Notes to the condensed consolidated financial information

1 Accounting policies

Basis of preparation

This condensed set of financial statements for the half year ended 30 June 2017 has been prepared in accordance with IAS 34 Interim Financial Reporting.

The Interim management report has been prepared using accounting policies consistent with International Financial Reporting Standards (IFRSs) as adopted by the European Union and in accordance with those disclosed in the Annual Report for the year ended 31 December 2016, which was filed with the Registrar of Companies on 30 May 2017.

Going concern

In determining the basis of preparation for the Interim management report, the directors have considered the Group's business activities, together with the factors likely to affect its future development, performance and position which are set out in the Financial overview. 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 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.

On 3 April 2017, the Group extended the £230m Revolving Credit Facility for five years to April 2022. The committed facilities as at 30 June 2017 were as follows:

- £230m Revolving Credit Facility maturing 3 April 2022

The Group's forecasts and projections, which cover a period of at least 12 months from the date of approval of this Interim management report, 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 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.

Changes in accounting policies

The same accounting policies, presentation and methods of computation are followed in the condensed set of financial statements as applied in the Group's latest annual audited financial statements.

No new or revised standards adopted in the current period have had a material impact on the Group's financial statements.

2 Business and geographical segments

The Group has 188 locations across the world serving a range of market sectors with various thermal processing services. The range and type of services offered is common to all market sectors.

In accordance with IFRS 8 Operating Segments, the segmentation of Group activity reflects the way the Group is managed by the chief operating decision maker, being the Group Chief Executive, who on a monthly basis reviews the operating performance of six operating segments, split between the Aerospace, Defence & Energy (ADE) and Automotive & General Industrial (AGI) business areas, as follows:

- ADE – Western Europe;
- ADE – North America;
- ADE – Emerging markets;
- AGI – Western Europe;
- AGI – North America; and
- AGI – Emerging markets.

The split of operating segments by geography reflects the divisional reporting structure of the Group.

In accordance with the aggregation criteria of IFRS 8, the operating segments are aggregated into the Group's two key business areas, ADE and AGI, the split being driven by customer behaviour and requirements. Customers in the ADE segment tend to operate and purchase more globally and have long supply chains, whilst customers in the AGI segment tend to purchase more locally and have shorter supply chains.

Bodycote plants do not exclusively supply services to customers of a given market sector. The allocation of plants between ADE and AGI is therefore derived by reference to the preponderance of markets served.

Notes to the condensed consolidated financial information continued

2 Business and geographical segments (continued)

	Half year to 30 June 2017			
Group	**ADE £m**	**AGI £m**	**Central costs and eliminations £m**	**Consolidated £m**
Revenue				
Total revenue	**136.1**	**209.6**	**–**	**345.7**
Result				
Headline operating profit prior to share-based payments and unallocated central costs	**31.6**	**38.6**	**–**	**70.2**
Share-based payments (including social charges)	**(0.9)**	**(1.7)**	**(0.7)**	**(3.3)**
Unallocated central costs	**–**	**–**	**(5.2)**	**(5.2)**
Headline operating profit/(loss)	**30.7**	**36.9**	**(5.9)**	**61.7**
Amortisation of acquired intangible fixed assets	**(0.8)**	**(1.5)**	**–**	**(2.3)**
Segment result	**29.9**	**35.4**	**(5.9)**	**59.4**
Finance costs				**(1.2)**
Profit before taxation				**58.2**
Taxation				**(14.6)**
Profit for the period				**43.6**

Inter-segment sales are not material.

The Group does not rely on any individual major customers.

	Half year to 30 June 2017			
Aerospace, Defence & Energy	**Western Europe £m**	**North America £m**	**Emerging markets £m**	**Total ADE £m**
Revenue				
Total revenue	**61.8**	**73.6**	**0.7**	**136.1**
Result				
Headline operating profit prior to share-based payments	**13.4**	**18.0**	**0.2**	**31.6**
Share-based payments (including social charges)	**(0.4)**	**(0.5)**	**–**	**(0.9)**
Headline operating profit	**13.0**	**17.5**	**0.2**	**30.7**
Amortisation of acquired intangible fixed assets	**(0.2)**	**(0.6)**	**–**	**(0.8)**
Segment result	**12.8**	**16.9**	**0.2**	**29.9**

	Half year to 30 June 2017			
Automotive & General Industrial	**Western Europe £m**	**North America £m**	**Emerging markets £m**	**Total AGI £m**
Revenue				
Total revenue	**129.6**	**54.7**	**25.3**	**209.6**
Result				
Headline operating profit prior to share-based payments	**25.1**	**6.4**	**7.1**	**38.6**
Share-based payments (including social charges)	**(1.2)**	**(0.3)**	**(0.2)**	**(1.7)**
Headline operating profit	**23.9**	**6.1**	**6.9**	**36.9**
Amortisation of acquired intangible fixed assets	**(0.2)**	**(1.3)**	**–**	**(1.5)**
Segment result	**23.7**	**4.8**	**6.9**	**35.4**

2 Business and geographical segments (continued)

Group	ADE £m	AGI £m	Central costs and eliminations £m	Consolidated £m
	Half year to 30 June 2016			
Revenue				
Total revenue	121.9	169.1	–	291.0
Result				
Headline operating profit prior to share-based payments and unallocated central costs	27.9	28.6	–	56.5
Share-based payments (including social charges)	(0.5)	(0.7)	(0.5)	(1.7)
Unallocated central costs	–	–	(5.5)	(5.5)
Headline operating profit/(loss)	27.4	27.9	(6.0)	49.3
Amortisation of acquired intangible fixed assets	(0.8)	(1.4)	–	(2.2)
Segment result	26.6	26.5	(6.0)	47.1
Investment revenue				0.1
Finance costs				(1.3)
Profit before taxation				45.9
Taxation				(12.6)
Profit for the period				33.3

Aerospace, Defence & Energy	Western Europe £m	North America £m	Emerging markets £m	Total ADE £m
	Half year to 30 June 2016			
Revenue				
Total revenue	55.9	65.5	0.5	121.9
Result				
Headline operating profit/(loss) prior to share-based payments	11.5	16.6	(0.2)	27.9
Share-based payments (including social charges)	(0.2)	(0.3)	–	(0.5)
Headline operating profit/(loss)	11.3	16.3	(0.2)	27.4
Amortisation of acquired intangible fixed assets	(0.1)	(0.7)	–	(0.8)
Segment result	11.2	15.6	(0.2)	26.6

Automotive & General Industrial	Western Europe £m	North America £m	Emerging markets £m	Total AGI £m
	Half year to 30 June 2016			
Revenue				
Total revenue	104.4	45.6	19.1	169.1
Result				
Headline operating profit prior to share-based payments	17.3	6.7	4.6	28.6
Share-based payments (including social charges)	(0.5)	(0.1)	(0.1)	(0.7)
Headline operating profit	16.8	6.6	4.5	27.9
Amortisation of acquired intangible fixed assets	(0.1)	(1.3)	–	(1.4)
Segment result	16.7	5.3	4.5	26.5

Notes to the condensed consolidated financial information continued

2 Business and geographical segments (continued)

Group	ADE £m	AGI £m	Central costs and eliminations £m	Consolidated £m
	Year ended 31 December 2016			
Revenue				
Total revenue	250.9	349.7	–	600.6
Result				
Headline operating profit prior to share-based payments and unallocated central costs	56.3	57.9	–	114.2
Share-based payments (including social charges)	(0.7)	0.6	(0.6)	(0.7)
Unallocated central costs	–	–	(13.9)	(13.9)
Headline operating profit/(loss)	55.6	58.5	(14.5)	99.6
Amortisation of acquired intangible fixed assets	(1.5)	(3.0)	–	(4.5)
Operating profit/(loss) prior to exceptional items	54.1	55.5	(14.5)	95.1
Acquisition costs	–	(0.6)	–	(0.6)
Segment result	54.1	54.9	(14.5)	94.5
Finance costs				(2.6)
Profit before taxation				91.9
Taxation				(24.9)
Profit for the year				67.0

Aerospace, Defence & Energy	Western Europe £m	North America £m	Emerging markets £m	Total ADE £m
	Year ended 31 December 2016			
Revenue				
Total revenue	115.1	134.7	1.1	250.9
Result				
Headline operating profit/(loss) prior to share-based payments	24.0	32.7	(0.4)	56.3
Share-based payments (including social charges)	(0.2)	(0.5)	–	(0.7)
Headline operating profit/(loss)	23.8	32.2	(0.4)	55.6
Amortisation of acquired intangible fixed assets	(0.3)	(1.2)	–	(1.5)
Segment result	23.5	31.0	(0.4)	54.1

Automotive & General Industrial	Western Europe £m	North America £m	Emerging markets £m	Total AGI £m
	Year ended 31 December 2016			
Revenue				
Total revenue	214.9	94.3	40.5	349.7
Result				
Headline operating profit prior to share-based payments	36.8	10.7	10.4	57.9
Share-based payments (including social charges)	0.4	0.1	0.1	0.6
Headline operating profit	37.2	10.8	10.5	58.5
Amortisation of acquired intangible fixed assets	(0.4)	(2.6)	–	(3.0)
Operating profit prior to exceptional items	36.8	8.2	10.5	55.5
Acquisition costs	(0.4)	(0.2)	–	(0.6)
Segment result	36.4	8.0	10.5	54.9

2 Business and geographical segments (continued)

Alternative performance measures

Bodycote uses various alternative performance measures (APMs), in addition to those reported under IFRS, as management believe these measures enable users of the financial statements to assess the underlying trading performance of the business. The APMs used include headline operating profit, headline earnings per share, headline profit before taxation, headline operating cash flow and free cash flow, together with current measures of revenue restated at constant exchange rates. These measures reflect the underlying performance of the business as they exclude the impact of amortisation of acquired intangible assets, exceptional items and the impact of foreign exchange movements.

The constant exchange rate comparison uses the current year reported segmental information, stated in the relevant functional currency, and translates the results into the presentational currency using the prior year's monthly exchange rates.

APMs are defined and reconciled to the IFRS statutory measures as follows:

- Headline operating profit and headline profit before taxation are defined in the Financial highlights section;
- Headline operating cash flow is reconciled in the Financial overview;
- Headline earnings per share is reconciled in note 5;
- Free cash flow is defined and reconciled in the Financial overview; and
- Revenue and headline operating profit at constant exchange rates are reconciled to revenue and headline operating profit in the table below.

	Half year to 30 June 2017			
	ADE £m	**AGI £m**	**Central costs and eliminations £m**	**Consolidated £m**
Revenue	**136.1**	**209.6**	**–**	**345.7**
Constant exchange rates adjustment	**(11.7)**	**(18.8)**	**–**	**(30.5)**
Revenue at constant exchange rates	**124.4**	**190.8**	**–**	**315.2**
Headline operating profit	**30.7**	**36.9**	**(5.9)**	**61.7**
Constant exchange rates adjustment	**(2.7)**	**(3.2)**	**0.1**	**(5.8)**
Headline operating profit at constant exchange rates	**28.0**	**33.7**	**(5.8)**	**55.9**

3 Provisions

	Restructuring £m	Restructuring environmental £m	Environmental £m	Total £m
1 January 2017	**6.7**	**6.6**	**7.2**	**20.5**
Increase in provision	**–**	**–**	**1.3**	**1.3**
Release of provision	**(0.3)**	**–**	**–**	**(0.3)**
Utilisation of provision	**(1.6)**	**(0.7)**	**(0.2)**	**(2.5)**
Exchange difference	**(0.1)**	**(0.2)**	**(0.3)**	**(0.6)**
30 June 2017	**4.7**	**5.7**	**8.0**	**18.4**
Included in current liabilities				**10.0**
Included in non-current liabilities				**8.4**
				18.4

The restructuring provision relates to the costs associated with the closure of a number of Heat Treatment sites.

The Group provides for the costs of environmental remediation that have been identified, either as part of acquisition due diligence, or in other circumstances where remediation by the Group is required. This provision is reviewed annually and is separated into restructuring environmental and environmental to identify separately environmental provisions relating to restructuring programmes from those arising in the ordinary course of business.

The majority of cash outflows in respect of these liabilities are expected to occur within five years.

Whilst the Group's use of chlorinated solvents and other hazardous chemicals continues to reduce, the Group remains exposed to contingent liabilities in respect of environmental remediation liabilities. In particular, the Group could be subjected to regulatory or legislative requirements to remediate sites in the future. However, it is not possible at this time to determine whether and to what extent any liabilities exist, other than for those recognised above. Therefore, no provision is recognised in relation to these items.