# Interim management report continued

## Financial overview

| | Half year to 30 June | |
|---|---|---|
| | **2017** **£m** | 2016 £m |
| Revenue | **345.7** | 291.0 |
| Headline operating profit | **61.7** | 49.3 |
| Amortisation of acquired intangible fixed assets | **(2.3)** | (2.2) |
| Operating profit | **59.4** | 47.1 |
| Net finance charge | **(1.2)** | (1.2) |
| Profit before taxation | **58.2** | 45.9 |

Revenue for the half year was £345.7m (2016: £291.0m), an increase of 18.8% compared to the same period last year. At constant exchange rates, revenue increased 8.3% (£24.2m). Favourable foreign exchange rate movements resulted in a £30.5m positive effect.

Headline operating profit increased to £61.7m (2016: £49.3m) and headline operating margin increased to 17.8% (2016: 16.9%). At constant exchange rates, headline operating profit increased £6.6m (13.4%).

The amortisation of acquired intangible assets arises from acquisitions in prior years. The charge has increased to £2.3m (2016: £2.2m).

Accordingly, operating profit increased to £59.4m (2016: £47.1m) and operating margin was 17.2% (2016: 16.2%).

The net finance charge for the Group was £1.2m, in line with 2016.

### Taxation

The tax charge in the first half of 2017 was £14.6m, compared to a charge of £12.6m for the same period of 2016. The effective tax rate was 25.1% (2016: 27.5%).

The headline tax rate, being stated before accounting for exceptional items and amortisation of goodwill and acquired intangibles, is 25.5% in the first six months of 2017 (2016: 27.5%). A number of the Group's key markets have rates of corporation tax above the Group average. Future profitability growth in these markets, therefore, is likely to place some upward pressure on the Group's blended corporation tax rate.

### Earnings per share

Basic headline earnings per share from operations for the half year were 23.6p (2016: 18.3p). Basic earnings per share from operations for the half year were 22.9p (2016: 17.5p). Diluted earnings per share were 22.9p (2016: 17.5p).

## Cash flow

| | Half year to 30 June | |
|---|---|---|
| | **2017** **£m** | 2016 £m |
| Headline operating profit | **61.7** | 49.3 |
| Add back non-cash items: | | |
| Depreciation and amortisation | **29.4** | 25.9 |
| Impairment of fixed assets | **0.4** | 0.2 |
| Share-based payments | **2.7** | 1.6 |
| Profit on disposal of property, plant and equipment | **(0.1)** | (0.1) |
| Headline EBITDA[1] | **94.1** | 76.9 |
| Net capital expenditure | **(29.7)** | (31.0) |
| Net working capital movement | **(4.5)** | (7.9) |
| Headline operating cash flow | **59.9** | 38.0 |
| Cash cost of restructuring | **(2.3)** | (4.3) |
| Operating cash flow | **57.6** | 33.7 |
| Interest | **(1.2)** | (0.9) |
| Taxation | **(14.3)** | (11.9) |
| Free cash flow[2] | **42.1** | 20.9 |

Free cash flow for the period was £42.1m compared to £20.9m in the first six months of 2016. The increase is mainly a result of the increase in headline EBITDA and lower restructuring cash outflows.

The net working capital outflow for the six month period amounted to £4.5m (2016: £7.9m). Receivables in the first half increased £9.8m (2016: £3.6m) as a result of increased trade and the normal seasonally higher revenues in May and June in comparison to November and December. Receivable days at 30 June 2017 are 61 days (31 December 2016: 63 days and 30 June 2016: 63 days). Payables increased £4.0m (2016: £6.3m decrease) and inventory decreased £0.5m (2016: £2.2m).

The utilisation of restructuring provisions resulted in a cash outflow of £2.3m (2016: £4.3m).

The Group continued to manage carefully its capital expenditure programme and is focused on growth in the higher value-added businesses and in particular the Specialist Technologies. Net capital expenditure for the first half was £29.7m (2016: £31.0m) and the ratio to depreciation was 1.0 times (2016: 1.2 times). The Group continues to invest in maintaining its assets to a high quality, as well as investing in the implementation of a new ERP system.

Income taxes paid during the first six months at £14.3m were £2.4m greater than the same period last year, reflecting the higher tax charge and timing of payments made in various tax jurisdictions.

1 Earnings before interest, tax, depreciation, amortisation, impairment, profit or loss on disposal of property, plant and equipment and share-based payments.
2 Free cash flow is defined as net cash from operating activities of £73.0m (2016: £52.8m) less net capital expenditure of £29.7m (2016: £31.0m) and net interest paid of £1.2m (2016: £0.9m).

### Net debt

Group net cash at 30 June 2017 was £17.7m (31 December 2016 net cash: £1.1m and 30 June 2016 net debt: £5.5m). No loans were drawn under the committed facilities at 30 June 2017, compared to £5.0m at 31 December 2016 and £7.4m at 30 June 2016. The Group continues to be able to borrow at competitive rates and therefore currently deems this to be the most effective means of funding.

### Borrowing facilities

The Group is financed by a mix of cash flows from operations, short-term borrowings, longer-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.

On 3 April 2017, the Group extended the £230m Revolving Credit Facility for five years to April 2022. At 30 June 2017, the Group had the following drawings and headroom under the committed facility:

| Facility | Expiry date | Facility £m | Facility utilisation £m | **Facility headroom £m** |
|---|---|---|---|---|
| £230m Revolving Credit | 3 April 2022 | 230.0 | – | **230.0** |

### Dividend

The Board has declared an interim dividend of 5.3p (2016: 5.0p) which represents an increase of 6.0% over the prior year. The interim dividend will be paid on 3 November 2017 to all shareholders on the register at the close of business on 6 October 2017.

## Principal risks and uncertainties

The directors have reconsidered the principal risks and uncertainties of the Group. The outcome of the Brexit negotiations is not expected to have a material transactional impact on the Group as customers are served locally and cross-border trading is minimal. The risk of a wider macro-economic effect as a result of the UK leaving the European Union is included as an element of the Group's existing market risk. Accordingly, the directors do not consider that the principal risks and uncertainties of the Group have significantly changed since the publication of the Annual Report for the year ended 31 December 2016. The risks and associated risk management processes, including financial risks, can be found on pages 24, 25, 26, 109 and 110 of the 2016 Annual Report, which is available at www.bodycote.com. The risks referred to and which could have a material impact on the Group's performance for the remainder of the current financial year relate to:

- Markets;
- Loss of key customers;
- Competitor action;
- Safety and health;
- Service quality;
- Major disruption at a facility;
- Information technology projects;
- Regulatory and legislative compliance;
- Liquidity;
- Interest rate fluctuation; and
- Currency exchange rate fluctuation.

## Going concern

As stated in note 1 to the condensed financial statements, the directors have formed a judgement, at the time of approving the condensed 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 condensed financial statements.