

Chairman's Letter to GKN Shareholders



Incorporated and registered in England and Wales with Registration No. 9800044

Directors:

Christopher Miller (*Chairman*)
David Roper (*Vice-Chairman*)
Simon Peckham (*Chief Executive*)
Geoffrey Martin (*Group Finance Director*)
Justin Dowley (*Non-executive Director*)
Elizabeth Hewitt (*Non-executive Director*)
David Lis (*Non-executive Director*)
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1 February 2018

Dear Shareholder

It is my pleasure to write to you in my role as both Chairman and co-founder of Melrose. I would like to take this opportunity to introduce Melrose and explain the background to our offer for GKN and why we are very excited about this opportunity to merge our two businesses.

As we announced on 17 January 2018, as a GKN shareholder, you will receive:

81 pence in cash
and 1.49 New Melrose Shares
for each GKN Share you hold

Based on yesterday's Melrose closing share price of 226.4 pence, the value of the shares you will receive under our offer is 337.3 pence. Therefore, together with the 81 pence in cash, our offer represents a total value of 418.3 pence per GKN share. This is the highest price that GKN has ever traded in the past 10 years (the 10 year average is in fact 243.0 pence per share). Since we

approached your Board, the GKN share price has risen from 326.3 pence to 422.8 pence today, which has already created approximately £1.7 billion of value for you.

We have intentionally structured our offer in such a way as to allow GKN shareholders to benefit in what we are confident will be a significant value creation opportunity. If you accept our offer we can together create a UK engineering and industrial powerhouse worth over £10 billion today in which GKN shareholders would be majority owners.

Since Guest Keen & Co acquired Nettlefolds in 1902, GKN has been involved in many businesses. At the beginning of the 1980s it employed approximately 69,000 people in the UK alone. Today that number is nearly 6,000. GKN also employs over 50,000 people outside the UK and its employees work hard to achieve market leading positions in many of its businesses around the world. However, in recent times it has become clear that the company is underperforming its potential and its competitors. Indeed, your Board has admitted as much publicly. We believe that, unless this underperformance is rectified, GKN, like other UK manufacturing companies before it, will continue to fail to achieve its potential for the benefit of customers, shareholders, employees, pensioners and the UK economy.

Over the following pages we explain the rationale of our offer, how as a management team we will re-energise and re-purpose the GKN businesses and why we believe we are best equipped to deliver that value to you.

Introducing Melrose and our strategy

I recognise that many of you may not have come across Melrose before our interest was made public, so I would like to take this opportunity to introduce ourselves and our philosophy.

My colleagues and I set up Melrose in 2003 with the primary objectives of transforming the fortunes of the companies we own and creating shareholder value in doing so. We are a UK premium public company listed on the London Stock Exchange, registered in Birmingham and led by a long-standing British management team with decades of experience. We specialise in acquiring good engineering companies, with strong market positions, which are underperforming their potential. Our objective is to look for opportunities where we are able to at least double shareholders' investments over a three to five year time scale.

We have always put our faith in public markets. We are not "private equity". Unlike many private equity companies, we are committed to improving our businesses through a focus on operations and do not use financial engineering; we do not rely on debt to boost returns and use only modest levels of leverage.

We apply our time-tested approach of delivering operational improvements, empowering management and investing heavily, to unlock potential for the benefit of all stakeholders – shareholders, employees, customers and pensioners included. On average, in the first five years of acquisition, we have invested an additional amount equivalent to a third of the original equity purchase price of our businesses in order to strengthen and grow them through investment in research and development, capital equipment to improve manufacturing efficiencies and bolt-on acquisitions that would benefit the businesses.

Our acquisition philosophy is to invest in research and development; at Elster and Nortek this has meant an R&D investment of approximately 4% of sales over the last five years, equating to over £230 million. As a result of our approach, we have overseen strong improvements across all of our businesses.

We also pursue strategic acquisitions to enhance our existing businesses, and, having successfully completed two of the largest institutional fund raisings for acquisitions in the UK over the last five years, we are confident that, if required to develop GKN through further acquisitions, we are better placed to do so than your existing Board.

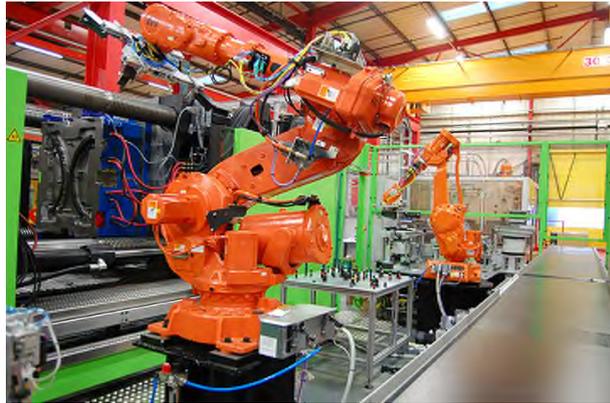
Our philosophy is to return the value created to shareholders in the form of cash distributions. We have already returned £4.3 billion to our shareholders, who continue to own a business with a market capitalisation today of £4.4 billion. It is pleasing that the beneficiaries of this value creation include the shareholders of previous acquisitions we have made.

Our track record

Over the last fifteen years, we have carried out four major acquisitions (with each acquisition typically comprising multiple businesses). We have nearly completed the full Melrose strategy cycle on the first three (McKechnie/Dynacast, FKI and Elster) and are making excellent progress on our most recent acquisition, Nortek, which is partly reflected in our market capitalisation.

May 2005: McKechnie/Dynacast

Our first acquisition was the combined McKechnie and Dynacast business, headquartered in Alcester, UK which we acquired from Cinven for £429 million, with Cinven becoming a 15% shareholder and a participant in future value creation.



As part of the acquisition process, to strengthen the businesses we deliberately and significantly reduced the leverage in

McKechnie/Dynacast from approximately £690 million to approximately £190 million (from 10.3x to 2.9x EBITDA) in order to facilitate substantial further investments (capital expenditure was equivalent to 1.0x depreciation) and to enable contributions at the appropriate rate into the pension schemes.

McKechnie is a supplier of specialist engineered components to the global aerospace industry. During our ownership we improved operating margins at McKechnie from 18% to 24% by optimising its cost base and focusing on profitable business.

Dynacast is a global provider of precision die cast components for a wide variety of industries including automotive, healthcare, consumer electronics, computers and peripherals. During our ownership we improved operating margins at Dynacast from 11% to 16% by successfully aligning capacity with customers and installing a success-driven organisational culture.

Overall we generated over £700 million in cash from the businesses versus an equity investment of approximately £240 million, resulting in a return of 3.0x on shareholders' investment. This includes direct returns to shareholders after disposals of £220 million in 2007 and £373 million in 2011. Cinven more than doubled the value of its investment in Melrose in the space of six months after the acquisition.

As you will see below, the McKechnie pension scheme was fully funded under our ownership and ultimately transferred to Honeywell, backed by a parent company guarantee.

July 2008: FKI

Our second acquisition was FKI, a UK publicly-listed conglomerate, which we acquired for approximately £1 billion. This comprised a number of diverse businesses and was, at the time, more than double the size of Melrose. Our offer for FKI was structured as approximately 50% in cash and 50% in new Melrose shares allowing the FKI shareholders to participate in the value creation potential.



As part of the acquisition process, to strengthen the businesses we deliberately reduced the leverage in FKI from approximately £470 million to approximately £340 million (from 3.7x to 2.7x EBITDA) in order to facilitate substantial further investments (capital expenditure was equivalent to 1.4x depreciation) and to enable contributions at the appropriate rate into the pension schemes.

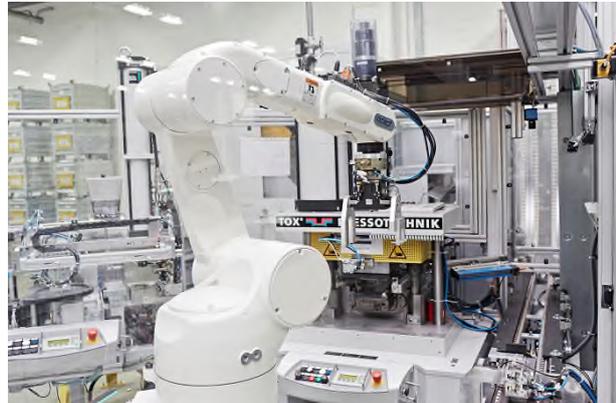
Our improvement initiatives were centred around refocusing the FKI conglomerate to allow each of its businesses to stand alone and making necessary investments to strengthen their market positions. We improved operating margin from 10% to 15% under our ownership and have since sold all of the businesses with the exception of Brush.

Overall we generated over £1.4 billion in cash from the businesses versus an equity investment of approximately £500 million, resulting in a return of 2.9x on shareholders' investment. This includes direct returns to shareholders after disposals of £595 million in 2014 and £200 million in 2015.

As you will see below, the FKI pension scheme was appropriately funded, and the main UK defined benefit scheme (excluding the Brush scheme, which is currently in surplus) was ultimately transferred to Honeywell, backed by a parent company guarantee.

August 2012: Elster

Elster, the most recent acquisition to have completed its improvement cycle, was a US publicly-listed, German-based manufacturer of meters operating through three separate divisions with different markets and drivers (Gas, Electricity, Water). Elster is a global company with presence in 135 countries, large contracts, long-standing customers and was on the cusp of a technology revolution with smart metering.



The business had lost its focus and identity with a centralised head office causing inefficiencies and issues for the businesses. We identified an opportunity and acquired Elster in 2012 for £1.8 billion, including £1.2 billion of equity (which was one of the largest equity raises in the UK market at the time).

Under our ownership we oversaw operating profit margins increase from 13% to 22%, representing a 70% improvement in just three years.

This was achieved by focusing each business on performance, end markets, customers and operations. We significantly expanded on an optimisation programme announced by Elster before our acquisition and significantly exceeded expectations.

As with FKI, we followed our approach of focusing on operational efficiencies and exiting loss-making sales first, followed by production optimisation and a focused investment programme (capital expenditure was equivalent to 1.3x depreciation), particularly in R&D as Elster was growing its “smart” capabilities.

In December 2015 we sold all three businesses as a package to Honeywell for £3.3 billion, representing approximately 14x 2014 headline EBITDA, and in February 2016 we returned £2.4 billion in cash to shareholders.

Overall we generated over £2.5 billion in cash from Elster versus an equity investment of approximately £1.2 billion, resulting in a return of 2.3x on shareholders’ investment.

August 2016: Nortek

Our most recent acquisition was Nortek, a global, diversified group which manufactures innovative air management, security, home automation and ergonomic and productivity solutions.



Nortek was a US publicly-listed company which we acquired in August 2016 for £2.2 billion with £1.6 billion in equity raised from our very supportive shareholder base. We

are only 18 months into our investment journey and Nortek is already responding well to the Melrose model having posted record results as at the half year and becoming the quickest turnaround in our history. The value of Nortek is partly reflected in our market capitalisation which is approximately £4.4 billion.

As part of the acquisition process we significantly reduced the leverage in Nortek from approximately \$1.4 billion to approximately \$670 million (from 5.1x EBITDA to approximately 2.5x EBITDA).

Having decentralised the business to free it from bureaucracy and reorganised it into three divisions (Air Management, Security and Smart Technology and Ergonomics), underlying profit is up approximately 50% in the first full year and approximately 65% when compared to the last full year prior to our acquisition. Nortek is now recording underlying operating margins of

approximately 15%, a full 5 percentage points of improvement.



The full benefits of our ongoing investments at a rate of 2.0x depreciation to implement the necessary improvement programmes are still unfolding alongside further improvements planned for 2018 as we look to maintain the pace of change in order to deliver further value for

shareholders.

We measure our success by the value that we deliver to shareholders. Overall, since Melrose's first acquisition in 2005, we have generated a total net shareholder value increase of £4.9 billion and have returned £4.3 billion of cash to shareholders.

Shareholders who invested £1 with us on our first acquisition, would now have approximately £18. In contrast, shareholders who invested £1 with GKN in 2005, or at the time of our first deal, would now own an investment worth approximately £3.34.

Over the same period, we have achieved a total shareholder return of over 3,000%, compared to an average of approximately 230% across the FTSE 350 constituents, making us the third best performer in the index while GKN is in 227th place.

Our plans to unlock GKN's potential

We believe that our team can bring about a transformation of GKN to unlock its full potential for the benefit of shareholders, employees, pensioners and customers alike. We will replicate our proven approach by supporting GKN's operational management to transform, invest in and grow their businesses. We consider a change of control is a vital first step needed to allow for this transformation.

We expect to re-energise and re-purpose GKN's operations to enable them to exceed GKN's own top-end group trading margin target of 10%¹. We believe that we can deliver significantly greater benefits to the shareholders of GKN than GKN could otherwise achieve on its own.

As part of our plan we will exit low margin sales over time, ensure appropriate costs and invest in operations to improve efficiencies so as to achieve improved profit growth, increased operating margins and strong profit conversion to cash. Melrose has already identified several immediate actions which it expects to implement which comprise: head office restructuring and consequent simplification of the management structure; change of culture to focus on performance and reduced cost base; focus on profitability, not sales; investment in operations to produce return rather than growth only; return management focus back to the business by changing incentives and ensuring targets are delivered; and fast economic-based decision making to create a speedy, flat and non-bureaucratic organisation.

To put the opportunity in context, if GKN simply achieved its divisional target margins in 2017 it would exceed consensus trading profit for 2017 by approximately £300 million (equivalent to approximately 40% of 2017 consensus trading profit).

While GKN has spent £3.2 billion on capital expenditure and acquisitions in the last five years (equivalent to approximately 50% of GKN's market capitalisation prior to approach), it has failed to translate this into margin improvement with full year 2017 group trading margin expected to be at the same level as it was back in 2011, below the low-end group trading margin target of 8%.

¹ This statement is not and is not intended as a profit forecast or a Quantified Financial Benefits Statement for the purposes of Rule 28 of the City Code and should not be interpreted as such.

In some cases GKN's business requires working with Governments and Regulators on security and other matters. As an established UK public company with relevant experience, we fully recognise our requirements in this regard and have no doubt that this is completely compatible with our approach.

Simplify and declutter GKN's business to drive improvement

Our philosophy is to simplify and declutter the businesses that we own. As previously announced, we expect to sell certain smaller businesses in the Aerospace and Driveline divisions, which we deem to be non-core, once they have been improved. By first improving these non-core businesses, we will ensure they deliver more, not less, value to their trusted customers both before and after any sale. Our margin improvement expectations are reliant on changing the internal ways of working within GKN, and not on altering the relationships with GKN's main customers.

We think it would be wrong to sell the Powder Metallurgy business or any of the other major businesses at this time given the substantial scope to improve them. However, we do think it would be appropriate, once improved, to consider a disposal of the Powder Metallurgy business in the medium term. Upon the disposal of Powder Metallurgy, consistent with its strategy, the Melrose Board intends to return the net proceeds to shareholders, taking into account the interests of all stakeholders including the GKN pension schemes.

With regard to the other businesses, Melrose has stated there is large scope to improve their performance. Melrose's typical timetable for achieving this improvement is a three to five year time horizon, although we consider GKN to be at the longer end of this scale. Once the businesses have been improved, Melrose will take the best course of action for all stakeholders, taking into account the unique requirements of each. Clearly this could include publicly listing any of these businesses on the London Stock Exchange as well as fund raising for appropriate strategic acquisitions to increase the market presence of these businesses.

Melrose believes that due to its current culture and leadership, GKN is not equipped to develop its businesses to their full potential. It believes that merging Melrose and GKN into a new combined entity is by far the best answer for GKN's shareholders, employees, customers and pensioners.

We do not intend any hasty separation of the Automotive and Aerospace businesses. We strongly believe that both businesses need investment and improvement and that any actions to immediately separate the businesses in preparation for a sale of one or the other would be value destructive. We expect GKN management to provide more clarity on their intentions in this regard in their forthcoming defence document, having stated on 12 January that they intend to separate the businesses.

Strengthen GKN's pension position

Melrose has been a good steward of pension schemes of the companies it has owned and is committed to looking after all stakeholders. The key pillars of our strategy are (i) to maintain

professional relationships with the trustees, (ii) to put in place on-going deficit reduction programmes, (iii) to maintain prudent levels of leverage and (iv) to implement one-off actions to de-risk liabilities when there is a window of opportunity to do so.

Our track record includes McKechnie (£0.2 billion liability which we improved from 58% funded to fully funded since acquisition) and FKI (£0.8 billion liability which we improved to 99% funded since acquisition). We transferred the majority of our defined benefit pension liabilities (£0.9 billion) to Honeywell, the US-listed multinational with a market capitalisation of over \$100 billion, as part of the sale of Elster in 2015. This led to a material improvement in the employer covenant for the scheme members because we negotiated a parent company guarantee from Honeywell for the pension scheme. The pension scheme in our Nortek business is well-funded while the scheme in our Brush business is now deficit free.

We confirm it is our intention to make a substantial voluntary cash contribution of £150 million to the GKN pension schemes within 12 months of the completion of our Offer. As Melrose's experience above has shown, the Melrose Board have the expertise to manage GKN's substantial defined pension liabilities for the benefit of pensioners as well as shareholders.

Value creation in action

Since we approached your Board, £1.7 billion of value has already been created as the GKN share price has risen from 326.3 pence to 422.8 pence today, an increase of 30% since we made our approach. The Melrose share price has also risen from 217.6 pence to 226.4 pence, which is an early indicator of the value of the Enlarged Group. Shareholders will benefit from further value creation given you would own the majority of Melrose's current businesses. In addition you will receive the immediate cash payment of £1.4 billion in respect of the 81 pence per share cash portion of the offer. In order to increase your participation in Melrose and therefore the anticipated value creation, you could choose to reinvest the 81 pence per share you receive directly into Melrose shares or alternatively take advantage of the mix and match facility that is being made available to you.

As I have explained above, our strategy is to realise the value of businesses once they have been improved. We expect to realise the value of our Nortek business over the next two to three years. If proceeds were equal to our market capitalisation today then approximately £2.5 billion of cash would be returned to you and your fellow GKN shareholders as majority holders in the business. This is in addition to the immediate cash payment of £1.4 billion referred to above and your retained majority shareholding in the merged group.

We are proud of our track record of providing shareholders with exceptional returns on equity on all our previous acquisitions and expect to repeat this success here.

Summary

It is accepted by your Board that GKN is in need of fundamental change.

Ultimately you as a GKN shareholder are faced with the choice between two management teams: the incumbent team at GKN or the Melrose team who have decades of experience of successfully turning around businesses. I believe that our team is uniquely qualified to make the changes needed at GKN and that a change of control is a necessary first step to unlocking the potential that exists within GKN that has been missed for so many years.

We are fully committed and prepared to deliver on this opportunity. As substantial shareholders ourselves (the Melrose Board owns approximately 3.7% of Melrose) we are highly motivated to continuing to deliver superior returns for shareholders.

Recommendation

Under our Offer of 418.3 pence per share, valued as at yesterday's close, you would receive 81 pence per share in cash and an investment in Melrose worth 337.3 pence per share, representing a premium of approximately 28% to the GKN share price before we made our approach.

Together we have the opportunity to build a better and stronger business, creating a UK-listed manufacturing powerhouse worth in excess of £10 billion today. Our Offer will give you the shareholders the opportunity to participate in the creation of considerable value from both the GKN and the Melrose businesses.

Our long-term track record clearly demonstrates the scale of the transformation we can make at GKN. We believe that we are the best team to achieve this and would welcome the opportunity to deliver this value for you.

We invite you to accept our Offer.

Yours sincerely

Handwritten signature of Christopher Miller in black ink.

Appendix

SOURCES OF INFORMATION AND BASES OF CALCULATION

1. The value of the shares that a GKN Shareholder will receive under our Offer of 337.3 pence per GKN Share held is calculated by multiplying the number of Melrose Shares per GKN share held, being 1.49, by the Closing Price of a Melrose Share on 31 January 2018 (being the Latest Practicable Date) of 226.4 pence;
2. The total value that a GKN Shareholder will receive under our Offer of 418.3 pence per GKN Share held is calculated by adding the value of the shares received per GKN Share, being 337.3 pence to the value of cash received per GKN Share, being 81 pence;
3. The 10 year average price of a GKN Share is based on share prices between 4 January 2008 and 5 January 2018 (being the last Business Day before the approach made by Melrose to the GKN Board in connection with the Acquisition), adjusted for the effects of the rights issue in July 2009 on share prices prior to that date;
4. The number of Issued GKN Shares is based on 1,717,572,609 shares in issue (excluding Treasury Shares) plus 26,654,634 of total options as provided by GKN subject to Rule 10, Note 3 of the Code;
5. The value created by the rise in the GKN share price is based on the increase in the Closing Price of a GKN Share between 5 January 2018, being 326.3p pence, and 31 January 2018 (being the Latest Practicable Date), being 422.8 pence. The value is calculated by multiplying the difference of 96.5 pence by the number of Issued GKN shares;
6. The number of Issued Melrose Shares is based on 1,941,200,503 shares in issue, as announced by Melrose on 18 January 2018;
7. The value of the combined group of over £10 billion is calculated by multiplying the total number of New Melrose shares issued as a result of the transaction (being the number of Issued GKN shares multiplied by 1.49) and adding to this the number of Issued Melrose Shares. This is subsequently multiplied by the Closing Price of a Melrose Share on 31 January 2018 (being the Latest Practicable Date), of 226.4 pence;
8. History of GKN extracted from “GKN: The Making of a Business, 1759 to 2009” by Andrew Lorenz;
9. The pre-acquisition leverage of 10.3x EBITDA in respect of the McKechnie/Dynacast acquisition is calculated from the financial information included in the acquisition prospectus from 2005 (McKechnie net debt and EBITDA being as at July 2004 and Dynacast net debt and EBITDA being as at December 2004, in both cases being the latest reported information prior to the acquisition). The post-acquisition leverage of 2.9x EBITDA is calculated using Melrose reported net debt at June 2005 and EBITDA per the prospectus, as set out above;
10. The return on shareholders’ investment of 3.0x in respect of the McKechnie/Dynacast acquisition is calculated based on initial equity outlay of £244 million and total cash return of £734 million;
11. The pre-acquisition leverage of 3.7x EBITDA in respect of the FKI acquisition is calculated from the financial information included in the Melrose annual report 2008 (which states acquisition debt) and the acquisition prospectus from 2008 (from which it is possible to calculate EBITDA as at March 2007, being the latest reported information prior to the acquisition). The post-acquisition leverage of 2.7x EBITDA is stated in the Melrose annual report 2008;
12. The return on shareholders’ investment of 2.9x in respect of the FKI acquisition is calculated based on initial equity outlay of £499 million and total cash return of £1,431 million;
13. The return on shareholders’ investment of 2.3x in respect of the Elster acquisition is calculated based on initial equity outlay of £1,168 million and total cash return of £2,643 million;
14. The pre-acquisition leverage of 5.1x EBITDA and post-acquisition of 2.5x EBITDA in respect of the Nortek acquisition is set out in the Melrose investor presentation dated 6 July 2016 and is based on EBITDA as at December 2015;
15. £1.00 of original investment in Melrose at the time of the first acquisition plus additional investment in subsequent capital raisings of £11.85 gives a net return of £17.65 after accounting for capital returns of £13.24, ordinary dividends of £2.05 and the market value of shares held of £14.21, based on the Closing Price of a Melrose Share on 5 January 2018 (being the last Business Day before the approach made by Melrose to the GKN Board in connection with the Acquisition);
16. £1.00 of original investment in GKN in May 2005 (the time of Melrose’s first acquisition) plus additional investment in subsequent capital raisings of £0.42 gives a net return of £3.34 after accounting for ordinary dividends of £0.68 and the market value of shares held of £3.09, based on the Closing Price of a GKN Share on 5 January 2018 (being the last Business Day before the approach made by Melrose to the GKN Board in connection with the Acquisition);
17. TSR source data from Datastream, from October 2003 (date of Melrose formation) to close of business on 5 January 2018;
18. GKN’s top-end group trading margin target based on the published target range of 8% - 10% first stated in its Annual Report for the financial year ended 31 December 2007 and repeated up until its Interim Results for the period ended 30 June 2017;

19. GKN consensus comprises all analyst notes available to Melrose since 13 October 2017 (date of GKN's trading statement) as at 12 January 2018 (date that Melrose's approach was made public) and includes divisional and group level estimates from the following analysts: Barclays (16 October 2017), Berenberg (16 October 2017), Deutsche Bank (16 October 2017), J P Morgan Cazenove (group level only, 16 October 2017), UBS (16 October 2017), Peel Hunt (17 October 2017), Citi (18 October 2017), Liberum (23 October 2017), Jefferies (9 November 2017) and Bank of America Merrill Lynch (16 November 2017). Estimates from the following analysts have been excluded from the consensus as they adjust estimated trading profit for the impairment charge in the Aerospace business: Bank of America Merrill Lynch (17 November 2017), Deutsche Bank (17 November 2017), J P Morgan Cazenove (6 December 2017), Investec (18 December 2017) and UBS (10 January 2018). Estimates from Investec (6 November 2017) have been excluded from the consensus as it is a connected adviser to Melrose;
20. GKN's divisional target ranges of 11% - 13% for Aerospace, 8 - 10% for Driveline and 9 - 11% for Powder Metallurgy first stated in the 2011 full-year results presentation and repeated up until the 2015 first half results presentation.

The minimum Aerospace sales full-year 2017 estimates per the consensus are £3,493 million, the maximum Aerospace sales full-year 2017 estimates are £3,668 million and the arithmetic average is £3,601 million.

The minimum Driveline sales full-year 2017 estimates per the consensus are £4,882 million, the maximum Driveline sales full-year 2017 estimates are £5,212 million and the arithmetic average is £5,087 million.

The minimum Powder Metallurgy sales full-year 2017 estimates per the consensus are £1,089 million, the maximum Powder Metallurgy sales full-year 2017 estimates are £1,175 million and the arithmetic average is £1,139 million.

The minimum Other division trading profit full-year 2017 estimate per the consensus is £4 million, the maximum is £18 million and the arithmetic average is £12 million.

The minimum central costs full-year 2017 estimate per the consensus is £25 million, the maximum is £33 million and the arithmetic average is £29 million.

In accordance with Rule 28.8(c) of the Code, the consensus estimates are not shown with the agreement or the approval of GKN.

Trading profit at top-end divisional targets has been derived as the arithmetical sum of applying top-end divisional target margins to respective consensus divisional revenues, adding consensus trading profit for the Other division and deducting consensus central costs;

21. The Melrose Board having reviewed and analysed the potential benefits of the Acquisition, based on their previous experience of improving performance of industrial companies, expects to re-energise and re-purpose GKN's operations to enable them to exceed GKN's own top-end group trading margin target of 10 per cent., under Melrose management.

The Melrose Board expects to deliver this improvement over the typical Melrose ownership timeframe of three to five years (which is flexible).

The Melrose Board believes that it would be possible to achieve this level of performance given the following:

- a) Melrose has a proven track record of improving the performance of companies it has owned with underlying margins increasing by 30% to 70% from their original level under Melrose ownership;
- b) GKN's trading profit margins historically have under-performed its targets;
 - i. the Melrose Board believes it will be able to deliver the performance that GKN originally had set out in its strategy as outlined in its full-year 2012 results presentation, and target divisional trading margins as per its 2011 annual report;
 - ii. in particular, trading profit margin in the Driveline division only marginally exceeded the 8% lower-end target margin in 2014 (8.1%) and 2015 (8.2%) and was below this in all other years since 2011; and
 - iii. the profitability of the Aerospace division has deteriorated over the last three years, to below the lower end of the target margin range of 11% - 13% (full-year 2015: 10.9%, full-year 2016: 9.9%, full-year 2017 consensus: 8.5%);
- c) there is a gap in the performance of GKN compared to its potential as demonstrated by relevant peer performance which Melrose would seek to narrow. This gap can be illustrated as follows:
 - i. Aerospace: full-year 2016 divisional trading profit margin for GKN was 9.9% and consensus full-year 2017 is 8.5% before adjustments for the inventory write off between £80 million and £130 million. This compares to the full-year 2016 average operating margin of a set of close peers (MTU Aero Engines and Spirit AeroSystems) of approximately 13%;
 - ii. Driveline: the divisional trading profit margin in 2016 was 7.7% (before restatement for the inclusion of Off-Highway Powertrain). However, if removing £435 million revenue of the China JV (as per the 2016 GKN Annual Report) and the corresponding trading profit of £76.5 million from the 2016 full-year management revenues of £4,216 million and £323 million trading profit, the rest of the Driveline business would have achieved management revenues of £3,781 million and trading profit of £246.5

million, which implies trading profit margin of approximately 6.5%. This compares to the full-year 2016 average operating margin of a peer set (American Axle & Manufacturing, BorgWarner, Dana (Light Vehicle Division) and Nexteer Automotive) of approximately 10%;

- d) limited disclosure in GKN's public accounts shows that costs outside of materials have increased as a percentage of sales from 43% in 2012 to 49% in 2016, which suggests accumulated operating inefficiencies over the recent years; and
- e) GKN's annual report discloses that the full-year 2016 corporate and unallocated costs were £21 million, which Melrose intends to review and assess.

Melrose is not able to provide an estimate of any non-recurring integration costs that may be necessary to achieve its expected improvement of GKN's performance. It is anticipated that any integration costs will be incurred over the course of the Melrose ownership period.

Aside from the integration costs, no material dis-synergies are expected in connection with the Acquisition. The Melrose existing businesses do not overlap with GKN.

Given that Melrose does not have access to GKN's internal information, the Board of Melrose have not been able to prepare any detailed integration plan besides the high level action points that have already been stated.

This statement of trading profit margin improvement relates to future actions and circumstances which by their nature involve risks, uncertainties and contingencies. As a consequence, the expected performance referred to may not be achieved, may be achieved later or sooner than estimated, or those achieved could be materially different from those estimated. In making this statement, Melrose took into account historical group trading profit margins as achieved by GKN.

This statement is not intended as a profit forecast or a Quantified Financial Benefits Statement for the purposes of Rule 28 of the City Code and should not be interpreted as such.

- 22. The market capitalisation of GKN prior to the approach is calculated by multiplying the Closing Price of a GKN Share as at 5 January 2018 (being the last Business Day before the approach made by Melrose to the GKN Board in connection with the Acquisition) by the number of Issued GKN shares;
- 23. The immediate cash payment of £1.4 billion is calculated by multiplying the value of cash that a GKN Shareholder will receive under our Offer per GKN share, being 81 pence, by the number of Issued GKN shares;
- 24. The £2.5 billion of value of investment in Melrose is calculated by multiplying the Melrose market capitalisation on 31 January 2018 (being the Latest Practicable Date) by the percentage stake in Melrose to be owned by GKN shareholders, being 57%. The 57% is calculated by dividing the number of New Melrose Shares to be issued to GKN shareholders (being 1.49 multiplied by the number of Issued GKN Shares) by the total of the number of Issued Melrose Shares plus the number of New Melrose Shares to be issued to GKN shareholders;
- 25. The premium calculation to the price per GKN Share used in this Announcement has been calculated by reference to the Closing Price on 5 January 2018 (being the last business day before the approach made by Melrose to the GKN Board in connection with the Acquisition) of 326.3 pence in respect of a GKN Share;

Certain figures included have been subject to rounding adjustments.

Important Notice

Each of the Melrose directors, whose names are set out on the "Board of Directors" page of the Melrose website at www.melroseplc.net/about-us/directors (the "Melrose Directors"), accepts responsibility for the information contained in this letter, provided that the only responsibility accepted by them in respect of information relating to GKN and the GKN directors, which has been compiled from published sources, is to ensure that such information is correctly and fairly reproduced and presented. To the best of the Melrose Directors' knowledge and belief (who have taken all reasonable care to ensure that such is the case), the information contained in this letter is in accordance with the facts and, where appropriate, does not omit anything likely to affect the import of such information.