

Finance Director's report



Financial overview

	2015	2014
	£m	£m
Revenue	567.2	609.1
Headline operating profit	102.1	111.1
Amortisation of acquired intangible fixed assets	(4.2)	(3.9)
Operating profit prior to exceptional items	97.9	107.2
Acquisition costs	–	(0.2)
Reorganisation costs	(20.0)	–
Operating profit	77.9	107.0
Net finance charge	(2.9)	(3.3)
Profit before taxation	75.0	103.7
Taxation	(18.8)	(24.4)
Profit for the year	56.2	79.3

Group revenue was £567.2m, a decrease of 6.9%, with revenues at constant exchange rates down 4.1% and foreign exchange rate movements having an adverse impact of 2.8%.

Headline operating profit for the year decreased by 8.1% from £111.1m to £102.1m and headline operating margin was 18.0% (2014: 18.2%). Headline operating profit at constant exchange rates decreased by £6.7m, whilst adverse foreign exchange rate movements decreased headline operating profit by a further £2.3m.

The amortisation of acquired intangible assets arises from acquisitions in prior years. The charge has increased to £4.2m (2014: £3.9m).

Operating profit was £77.9m (2014: £107.0m) after charging £4.2m (2014: £3.9m) in respect of the amortisation of acquired intangible assets, £nil (2014: £0.2m) of acquisition costs and reorganisation costs of £20.0m (2014: £nil).

Headline operating cash flow¹ for the Group was £81.6m (2014: £100.0m). This was 80% of headline operating profit (2014: 90%). Net capital expenditure was 1.2 times depreciation (2014: 1.0 times) as the Group continued to follow its strategy of investing in Specialist Technologies and greenfield facilities in higher growth markets. There was a working capital outflow in the year mainly due to an increase in receivable days caused by lower than anticipated cash collection in December and a decrease in payables, arising primarily due to a reduction in accruals for variable staff costs.

After deducting interest and tax, the Group recorded positive free cash flow² of £47.4m (2014: £75.1m).

Exceptional costs

Total exceptional costs charged to the income statement amounted to £20.0m (2014: £0.2m). Of this, reorganisation costs amounting to £23.8m (2014: £nil) were incurred, offset by a profit on disposal of the Group's Brazilian and Indian operations of £3.8m (2014: £nil). Cost savings of £4m as a result of the reorganisation were realised in 2015 and a further £6m are anticipated in 2016. In 2015 no acquisition costs were expensed (2014: £0.2m).

Restructuring provisions outstanding at 31 December 2015 totalled £14.7m (2014: £9.4m), £11.0m is expected to be spent in 2016 and £3.7m in 2017 and later. All expenditure after the end of 2016 relates to ongoing environmental remediation, primarily in the USA.

1. Headline operating cash flow is reconciled on page 15.
2. Free cash flow is reconciled on page 15.
3. Headline EBITDA is reconciled on page 15.

Profit before taxation

Headline profit before taxation was £99.2m (2014: £107.8m). Profit before taxation was £75.0m (2014: £103.7m). These amounts are reconciled as follows:

	2015 £m	2014 £m
Headline operating profit	102.1	111.1
Net finance charge	(2.9)	(3.3)
Headline profit before taxation	99.2	107.8
Amortisation of acquired intangible fixed assets	(4.2)	(3.9)
Profit before taxation prior to exceptional items	95.0	103.9
Acquisition costs	–	(0.2)
Reorganisation costs	(20.0)	–
Profit before taxation	75.0	103.7

Finance charge

The net finance charge was £2.9m compared to £3.3m in 2014. The net interest payable is higher as a result of lower average net cash during the year, offset by lower bank and financing charges and a lower pension finance charge.

	2015 £m	2014 £m
Net interest payable	0.3	0.2
Financing costs	1.5	1.6
Bank and other charges	0.8	0.9
Pension finance charge	0.3	0.6
Net finance charge	2.9	3.3

Taxation

The taxation charge was £18.8m for the year (2014: £24.4m).

The effective taxation rate of 25.1% (2014: 23.5%) resulted from the blending of differing tax rates in each of the countries in which the Group operates. The increase in the taxation rate is primarily due to more of the Group's profits deriving from countries with a higher rate of tax.

The headline taxation rate for 2015 was 24.4% (2014: 22.7%), being stated before accounting for exceptional items and amortisation of goodwill and acquired intangibles.

In recent years the Group's effective tax rate has benefited from the use of historical tax losses, the majority of the remaining benefits of which are reflected in the 2015 taxation rate. As a result it is expected that the underlying Group effective taxation rate will be approximately 28% going forward, all other things remaining equal.

Earnings per share

Basic headline earnings per share (as defined in note 10) decreased to 39.5p from 43.8p. Basic earnings per share for the year decreased to 29.6p from 41.7p.

Dividend and dividend policy

The Group aims to pay ordinary dividends so that dividend cover will be at or above 2.0 times earnings (see note 10). The Board may also recommend payment of a supplemental distribution to shareholders. The amount of any supplemental distribution will be assessed in light of the cash position of the Group, along with funding requirements for both organic growth and acquisitions.

The Board has recommended a final ordinary dividend of 10.3p (2014: 9.8p) bringing the total ordinary dividend to 15.1p per share (2014: 14.4p). The Board has also recommended a supplemental distribution, by way of a special dividend, amounting to 10.0p per share (2014: 20.0p). If approved by shareholders, the final ordinary dividend of 10.3p per share for 2015 and the supplemental distribution of 10.0p per share for 2015 will be paid on 3 June 2016 to all shareholders on the register at the close of business on 22 April 2016.

Capital structure

The Group's balance sheet at 31 December 2015 is summarised below:

	Assets £m	Liabilities £m	Net Assets £m
Property, plant and equipment	429.6	–	429.6
Goodwill and intangible assets	175.2	–	175.2
Current assets and liabilities	152.7	(160.9)	(8.2)
Other non-current assets and liabilities	0.6	(11.3)	(10.7)
Retirement benefit obligations	–	(17.9)	(17.9)
Deferred tax	31.2	(61.9)	(30.7)
Total before net cash	789.3	(252.0)	537.3
Net cash	16.2	(3.9)	12.3
Net assets as at 31 December 2015	805.5	(255.9)	549.6
Net assets as at 31 December 2014	825.1	(254.2)	570.9

Net assets decreased by £21.3m (3.7%) to £549.6m (2014: £570.9m). At constant exchange rates, net assets decreased by £10.9m (1.9%). The major movements compared to 31 December 2014 were a decrease in net cash of £23.4m, an increase in goodwill and intangible assets of £3.1m and a decrease in property, plant and equipment of £5.0m.

The decrease in property, plant and equipment was predominantly due to additions of £61.1m offset by depreciation of £48.8m, asset impairments of £9.0m, foreign exchange movements of £3.8m, disposals of subsidiaries of £1.0m, transfer of assets to assets held for sale of £0.3m and other asset disposals of £3.2m.

The increase in goodwill and intangible assets was due to continuing investment of £5.6m in Group IT systems, amortisation charge of £5.0m and foreign exchange movements of £2.6m.

Finance Directors' report continued

Net cash

Group net cash at 31 December 2015 was £12.3m (2014: £35.7m). The Group continues to have access to committed facilities at competitive rates and therefore currently deems this to be the most effective means of funding.

Cash flow

The net decrease in cash and cash equivalents was £23.6m (2014: £21.3m increase), made up of net cash from operating activities of £111.3m (2014: £131.6m), less investing activities of £59.9m (2014: £54.8m) and less cash used in financing activities of £75.0m (2014: £55.5m).

The decrease in net cash flow from operating activities from £131.6m to £111.3m was driven primarily by the decrease in headline EBITDA³ from £165.5m to £149.2m and a £6.3m decrease in payables.

Net cash outflows from investing activities increased from £54.8m to £59.9m, primarily as a result of greater investment in property, plant and equipment in 2015 compared to the prior year. The level of net capital expenditure in 2015 was £61.3m (2014: £53.8m), consistent with plans to increase the Group's capacity in Specialist Technologies and in high growth markets.

Net cash outflows used in financing activities increased from £55.5m to £75.0m, due primarily to the increase in dividend payments, from £45.2m in 2014 to £66.0m in 2015.

There has been a continued focus on cash collection, although receivable days at 31 December 2015 increased by two to 62 days (2014: 60 days).

Net interest payments for the year were £2.6m (2014: £2.7m). Tax payments were £23.2m (2014: £19.0m).

Capital expenditure

Net capital expenditure (capital expenditure less proceeds from asset disposals) for the year was £61.3m (2014: £53.8m). The multiple of net capital expenditure to depreciation was 1.2 times (2014: 1.0 times). Major capital projects which were in progress during 2015 include a new high pressure HIP in the USA, the creation of a new S³P facility in France, a new LPC facility in Mexico, the establishment of an aerospace focused facility in South East Poland, and the creation of Classical Heat Treatment facilities in Poland and China. The Group also continued to invest in the implementation of a new ERP system. As a consequence of the timing of these key projects, the value of assets under construction has increased by £9.6m, from £42.0m in 2014 to £51.6m in 2015.

Borrowing facilities

The Group is financed by a mix of cash flows from operations, short-term borrowings, long-term loans and finance leases. The Group's funding policy aims to ensure continuity of finance at reasonable cost, based on committed and uncommitted facilities and loans from several sources over a spread of maturities. The Group continues to have access to committed facilities at competitive rates and therefore currently deems this to be the most effective means of long-term funding.

The total undrawn committed facility funding available to the Group at 31 December 2015 was £230.0m (2014: £230.0m). The Group also has access to a US\$10m committed letter of credit facility maturing in August 2016.

At 31 December 2015, the Group had the following committed facilities:

Facility	Expiry Date	Facility £m	Loan and Letter of Credit Utilisation £m	Facility Headroom £m
£230m Revolving Credit	3 July 2019	230.0	–	230.0
\$10m Letter of Credit	31 August 2016	6.8	1.8	5.0
		236.8	1.8	235.0

Capital management

The Group manages its capital to ensure that entities in the Group will be able to continue as going concerns, while maximising the return to shareholders. The capital structure of the Group consists of debt, which includes borrowings, cash and cash equivalents, and equity attributable to equity holders of the parent, comprising capital, reserves and retained earnings.

The capital structure is reviewed regularly by the Board. The Group's policy is to maintain gearing, determined as the proportion of net debt to total capital, within defined parameters, allowing movement in the capital structure appropriate to the business cycle and corporate activity. Due to the net cash position at 31 December 2015 the gearing ratio is 0% (2014: 0%).

Defined benefit pension arrangements

The Group has defined benefit pension obligations in the UK, Germany, Switzerland, Liechtenstein and the USA and cash lump sum obligations in France, Italy and Turkey, the liabilities for which are reflected in the Group balance sheet.

The net deficits in these arrangements are as follows:

	2015 £m	2014 £m
Funded:		
UK	2.7	1.0
Other Western Europe	2.0	1.6
North America	0.5	0.6
	5.2	3.2
Unfunded:		
Western Europe	12.6	13.7
Emerging markets	0.1	0.1
	12.7	13.8
Total deficit	17.9	17.0

The UK plan is closed to new entrants but the 66 active members continue to accrue benefits. The arrangements in France, Italy and Turkey are open to new members. All other arrangements are closed to new entrants.

UK Scheme liabilities have decreased by £3.4m over the year (2014: £103.3m, 2015: £99.9m). This is largely due to a change in the actuarial assumptions used to assess the present value of the liabilities. Most notably, the discount rate assumption has increased from 3.30% in 2014 to 3.50% in 2015 which has resulted in a decrease in the liabilities and was only partially offset by an increase in the inflation assumptions over the year by 0.10%.

Scheme assets decreased in the year by £0.9m to £101.4m (2014: £102.3m).

The assumptions used indicate a surplus of £1.5m. As the Group is not automatically entitled to recover this amount it is required to recognise additional liabilities under IFRIC14 to reflect existing future contractual commitments to the scheme of £4.2m. This results in a reported liability of £2.7m.

The liability for the other European Schemes decreased by £0.7m. The key reason for the decrease in the deficit in the European Schemes is an increase in the discount rate assumptions used in most countries due to rises in corporate bond yields over the year.

Post balance sheet events

There are no post balance sheet events that require disclosure in the financial statements.

Going concern

In determining the basis of preparation for the Annual Report and the Group's viability statement made on page 27, the directors have considered the Group's business activities, together with the factors likely to affect its future development, performance and position. This includes an overview of the Group's financial position, cash flows, liquidity position and borrowing facilities.

The Group meets its working capital requirements through a combination of cash resources, committed and uncommitted facilities and overdrafts. The overdrafts and uncommitted facilities are repayable on demand but the committed facilities are due for renewal as set out below. There is sufficient headroom in the committed facility covenants to assume that these facilities can be operated as contracted for the foreseeable future.

The committed facilities as at 31 December 2015 were as follows:

- £230m Revolving Credit Facility maturing 3 July 2019
- \$10m Letter of Credit Facility maturing 31 August 2016

The December 2015 weighted average life of the committed facilities was 3.4 years.

The Group's forecasts and projections, taking account of reasonable potential changes in trading performance, show that the Group should be able to operate within the level of its current committed facilities.

The directors have reviewed forecasts and projections for the Group's markets and services, assessing the committed facility and financial covenant headroom, central liquidity and the Group's ability to access further funding. The directors also reviewed downside sensitivity analysis over the forecast period, thereby taking into account the uncertainties arising from the current economic environment. Following this review, the directors have formed a judgement, at the time of approving the financial statements, that there is a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason the directors continue to adopt the going concern basis in preparing the financial statements.

D.F. Landless

Group Finance Director
25 February 2016