would be expected to have a material impact on the Group.

u) New standards and interpretations not yet adopted
A number of new standards and amendments to standards and interpretations are effective for annual periods beginning after 1 January 2013, and have not been applied in preparing these consolidated financial statements. None of these is expected to have a significant effect on the consolidated financial statements of the Group, except the following:

IAS 19, 'Employee benefits', was amended in June 2011. The impact on the Group will be as follows: to recognise immediately all past service costs; and to replace interest cost and expected return on plan assets with a net interest amount that is calculated by applying the discount rate to the net defined benefit liability (asset).

The Group is yet to assess the full impact of the amendments.

2. Segment reporting

The Group manufactures and sells high-performance foams and licenses related technology for specialist markets worldwide. Zotefoams' activities are categorised as follows:

- Polyolefins: these foams are made from olefinic homopolymer and copolymer resin. The most common resin used is polyethylene. Included in this segment are microZOTE® foams made using polyolefin resins.
- High-Performance Polymers ('HPP'): these foams exhibit high-performance on certain key properties, such as improved chemical, flammability or temperature performance, due to the resins on which they are based. Turnover in the segment is currently mainly derived from our ZOTEK® F foams and T-Tubes® insulation both made from PVDF fluoropolymer. Other products either commercially launched or being assessed in development include foams made from polyamide (nylon) and Pebax®.
- MuCell Extrusion LLC ('MEL'): licenses microcellular foam technology and sells related machinery.

There are no transactions between reportable segments apart from the sale of minor equipment and a $50,000 licence fee from MEL to microZOTE®, within our polyolefin segment.

We have reclassified microZOTE® closed-cell roll foams made from polyolefin resins from our HPP segment to our Polyolefins segment. This reflects management reporting lines with polyolefin microZOTE® products now being managed by our Polyolefin management team. The segment results for microZOTE® are as follows:

	Year ended 31 December 2012 £000	Year ended 31 December 2011 £000
Revenue	55	33
Depreciation	(148)	(141)
Segment loss	(477)	(532)

	Polyolefins		HPP		MEL		Eliminations		Consolidated	
	2012 £000	2011 Restated £000	**2012 £000**	2011 Restated £000	**2012 £000**	2011 £000	**2012 £000**	2011 £000	**2012 £000**	2011 £000
Revenue	**42,295**	40,531	**3,595**	2,380	**1,330**	1,329	**(32)**	(32)	**47,188**	44,208
Segment profit/(loss)	**6,434**	5,682	**(82)**	(175)	**(322)**	143	**–**	–	**6,030**	5,650
Acquisition costs	**–**	–	**–**	–	**–**	–	**–**	–	**–**	(60)
Operating profit	**–**		**–**	–	**–**	–	**–**	–	**6,030**	5,590
Net financing costs	**–**		**–**	–	**–**	–	**–**	–	**(104)**	(125)
Taxation	**–**		**–**	–	**–**	–	**–**	–	**(1,198)**	(911)
Profit for the year	**–**		**–**	–	**–**	–	**–**	–	**4,728**	4,554
Segment assets	**41,465**	40,927	**5,398**	3,496	**6,204**	6,602	**–**	–	**53,067**	51,025
Unallocated assets	**–**	–	**–**	–	**–**	–	**–**	–	**460**	490
Total assets									**53,527**	51,515
Segment liabilities	**(16,017)**	(11,302)	**(194)**	(581)	**(204)**	(2,428)	**–**	–	**(16,415)**	(14,311)
Unallocated liabilities	**–**	–	**–**	–	**–**	–	**–**	–	**(1,422)**	(1,952)
Total liabilities									**(17,837)**	(16,263)
Depreciation	**2,833**	2,796	**146**	115	**33**	26	**–**	–	**3,012**	2,937
Amortisation	**–**	–	**–**	–	**300**	276	**–**	–	**300**	276
Capital expenditure:										
Tangible fixed assets	**3,522**	2,527	**158**	101	**3**	116	**–**	–	**3,683**	2,744
Intangible fixed assets	**–**	–	**–**	–	**63**	311	**–**	–	**63**	311

Unallocated assets and liabilities are made up of corporation tax and deferred tax assets and liabilities.

Financial Statements

Notes continued

2. Segment reporting continued

Geographical segments

Polyolefins, HPP and MEL are managed on a worldwide basis but operate from UK and US locations. In presenting information on the basis of geographical segments, segmental revenue is based on the geographical location of customers. Segment assets are based on the geographical location of assets.

	United Kingdom £000	Europe £000	North America £000	Rest of the world £000	Total £000
For the year ended 31 December 2012					
Revenue from external customers	**9,949**	**21,063**	**12,877**	**3,299**	**47,188**
Non-current assets	**22,227**	**–**	**8,890**	**–**	**31,117**
Capital expenditure	**3,656**	**–**	**27**	**–**	**3,683**
For the year ended 31 December 2011					
Revenue from external customers	9,185	21,288	10,886	2,849	44,208
Non-current assets	21,098	–	10,064	–	31,162
Capital expenditure	2,492	–	252	–	2,744

Non-current assets do not include financial instruments, deferred tax assets or post-employment assets.

Major customer

Revenues from one customer of the Group represents approximately £6,522k (2011: £5,843k) of the Group's total revenues.

3. Expenses and auditors' remuneration

	2012 £000	2011 £000
Included in profit for the year are:		
Operating lease charges	**143**	92
Amortisation	**300**	276
Depreciation	**3,012**	2,937
Research and development costs expensed	**869**	897
Net exchange losses/(gains)	**360**	(53)
Auditors' remuneration:		
Group – audit of these financial statements	**70**	83
– fees receivable by the auditors and their associates in respect of other services:		
– other services pursuant with legislation	**15**	40
– audit work relating to subsidiaries	**10**	14
– other services relating to taxation	**–**	36
– other services relating to acquisition of associate	**–**	7
	95	180

4. Staff numbers and expenses

The average number of people employed by the Group and Company (including Directors) during the year, analysed by category, was as follows:

	Number of employees			
	Group		Company	
	2012	2011	**2012**	2011
Production	**142**	130	**134**	123
Maintenance	**16**	18	**14**	15
Distribution and marketing	**48**	49	**38**	40
Administration and technical	**89**	76	**74**	64
	295	273	**260**	242

4. Staff numbers and expenses continued

The aggregate payroll costs of these persons were as follows:

	Group		Company	
	2012 £000	2011 £000	**2012 £000**	2011 £000
Wages and salaries	**9,909**	8,574	**8,382**	7,215
Social security costs	**1,084**	978	**899**	815
Share-based payments	**161**	125	**143**	125
Other pension costs	**641**	602	**593**	555
	11,795	10,279	**10,017**	8,710

Details of individual Directors' emoluments, pension costs and share options are dealt with on pages 23 to 27 in the Directors' Remuneration Report.

5. Finance income and costs

Financial income

	2012 £000	2011 £000
Interest on bank deposits	**3**	5
Expected return on assets of defined benefit pension fund	**1,026**	1,130
	1,029	1,135

Finance costs

	2012 £000	2011 £000
On bank loans and overdrafts	**33**	50
Interest on defined benefit pension obligation	**1,100**	1,210
	1,133	1,260

6. Taxation

	Note	**2012 £000**	2011 £000
UK corporation tax		**1,112**	1,153
Overseas taxation		**(13)**	37
Adjustment to prior year UK tax charge		**(92)**	(59)
Current taxation		**1,007**	1,131
Deferred taxation	17	**191**	(220)
Total tax charge		**1,198**	911

Factors affecting the tax charge

The tax charge for the year is lower (2011: lower) than the standard rate of corporation tax in the UK of 24.5% (2011: 26.5%). The differences are explained below:

	2012 £000	2011 £000
Tax reconciliation		
Profit before tax	**5,926**	5,465
Tax at 24.5% (2011: 26.5%)	**1,452**	1,448
Effects of:		
Research and development tax credits and other allowances less expenses not deductible for tax purposes	**13**	(155)
Overseas earnings and effect of US tax losses	**(81)**	(225)
Change in deferred tax rate to 23%	**(94)**	(98)
Adjustments to UK corporation tax charge in respect of previous periods	**(92)**	(59)
Total tax charge	**1,198**	911

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7. Dividends and earnings per share

	2012 £000	2011 £000
Final dividend prior year of 3.30p (2010: 3.15p) net per 5.0p ordinary share	**1,291**	1,216
Interim dividend of 1.7p (2011: 1.6p) net per 5.0p ordinary share	**665**	619
Dividends paid during the year	**1,956**	1,835

The proposed final dividend for the year ended 31 December 2012 of 3.50p per share (2011: 3.30p) is subject to approval by shareholders at the AGM and has not been recognised as a liability in these financial statements. The proposed dividend would amount to £1,394,000 if paid to all the shares in issue.

Earnings per ordinary share

Earnings per ordinary share is calculated by dividing profit after tax attributable to equity holders of the Parent Company of £4,728,000 (2011: £4,497,000) by the weighted average number of shares in issue during the year excluding own shares held by employee trusts which are administered by independent trustees. The number of shares held in the trust at 31 December 2012 was 719,262 (2011: 1,160,954). Distribution of shares from the trust is at the discretion of the trustees. Diluted earnings per ordinary share adjusts for the potential dilutive effect of share option schemes in accordance with IAS 33.

	2012	2011
Average number of ordinary shares issued	**38,988,658**	38,231,656
Deemed issued for no consideration	**678,911**	898,078
Diluted number of ordinary shares issued	**39,667,569**	39,129,734

8. Profit for the financial year

The Group accounts do not include a separate Income Statement for Zotefoams plc (the Parent undertaking) as permitted by Section 408 of the Companies Act 2006. The Parent Company profit after tax for the financial year is £4,341,000 (2011: £3,885,000).

9. Property, plant and equipment

a) Group

	Land and buildings £000	Plant and equipment £000	Fixtures and fittings £000	Under construction £000	Total £000
Cost					
Balance at 1 January 2011	15,065	44,781	2,524	1,783	64,153
Additions	57	191	263	2,242	2,753
Disposals	–	(569)	234	(3)	(338)
Reclassifications	–	443	139	(582)	–
Effect of movement in foreign exchange	35	50	8	–	93
Balance at 31 December 2011	15,157	44,896	3,168	3,440	66,661
Balance at 1 January 2012	15,157	44,896	3,168	3,440	66,661
Additions	177	1,121	324	2,025	3,647
Reclassifications	–	2,771	–	(2,771)	–
Effect of movement in foreign exchange	(201)	(227)	(16)	–	(444)
Balance at 31 December 2012	**15,133**	**48,561**	**3,476**	**2,694**	**69,864**
Depreciation and impairment					
Balance at 1 January 2011	6,696	29,708	2,152	–	38,556
Depreciation charge for the year	602	2,172	163	–	2,937
Disposals	–	(346)	11	–	(335)
Effect of movement in foreign exchange	18	47	5	–	70
Balance at 31 December 2011	7,316	31,581	2,331	–	41,228
Balance at 1 January 2012	7,316	31,581	2,331	–	41,228
Depreciation charge for the year	604	2,178	230	–	3,012
Effect of movement in foreign exchange	(85)	(149)	(11)	–	(245)
Balance at 31 December 2012	**7,835**	**33,610**	**2,550**	**–**	**43,995**
Net book value					
At 1 January 2011	8,369	15,073	372	1,783	25,597
At 31 December 2011 and 1 January 2012	7,841	13,315	837	3,440	25,433
At 31 December 2012	**7,298**	**14,951**	**926**	**2,694**	**25,869**

9. Property, plant and equipment continued

Included in plant and machinery for both the Company and the Group are assets with a net book value of £7,928,000 (2011: £3,332,000) pledged as security for bank loans.

During the year both the Company and the Group commenced a number of programmes to construct and refurbish plant and equipment and fixtures and fittings. Costs incurred up to the balance sheet date totalled £2,694,000 (2011: £3,440,000) for the Group.

b) Company

	Land and buildings £000	Plant and equipment £000	Fixtures and fittings £000	Under construction £000	Total £000
Cost					
Balance at 1 January 2011	10,590	40,197	2,285	1,783	54,855
Additions	–	104	157	2,242	2,503
Disposals	–	(569)	234	(3)	(338)
Reclassifications	–	443	139	(582)	–
Balance at 31 December 2011	10,590	40,175	2,815	3,440	57,020
Balance at 1 January 2012	10,590	40,175	2,815	3,440	57,020
Additions	177	1,101	318	2,024	3,620
Reclassifications	–	2,771	–	(2,771)	–
Balance at 31 December 2012	**10,767**	**44,047**	**3,133**	**2,693**	**60,640**
Depreciation and impairment					
Balance at 1 January 2011	5,055	26,819	1,958	–	33,832
Depreciation charge for the year	421	1,861	143		2,425
Disposals	–	(346)	11	–	(335)
Balance at 31 December 2011	5,476	28,334	2,112	–	35,922
Balance at 1 January 2012	5,476	28,334	2,112	–	35,922
Depreciation charge for the year	414	1,891	186	–	2,491
Disposals	–	–	–	–	–
Balance at 31 December 2012	**5,890**	**30,225**	**2,298**	**–**	**38,413**
Net book value					
At 1 January 2011	5,535	13,378	327	1,783	21,023
At 31 December 2011 and 1 January 2012	5,114	11,841	703	3,440	21,098
At 31 December 2012	**4,877**	**13,822**	**835**	**2,693**	**22,227**

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10. Intangible assets

Group

	Marketing related £000	Customer related £000	Technology related £000	MEL goodwill £000	Total intangibles £000
Cost					
Balance at 1 January 2011	203	161	3,471	1,874	5,709
Additions	–	–	311	–	311
Effect of movement in foreign exchange	1	1	38	81	121
Balance at 31 December 2011	204	162	3,820	1,955	6,141
Balance at 1 January 2012	204	162	3,820	1,955	6,141
Additions	–	63	–	–	63
Effect of movement in foreign exchange	(8)	(71)	(105)	(85)	(269)
Balance at 31 December 2012	**196**	**154**	**3,715**	**1,870**	**5,935**
Amortisation					
Balance at 1 January 2011	10	13	101	–	124
Charge for the year	20	26	230	–	276
Effect of movement in foreign exchange	1	1	10	–	12
Balance at 31 December 2011	31	40	341	–	412
Balance at 1 January 2012	31	40	341	–	412
Charge for the year	20	37	243	–	300
Effect of movement in foreign exchange	(2)	(3)	(20)	–	(25)
Balance at 31 December 2012	**49**	**74**	**564**	**–**	**687**
Net book value					
At 1 January 2011	193	148	3,370	1,874	5,585
At 1 January 2012	173	122	3,479	1,955	5,729
At 31 December 2012	**147**	**80**	**3,151**	**1,870**	**5,248**

The Group tests annually for impairment or more frequently if there are indications that goodwill may be impaired.

Goodwill arising on acquisition is allocated to the cash generating unit ('CGU') that is expected to benefit, being MEL. The recoverable amount of the MEL CGU is determined using value in use calculations which use cash flow projections based on financial budgets and forecasts approved by management over the next seven years. For periods beyond this, cash flows are extrapolated using long-term growth rates.

Other assumptions such as market growth and margins are based on past experience and management's expectations.

Key assumptions:
Long-term growth rate 2.5%
This growth rate is based on a prudent assessment of past experience and future estimations of market expectations.

Discount rate 14%
The pre-tax discount rates applied to the cash flow forecasts for the MEL CGU are derived from the pre-tax weighted average cost of capital for the Group adjusted for local economic and political risks.

The goodwill of £1.87 million is measured against the discounted future cash flow projections of MEL. The long-term average growth rate used was 2.5% pa and the risk adjusted pre-tax discount rate was 14%.

10. Intangible assets continued

Sensitivity to changes in assumptions

There is sufficient headroom for the MEL CGU so that management believe that no reasonable change in any of the above assumptions would cause the carrying value of MEL goodwill to exceed its recoverable amount.

Company

	MuCell licence £000
Cost	
Balance at 1 January 2011	150
Additions	32
Disposal	(150)
Balance at 31 December 2011	32
Balance at 1 January 2012	32
Additions	–
Disposal	(32)
Balance at 31 December 2012	**–**
Amortisation	
Balance at 1 January 2011	(125)
On disposals	150
Charge for the year	(57)
Balance at 31 December 2011	(32)
Balance at 1 January 2012	(32)
On disposals	32
Charge for the year	–
Balance at 31 December 2012	**–**
Net book value	
At 1 January 2011	–
At 31 December 2011 and 1 January 2012	–
At 31 December 2012	**–**

11. Investment in subsidiaries

	Company	
	2012 £000	2011 £000
Shares in Group undertakings – at cost	**9,646**	7,157
Provision against the value of investment in subsidiary	**(3,294)**	(3,294)
Loan to Group undertakings	**–**	2,489
	6,352	6,352

The investment consists of the entire ordinary share capital of Zotefoams International Limited. Investments in the prior year included a loan of £2,489,000 loan to Zotefoams International Limited. In September 2012 this loan was converted into equity.

The following is a complete list of the subsidiary undertakings of the Company:

	Ownership	Incorporated in:
Zotefoams International Limited	100%	Great Britain
Zotefoams Pension Trustees Limited	100%	Great Britain
Zotefoams Hong Kong Limited (indirectly owned)	100%	Hong Kong
Zotefoams Inc. (indirectly owned)	100%	USA
MuCell Extrusion LLC (indirectly owned)	100%	USA

The principal activities of the subsidiary undertakings are as follows: Zotefoams Inc. purchases, manufactures and distributes cross-linked block foams and Zotefoams International Limited is a holding company. MuCell Extrusion LLC holds and develops microcellular foam technology which it licenses to customers. Zotefoams Pension Trustees Limited and Zotefoams Hong Kong Limited are currently dormant. In the opinion of the Directors the investments in the Company's subsidiary undertakings are worth at least the amount at which they are stated in the Balance Sheet.

The Company has a representative office in China.

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11. Investment in subsidiaries continued

Business combinations

During the year the remaining consideration of $3.5m due on the acquisition of MuCell Extrusion LLC was settled. Of this consideration $2.0m was paid in January 2012 and $1.5m was paid in July 2012.

12. Inventories

	Group		Company	
	2012 £000	2011 £000	**2012 £000**	2011 £000
Raw materials and consumables	**2,992**	2,622	**2,639**	2,198
Work in progress	**1,662**	1,397	**1,238**	1,341
Finished goods	**1,986**	1,908	**1,570**	1,174
	6,640	5,927	**5,447**	4,713

The carrying amount of inventories subject to retention of title clauses is £259,000 (2011: £201,000).

In 2012 the value of inventory recognised by the Group as an expense in cost of goods sold was £31,172,000 (2011: £28,122,000).

13. Trade and other receivables

		Group		Company	
	Note	**2012 £000**	2011 £000	**2012 £000**	2011 £000
Amounts falling due within one year:					
Trade receivables	19	**10,509**	9,654	**7,839**	7,370
Fair value derivatives	19	**56**	49	**56**	49
Amounts owed by Group undertakings	23	**–**	–	**3,231**	3,273
Other receivables		**245**	452	**245**	452
Prepayments and accrued income		**802**	378	**690**	335
		11,612	10,533	**12,061**	11,479
Trade receivables are shown net of:					
impairment losses		**139**	241	**98**	157

14. Cash and cash equivalents/bank overdrafts

	Group		Company	
	2012 £000	2011 £000	**2012 £000**	2011 £000
Cash and cash equivalents per balance sheet	**3,698**	3,403	**3,178**	1,611
Cash and equivalents per cash flow statements	**3,698**	3,403	**3,178**	1,611

15. Trade and other payables

		Group		Company	
	Note	**2012 £000**	2011 £000	**2012 £000**	2011 £000
Trade payables		**1,501**	1,615	**1,419**	1,459
Deferred consideration		**–**	2,252	**–**	–
Other creditors including taxation and social security:					
Other taxation and social security		**276**	249	**271**	244
Fair value derivatives	19	**94**	100	**94**	100
Amounts owed to Group undertakings	23	**–**	–	**–**	21
Other payables		**535**	577	**448**	437
Accruals and deferred income		**2,515**	3,094	**2,202**	2,880
		4,921	7,887	**4,434**	5,141

16. Interest-bearing loans and borrowings

	Note	Group 2012 £000	Group 2011 £000	Company 2012 £000	Company 2011 £000
Bank loans		**1,360**	660	**1,360**	660
Amounts due to Group undertakings	23	**–**	–	**–**	322
Amounts falling due within one year		**1,360**	660	**1,360**	982
Bank loans		**2,962**	820	**2,962**	820
Amounts falling due in more than one year		**2,962**	820	**2,962**	820
	19	**4,322**	1,480	**4,322**	1,802

In December 2012 Zotefoams plc took out a £3.5m mortgage, repayable over five years in equal quarterly instalments. Interest on the mortgage is charged at 3.5%. This facility is secured over specific plant assets.

17. Deferred tax assets and liabilities

Recognised deferred tax assets and liabilities – Group

Deferred tax assets and liabilities are attributable to the following:

	Assets 2012 £000	Assets 2011 £000	Liabilities 2012 £000	Liabilities 2011 £000	Net 2012 £000	Net 2011 £000
Property, plant and equipment	**–**	–	**1,745**	1,742	**1,745**	1,742
Rolled-over gain	**–**	–	**742**	806	**742**	806
Inventories	**(110)**	(140)	**–**	–	**(110)**	(140)
Financial instruments	**(9)**	(13)	**–**	–	**(9)**	(13)
Defined benefit scheme and share option charges	**(1,857)**	(1,370)	**–**	–	**(1,857)**	(1,370)
Tax value of recognised losses carried forward	**(350)**	(350)	**–**	–	**(350)**	(350)
Tax (assets)/liabilities	**(2,326)**	(1,873)	**2,487**	2,548	**161**	675
Set off tax	**1,866**	1,383	**(1,866)**	(1,383)	**–**	–
Net tax (assets)/liabilities	**(460)**	(490)	**621**	1,165	**161**	675

During the year, as a result of the changes in the UK corporation tax rate to 24%, which was substantially enacted on 26 March 2012 and was effective from 1 April 2012; and to 23%, which was substantially enacted on 3 July 2012 and will be effective from 1 April 2013, the relevant deferred tax balances have been remeasured.

A further reduction to the UK corporation tax rate has been announced. The change proposes to reduce the rate to 22% from 1 April 2014. The change had not been substantively enacted at the balance sheet date and, therefore, is not recognised in these financial statements.

Unrecognised deferred tax assets

The Group has $4.2m (2011: $3.7m) of tax losses carried forward in the USA which expire between 2022 and 2026 under current tax legislation. At year end exchange rates these tax losses have a value of £2.6m (2011: £2.4m). The Group has only recognised £1.0m (2011: £1.0m) of these tax losses as a deferred tax asset representing what the Board consider to be a reasonable estimate of the expected US tax utilisation in the near future. During the year losses of £0.1m were used and additional losses of £0.1m were recognised. At a 35% tax rate these tax losses are £0.9m (2011: £0.8m) of which £0.4m has been recognised (2011: £0.4m).

Movement in deferred tax during the year

	Balance 1 January 2012 £000	Recognised in income £000	Recognised in equity £000	**Balance 31 December 2012 £000**
Property, plant and equipment	1,742	3	–	**1,745**
Rolled-over gain	806	(64)	–	**742**
Inventories	(140)	30	–	**(110)**
Financial instruments	(13)	–	4	**(9)**
Defined benefit scheme and share option charges	(1,370)	222	(709)	**(1,857)**
Tax value of recognised losses carried forward	(350)	–	–	**(350)**
	675	191	(705)	**161**

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17. Deferred tax assets and liabilities continued

Movement in deferred tax during the prior year

	Balance 1 January 2011 £000	Recognised in income £000	Recognised in equity £000	Balance 31 December 2011 £000
Property, plant and equipment	2,050	(308)	–	1,742
Rolled-over gain	902	(96)	–	806
Inventories	(91)	(49)	–	(140)
Financial instruments	(19)	–	6	(13)
Defined benefit scheme and share option charges	(1,616)	322	(76)	(1,370)
Tax value of recognised losses carried forward	(261)	(89)	–	(350)
	965	(220)	(70)	675

Deferred tax assets and liabilities – Company

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2012 £000	2011 £000	**2012 £000**	2011 £000	**2012 £000**	2011 £000
Property, plant and equipment	**–**	–	**1,745**	1,742	**1,745**	1,742
Rolled-over gain	**–**	–	**742**	806	**742**	806
Financial instruments	**(9)**	(13)	**–**	–	**(9)**	(13)
Defined benefit scheme and share option charges	**(1,857)**	(1,370)	**–**	–	**(1,857)**	(1,370)
Tax (assets)/liabilities	**(1,866)**	(1,383)	**2,487**	2,548	**621**	1,165
Set off tax	**1,866**	1,383	**(1,866)**	(1,383)	**–**	–
Net tax liabilities	**–**	–	**621**	1,165	**621**	1,165

Movement in deferred tax during the year

	Balance 1 January 2012 £000	Recognised in income £000	Recognised in equity £000	**Balance 31 December 2012 £000**
Property, plant and equipment	1,742	3	–	**1,745**
Rolled-over gain	806	(64)	–	**742**
Financial instruments	(13)	–	4	**(9)**
Defined benefit scheme and share option charges	(1,370)	222	(709)	**(1,857)**
	1,165	161	(705)	**621**

Movement in deferred tax during the prior year

	Balance 1 January 2011 £000	Recognised in income £000	Recognised in equity £000	Balance 31 December 2011 £000
Property, plant and equipment	2,050	(308)	–	1,742
Rolled-over gain	902	(96)	–	806
Financial instruments	(19)	–	6	(13)
Defined benefit scheme and share option charges	(1,616)	322	(76)	(1,370)
	1,317	(82)	(70)	1,165

18. Share capital

	2012 £	2011 £
Allotted, called-up and fully paid		
At 31 December		
Equity: 39,831,312 (2011: 39,831,312) ordinary shares of 5.0p each	**1,991,566**	1,991,566

Details of share options are provided in note 22 to the accounts on page 67.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled, on a poll, to one vote per share at meetings of the Company.

19. Financial instruments and financial risk management

Policy

The Company's and Group's principal financial instruments include bank loans, cash and short-term deposits the main purpose of which is to raise finance for the Company's and Group's operations. Foreign exchange derivatives are used to help manage the Company's and Group's currency exposure. It is and has been throughout the year under review, the Company's and Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Company's and Group's financial instruments are credit risk, interest rate risk, liquidity risk and foreign currency risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below. These policies have remained fundamentally unchanged throughout the year.

Credit risk

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. The Company and Group do not require collateral in respect of financial assets.

In 2012 and 2011, the Company and Group had credit insurance to mitigate this risk. However, the uninsured exposure as at 31 December 2012 was £3,002,000 (2011: £2,461,000) so elements of risk remain.

At the balance sheet date there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the Balance Sheet.

Trade receivables can be analysed as follows:

	Group 2012 £000	Group 2011 £000	**Company 2012 £000**	Company 2011 £000
Amounts neither past due or impaired	**8,139**	7,583	**5,930**	5,490
Amounts past due but not impaired				
Less than 60 days	**1,112**	1,102	**651**	911
More than 60 days	**–**	–	**–**	–
Total past due but not impaired	**1,112**	1,102	**651**	911
Amounts impaired	**1,397**	1,210	**1,356**	1,126
Impairment allowance	**(139)**	(241)	**(98)**	(157)
Carrying amount of impaired receivables	**1,258**	969	**1,258**	969
Trade receivables net of allowances	**10,509**	9,654	**7,839**	7,370

The normal terms of trade are in the range 30-90 days from the end of the month of invoice.

The Company and the Group make provisions against trade and other receivables, such provisions being based on the previous credit history of the debtor and if the debtor is in receivership or liquidation.

The credit quality of trade receivables that are neither past due nor impaired is assessed on an individual basis, based on credit ratings and experience. Management believes adequate provision has been made for trade receivables.

Interest rate risk

The Company and Group finance their operations through a mixture of retained profits and bank borrowings. The Company and Group borrow in the desired currency generally at a variable rate of interest.

The interest rate profile of the Company's and Group's borrowings at 31 December was:

	2012				2011			
	Effective interest rate	**Fixed rates £000**	**Variable rates £000**	**Total £000**	Effective interest rate	Fixed rates £000	Variable rates £000	Total £000
Sterling – mortgage	**2.0**	**–**	**822**	**822**	2.0	–	1,480	1,480
Sterling – mortgage	**–**	**3.5**	**3,500**	**3,500**	–	–	–	–
Total	**2.0**	**3.5**	**4,322**	**4,322**	2.0	–	1,480	1,480

The interest rate payable on the multi-currency overdraft is determined by LIBOR plus a bank margin.

In addition to the above the Company owes amounts to Group undertakings of £nil on which interest was charged (2011: £322,000 and interest of 2.25%).

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19. Financial instruments and financial risk management continued

Liquidity risk

The following are the contractual maturities of financial liabilities, including estimated payments and excluding the effect of netting agreements:

Group	2012 Carrying amount £000	2012 Contractual cash flows £000	2012 1 year or less £000	2012 1 to 2 years £000	2012 2 to 5 years £000	2011 Carrying amount	2011 Contractual cash flows £000	2011 1 year or less £000	2011 1 to 2 years £000	2011 2 to 5 years £000
Non-derivative financial liabilities										
Secured bank loans	**4,322**	**4,322**	**1,360**	**862**	**2,100**	1,480	1,480	660	660	160
Trade and other payables	**2,036**	**2,036**	**2,036**	**–**	**–**	4,444	4,444	4,444	–	–

Company	2012 Carrying amount £000	2012 Contractual cash flows £000	2012 1 year or less £000	2012 1 to 2 years £000	2012 2 to 5 years £000	2011 Carrying amount	2011 Contractual cash flows £000	2011 1 year or less £000	2011 1 to 2 years £000	2011 2 to 5 years £000
Non-derivative financial liabilities										
Secured bank loans	**4,322**	**4,322**	**1,360**	**862**	**2,100**	1,480	1,480	660	660	160
Trade and other payables	**1,867**	**1,867**	**1,867**	**–**	**–**	1,917	1,917	1,917	–	–

The Company's and Group's objective is to maintain a balance of continuity of funding and flexibility through the use of overdrafts, loans and finance leases as applicable. The maturity profile of the Company's and Group's borrowings is shown above.

The Company and Group have a short-term multi-currency overdraft facility of £4.9m which is freely transferable. This facility is repayable on demand and is utilised by the Company and the Group under a cross-guarantee structure.

In January 2009 the Company took out a £3.3m mortgage, repayable over five years in equal quarterly instalments. This facility is secured over specific plant assets. At 31 December 2012 £0.8m of this mortgage was outstanding and £2.5m had been repaid. This loan has no major financial operating covenants.

In December 2012 the Company took out a £3.5m mortgage, repayable over five years in equal quarterly instalments. This facility is secured over specific plant assets. At 31 December 2012 £3.5m of this mortgage was outstanding. This loan has no major financial operating covenants.

Cash flow forecasts are produced to monitor the expected cash flow requirements of the Company and Group against the available facilities.

Foreign currency risk

The Company and Group are exposed to foreign currency risk on sales, purchases, assets and liabilities which are denominated in a currency other than sterling. The currencies giving rise to this risk are primarily the euro and the US dollar.

The euro and US dollar rates used in preparing the accounts are as follows:

	2012 Average	2012 Closing	2011 Average	2011 Closing
Euro/sterling	**1.23**	**1.23**	1.15	1.20
US dollar/sterling	**1.59**	**1.63**	1.61	1.55

The Company and Group hedge a proportion of their estimated cash exposure in respect of trade and other receivables, trade and other payables and forecast sales receipts and purchase payments for the next nine months. The Company and Group use forward exchange contracts to hedge their foreign currency risk. As at 31 December 2012 these forward currency contracts covered approximately two-thirds of the estimated net cash foreign exchange exposure for the next nine months. Further details are shown opposite.

19. Financial instruments and financial risk management continued

In respect of other monetary assets and liabilities held in currencies other than the euro and the US dollar, the Company and Group ensure that the net exposure is kept to a manageable level by buying or selling foreign currencies at spot rates where necessary to address short-term imbalances.

Where possible the Group tries to hold the majority of its cash and cash equivalent balances in the local currency of the respective entity.

The table below shows financial instruments not in the domestic currency of the individual company they are held by:

Group – 2012	**Euro £000**	**US Dollar £000**	**Other £000**	**Total £000**
Cash and cash equivalents	**260**	**(404)**	**(57)**	**(201)**
Trade receivables	**3,852**	**650**	**352**	**4,854**
Trade payables	**(968)**	**(76)**	**–**	**(1,044)**

Group – 2011	Euro £000	US Dollar £000	Other £000	Total £000
Cash and cash equivalents	(363)	10	(20)	(373)
Trade receivables	3,774	330	288	4,392
Trade payables	(1,041)	(11)	–	(1,052)

Company – 2012	**Euro £000**	**US Dollar £000**	**Other £000**	**Total £000**
Cash and cash equivalents	**260**	**(404)**	**(57)**	**(201)**
Trade receivables	**3,852**	**650**	**352**	**4,854**
Trade payables	**(968)**	**(76)**	**–**	**(1,044)**

Company – 2011	Euro £000	US Dollar £000	Other £000	Total £000
Cash and cash equivalents	(363)	10	(20)	(373)
Trade receivables	3,774	330	288	4,392
Trade payables	(1,041)	(11)	–	(1,052)

Forecast transactions

The Company and Group classify their forward exchange contracts hedging forecast transactions as cash flow hedges and state them at fair value. The net fair value of forward exchange contracts used as hedges of forecast transactions at 31 December 2012 was a net liability of £38,000 (2011: net liability of £51,000) comprising assets of £56,000 (2011: £49,000) and liabilities of £94,000 (2011: £100,000).

Recognised assets and liabilities

Changes in the fair value of forward exchange contracts that economically hedge monetary assets and liabilities in foreign currencies and for which no hedge accounting is applied are recognised in the Income Statement. Both the changes in fair value of the forward contracts and the foreign exchange gains and losses relating to the monetary items are recognised as part of administrative expenses (see note 3).

The maturity profile of the forward contracts as at 31 December is as follows:

Company and Group:

	2012				2011			
	Foreign currency ‘000	**Contract value £000**	**Transaction fair value £000**	**Contract fair value £000**	Foreign currency ‘000	Contract value £000	Transaction fair value £000	Contract fair value £000
Sell EUR	**€4,025**	**3,213**	**3,289**	**(76)**	€2,130	1,837	1,793	44
Sell USD	**$8,200**	**5,110**	**5,072**	**38**	$4,450	2,791	2,886	(95)

Sensitivity analysis

In managing currency risks the Company and Group aim to reduce the impact of short-term fluctuations on their earnings. Over the longer-term, however, changes in foreign exchange and interest rates would have an impact on earnings.

Short-term fluctuations in interest rates are not hedged as the Company and Group, at present, do not consider them material. At 31 December 2012 it is estimated that a general increase of one percentage point in interest rates would decrease the Company’s and Group’s profit before tax by approximately £43,000 (2011: £15,000).

Financial Statements

Notes continued

19. Financial instruments and financial risk management continued

At 31 December 2012 it is estimated that an increase of one percentage point in the value of sterling against the euro and US dollar would decrease the Company's and Group's profit before tax by approximately £59,000 (2011: £73,000) before forward exchange contracts and £26,000 (2011: £55,000) after forward exchange contracts are included for the euro and £85,000 (2011: £89,000) for the US dollar before forward exchange contracts and £38,000 (2011: £60,000) after forward exchange contracts are included.

The Company and Group have significant undertakings in the USA whose revenue and expenses are denominated in US dollars. They also make a significant proportion of their sales to European customers and these revenues are predominantly in euros. It was the Company's and Group's policy in 2012 to hedge the foreign currency cash flows of invoiced sales net of expected foreign currency expenditure. Hedging is achieved by the use of foreign currency contracts expiring in the month of expected cash flow.

Fair values

The fair values together with the carrying amounts shown in the Balance Sheet are as follows:

Group

	2012		2011	
	Carrying amount £000	**Fair value £000**	Carrying amount £000	Fair value £000
Trade and other receivables	**10,754**	**10,754**	10,106	10,106
Cash and cash equivalents	**3,698**	**3,698**	3,403	3,403
Forward exchange contracts – assets	**56**	**56**	49	49
– liabilities	**(94)**	**(94)**	(100)	(100)
Secured bank loans	**(4,322)**	**(4,325)**	(1,480)	(1,485)
Trade and other payables	**(2,036)**	**(2,036)**	(4,444)	(4,444)

Company

	2012		2011	
	Carrying amount £000	**Fair value £000**	Carrying amount £000	Fair value £000
Trade and other receivables	**11,315**	**11,315**	11,095	11,095
Cash and cash equivalents	**3,178**	**3,178**	1,611	1,611
Forward exchange contracts – assets	**56**	**56**	49	49
– liabilities	**(94)**	**(94)**	(100)	(100)
Secured bank loans	**(4,322)**	**(4,325)**	(1,480)	(1,485)
Trade and other payables	**(1,867)**	**(1,867)**	(1,917)	(1,917)

Estimation of fair values

The following summarises the major methods and assumptions used in estimating fair values of financial instruments reflected in the table above. They are classified according to the following fair value hierarchy:

- Level 1: quoted process (unadjusted) in active markets for identical assets or liabilities
- Level 2: inputs other than quoted process included within Level 1 that are observable for the asset or liability, either directly (ie as prices) or indirectly (derived from prices)
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs)

Derivatives are valued at fair value using exchange rates and market interest rates at the balance sheet date.

Trade and other receivables are valued at fair value which is estimated as the present value of future cash flows, discounted at the market rate of interest at the balance sheet date if the effect is material.

Cash and cash equivalents are valued at fair value which is estimated as its carrying value where cash is repayable on demand.

Interest-bearing borrowings are valued at fair value which is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the balance sheet date.

Capital management

The Company and Group define the capital that they manage as the Company's and Group's total equity. The Company's and Group's policy for managing capital is to maintain a strong balance sheet with the objective of maintaining customer, supplier and investor confidence in the business and to ensure that the Company and Group have sufficient resources to be able to invest in future development and growth of the business. The Board of Directors monitors the return on capital which the Company and Group define as profit before tax excluding exceptional items divided by average net assets. Goodwill, intangible assets and any associated amortisation are excluded from this calculation. The Board of Directors also monitors the level of dividends paid to ordinary shareholders. The Group and Company are primarily financed by ordinary shares and retained profits.

20. Commitments

	2012 £000	2011 £000
(i) Capital contracts at the end of the financial year for which no provision has been made	**953**	1,029
(ii) The Group has non-cancellable operating lease rentals, which are payable as follows:		
– within one year	**98**	41
– between two and five years	**6**	17

During the year ended 31 December 2012 £143,000 was recognised as an expense in the Income Statement in respect of operating leases (2011: £92,000).

The above amounts apply to both the Company and the Group.

21. Employee benefits

The Group and Company operate one defined benefit pension scheme in the UK which offers both pensions in retirement and death benefits to members. Pension benefits are related to the members' final salary at retirement and their length of service. Since 1 October 2001 the scheme has been closed to new members.

From 31 December 2005 future accrual of benefits for existing members of the scheme ceased.

Contributions to the plan for the year from the Company were £55,000 per month, a rate agreed with the Company and the Trustees following the triennial review in April 2008 to apply from January 2009 until June 2016. During the year and following the 2011 triennial annual review the Company agreed with the Trustees to continue these contributions at £55,000 per month to September 2013 after which they will fall to £13,000 per month. These contribution rates are scheduled to be reviewed again after the results of the next triennial review.

The Company has opted to recognise all actuarial gains and losses immediately in Other Comprehensive Income. An actuarial valuation of the scheme was carried out as at 5 April 2011 and the results have been updated to 31 December 2012 by a qualified independent actuary. The major assumptions used by the actuary were (in nominal terms) as follows:

	As at 31 December 2012	As at 31 December 2011	As at 31 December 2010
Discount rate	**4.30%**	4.90%	5.30%
Expected return on plan assets	**5.33%**	5.75%	6.21%
Rate of salary increase	**n/a**	n/a	n/a
Rate of increase to pensions in payment	**3.60%**	3.60%	3.70%
Rate of inflation	**2.40%**	2.00%	3.20%
Mortality assumption	**S1PA CMI**	S1PA CMI	PCA00 MC
Life expectancy from age 65 of current male pensioners	**22.0 years**	21.9 years	21.7 years
Commutation assumption	**75% of members take maximum cash**	75% of members take maximum cash	75% of members take maximum cash

The mortality tables used above are those published by the Institute and Faculty of Actuaries, with allowance for improvements in member longevity in line with the 'CMI model' with a long-term improvement rate of 1.0% per annum. These rates suggest that a man aged 65 retiring at 31 December 2012 could expect to live, on average, until age 87. A 5% change in this life expectancy would increase the IAS19 liability by approximately £0.9m (£0.7m after deferred tax), all other things being equal.

The overall expected return on assets assumption of 5.33% as at 31 December 2012 has been derived by calculating the weighted average of the expected rate of return for each asset class. The following approach has been used to determine the expected rate of return for each asset class:

- Equities – allowance for an additional return of 4.50% above that available on UK government securities.
- Fixed interest securities – current market yields.
- Cash – based on the Bank of England base rate.

Financial Statements

Notes continued

21. Employee benefits continued

Present value of scheme assets:

	Year ended 31 December 2012		Year ended 31 December 2011		Year ended 31 December 2010	
	Long-term rate of return expected	**Market value £000**	Long-term rate of return expected	Market value £000	Long-term rate of return expected	Market value £000
Equities	**6.8%**	**12,497**	7.0%	12,345	7.3%	13,624
Bonds	**3.2%**	**5,254**	3.6%	3,989	4.0%	3,262
Other	**0.5%**	**1,412**	0.5%	1,301	0.5%	1,198
Insured pensioners		**192**		179		172
		19,355		17,814		18,256

Present value of defined obligation:

Funded plans	**26,527**	22,758
Total	**26,527**	22,758
Deficit in the scheme	**(7,172)**	(4,944)
Related deferred tax asset	**1,650**	1,236
Net pension liability	**(5,522)**	(3,708)

Reconciliation of opening and closing balances of the present value of the defined benefit obligation:

Benefit obligation at beginning of year	**22,758**	23,215
Interest cost	**1,100**	1,210
Actuarial losses/(gains)	**3,274**	(891)
Benefits and expenses paid	**(605)**	(776)
Benefit obligation at end of year	**26,527**	22,758

Reconciliation of opening and closing balances of the fair value of plan assets:

Fair value of plan assets at beginning of year	**17,814**	18,256
Expected return on plan assets	**1,026**	1,130
Actuarial gains/(losses)	**460**	(1,456)
Contributions by employer	**660**	660
Benefits and expenses paid	**(605)**	(776)
Fair value of plan assets at end of year	**19,355**	17,814

The amounts recognised in the Income Statement are:

Interest on obligation	**1,100**	1,210
Expected return on plan assets	**(1,026)**	(1,130)
Total expense	**74**	80

The expense/(income) is recognised in the following line items in the Income Statement:

	Group and Company	
	2012 £000	2011 £000
Financial income	**(1,026)**	(1,130)
Finance costs	**1,100**	1,210
	74	80

21. Employee benefits continued

Actuarial (losses)/gains shown in Other Comprehensive Income since 1 January 2008:

	2012 £000	2011 £000	2010 £000	2009 £000	2008 £000
Balance as at 1 January	**(2,824)**	(2,259)	(2,567)	131	1,789
Actuarial (losses)/gains	**(2,814)**	(1,705)	308	(2,698)	(1,658)
Effect of revaluation of defined benefit scheme under CPI	–	1,140	–	–	–
Balance as at 31 December	**(5,638)**	(2,824)	(2,259)	(2,567)	131

History of scheme assets, obligations and experience adjustments

	As at 31 December 2012 £000	As at 31 December 2011 £000	As at 31 December 2010 £000	As at 31 December 2009 £000	As at 31 December 2008 £000
Present value of defined benefit obligation	**26,527**	22,758	23,215	22,211	17,396
Fair value of scheme assets	**19,355**	17,814	18,256	16,428	13,869
Deficit in the scheme	**(7,172)**	(4,944)	(4,959)	(5,783)	(3,527)
Experience adjustments arising on scheme liabilities	**(43)**	739	(30)	(650)	518
Experience item as a percentage of scheme liabilities	**0%**	(3)%	0%	3%	(3)%
Experience adjustments arising due to change in valuation basis	**(3,231)**	152	(499)	(3,888)	2,234
Experience adjustments arising on scheme assets	**460**	(1,456)	837	1,840	(4,410)
Experience item as a percentage of scheme assets	**2%**	(8)%	5%	11%	(32)%

Other pension schemes

On 1 January 2006 a separate stakeholder scheme was set up for those employees who were originally in the closed defined benefit pension scheme. The contributions paid by the Company in 2012 were £440,000 (2011: £447,000).

In addition to this scheme, the Company operates a stakeholder scheme which is open to employees who joined after 1 October 2001. The contributions paid by the Company in 2012 were £144,000 (2011: £108,000).

For certain non-UK based employees of the Company, the Company makes contributions into individual schemes. The contributions paid by the Company in 2012 were £9,000.

For US based employees, Zotefoams Inc. operates a 401(k) plan. The contributions paid by Zotefoams Inc. in 2012 were £48,000 (2011: £46,000).

22. Share-based payments

The Company has share option schemes that entitle senior management personnel to purchase shares in the Company. Options are exercisable at a price equal to the average quoted closing market price of the Company's shares on the day before or on the three dealing days before the option is granted. The vesting period is three years. If the options remain unexercised after a period of ten years from the date of grant, the options expire. Depending on the circumstances options are normally forfeited if the employee leaves the Group before the options vest.

In 2007 the Company introduced a LTIP scheme for senior management personnel. Shares are awarded in the Company and vest after three years to the extent performance conditions are met. Dependant on the circumstances awards are normally forfeited if the employee leaves the Group before the award vests.

In 2007 the Company also introduced a Deferred Bonus Plan. Executive bonuses over 40% of bonusable salary are held as deferred shares for three years. Depending on the circumstances awards are normally forfeited if the employee leaves the Group before the award vests.

Details of the vesting conditions for the share, share option and LTIP awards are given in the Directors' Remuneration Report on page 26.

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Notes continued

22. Share-based payments continued

Details of the options outstanding during the year are as follows:

	2012 Number of share options	2012 Weighted average exercise price (p)	2011 Number of share options	2011 Weighted average exercise price (p)
Outstanding at beginning of the period	**368,173**	**90.3**	570,307	91.0
Exercised during the period	**(23,430)**	**106.7**	(159,960)	88.6
Granted during the period	**84,160**	**178.2**	–	–
Forfeited during the period	**–**	**–**	(42,174)	106.7
Outstanding at the end of the period	**428,903**	**106.7**	368,173	90.3
Exercisable at the end of the period	**297,376**	**88.3**	320,806	89.7

The options outstanding at 31 December 2012 have an exercise price of between 72.5p and 179.0p (2011: 72.5p and 106.7p) and a weighted contractual life of eight years (2011: eight years).

The weighted average share price at the date of exercise for share options exercised in 2012 was £1.76 (2011: £1.49).

The fair value received in return for share options granted are measured by reference to the fair value of share options granted. The estimate of fair value of the services received measured is based on a Black-Scholes model. The contractual life of the option (ten years) is used as an input into this model. No allowance is made for early leavers.

Details of the LTIP awards outstanding during the year are as follows:

	2012 Number of share options	2012 Weighted average exercise price (p)	2011 Number of share options	2011 Weighted average exercise price (p)
Outstanding at beginning of the period	**700,050**	**–**	775,800	–
Exercised during the period	**(363,311)**	**–**	(96,352)	–
Granted during the period	**145,723**	**–**	167,415	–
Forfeited during the period	**–**	**–**	(100,529)	–
Lapsed during the period	**(30,109)**	**–**	(46,284)	–
Outstanding at the end of the period	**452,353**	**–**	700,050	–
Exercisable at the end of the period	**–**	**–**	–	–

Details of the Deferred Bonus Plan awards outstanding during the year are as follows:

	2012 Number of share options	2012 Weighted average exercise price (p)	2011 Number of share options	2011 Weighted average exercise price (p)
Outstanding at beginning of the period	**35,826**	**–**	57,137	–
Exercised in the period	**–**	**–**	(31,653)	–
Granted during the period	**–**	**–**	19,293	–
Forfeited during the period	**–**	**–**	(8,951)	–
Outstanding at the end of the period	**35,826**	**–**	35,826	–
Exercisable at the end of the period	**–**	**–**	–	–

22. Share-based payments continued

Fair value of share options and assumptions

The expected volatility is based on historic volatility for a three year period prior to the award.

	19 March 2010	19 March 2010	31 March 2011	**4 April 2012**	**9 May 2012**	**13 August 2012**
Share price (p)	99.0	95.0	153.5	**186.5**	**179.0**	**176.2**
Exercise price (p)	nil	95.0	nil	**nil**	**179.0**	**176.2**
Expected volatility	35%	35%	35%	**35%**	**35%**	**35%**
Option life	Five years	Five years	Five years	**Five years**	**Five years**	**Five years**
Expected dividends (p) (assumed to be increasing at 2.5% pa)	nil	4.5	nil	**nil**	**5.0**	**5.0**
Risk-free interest rate (based on national government bonds)	1.3%	1.3%	1.3%	**1.3%**	**2.0%**	**2.0%**
Fair value at grant date (p)	99.0	19.0	153.5	**186.5**	**47.0**	**46.0**

The share option awards are granted under a service condition and a performance condition. There are no market conditions associated with the share options. The LTIP awards are granted under a service condition and a performance condition, part of which is a market condition. The Deferred Bonus Plan awards are granted under a service condition.

The amounts recognised in the Income Statement for equity-settled share-based payments are as follows:

		Group and Company	
		2012 £000	2011 £000
Within administrative expenses	– share-based payment charge	**161**	125
	– related National Insurance	**84**	(5)
Element of the above relating to Directors of Zotefoams plc		**97**	108

23. Related parties

Directors

The Directors of the Company as at 31 December 2012 and their immediate relatives control approximately 1.5% of the voting shares of the Company. Details of Directors' pay and remuneration are given in the Directors' Remuneration Report on page 25. The Executive Directors are considered to be the only key management personnel.

Transactions with key management personnel

The compensation of key management personnel is as follows:

	Group		Company	
	2012 £000	2011 £000	**2012 £000**	2011 £000
Key management emoluments including social security costs	**597**	478	**597**	478
Company contributions to money purchase pension plan	**66**	64	**66**	64
Share related awards	**97**	108	**97**	108
	760	650	**760**	650

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Notes continued

23. Related parties continued

Subsidiaries

The Company owns 100% of the shares of Zotefoams International Limited, which is incorporated in the UK. Zotefoams International Limited owns 100% of the shares in Zotefoams Inc., which is incorporated in the USA. Common control exists between the Company and Zotefoams Employee Benefit Trust (EBT) and Zotefoams EBT has therefore been consolidated as described in note 1b.

Zotefoams Inc. owns 100% of the ownership units of MuCell Extrusion LLC, which is incorporated in the USA. The other subsidiaries of the Company are currently dormant.

Balances between the Company and these subsidiaries are as follows:

	Loan owed to		Loan owed by		Payables owed to		Receivables owed by		Investment in	
	2012 £000	2011 £000	**2012 £000**	2011 £000	**2012 £000**	2011 £000	**2012 £000**	2011 £000	**2012 £000**	2011 £000
Zotefoams Inc.*	**–**	322	**–**	–	**–**	–	**3,231**	3,273	**–**	–
MuCell Extrusion LLC	**–**	–	**–**	–	**–**	21	**–**	–	**–**	–
Zotefoams International Limited	**–**	–	**–**	2,489	**–**	–	**–**	–	**6,352**	3,863

*Loans with Zotefoams Inc. are interest bearing.

During the year the loan of £2,489k owed by Zotefoams International Limited to the Company was converted into equity.

In addition there is a net payable balance of £347k owed by MuCell Extrusion LLC to Zotefoams Inc.

24. Accounting estimates and judgements

In the application of the Group's accounting policies, which are described in note 1, the Directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities which are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other facts that are considered relevant. Actual amounts may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision only affects that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Key sources of estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are disclosed below.

i) Property, plant and equipment

In relation to the Group's property, plant and equipment, useful economic lives and residual values of assets have been established using historical experiences and an assessment of the nature of the assets involved. Assets are assessed on an ongoing basis to determine whether circumstances exist that could lead to a potential impairment of the carrying value of such assets. No circumstances have been identified to suggest that this is the case.

ii) Intangible assets

The determination of goodwill and intangible assets requires judgements made by the Directors. Goodwill is reviewed annually to assess the requirement for impairment. Other intangible assets are assessed on an ongoing basis to determine whether circumstances exist that could lead to the conclusion that the carrying value of such assets is not supportable. Such calculations require judgement relating to the appropriate discount factors and long-term growth prevalent in particular markets as well as short-term business performance. The Directors also draw upon experience in making these judgements.

iii) Pensions assumptions

The valuation of pension scheme liabilities is calculated in accordance with Group policy. The valuation is prepared by an independent qualified actuary but significant judgements are required in relation to the assumptions for pension increases, inflation, the discount rate applied, investment returns and member longevity which underpin the valuations. Note 21 contains information about the assumptions relating to retirement benefit obligations.

Key judgements

Development costs

Under IAS 38 development costs must be capitalised when specified criteria have been met. Following a review of the Company's research and development expenditure, because of the uncertainties which still exist on the development of new products, it was concluded that no material development costs met the IAS 38 criteria require for capitalisation and therefore all development costs have been expensed.

Notice of the 2013 Annual General Meeting

THIS DOCUMENT IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION
If you are in any doubt as to the action you should take, you are recommended to seek your own personal advice from your stockbroker, accountant or other independent professional adviser authorised under the Financial Services and Markets Act 2000.

If you have sold or otherwise transferred all of your ordinary shares in Zotefoams plc, you should forward this document and other documents enclosed (except the personalised form of proxy) as soon as possible to the stockbroker, bank or other agent through whom the sale or transfer was effected for transmission to the purchaser or transferee.

Notice is hereby given that the Annual General Meeting (the 'AGM') of Zotefoams plc (the 'Company') will be held at the registered office of the Company, 675 Mitcham Road, Croydon CR9 3AL on 15 May 2013 at 10.00 a.m. for the following purposes:

Ordinary business
To consider and, if thought fit, pass resolutions numbered 1 to 11 below as ordinary resolutions:

1. To receive the audited annual accounts of the Company for the year ended 31 December 2012, together with the Directors' Report, the Directors' Remuneration Report and the Auditor's Report on those annual accounts, the Directors' Report and that section of the Remuneration Report subject to audit.
2. To approve the Directors' Remuneration Report for the year ended 31 December 2012 in accordance with Section 439 of the Companies Act 2006.
3. To declare a final dividend for the year ended 31 December 2012 of 3.5 pence per ordinary share, such dividend to be payable on 23 May 2013 to shareholders who are on the register of members of the Company at the close of business on 26 April 2013.
4. To re-elect M-L Clayton as a Director who retires by rotation.
5. To re-elect R J Clowes as a Director who retires by rotation.
6. To re-elect N G Howard as a Director who retires by rotation.
7. To re-elect C G Hurst as a Director who retires by rotation.
8. To re-elect D B Stirling as a Director who retires by rotation.
9. To re-elect A Walker as a Director who retires by rotation.
10. That PricewaterhouseCoopers LLP be and is hereby appointed as Auditor of the Company to hold office from the conclusion of the AGM until the conclusion of the next general meeting at which accounts are laid before the Company.
11. To authorise the Directors to determine the Auditor's remuneration.

Special business
To consider and, if thought fit, to pass the following resolutions of which resolution 12 will be proposed as an ordinary resolution and resolutions 13, 14 and 15 will be proposed as special resolutions:

12. That, in substitution for any equivalent authorities and powers granted to the directors prior to the passing of this resolution, the Directors be and they are generally and unconditionally authorised pursuant to Section 551 of the Companies Act 2006 (the 'Act'):

(a) to exercise all powers of the Company to allot shares in the Company, and grant rights to subscribe for or to convert any security into shares of the Company (such shares, and rights to subscribe for or to convert any security into shares of the Company being 'relevant securities') up to an aggregate nominal amount of £663,855 (such amount to be reduced by the nominal amount of any allotments or grants made under paragraph (b) below in excess of £663,855); and further

(b) to allot equity securities (as defined in Section 560 of the Act) up to an aggregate nominal amount of £1,327,710 (such amount to be reduced by the nominal amount of any allotments or grants made under paragraph (a) above) in connection with an offer by way of rights issue:

(i) in favour of holders of ordinary shares in the capital of the Company, where the equity securities respectively attributable to the interests of all such holders are proportionate (as nearly as practicable) to the respective number of ordinary shares in the capital of the Company held by them; and

(ii) to holders of any other equity securities as required by the rights of those securities or as the directors otherwise consider necessary,

but subject to such exclusions or other arrangements as the directors may deem necessary or expedient to deal with treasury shares, fractional entitlements or legal, regulatory or practical problems arising under the laws or requirements of any overseas territory or by virtue of shares being represented by depository receipts or the requirements of any regulatory body or stock exchange or any other matter whatsoever;

(c) provided that, unless previously revoked, varied or extended, this authority shall expire on the earlier of 30 June 2014 and the conclusion of the next Annual General Meeting of the Company, except that the Company may at any time before such expiry make an offer or agreement which would or might require relevant securities to be allotted after such expiry and the Directors may allot relevant securities in pursuance of such an offer or agreement as if this authority had not expired.

Notice of the 2013 Annual General Meeting continued

13. That the Directors be and they are empowered pursuant to Section 570(1) of the Act to allot equity securities (as defined in Section 560(1) of the Act) of the Company wholly for cash pursuant to the authority of the Directors under Section 551 of the Act conferred by resolution 12 above, and/or by way of a sale of treasury shares for cash (by virtue of Section 573 of the Act), in each case as if Section 561(1) of the Act did not apply to such allotment provided that:

(a) the power conferred by this resolution shall be limited to:

(i) the allotment of equity securities and sale of treasury shares for cash in connection with an offer of, or invitation to apply for, equity securities (but in the case of the authority granted under paragraph (b) of resolution 12, by way of a rights issue only):

(A) in favour of holders of ordinary shares in the capital of the Company, where the equity securities respectively attributable to the interests of all such holders are proportionate (as nearly as practicable) to the respective number of ordinary shares in the capital of the Company held by them; and

(B) to holders of any other equity securities as required by the rights of those securities or as the Directors otherwise consider necessary,

but subject to such exclusions or other arrangements as the Directors may deem necessary or expedient to deal with treasury shares, fractional entitlements or legal, regulatory or practical problems arising under the laws or requirements of any overseas territory or by virtue of shares being represented by depository receipts or the requirements of any regulatory body or stock exchange or any other matter whatsoever; and

(ii) in the case of the authority granted under paragraph (a) of resolution 12 and/or in the case of any sale of treasury shares for cash, the allotment, otherwise than pursuant to sub-paragraph (i) above, of equity securities or sale of treasury shares up to an aggregate nominal value equal to £99,578; and

(b) unless previously revoked, varied or extended, this power shall expire on the earlier of 30 June 2014 and the conclusion of the next Annual General Meeting of the Company except that the Company may before the expiry of this power make an offer or agreement which would or might require equity securities to be allotted (and treasury shares to be sold) after such expiry and the Directors may allot equity securities (and sell treasury shares) in pursuance of such an offer or agreement as if this power had not expired.

14. That the Company be and is hereby unconditionally and generally authorised for the purposes of Section 701 of the Act to make market purchases (within the meaning of Section 693(4) of the Act) of its ordinary shares of 5 pence each ('Ordinary Shares') provided that:

(a) the maximum number of Ordinary Shares authorised to be purchased is 3,983,131;

(b) the minimum price which may be paid for any such Ordinary Share is 5 pence;

(c) the maximum price which may be paid for an Ordinary Share shall be an amount equal to 105% of the average middle market quotations for an Ordinary Share as derived from the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the Ordinary Share is contracted to be purchased; and

(d) this authority shall, unless previously renewed, revoked or varied, expire on the earlier of 30 June 2014 and the conclusion of the next Annual General Meeting, but the Company may enter into a contract for the purchase of Ordinary Shares before the expiry of this authority which would or might be completed (wholly or partly) after its expiry.

15. That a general meeting other than an annual general meeting may be called on not less than 14 clear days' notice.

Dated: 21 March 2013

By order of the Board

Registered Office:
675 Mitcham Road
Croydon
CR9 3AL

J W Kindell
Company Secretary

Notes

(i) Pursuant to Part 13 of the Companies Act 2006 and to Regulation 41 of the Uncertificated Securities Regulations 2001 (as amended), only those members registered in the register of members of the Company at the close of business on 13 May 2013 (or if the AGM is adjourned, 48 hours before the time fixed for the adjourned AGM) shall be entitled to attend and vote at the AGM in respect of the number of shares registered in their name at that time. In each case, changes to the register of members after such time shall be disregarded in determining the rights of any person to attend or vote at the AGM.

(ii) If you wish to attend the AGM in person please bring the accompanying attendance card and present this to the Company's reception desk on arrival.

(iii) A member who is entitled to attend, speak and vote at the AGM may appoint a proxy to attend, speak and vote instead of him. A member may appoint more than one proxy provided each proxy is appointed to exercise rights attached to different shares (so a member must have more than one share to be able to appoint more than one proxy). A proxy need not be a member of the Company but must attend the AGM in order to represent you. A proxy must vote in accordance with any instructions given by the member by whom the proxy is appointed. Appointing a proxy will not prevent a member from attending in person and voting at the AGM (although voting in person at the AGM will terminate the proxy appointment). A proxy form is enclosed or has been sent to you separately. The notes to the proxy form include instructions on how to appoint the Chairman of the AGM or another person as a proxy. You can only appoint a proxy using the procedures set out in these Notes and in the notes to the proxy form.

(iv) To be valid, a proxy form, and the original or duly certified copy of the power of attorney or other authority (if any) under which it is signed or authenticated, should reach the Company's registrars, Computershare Investor Services plc, The Pavilions, Bridgwater Road, Bristol BS99 6ZY, by no later than 10.00 a.m. on 13 May 2013.

(v) The proxy form includes details on how to vote electronically. The notes to the proxy form also include instructions on how to appoint a proxy by using the CREST proxy appointment service. You may not use any electronic address provided either in this notice of AGM or in any related documents (including the proxy form) to communicate with the Company for any purposes other than those expressly stated.

(vi) In the case of joint holders of shares, the vote of the first named in the register of members who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of other joint holders.

(vii) The following information is available at www.zotefoams.com: (1) the matters set out in this notice of AGM; (2) the total numbers of shares in the Company, and shares in each class, in respect of which members are entitled to exercise voting rights at the AGM; (3) the totals of the voting rights that members are entitled to exercise at the AGM, in respect of the shares of each class; and (4) members' statements, members' resolutions and members' matters of business received by the Company after the first date on which notice of the AGM was given.

(viii) If you are a person who has been nominated by a member to enjoy information rights in accordance with Section 146 of the Companies Act 2006, Notes (iii) to (v) above do not apply to you (as the rights described in these Notes can only be exercised by members of the Company) but you may have a right under an agreement between you and the member by whom you were nominated to be appointed or to have someone else appointed, as a proxy for the meeting. If you have no such right or do not wish to exercise it, you may have a right under such an agreement to give instructions to the member as to the exercise of voting rights.

(ix) A member that is a company or other organisation not having a physical presence cannot attend in person but can appoint someone to represent it. This can be done in one of two ways: either by the appointment of a proxy (described in Notes (iii) to (v) above) or of a corporate representative. Members considering the appointment of a corporate representative should check their own legal position, the Company's Articles of Association and the relevant provision of the Companies Act 2006.

(x) Members attending the AGM have the right to ask, and, subject to the provisions of the Companies Act 2006, the Company must cause to be answered, any questions relating to the business being dealt with at the AGM.

(xi) As at the close of business on 21 March 2013, the Company's issued share capital comprised 39,831,312 ordinary shares of 5 pence each. Each ordinary share carries the right to one vote at a general meeting of the Company. No ordinary shares were held in treasury and accordingly the total number of voting rights in the Company as at the close of business on 21 March 2013 is 39,831,312.

(xii) Shareholders should note that it is possible that, pursuant to requests made by shareholders of the Company under Section 527 of the Companies Act 2006, the Company may be required to publish on a website a statement setting out any matter relating to: (i) the audit of the Company's accounts (including the auditor's report and the conduct of the audit) that are to be laid before the AGM; or (ii) any circumstance connected with an auditor of the Company ceasing to hold office since the previous meeting at which annual accounts and reports were laid in accordance with Section 437 of the Companies Act 2006. The Company may not require the shareholders requesting any such website publication to pay its expenses in complying with Sections 527 or 528 of the Companies Act 2006. Where the Company is required to place a statement on a website under Section 527 of the Companies Act 2006, it must forward the statement to the Company's auditor not later than the time when it makes the statement available on the website. The business which may be dealt with at the AGM includes any statement that the Company has been required under Section 527 of the Companies Act 2006 to publish on a website.

(xiii) Copies of the Executive Directors' service contracts with the Company and any of its subsidiary undertakings, deeds of indemnity in favour of the Directors and letters of appointment of the Non-Executive Directors are available for inspection at the registered office of the Company during the usual business hours on any weekday (Saturday, Sunday or public holidays excluded) from the date of this notice until the conclusion of the AGM.

Explanatory notes to the resolutions

Ordinary Business

Resolution 1 – Receiving the accounts and reports

All quoted companies are required by law to lay their annual accounts and reports before a general meeting of the Company, together with the Directors' Report, Directors' Remuneration Report, and Auditor's Report on the accounts, the Directors' Report and the section of the Directors' Remuneration Report subject to audit. At the AGM, the Directors will present these documents to the shareholders for the financial year ended 31 December 2012.

Resolution 2 – Remuneration Report

All quoted companies are required by law to produce for each financial year a Directors' Remuneration Report which sets out the Remuneration Committee's policy in relation to Directors' remuneration, together with the remuneration and benefits paid to Directors during the year. The Company is also required to put an ordinary resolution to shareholders approving the report at the meeting at which the Company's report and accounts for that year are laid. Accordingly, resolution 2 seeks the approval of the Directors' Remuneration Report which is set out on pages 23 to 27 of the report and accounts for the financial year ended 31 December 2012.

The vote is advisory in nature and will have no effect on the remuneration of individual Directors for the year under review. It will, however, provide shareholders with the means to express their opinion concerning remuneration matters and promote dialogue in respect of policy.

Resolution 3 – Declaration of dividend

This resolution concerns the Company's final dividend payment. The Directors are recommending a final dividend of 3.5 pence per ordinary share in respect of the year ended 31 December 2012 which, if approved, will be payable on 23 May 2013 to the shareholders on the register of members on 26 April 2013.

Resolutions 4 to 9 – Re-election of directors

The UK Corporate Governance Code requires all directors of FTSE 350 companies to stand for annual re-election. Whilst the Company is not within the FTSE 350, best practice for listed companies is to follow this requirement and, therefore, the Board has decided for this year that all the Directors will stand for annual re-election. Resolutions 4 to 9 concern the re-election of M-L Clayton, R J Clowes, N G Howard, C G Hurst, D B Stirling and A Walker.

Biographies for the Directors are set out on pages 18 and 19 of the report and accounts for the year ended 31 December 2012. The Chairman having undertaken performance reviews of the Directors and the Non-Executive Directors of the Chairman, the Board is satisfied that each Director continues to be effective and demonstrates commitment to the role and recommends that each Director should be re-elected.

Notice of the 2013 Annual General Meeting continued

Resolutions 10 and 11 – Appointment of Auditor and their remuneration
Resolution 10 concerns the appointment of PricewaterhouseCoopers LLP as the Company's Auditor, to hold office until the conclusion of the Company's next general meeting where accounts are laid.

As part of good practice, the Audit Committee recommended to the Board that the Company's audit be put to competitive tender, as KPMG Audit plc ('KPMG') had been the Company's Auditor since the Company's listing in 1995. A formal tender process was initiated in May 2012 and, following proposals and presentations from three firms (including KPMG), PricewaterhouseCoopers LLP was successful in the process. As a consequence, KPMG resigned as the Company's Auditor and the Board appointed PricewaterhouseCoopers LLP to fill the casual vacancy.

Resolution 11 authorises the Directors to determine the Auditor's remuneration.

Special Business
Resolution 12 – Power to allot shares
This resolution grants the Directors authority to allot shares in the capital of the Company and other relevant securities up to an aggregate nominal value of £663,855, representing approximately one-third (33.33%) of the nominal value of the issued ordinary share capital of the Company as at 21 March 2013, being the latest practicable date before publication of this notice. In addition, in accordance with the latest institutional guidelines issued by the Association of British Insurers ('ABI'), paragraph (b) of resolution 12 grants the Directors authority to allot further equity securities up to an aggregate nominal value of £1,327,710, representing approximately two-thirds (66.67%) of the nominal value of the issued ordinary share capital of the Company as at 21 March 2013, being the latest practicable date before publication of this notice. This additional authority may be only applied to fully pre-emptive rights issues.

The intention of the authority granted pursuant to paragraph (b) of resolution 12 is to preserve maximum flexibility and if the Directors do exercise this authority, they intend to follow best practice as regards its use (including the Directors standing for re-election in certain cases), as recommended by the ABI.

The Company does not currently hold any shares as treasury shares within the meaning of Section 724 of the Companies Act 2006 ('Treasury Shares').

The Directors do not have any present intention of exercising the authorities conferred by resolution 12 but they consider it desirable that the specified amount of authorised but unissued share capital is available for issue so that they can more readily take advantage of possible opportunities.

Unless revoked, varied or extended, this authority will expire at the conclusion of the next AGM of the Company or 30 June 2014, whichever is the earlier.

Resolution 13 – Authority to allot shares disregarding pre-emption rights
This resolution authorises the Directors in certain circumstances to allot equity securities for cash other than in accordance with the statutory pre-emption rights (which require a company to offer all allotments for cash first to existing shareholders in proportion to their holdings). The relevant circumstances are either where the allotment takes place in connection with a rights issue or the allotment is limited to a maximum nominal amount of £99,578, representing approximately 5% of the nominal value of the issued ordinary share capital of the Company as at 21 March 2013 being the latest practicable date before publication of this notice. Unless revoked, varied or extended, this authority will expire at the conclusion of the next AGM of the Company or 30 June 2014, whichever is the earlier.

The Directors consider that the power proposed to be granted by resolution 13 is necessary to retain flexibility, although they do not have any intention at the present time of exercising such power.

Resolution 14 – Authority to purchase shares (market purchases)
This resolution authorises the Board to make market purchases of up to 3,983,131 ordinary shares (representing approximately 10% of the Company's issued ordinary shares as at 21 March 2013, being the latest practicable date before publication of this notice). Shares so purchased may be cancelled or held as Treasury Shares. The authority will expire at the end of the next AGM of the Company or 30 June 2014, whichever is the earlier. The Directors intend to seek renewal of this authority at subsequent AGMs.

The minimum price that can be paid for an ordinary share is 5 pence being the nominal value of an ordinary share. The maximum price that can be paid is 5% over the average of the middle market prices for an ordinary share, derived from the Daily Official List of the London Stock Exchange, for the five business days immediately before the day on which the share is contracted to be purchased.

The Directors intend to exercise this right only when, in light of the market conditions prevailing at the time and taking into account all relevant factors (for example, the effect on earnings per share), they believe that such purchases are in the best interests of the Company and shareholders generally. The overall position of the Company will be taken into account before deciding upon this course of action. The decision as to whether any such shares bought back will be cancelled or held in treasury will be made by the Directors on the same basis at the time of the purchase.

As at 21 March 2013, being the latest practicable date before publication of this notice, there were outstanding awards under the Company's long-term incentive schemes in respect of 915,016 ordinary shares in the capital of the Company representing 2.3% of the Company's issued ordinary share capital. If the authority to purchase the Company's ordinary shares were exercised in full, such options would represent 2.6% of the Company's issued ordinary share capital.

Resolution 15 – Notice period for general meetings
Under the Companies Act 2006, a listed company must give at least 21 days' notice of its general meetings. However, this Act enables general meetings (other than AGMs) to be held on shorter notice of not less than 14 days provided the shareholders have given their consent at the previous AGM or a general meeting held since the last AGM, Resolution 15 seeks such approval similar to the resolution that was passed last year. The approval will be effective until the Company's next AGM, when it is intended that a similar resolution will be proposed. The Directors will always endeavour to give as much notice as possible of general meetings, but would like to have the flexibility to call a general meeting on the shorter permitted notice period for time sensitive matters that are clearly in the shareholders' interests. If the authority is used, the Company will offer the ability, as required by the Companies Act 2006, to vote electronically.

Recommendation
The Directors consider that the proposals being put to the shareholders at the AGM are in the best interests of the Company and of the shareholders as a whole. Accordingly, the Directors recommend that you vote in favour of the resolutions set out in the Notice of the AGM, as they intend to do in respect of their own beneficial holdings of ordinary shares.

Five Year Trading Summary

	2012 £m	2011 £m	2010 restated £m	2009 £m	2008 £m
Turnover	**47.2**	44.2	39.9	31.8	34.8
Operating profit (excluding exceptional items)	**6.0**	5.6	4.8	3.4	4.0
Profit before tax (excluding exceptional items)	**5.9**	5.5	4.7	3.2	3.9
Profit before tax (including exceptional items)	**5.9**	5.5	5.3	2.7	3.9
Profit after tax (including exceptional items)	**4.7**	4.6	4.3	2.2	3.0
Capital expenditure	**3.7**	2.7	2.7	3.4	1.4
Cash generated from the operations	**6.3**	6.1	7.2	7.0	5.8
Basic earnings per share excluding exceptional items (p)	**12.1**	11.8	10.2	6.8	8.3
Basic earnings per share including exceptional items (p)	**12.1**	11.8	11.8	5.9	8.3
Dividends per ordinary share (p)	**5.20**	4.90	4.65	4.50	4.50

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Registrars
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Financial Calendar

Financial Calendar

AGM	15 May 2013
Payment of final dividend	23 May 2013 to shareholders on the register at the close of business on 26 April 2013
Announcement of 2013 interim results	August 2013
Payment of interim dividend	October 2013
Announcement of 2013 results	March 2014

Registrars
Enquiries concerning the holding of ordinary shares in the Company should be addressed to the registrars who should also be notified of any changes in a holder's address.

The registrars are: Computershare Investor Services Plc, The Pavilions, Bridgwater Road, Bristol BS99 6ZZ.
Telephone: 0870 707 1424
www.investorcentre.co.uk/contactus

Website
The Company has a website (www.zotefoams.com) which provides information on the business and products.

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