Melrose

Buy
Improve
Sell

Strictly private and confidential

Melrose Industries PLC

Full Year Results

Twelve months to 31 December 2017

20 February 2018

Contents

Sections

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Highlights

Highlights in 2017

£m	Underlying[1] results	Statutory results
Revenue	**2,092.2**	**2,092.2**
Operating profit/(loss)	**278.4**	**(6.9)**
Profit/(loss) before tax	**257.7**	**(27.6)**
Diluted earnings per share	**9.8p**	**(1.2)p**

- Nortek underlying[1] results are better on all measures; revenue growth is 2%[2] with increased momentum in the second half of the year when sales were up 4%[2], the operating margin is 15.2%, operating profit is up 52%[3] on last year and up 67%[3] on the last full year prior to acquisition
- The underlying[1] results are a key measure of performance and are shown alongside the statutory results. As 2017 was the first full year of Nortek ownership by Melrose, significant restructuring costs were incurred and, following the structural decline of the core gas turbine market for Brush, its balance sheet value has been reduced to £300 million. These two items are included in the adjustments made between statutory and underlying[1] results
- Consultations with employees have commenced to implement a restructuring plan which, when complete, will position Brush well for the future
- Cash generation is strong, with a record performance from Nortek. Net debt was £572 million representing leverage of 1.9x[4] underlying[1] EBITDA[5], significantly lower than at the time of the Nortek acquisition only sixteen months previously
- In line with the Melrose strategy, advisors have been appointed to confirm the appropriate future process and timetable for the disposal of Ergotron, Inc
- The proposed final dividend of 2.8 pence (2016: 1.9 pence) per share together with the interim dividend of 1.4 pence (2016: 0.3 pence[6]) results in a 91% increase in the full year dividend of 4.2 pence per share (2016: 2.2 pence[6])

Chris Miller, Executive Chairman said:

"We are delighted with the performance Nortek is achieving freed from the previous culture of 'head office knows best'. Substantial long-term value is being created with significant investment in new technology, new products and operations. Brush is implementing a restructuring plan to reflect its changed market place which will position it well for the future. We are convinced that GKN would gain significantly from becoming part of an enlarged £10 billion UK industrial powerhouse, benefitting from the proven Melrose operating model."

1. Considered by the Board to be a key measure of performance. A reconciliation of the statutory result to underlying performance is given on slide 7
2. At constant currency and adjusting revenue growth for exited sales channels
3. Adjusted for constant currency. Using the 2016 underlying[1] profit of $241.0 million from the audited financial statements used for the Step Up to the Premium List and using the 2015 underlying[1] operating profit of $220.1 million from the circular produced for the acquisition of Nortek
4. Using net debt at average exchange rates
5. Underlying[1] operating profit before depreciation and amortisation
6. 2016 interim dividend adjusted to include the effects of the 2016 Rights Issue

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Summary financial results

Income Statement

Full year to 31 December 2017

Continuing operations	£m
Revenue	2,092.2
Operating loss	(6.9)
Loss before tax	(27.6)
Tax	3.7
Loss after tax	(23.9)
Underlying[1] operating profit	278.4
Underlying[1] profit before tax	257.7
Underlying[1] profit after tax	190.9
Underlying[1] diluted earnings per share	9.8 pence

- Full statutory numbers are followed by the underlying[1] numbers which the Melrose Board believes to be a key measure of trading performance

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1. Considered by the Board to be a key measure of performance. A reconciliation of the statutory result to underlying performance is given on slide 7

Reconciliation of statutory results to underlying performance

- A reconciliation of the statutory results to the underlying performance

	£m
2017 statutory loss before tax	(27.6)
Impairment of Brush assets	144.7
Amortisation of intangible assets	81.4
Restructuring costs	35.0
Acquisition and disposal costs	5.8
Melrose equity-settled compensation scheme (LTIP)	24.2
Release of fair value items	(5.8)
2017 underlying profit before tax	257.7

- Items excluded from underlying results are significant in size or volatility or by nature are non-trading or non-recurring, or any item released to the income statement that was previously a fair value item booked on acquisition
- Impairment charges of £144.7 million in the Brush business, including closure of Brush China
- Restructuring charges of £35.0 million, primarily in respect of Nortek

Restructuring costs	£m
Air Management	19.0
Security & Smart Technology	6.7
Ergonomics	2.1
Nortek central	1.3
Brush	5.9
Total	**35.0**

2017 underlying[1] operating results by division

£m	Air Management	Security & Smart Technology	Ergonomics	Energy
Revenue	1,159.6	440.7	272.9	219.0
Underlying[1] operating profit	146.1	70.7	69.6	17.5
Underlying[1] operating margin	12.6%	16.0%	25.5%	8.0%
Revenue growth[2,3]	+3%	+2%	-3%	-14%
Underlying[1] operating profit growth[2,3]	+55%	+49%	-6%	-47%
Underlying[1] margin increase[2,3]	+4.8ppts	+5.0ppts	-0.8ppts	-5.0ppts

- Nortek Group underlying[1] operating profit of £284.3 million, 52%[2,3] higher than last year and 67%[2,4] higher than 2015
- Nortek Group underlying[1] operating margin has increased from 9.7% to 15.2%, a rise of 5.5 percentage points
- Increased Nortek sales momentum in the second half of the year when sales were up 4%[2] compared to the second half of 2016
- Brush market conditions have worsened, action being taken. Restructuring cash cost expected to be c.£40 million and expected to mitigate current £12 million annual losses of the Turbogenerators business and align it to the new market conditions
- The underlying[1] operating profit in Brush of £17.5 million included £2.1 million of losses incurred within the Brush China factory prior to closure

1. Considered by the Board to be a key measure of performance. A reconciliation of the statutory result to underlying performance is given on slide 7
2. At constant currency and adjusting revenue growth for exited sales channels
3. Full year 2017 results compared with full year 2016 results. Nortek's results for last year are based on the Nortek 2016 full year revenue of $2,480.7 million and underlying operating profit of $241.0 million as reported in the audited financial statements used for the Step Up to the Premium Listing of the London Stock Exchange
4. Full year 2017 results compared with full year 2015 results, using the 2015 underlying[1] operating profit of $220.1 million included in the circular produced for the Nortek acquisition

Foreign exchange → forward looking

	2017		2016	
	USD	CNY	USD	CNY
12 month average rates	1.29	8.71	1.36	8.99
4 month average rates (Sep – Dec)	n/a	n/a	1.26	8.56
Closing rates	1.35	8.80	1.23	8.57

On-going sensitivity of profit to translation and unhedged transaction exchange risk £m	Increase/(decrease) in underlying[1] operating profit
For every 10 percent strengthening of the USD	27.3
For every 10 percent strengthening of the CNY	(4.7)

On-going sensitivity of profit to translation and full transaction exchange rate risk £m	Increase/(decrease) in underlying[1] operating profit
For every 10 percent strengthening of the USD	31.9
For every 10 percent strengthening of the CNY	(23.8)

- Significant profit sensitivity to US Dollar exchange rate

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Summary financial results

Cash performance

Strong cash generation, significant investment

£m	Group FY 2017	Nortek	Brush
Underlying[1] operating profit	278.4	284.3	17.5
Depreciation	34.7	25.5	9.2
Working capital movement	(16.1)	(17.4)	1.8
Operating cash flow (pre capex)	**297.0**	**292.4**	**28.5**
EBITDA[2] profit conversion to cash (pre capex) %	**95%**	**94%**	**107%**
Net capital expenditure	(48.8)	(46.3)	(2.5)
Operating cash flow (post capex)	248.2	246.1	26.0
Net interest and net tax paid	(30.7)	(15.1)	(0.5)
Defined benefit pension contributions	(4.2)	(4.1)	(0.1)
Incentive scheme tax related payments (including employer's tax)	(147.9)	-	-
Restructuring	(48.6)	(43.9)	(4.7)
Other	(31.8)	(21.5)	(1.2)
Cash generated from trading (after all costs including tax)	**(15.0)**	**161.5**	**19.5**

Underlying[1] profit conversion to cash	
Air Management	97%
Security & Smart Technology	86%
Ergonomics	103%
Nortek Group	94%
Brush	107%

- Good cash performance in 2017
- Underlying[1] profit conversion to cash of 95% for the Group
- Group leverage of 1.9x[3] significantly lower than at the time of the Nortek acquisition sixteen months ago
- Net cash capital investment of 1.8x depreciation in Nortek
- The defined benefit pension contributions were lower than last year because, following the disposal of Elster, the contribution schedule for the Brush pension scheme was paid early in 2016

1. Considered by the Board to be a key measure of performance. A reconciliation of the statutory result to underlying performance is given on slide 7
2. Underlying[1] operating profit before depreciation and amortisation
3. Net debt at average exchange rates divided by underlying[1] EBITDA[2]

Balance Sheet – working capital, capital expenditure, tax

£m	31 Dec 2017
Fixed assets, intangible assets and goodwill	2,456.5
Net working capital	241.0
Pensions and retirement benefits	(17.6)
Provisions	(209.8)
Deferred tax and current tax	(26.2)
Other	13.1
Net debt	(571.8)
Net assets	**1,885.2**

- Significant capital investment into Nortek, more benefits to come
- The main Brush UK defined benefit scheme is in surplus due to being funded properly under Melrose ownership
- Underlying[1] tax rate of 26%. 2018 expected to be 24%
- Net debt of £571.8 million, equal to 1.9x[2] EBITDA[3]

Working capital

£241.0m

Working capital is 12% of revenue

Capital expenditure - Nortek

1.8x dep'n

Significant capital investment into Nortek

Tax

26%

Underlying[1] tax rate

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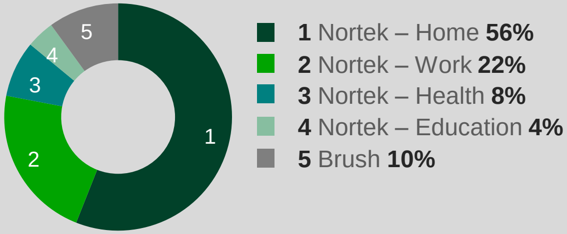
Summary of operating divisions

- Nortek
- Brush

Revenue by end market



Nortek

90% of Melrose[1]

Nortek is a global, diversified group which manufactures innovative air management, security, home automation and ergonomic and productivity solutions

1. Based on 2017 revenue for all continuing businesses

Nortek

NORTEK

- Nortek trading has been transformed more comprehensively and faster than envisaged at the time of acquisition
- Second half performance stronger than the first half
- Underlying[1] operating margins in excess of 15%, being the original three to five year aim at the time of acquisition
- Underlying[1] operating profit up 52%[2,3] and margin up 5.5ppts[3]

	Underlying[1] operating margin achieved	Underlying[1] profit growth v last year[2,3]	Underlying[1] margin growth v last year[2,3]	Underlying[1] profit conversion to cash
Nortek Group	15.2%	+52%	+5.5ppts	94% (104% since acquisition)
Air Management	12.6%	+55%	+4.8ppts	
Security & Smart Technology	16.0%	+49%	+5.0ppts	
Ergonomics	25.5%	-6%	-0.8ppts	

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Nortek

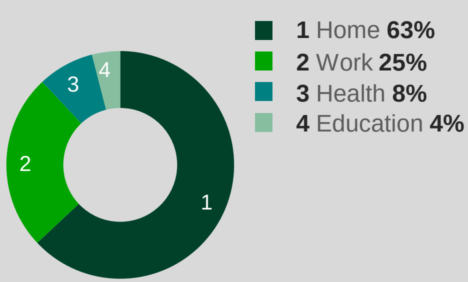
NORTEK

Nortek – underlying[1] results

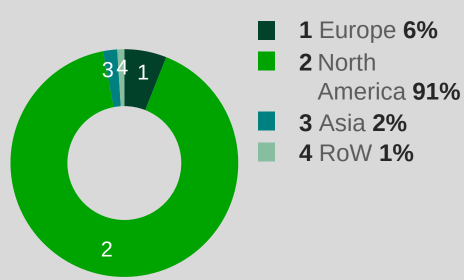
£m	Nortek Group[5] FY 2017	Nortek Group[5] Growth[3,4]	Air Management FY 2017	Air Management Growth[3,4]	Security & Smart Technology FY 2017	Security & Smart Technology Growth[3,4]	Ergonomics FY 2017	Ergonomics Growth[3,4]
Revenue	1,873.2	**+2%**	1,159.6	**+3%**	440.7	**+2%**	272.9	**-3%**
Underlying[1] EBITDA[2]	309.8	**+40%**	165.0	**+41%**	73.8	**+41%**	72.4	**-6%**
Underlying[1] EBITDA[2] margin %	16.5%	**+5.1ppts**	14.2%	**+4.6ppts**	16.7%	**+4.6ppts**	26.5%	**-0.9ppts**
Underlying[1] operating profit	284.3	**+52%**	146.1	**+55%**	70.7	**+49%**	69.6	**-6%**
Underlying[1] operating margin %	15.2%	**+5.5ppts**	12.6%	**+4.8ppts**	16.0%	**+5.0ppts**	25.5%	**-0.8ppts**

- Underlying[1] operating profit up 52%[3,4] and underlying[1] operating margin up 5.5ppts
- Significant margin improvement in Air Management and Security & Smart Technology businesses
- Many actions completed and more underway to improve performance

Revenue by end market



Revenue by geographical destination



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4. Full year 2017 results compared with full year 2016 results. Nortek's results for last year are based on the Nortek 2016 full year revenue of $2,480.7 million, underlying operating profit of $241.0 million, depreciation of property, plant and equipment of $34.7 million and amortisation of computer software of $8.6 million as reported in the audited financial statements used for the Step Up to the Premium Listing of the London Stock Exchange
5. Includes Nortek central costs

Nortek – actions achieved and underway

NORTEK

Air Management

Management changes

Further consolidation of the two HVAC businesses into one management team

Appointment of a new CEO for the AQH business

Investment

Significant capital investment at HVAC facilities including over £12m of investment across the NAS manufacturing base to increase the capacity of its clean room, premium air handler and healthcare operating room capabilities and over £9m for new machinery and updated technologies for Residential and Light Commercial facilities

Significant investment in the R&D centre in Saskatoon

Investment in AQH of over £16m to improve manufacturing processes and introduce more automation. Expanded distribution and warehouse operations at Hartford

Exiting of lower margin sales channels

Exit of unprofitable sales in South America and company owned retail outlets in the US

Sale of loss-making Best EMEA operations

Restructuring and cost reductions

Commercial HVAC head office closed and consolidated into single HVAC head office in St Louis

Closure of the Folkestone facility and relocation to Brierley Hill

Rationalisation of manufacturing footprint within the AQH business including the planned closure of the Mississauga facility and relocation of production to Hartford and Drummondville

Decentralising of functions

Warehouse and distribution functions brought in-house

Security & Smart Technology

Management changes

Consolidation of Security & Smart Technology under one management team incorporating Nortek Security & Control, Core Brands and GTO Access Systems

Investment

Investment in the development of touchscreen security panel ahead of a major new product launch

Investment in Cloud based service platform

Restructuring and cost reductions

Closure of the Hong Kong office, warehouse consolidation and reorganisation of engineering

Planned move to new Carlsbad location to allow greater consolidation of Security & Smart Technology back office, including combined operations, engineering and finance

Decentralising of functions

Warehouse and distribution functions brought in-house

Ergonomics

Investment for growth

Investment for tooling to enter the large furniture market, insertion machines and new healthcare carts

Expansion into digital sales channels and new geographical markets

Exiting of lower margin sales channels

Ongoing review and discontinuance of lower margin products and lines

Decentralising of functions

Warehouse and distribution functions brought in-house

Brush

10% of Melrose[1]

Brush Turbogenerators is a market leading independent manufacturer of electricity generating equipment for the power generation, industrial, oil & gas and offshore sectors

1. Based on 2017 revenue for all continuing businesses

Brush

Brush – underlying[1] results

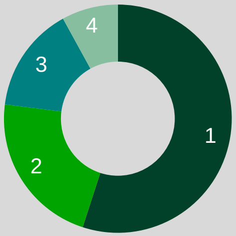
	Brush	
£m	FY 2017	Growth[3]
Revenue	219.0	**-14%**
Underlying[1] EBITDA[2]	26.7	**-37%**
Underlying[1] EBITDA[2] margin %	12.2%	**-4.5ppts**
Underlying[1] operating profit	17.5	**-47%**
Underlying[1] operating margin %	8.0%	**-5.0ppts**
Order intake	*220.9*	***-3%***
Book to bill %	*101%*	

- Structural decline in core turbogenerator market
- Brush sales of generators reduced from 2012 peak of 208 generators, approximately 50 expected in 2018
- Restructuring action underway which will strengthen Brush
- Underlying[1] operating profit of £17.5 million included £2.1 million of losses incurred within the Brush China factory prior to closure

Revenue by end market

£m	FY 2017	Growth[3]
Generators[4]	70.2	**-33%**
Aftermarket	76.0	**+1%**
Switchgear	47.5	**+7%**
Transformers	25.3	**-18%**
Total	**219.0**	**-14%**

Revenue by geographical destination



1 Europe **55%**
2 North America **22%**
3 Asia **15%**
4 RoW **8%**

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2. Operating profit before depreciation and amortisation
3. At constant currency
4. Includes Harrington Generators International

Brush restructuring for new market conditions

- Previously announced structural market changes caused by global environmental policy
- Fall in gas turbine market volumes of >60% from 2011 peak
  - Brush's turbogenerator sales fallen from 122 units in 2016 to c.50 expected in 2018
- Entered into a consultation with employees in relation to restructuring Turbogenerators:
  - Closure of Ridderkerk (Netherlands) production facility and transfer of 4-pole production facility to Czech Republic
  - Changshu (China) factory has already been closed
  - Entry into consultation process in respect of 2-pole turbogenerator production at Loughborough
- Cash cost of restructuring c.£40m - expected to be materially complete in 2018
- Expected to mitigate £12m annual losses of the Turbogenerators business and to align to new market conditions
- Carrying value of Brush reduced to £300m
- Melrose remains fully committed to supporting management to be positioned for best possible long-term future

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Questions