4 March 2021

MELROSE INDUSTRIES PLC

AUDITED RESULTS
FOR THE YEAR ENDED 31 DECEMBER 2020

Melrose Industries PLC today announces its audited results for the year ended 31 December 2020.

Highlights

	Adjusted[1] results		Statutory results	
Continuing operations	**2020 £m**	2019 £m	**2020 £m**	2019 £m
Revenue	**9,361**	11,592	**8,770**	10,967
Operating profit/(loss)	**340**	1,102	**(338)**	318
Profit/(loss) after tax	**120**	699	**(523)**	55
Diluted earnings per share	**2.4p**	14.3p	**(10.8)p**	0.9p
Free cash flow	**628**	591	**n/a**	n/a
Net debt	**2,847**	3,283	**n/a**	n/a

Group

- Trading was at the top end of management expectations throughout the second half of 2020. Excluding Aerospace, the other divisions on average achieved increased second half revenue over 2019 of 2%[2] and 9%[2] in the final quarter

- Adjusted[1] free cash generation was £628 million, 6% higher than 2019, prior to £172 million of restructuring costs. In achieving this cashflow investment levels in R&D and new products have been protected and working capital levels significantly improved, with more to come

- The strong cash generation resulted in Group net debt[1] reducing by over £400 million (13% of net debt) to £2.85 billion at the end of 2020 (31 December 2019: £3.3 billion). Year end leverage[1] was 4.1x EBITDA, but annualising the second half performance the proforma leverage[1] was approximately 3.2x EBITDA

- The Group made an adjusted[1] operating profit of £340 million in 2020. The statutory operating loss was £338 million; of the £678 million adjusting items, only £178 million were cash items, almost all related to restructuring

- Savings from restructuring projects underway in GKN are expected to improve the 2021 trading performance by approximately £125 million, with more to come

- The accounting deficit on the GKN UK defined benefit pension schemes has been cut by over 80% from £0.7 billion just before acquisition to £0.1 billion

- A sale process for Nortek Air Management has commenced; the business is trading very strongly, but there can be no certainty a disposal will be completed

- An Investor Day for GKN Automotive and Powder Metallurgy will be held on 20 May which will focus on the significant improvements made to the businesses, and their sustainable growth prospects from exciting new technologies

- A final dividend is proposed of 0.75 pence per share for 2020 given the excellent cash generation achieved in the year. The Board recognises the importance of dividends to shareholders and is pleased Melrose has returned to paying a dividend. A progressive dividend policy is intended to be reintroduced for future periods

Divisions

- No recovery has been seen in the civil aerospace market and this is not expected to change in 2021. Sales for the division were down 27%[2] in 2020 compared to last year, which was within the expected range. Good progress is being made in adapting this business to the current demand levels, improving working capital and continuing to develop new technologies by investing heavily in R&D

- Sales and margins recovered sharply in the second half of 2020 in Automotive and Powder Metallurgy. The second half adjusted[1] operating margins of Automotive recovered to 6.5% and Powder Metallurgy recovered to 8.3%. The final quarter of 2020 saw sales ahead of Q4 2019 although overall sales for the year were down

- Nortek Air Management is trading very strongly with sales for 2020 up 5%[2] year on year. Margins are also growing and reached 17.3% in the second half of the year, doubling since acquisition

Justin Dowley, Chairman of Melrose Industries PLC, today said:

"Whilst the COVID-19 crisis has had a major detrimental effect this year, Melrose has generated record cash flows and continued to invest to improve our businesses. All of this positions the Group well for a good recovery and strong performance in the future. Amidst these difficult conditions, Melrose has also managed to significantly reduce the £1 billion GKN UK pension scheme funding deficit that we inherited at the time of acquisition."

1. Described in the glossary to the Preliminary Announcement and are considered by the Board to be a key measure of performance
2. Growth is calculated at constant currency against 2019 results

ENDS

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CHAIRMAN'S STATEMENT

I am pleased to report our 18th set of annual results since flotation in 2003.

CALENDAR YEAR 2020

The past year has been one of the most challenging Melrose has experienced since it was established. We started the year with good momentum, as a number of the improvements being made to unlock the full potential of the GKN businesses began to take hold. However, the impact of the COVID-19 pandemic in March was both immediate and significant. Within weeks, governments across the globe had imposed wide ranging restrictions, impacting both supply and demand and causing a large number of our factories to temporarily close.

Without delay, we took the difficult decision to prioritise cash generation to put the Group in the best position to emerge strongly from the crisis. We again thank our shareholders and banking syndicate for their support as we took the early and decisive action necessary to adapt to the crisis and reshape the Group for the new post-COVID landscape.

That decision has been very successful, with adjusted free cash flow for the Group improving on an already strong 2019 by 6% to £628 million. This contributed to reducing net debt by 13% to £2.85 billion, whilst ensuring that the level of investment in R&D and new products was protected. This cashflow has enabled us to undertake the necessary improvement plans for the businesses sooner than we had thought would be possible earlier in the year when the pandemic took hold.

All of this has had a noticeable impact on the results we announce today. We achieved statutory revenue for the Melrose Group of £8,770 million (2019: £10,967 million), with an adjusted operating profit of £340 million (2019: £1,102 million) based on a statutory operating loss of £338 million (2019: profit of £318 million). While these results show a sharp decline, they are mostly impacted by events at the height of the crisis in the second quarter, with the end markets for all businesses except GKN Aerospace showing good signs of a return in the fourth quarter to give confidence for the coming year.

I would like to thank all employees for their efforts this year in the most challenging circumstances.

DIVIDEND

Having taken the decision to withdraw the final 2019 dividend and not pay an interim 2020 dividend due to the impact of the global pandemic, the Board is particularly pleased that the stability and performance of the Group since then has enabled us to propose a final dividend for 2020 of 0.75 pence per share (2019: nil). With no 2020 interim dividend having been paid, this represents the total dividend for the year (2019: 1.7 pence). It should be noted that all payments received by the Group under the UK Coronavirus Job Retention Scheme were fully repaid last year.

The Board recognises the importance of dividends to its shareholders and, with the worst of the COVID-19 crisis we hope behind us and the actions taken to reshape the Group, the Board expects to return to its progressive dividend policy for future periods. The final dividend will be paid on 19 May 2021 to those shareholders on the register at 6 April 2021, subject to approval at the Annual General Meeting ("AGM") on 6 May 2021.

PENSIONS

In spite of the difficulties presented by the COVID-19 crisis, our excellent track record in improving the funding position of pension schemes under our stewardship has continued at pace. We are delivering on our commitment to GKN pension members ahead of schedule by significantly reducing the accounting deficit in their UK defined benefit pensions schemes to just over £100 million, which represents a reduction in the accounting deficit of over 80% compared to pre-acquisition.

BOARD MATTERS

As announced previously, co-founder and Executive Vice Chairman David Roper agreed to delay his retirement to assist the Company in navigating the challenges presented by the pandemic. His knowledge and experience have been very helpful in ensuring the Group ended the year in a strong position. David's retirement will now take effect at the end of May. We thank him for his long and successful service, particularly for the last twelve months, and wish him all the best. We will miss him.

The Board's decision to delay David's retirement was the reason we did not achieve our goal of 33% female board members by the end of last year as we had intended. The middle of the crisis was not the time to lose someone of David's experience, but this is now being addressed. As part of the wider Board succession plans, along with David's departure in May, we are currently at the initial stages of conducting a search for a further female non-executive director.

PURPOSE, STRATEGY AND SUSTAINABILITY

Melrose was founded in 2003 to empower businesses to unlock their full potential for the collective benefit of stakeholders, whilst providing shareholders with a superior return on their investment. This has been delivered through Melrose's 'Buy, Improve, Sell' strategy, which means we buy good quality manufacturing businesses that are underperforming their potential and then invest heavily to improve performance and productivity as they become stronger, better businesses under our stewardship. At the appropriate time, we identify new owners who will take them to the next stage of their development and return proceeds to our shareholders.

From a sustainability perspective, Melrose is committed to reducing greenhouse gas emissions in the Group to net zero by 2050. Clearly the nature of our model means the Group will fundamentally change within that timescale as we sell businesses and buy others. We provide the focus and investment to improve our businesses' sustainability and value to the benefit of all stakeholders. Melrose sees this as a key part of our stewardship: environmental, social and governance (ESG) priorities have always been central to our 'Buy, Improve, Sell' strategy. Our factories are focused on delivering year on year economically justifiable improvements in waste and emissions and have achieved an 11% reduction in emissions in 2020.

The importance of ESG in our product development strategy is clearly evident in initiatives such as:

- GKN Automotive's P4 eDrive powertrains which reduce CO2 emissions by up to 100%;
- Nortek Air Management's StatePoint technology, which enables savings of up to 30% for energy consumption and up to 90% for water usage in giant data centre cooling systems around the world; and
- GKN Aerospace's H2Gear initiative to develop a ground-breaking UK hydrogen propulsion system to power a zero emissions aircraft.

We are focused on improving our businesses for the good of shareholders, the environment and other stakeholders. Technological development will be at the forefront of creating a better environment. We were also pleased to play a leading role in the UK's award-winning Ventilator Challenge Consortium, which produced more than 13,000 life-saving ventilators.

Disclosures are an increasingly important part of this improvement strategy. We are committed to informing our shareholders and wider audiences of the improvements we are making. Our 2020 Sustainability Report builds on our inaugural report last year, not only providing information on our performance during 2020, but also greater insight into our materiality mapping, alignment with United Nations Sustainable Development Goals and our sustainability roadmap for 2021 as we prepare for reporting on Task Force on Climate Related Financial Disclosures next year.

We welcome the evolving focus and clarity on ESG matters as yet another opportunity to demonstrate how we build better, stronger businesses. The nature of the businesses we buy is that they often have challenges to decarbonise, but can become sustainable themselves and help transform the sectors they serve. In doing so we not only deliver significant financial returns, but also significant ESG returns to stakeholders. I refer you to the Sustainability Report for full details.

OUTLOOK 2021

2020 was dominated by the impact of the global pandemic as we worked closely with our businesses to overcome the unprecedented challenges that arose. The aerospace sector has been particularly hard hit and a recovery looks some way off while global travel restrictions remain. Nonetheless, GKN Aerospace remains a very good business with a growing Defence division and is taking the improvement steps to ensure it is well positioned for when the recovery does emerge.

Encouragingly, the end markets for our other businesses ended the year with good momentum, providing some optimism for the year ahead. Doubtless, challenges remain, particularly in the management of supply chains in 2021. The Group's strong performance throughout the pandemic has been a validation of the business model. Your Board continues to see significant value creation opportunities in the businesses we hold and believes Melrose is well positioned to seize future opportunities as they present themselves.

Justin Dowley
Chairman
4 March 2021

CHIEF EXECUTIVE'S REVIEW

We entered one of the most challenging years in Melrose's history with good momentum as our investments in operational improvements in the GKN businesses since acquisition began to take hold. Results in the first quarter showed all businesses making good progress. However, the speed and scale of the onset of the COVID-19 pandemic in March forced a quick and strong adjustment in approach for the entire Group.

With major disruptions to supply chains and customer demand, we took the decision to focus on cash generation as many of our sites were shut for lengthy periods during the second quarter of the year. The principal driver for this was highly disciplined working capital management practices, based on strict inventory control and backed by forensic weekly cash management calls with each business.

The high degree of uncertainty and volatility meant that we focused on ensuring the Group would emerge strongly and swiftly into the post COVID-19 business and customer environment. We took all actions necessary, including agreeing temporary covenant relief from our supportive banking syndicate, withdrawing the dividend, and implementing across-the-board cost control initiatives.

The impact of these decisions is clear from these results. Profit did decline significantly, albeit ending ahead of expectations at the height of the pandemic. The performance on cash generation has been exceptional. Our businesses have responded to the challenge laudably, generating £628 million in gross cash across the period. We are extremely grateful for the hard work from all our employees to produce this performance. Performance in the second half, if annualised, was consistent with proforma debt leverage of approximately 3.2x EBITDA. This demonstrates the performance of our businesses this year and gives a sense of their capabilities as markets return.

Another key priority throughout the crisis has been the health and safety of our workforce. Keeping workers safe has always been a top priority, but never more so than during the global pandemic. Like the wider community, our businesses experienced COVID-19 cases at sites across the globe, but there has been an intense focus on securing all the necessary PPE and implementing changes to processes and other measures to protect our employees.

Pleasingly, this also translated into an improvement across all our key health and safety performance indicators, a trend we are keen to continue into this year. Within this focus on workers' safety, our businesses sought to minimise disruption to their production schedules wherever possible. Although there were undoubted challenges, particularly with forced site closures at the height of the pandemic, this has been very successful and I thank our employees for their hard work and dedication in this area during this particularly difficult time.

The second half of the year saw an easing of some of the more extreme volatility, as all our end markets except aerospace showed some signs of recovery, resulting in the Group (excluding GKN Aerospace) having a 2% year on year sales growth for the second half of the year and 9% year on year growth for the final quarter alone, providing some helpful momentum into the new year.

The strong cash generation meant we were able to undertake the necessary restructuring programmes in the second half of the year to ensure the businesses were adapted to meet the new reduced demand levels. Group restructuring programmes are expected to deliver over £125 million full year benefit for 2021. We acknowledge that such actions are very difficult for those affected but they are unfortunately necessary in these difficult times.

On acquisition we inherited onerous GKN contracts and we have encouraged all GKN businesses to take significant steps during the year to resolve a number of the most material examples. Since our acquisition, these actions, undertaken with the support of key customers, have helped to reduce the exposure by over 60%.

We have been mindful throughout the crisis of preserving the technology leadership of our businesses, despite the financial challenges. We have continued to invest in cutting edge technologies across our businesses, with a particular focus towards sustainable products that assist our key customers. In parallel with our Group commitment to achieve the target of net zero greenhouse gas emissions by 2050, our businesses are also key partners with their customers in the drive to decarbonise some of the world's most challenging sectors. Your Group is at the forefront of the drive to reduce carbon emissions in the key sectors of transport and data communication with world leading technology.

Some of these developments are well established and are already generating benefits, like GKN Automotive's eDrive solutions that have sold over 1.3 million units and save up to 100% of carbon emissions, GKN Aerospace's additive manufacturing expertise making aircraft lighter and more efficient and Nortek Air Management's StatePoint Technology that delivers up to 30% energy and 90% water savings in cooling systems for the fast growing data centre market. Others, like GKN Aerospace's H2Gear, Wing of Tomorrow and Powder Metallurgy's hydrogen fuel storage, are just starting to deliver on their promise. Our investments are critical to these long-term developments and we will continue to invest at pace to ensure our businesses hold their place at the forefront of technology leadership.

For the businesses themselves, GKN Aerospace has endured a very difficult year reflecting the wider sector experience, with sales for the division down 27% and the business doing well to stay profitable on an adjusted basis this year. It is nonetheless continuing to invest in technology, with the Global Technology Centre in Filton, UK, due to become fully operational later this year. GKN Aerospace has not seen recovery in its civil markets yet, although we believe it will start to do so towards the end of the year. In the meanwhile there has been a focus on cost reduction which should position the business for an improvement in performance this year.

Both GKN Automotive and GKN Powder Metallurgy entered the year with the lingering effects of the global automotive sector downturn, which was materially compounded by the pandemic in the second quarter. However, as restrictions eased in the second half of the year, a combination of low global stock levels and pent up demand contributed to a strong recovery. Although this is not expected to continue at quite the same intensity, it does provide momentum for this year. Pleasingly, the second half market return has been matched by a strong improvement in adjusted operating margins by both businesses, delivering 6.5% and 8.3% respectively for the half year, with further gains to come. We will provide further insight for both GKN Automotive and Powder Metallurgy at the Investor Day now scheduled for May, with full details to be confirmed in due course.

Nortek Air Management has enjoyed a record year with 5% sales growth and adjusted operating margins for the second half over 17%. HVAC enjoyed a very strong year in which it began delivering on the exciting promise of its world leading StatePoint Technology®. With the first customer installation completed and accelerating production planning for the second, StatePoint has a fast growing sales pipeline. Similarly, our substantial investments over recent years in new product development for AQH resulted in market share gains across a number of platforms and a strong performance for the year. We have recently commenced a formal sale process for the division. While the outcome remains uncertain, we are hopeful that the outstanding performance of the businesses will translate into a good result for both them and our shareholders.

In the Other Industrial division, we continued to streamline the Group with the sale of non-core businesses, GKN Wheels & Structures being the latest. The remaining businesses felt the effect of the pandemic, with action being taken to reshape them for the new demand profile. For Brush, travel restrictions have presented difficulties for their Services business, but Generators and Transformers enjoyed a strong year and have a solid order book for 2021. Ergotron had a mixed year, with Healthcare initially benefiting from the increase in medical spending, but Office understandably suffering due to widespread business closures. Nortek Control continued its important product development, which is expected to deliver benefits in the coming year.

Further details for each business are included in the divisional summaries below.

AEROSPACE DIVISION

GKN Aerospace is a global tier 1 aerospace business with market-leading positions driven by technological innovation, advanced processes and engineering excellence that help aircrafts fly safely, faster, further, and more sustainably. Following a reorganisation in 2019, GKN Aerospace is structured according to its three core customer markets – Civil Airframe, Defence and Engines. It operates in 14 countries. GKN Aerospace's technology is used throughout the aerospace industry: from high-use single aisle aircraft and the world's longest haul passenger planes, through to business jets, helicopters, the world's most advanced fighter jets and space launchers.

Improvements in 2019 meant that the business made a strong start to the year, with performance comfortably in line with expectations until mid-March. However, the impact of COVID-19, and in particular the widespread introduction of global travel restrictions, had a swift and material impact on the business. Along with the rest of the aerospace sector, GKN Aerospace experienced a rapid decline in sales which included a reduction of approximately 50% across its Civil Airframe and Civil Engines markets in the second quarter that persisted for the rest of the year. Although partially offset by the refocus towards the Defence business, which experienced 8% sales growth across the year, 2020 was undoubtedly an extremely challenging year for GKN Aerospace overall, in line with the rest of the aerospace industry.

In order to mitigate the impact of such a significant market decline the business quickly implemented strict cash management measures and with a focus on control over inventory achieved a cash conversion before capital expenditure of 328%. As soon as it became apparent that the COVID-19 impact was not going to be temporary, GKN Aerospace undertook appropriate production rescheduling to rebalance the business with its new commercial and operating environments. Unfortunately, this has meant a reduction in the workforce during 2020. Together, these initiatives have been critical to the business achieving a relatively small adjusted profit for the year and will be of considerable benefit during 2021, even without any recovery in the aerospace market. In parallel the business continued to implement its 'One Aerospace' global model, which was introduced during 2020 to further integrate and streamline business operations to create a much leaner operating model.

The onset of the COVID-19 pandemic brought into sharp focus the health, safety and protection of the GKN Aerospace workforce and the communities in which it operates. In close cooperation with public authorities, the business rapidly took decisive action to ensure that employees could continue to operate safely throughout the pandemic. Business planning was refocused on mapping the expected future impact of COVID-19 across the organisation, its customers and supply chains. The business also made a material contribution to its local communities, manufacturing PPE within a number of its facilities and performing a leading role in the UK's award-winning Ventilator Challenge Consortium, which produced more than 13,000 life-saving ventilators.

Despite uncertain commercial markets, GKN Aerospace's continued progress and investment in technology led to several landmark achievements in 2020. Critically, it strengthened its position as a key partner to both existing major blue-chip OEMs and small-scale start-up customers to create the next generation of sustainable aircraft. In combination, GKN Aerospace is at the forefront of technology in wings, additive manufacturing and power generation and will continue to play a leading part in the drive to reduce emissions from airflight.

Civil Airframe continued its development of the Wing of Tomorrow with the National Composites Centre and initiated a new collaboration with Eviation to design and manufacture the wings, aircraft tail and electrical wiring systems for Alice, a ground-breaking regional electric aircraft. In Engines, GKN Aerospace's world-leading additive manufacturing capability has led to the introduction of lighter and more efficient fan case mount rings, leading to a reduction of 20% in emissions and additionally has accelerated the inaugural flight testing of light-weight, recycled thermoplastic components with Bell on the V-280 Valor helicopter. It has commenced development of H2Gear, an exciting new hydrogen propulsion system for a zero emissions aircraft. In 2021, GKN Aerospace will also commence full operations at its flagship £32 million Global Technology Centre in Filton, UK, to work in partnership with the business's existing Global Technology Centres in the USA, Sweden and The Netherlands.

Throughout the year, GKN Aerospace further cemented its strategic position in the important Asia market that is benefiting from a relatively faster recovery after the initial wave of the COVID-19 pandemic. In addition to the establishment of two wholly owned production sites, one for windows in China and the other for engine components in Malaysia, GKN Aerospace also entered into a new strategic joint venture with a COMAC subsidiary to manufacture advanced aerostructures in Jingjiang, Jiansu Province, China. The state-of-the-art 80,000m^2 facility in Jingjiang will be GKN Aerospace's first aerostructures JV in China, and offers the opportunity to become an important part of local supply of advanced aerostructures in the region.

Outlook

After a particularly challenging 2020, GKN Aerospace does not expect meaningful recovery in its civil markets in 2021. The restructuring work in 2020 provides a good base for further adjustment this year to adapt GKN Aerospace to the current realities of the aerospace sector. Continued progress in the implementation of its 'One Aerospace' lean operating model will enable the business to further strengthen its customer relationships and reduce costs and it remains well positioned to maintain a leading role in the sustainable recovery of civil aviation. Whilst the timing of recovery for the civil aviation markets remains uncertain, the business has benefited from increased Defence sales. As the market returns, the reshaped GKN Aerospace has the technology leadership to deliver profitable and sustainable growth in the years ahead.

AUTOMOTIVE DIVISION

GKN Automotive is a global leader in drive systems for all segments of the automotive industry, from the smallest ultra-low-cost cars to the most sophisticated premium vehicles demanding the most complex driving dynamics. 90% of the world's automotive manufacturers choose GKN Automotive and almost 50% of cars sold worldwide use GKN Automotive technologies. GKN Automotive has operations in 20 countries and is primarily organised around two major business divisions: (i) Driveline, the global leader in driveline technologies with an extensive portfolio of products covering sideshafts, propshafts and constant velocity joints for every type of propulsion system whether that be hybrid, electric or internal combustion; and (ii) ePowertrain, a global leader and pioneer with over 18 years' experience in electric drive technologies ("eDrive") and intelligent all-wheel drive ("AWD") systems.

In 2020, as a result of COVID-19, the global automotive industry experienced a 17% decline in light vehicle production compared to 2019. All GKN Automotive operational facilities globally were forced to close for varying durations throughout the year.

In line with the market, GKN Automotive sales declined 19% year on year. With the exception of China, this sales decline was consistent across all regions. The market rebound in China in the second half of the year resulted in an annual drop in sales of only 4% compared to 2019. Fourth quarter sales for GKN Automotive overall were 8% higher year on year, reflecting an encouraging return in demand levels towards the end of 2020.

The reaction of the organisation to the pandemic was commendable. The business remained responsive and agile throughout the crisis whilst GKN Automotive employees demonstrated care and respect for their colleagues and their local communities.

Despite the revenue challenges resulting from COVID-19, GKN Automotive's operating performance was robust. Disciplined execution of cost reduction initiatives and a rigorous focus on key operational levers, resulted in an adjusted operating profit margin of 6.5% for the second half of the year. The 'Full Potential' transformation programme significantly contributed to this performance and delivered over £70 million of cost savings in 2020 through procurement, fixed cost reduction, commercial discipline and operating excellence. A continued focus on working capital and rigorous cash management throughout 2020 also resulted in strong cash generation for the business, with a conversion rate before capital expenditure of 153% for the full year.

In 2020 the Driveline division increased its focus on new-energy vehicles and significantly expanded its product range to further strengthen its industry-leading position. It executed 36 new programme launches and implemented operational efficiency initiatives whilst managing the operational challenges of COVID-19. In parallel, the team secured over £4 billion of lifetime revenue in new contracts. Its expertise in high performance shafts is in high demand in electric vehicle production, meaning it is well placed to benefit from the growth in electric vehicles. Driveline components are already enjoying an equivalent market share in hybrid and electric vehicles as they do in their existing markets based on its differentiated market leading technology in this exciting, growing sector.

At the start of the year, GKN Automotive announced a strategic collaboration with Delta Electronics Inc, a global power electronics specialist. This partnership will enhance ePowertrain's existing capabilities and accelerate the time to market for innovative, cost competitive eDrive systems. Eight eDrive systems were launched for four global OEMs, over ten brands and 13 different PHEV and BEV models in the year. The business also completed its first phase of in-house eMotor industrialisation.

China continues to be a key strategic market for GKN Automotive, through its 50% interest in the long-standing joint venture, Shanghai GKN HUAYU Driveline Systems ("SDS") with local partner HASCO. One of the first parts of the business to feel the effects of the pandemic, it also benefited from the strong, early recovery of the Chinese market, limiting SDS sales reduction for the year to 4% whilst still implementing operational improvement measures.

Outlook

2021 is set to be a year of recovery for the industry and one of continued transformation for GKN Automotive, as margin improvement initiatives will provide real substance to the recovery seen in the second half of 2020. The Driveline business will continue to reinforce its industry leading position, focusing on margin expansion and top-line growth through the delivery of operational excellence and industrial initiatives. ePowertrain will accelerate the growth of eDrive through continued expansion of in-house software, mechatronics, and system integration capabilities, and capitalising on the strategic partnership with Delta Electronics. Whilst the speed of recovery is unclear and may increase the risk of supply chain issues, we are confident that GKN Automotive will continue to improve its business.

POWDER METALLURGY DIVISION

GKN Powder Metallurgy is a global leader in both precision powder metal parts for the automotive and industrial sectors, and the production of metal powder, through its prized vertically integrated business platform. In 2020 GKN Powder Metallurgy streamlined its organisation into three divisions: (i) Sinter Metals – the world's leading manufacturer of precision automotive components and components for industrial and consumer applications spread across its Precision and Structural segments; (ii) Hoeganaes – the world's second largest manufacturer of metal powder, the essential raw material for powder metallurgy, with manufacturing facilities in North America, Europe, and China; and (iii) Additive – a leading digital manufacturer of additive manufacturing parts, both metals and polymer, and materials for prototypes, manufactured through a global, digitally connected print-network.

After a strong performance during the first quarter of 2020, the COVID-19 pandemic caused significant disruption throughout the rest of the year. By the middle of March 2020, production across the GKN Powder Metallurgy business was forced to cease in almost all countries. This presented a number of unprecedented challenges throughout the business and its key end-markets. GKN Powder Metallurgy met those setbacks with the rapid implementation of sharp, rigorous discipline with respect to finances and operations.

A renewed focus on tight resource management was immediately implemented, characterised within the business's operations by flexible work patterns and restructuring programmes to match the new demand levels. Such operational initiatives sat alongside a strong focus on preserving cash, resulting in a conversion rate before capital expenditure of 156% for the year, including ensuring strong and well-controlled working capital management, and reducing capital expenditure.

The positive impact of the business's strict financial and operational control during 2020 was reflected in reductions in productive inventory days by 25%, and approximately a 33% reduction in overdue receivables. This focus strengthened the business's foundations and enabled GKN Powder Metallurgy to continue to provide customers with the strong support free from disruption they required during uncertain times.

With the second quarter of 2020 characterised by these initial responses to the pandemic, the third quarter transitioned towards a quick recovery, with the final quarter of the year seeing a 7% revenue increase compared to the final quarter of 2019, requiring management to cope with some capacity constraint issues. New business wins during the year reached £150 million on an annualised basis, particularly targeted to better margin sinter metals production.

Full year adjusted operating profit margin of 4.3% is a combination of close to break even in the first half and a strong recovery in the second, with the fourth quarter margins above 8%.

Despite the trading challenges GKN Powder Metallurgy continued to invest in its cutting edge technology, integrating its Forecast 3D acquisition into its Additive segment and broadening the range of products to include non-metal. 2020 also saw the first prototype production of its exciting new sustainable metal hybrid hydrogen storage system. Initial market interest looks very promising and this will become a key focus and potential source of growth in the mid term future.

Outlook

The delivery of operational improvement opportunities started in 2020 and strategic rationalisations will remain the key drivers for GKN Powder Metallurgy in achieving its margin targets in due course. Further investment in all business units including Additive Manufacturing, and the business's new sustainable hydrogen systems, supported by digitised manufacturing upgrades will help GKN Powder Metallurgy continue its expected strong trajectory as its core markets move towards recovery. The business is optimistic that the actions initiated in 2020 will support its performance for the year ahead.

NORTEK AIR MANAGEMENT DIVISION

The Nortek Air Management division comprises (i) Nortek Global HVAC ("HVAC") and (ii) Air Quality and Home Solutions ("AQH"), both of which delivered a very strong performance in 2020.

NORTEK GLOBAL HVAC

The Nortek Global HVAC ("HVAC") business includes the custom and commercial business of Nortek Air Solutions, the residential and light commercial business of HVAC and the dedicated data centre business of StatePoint Liquid Cooling. It employs a strategic framework of sustained profitable growth, operational excellence, technological innovation, and a commitment to its customers.

The COVID-19 pandemic caused some uncertainty within HVAC's end-markets during the first half of 2020, but its markets quickly recovered after that. By focusing on its core values, coupled with an unwavering dedication to the safety of its people, the business successfully overcame the unprecedented global challenges posed by the pandemic. It executed a series of operational excellence initiatives to support its continued pursuit of increased productivity and margin expansion through further quality improvements, increased plant utilisation, innovative process optimisation and increased productivity. There is much more to come.

The immediate result was good revenue growth for the year of 4%, with strong growth in the second half of 17%, 126% cash conversion before capital expenditure and expanded adjusted operating margins to 15.5%. Critical initiatives implemented in 2020 laid strong and supportive foundations for achieving the business's core strategy to further expand margins and achieve profitable growth over the longer term, whilst simultaneously improving its products' sustainability performance for the benefit of its customers.

HVAC has successfully completed delivery of its first Statepoint customer installation, in Europe, a major milestone for the business, and accelerated the production of the second, in Singapore. The ability to achieve up to 30% power and 90% water consumption savings clearly demonstrates StatePoint's superior performance and geographic flexibility in the design and construction of world-class hyperscale data centres across the world. HVAC also developed its next iteration of StatePoint Technology® in the form of the HyperScale Data Centre, and further developed its technology roadmap for future StatePoint Technology® products. HVAC's longstanding commitment to technological innovation and continuous improvement has maintained its technological agility in addressing the key sustainability challenges faced by the data centre sector, which are driven by global megatrends such as reducing energy usage intensity, improving water efficiency, and the expansion of broader air management standards.

Building on its market leading position in data centres, during 2020 HVAC continued to harness the advantages of its technology leadership to target further mission critical and highly complex adjacent product lines, including unit heaters and furnaces, light commercial dedicated outdoor air systems, and manufactured housing solutions. The residential business faced market challenges, but HVAC continued to advance further operational efficiency initiatives to overcome their impact.

Outlook

Although the COVID-19 pandemic resulted in a slightly unpredictable market during the first half of 2020, the strong recovery during the second half of 2020 is carrying into 2021. HVAC sees the significant regulatory changes currently impacting its sector as a further opportunity to differentiate itself from its peers to its advantage. Added to this, the continuing market recovery is expected to be underpinned by a fast growing global data centre demand, a robust replacement cycle in residential, a recovery in commercial construction driven by the institutional markets, and new opportunities in the retrofit segment. The business is excited about its prospects for the coming year and beyond.

AIR QUALITY AND HOME SOLUTIONS

AQH is a leading manufacturer of ventilation products for the professional building remodelling and replacement market, the residential new construction market, and the consumer DIY market. It supplies to distributors and dealers of electrical and lighting products, kitchen and bathroom dealers, retail home centres and private label customers from its four manufacturing locations around the world. AQH enjoys a leading market share and installed base in US residential ventilation fans and range hoods.

A strong second half recovery after the COVID-19 downturn in the second quarter, resulted in a 6% annual sales growth over the prior year. The recovery was bolstered by the strong bounce back in the housing market, the surge in remodelling activity and the new product launches. The result was increased sales in every region and business unit over last year. Specific category growth of 25% in fresh air systems in North America helped to drive growth in 2020 and momentum for the coming year.

The significant investment in new product development over recent years is now yielding results and creating momentum moving into 2021. The business continued to invest in its product portfolio across multiple categories, with an overarching purpose to address demand for ‘whole house’ ventilation solutions. Timely new ventilation products are now launching in multiple segments of fresh air, cooking, bath and whole house.

COVID-19 accelerated the business’s efforts to build on the momentum of new products centred around fans that eliminate bacteria. Lockdown measures drove significant further growth from digital sales channels including Amazon, which will provide a further focus for sales development into 2021. Digital sales were again 30% more than prior year, becoming a real strength for the business. The Zephyr business continues to bring innovation and market disrupting products to the appliance channel with unique kitchen designs and features.

As part of its continuous improvement programme, AQH continued to drive production efficiencies and cost savings, and generated further margin opportunities through product transfers, manufacturing optimisation, sourcing initiatives and supplier proximity improvements. The business maintained its strong focus on, and investment in, optimising its manufacturing footprint, and increasing capacity.

Outlook

Continued momentum is expected in the North American market due to forecast strong first half housing demand. In addition, growth will continue to be driven by a continuous pipeline of new product development, scheduled product extensions, and capitalising on the desire to ventilate for fresh air. Operationally, additional optimisations in supply chain, logistics and products are planned for 2021 which will continue to have sales and margin benefits. The business is very optimistic about 2021.

OTHER INDUSTRIAL DIVISION

The Other Industrial Division comprises (i) Brush, (ii) Nortek Control, and (iii) Ergotron. GKN Wheels & Structures was sold during the year and was classified as a discontinued operation.

BRUSH

Brush is a leading independent provider of Turbogenerators, Transformers and Switchgear, and a provider of Services across these core product segments. Trading conditions initially proved challenging in 2020 primarily due to COVID-19 but enjoyed some recovery in the second half. The now reshaped business successfully mitigated the impact of the pandemic, by taking proactive measures to control costs, supplemented by tight working capital and cash management initiatives which resulted in cash conversion before capital expenditure of 121%. Turbogenerators, Transformers and DC Switchgear all performed well and worked to offset the decline in Field Services across all product segments due to COVID-19 travel restrictions and related deferrals to maintenance activities.

The business continued to invest in product development across all of its segments, including broadening its product range in Switchgear and Transformers and enhancing its Turbogenerators' product portfolio. Such investment further enabled Brush to benefit from macro trends by delivering products that promote sustainable energy infrastructure and transmission, green efficiencies, and less consumption.

Outlook

Brush is now a profitable, cash generative business. Having demonstrated that it is more agile than ever before, it has secured a positive order backlog stretching well into 2021 and beyond, and firm foundations for improvement based upon a more diversified customer portfolio across a broad range of traditional and emerging end-markets. After implementing a strategic growth plan for 2021, the business is increasingly confident of a good performance in the coming years.

NORTEK CONTROL (formerly Security & Smart Technology)

Nortek Control is a leading developer and manufacturer of security, home automation, access control, health and artificial intelligence technologies for the residential and commercial markets, principally in North America. Nortek Control continues to bolster its expertise in the design and manufacture of analytics-embedded wireless connectivity devices, to leverage its strong brand presence in professional security, integrator and custom installer channels.

After a reasonable start to 2020, the impact of COVID-19 was significant as restrictions to access for professional installers onsite, traditionally a key driver for sales growth, was curtailed. This was somewhat offset by growth in the home automation market and perimeter access markets, as well as increased awareness of customers' home security requirements in the second half of the year.

With a new management team in place focused on innovation and technology leadership, Nortek Control has a strong pipeline of exciting new product introductions planned for 2021. The transition of production out of China, in response to increasing tariffs, was also completed in 2020, with the majority of products now being produced in Mexico and Malaysia.

Outlook

Whilst the impact of COVID-19 will extend into 2021 in restricting important installer access, the launch of its highly-anticipated new residential security panel EDGE and other new products provide some level of optimism. This and the transition of manufacturing to countries less impacted by tariffs, mean the business is positioned to achieve an improved performance in 2021.

ERGOTRON

Ergotron is a leading designer, manufacturer and distributor of ergonomic products for use in a variety of working, learning and healthcare environments. Based near Minneapolis, US, Ergotron comprises four business segments: Healthcare, Office, Education and Industrial.

International growth in Asia and in the global Healthcare sector in 2020 partially offset the headwinds of the COVID-19 pandemic, resulting in a decline in revenue of 11% for the year. The growth in Asia was primarily driven by the Education and Office segments of the Japanese market.

In Healthcare, demand growth primarily centred around increased requirements for medical carts as health systems prepared for and battled with COVID-19. Changes in working patterns triggered by the pandemic caused significant market disruption for the Office segment in the US and a reshaping of its product development plans to realign to future demand. Several strategic operational and cost optimisations implemented during 2020 helped grow adjusted operating margins to 23.9% and are expected to deliver further benefits in the coming year.

Outlook

Ergotron expects growth in 2021, led by a limited recovery in the Office and ongoing growth in the Healthcare segment. Ergotron's expected refocus on to the Industrial sector will provide another area of longer term growth. Strong cost control and new product launches should also support an improved 2021.

Simon Peckham
Chief Executive
4 March 2021

FINANCE DIRECTOR'S REVIEW

The Group's trading conditions and results in the year ended 31 December 2020 were significantly disrupted by the worldwide impact of COVID-19. Despite the second half showing signs of improvement, the Group's results for the year are substantially lower than last year.

MELROSE GROUP RESULTS – CONTINUING OPERATIONS

Statutory results:

The statutory IFRS results are shown on the face of the Income Statement and show revenue of £8,770 million (2019: £10,967 million), an operating loss of £338 million (2019: profit of £318 million) and a loss before tax of £535 million (2019: profit of £106 million). The diluted earnings per share ("EPS"), calculated using the weighted average number of shares in issue during the year of 4,858 million (2019: 4,858 million), were a loss of 10.8 pence (2019: profit of 0.9 pence).

Adjusted results:

The adjusted results are also shown on the face of the Income Statement. They are adjusted to include the revenue and operating profit from equity accounted investments ("EAIs") and to exclude certain items which are significant in size or volatility or by nature are non-trading or non-recurring, or are items released to the Income Statement that were previously a fair value item booked on an acquisition. It is the Group's accounting policy to exclude these items from the adjusted results, which are used as an Alternative Performance Measure ("APM") as described by the European Securities and Markets Authority ("ESMA"). APMs used by the Group are defined in the glossary to the Financial Statements.

The Melrose Board considers the adjusted results to be an important measure used to monitor how the businesses are performing as they achieve consistency and comparability between reporting periods when all businesses are held for the complete reporting period.

The adjusted results for the year ended 31 December 2020 show revenue of £9,361 million (2019: £11,592 million), an operating profit of £340 million (2019: £1,102 million) and a profit before tax of £153 million (2019: £889 million). Adjusted diluted EPS were 2.4 pence (2019: 14.3 pence).

Tables summarising the statutory results and adjusted results by reportable segment are shown later in this review.

RECONCILIATION OF STATUTORY RESULTS TO ADJUSTED RESULTS

The following tables reconcile the Group statutory revenue and operating (loss)/profit to adjusted revenue and adjusted operating profit:

Continuing operations:	2020 £m	2019 £m
Statutory revenue	**8,770**	**10,967**
Adjusting item:		
Revenue from equity accounted investments (“EAIs”)	591	625
Adjusted revenue	**9,361**	**11,592**

Adjusting revenue item:

The Group has some investments in which it does not hold full control (“EAIs”), the largest of which is a 50% interest in Shanghai GKN HUAYU Driveline Systems (“SDS”), within the Automotive business. During the year ended 31 December 2020, EAIs in the Group generated £591 million of revenue (2019: £625 million), which is not included in the statutory results but is shown within adjusted revenue so as not to distort the operating margins reported in the businesses when the adjusted operating profit from these EAIs is included.

Continuing operations:	2020 £m	2019 £m
Statutory operating (loss)/profit	**(338)**	**318**
Adjusting items:		
Amortisation of intangible assets acquired in business combinations	526	534
Restructuring costs	220	238
Write down of assets	184	179
Currency movements in derivatives and movements in associated financial assets and liabilities	(182)	(55)
Net release of fair value items	(118)	(153)
Other	48	41
Adjustments to statutory operating (loss)/profit	**678**	**784**
Adjusted operating profit	**340**	**1,102**

Adjusting items to operating (loss)/profit are consistent with prior years and include:

The amortisation charge on intangible assets acquired in business combinations of £526 million (2019: £534 million), which is excluded from adjusted results due to its non-trading nature and to enable comparison with companies that grow organically. However, where intangible assets are trading in nature, such as computer software and development costs, the amortisation is not excluded from adjusted results.

Restructuring and other associated costs in the year totalling £220 million (2019: £238 million), which are shown as adjusting items due to their size and non-trading nature, during the year ended 31 December 2020 these included:

- A charge of £110 million (2019: £79 million) within the Aerospace division primarily relating to costs incurred globally to reduce the business' headcount and cost structure in reaction to the significant impact that COVID-19 is having on the aerospace industry. This charge also included costs in respect of the continuation of the business' global integration, announced last year, to create "One Aerospace", ensuring the business is well positioned and able to react to changes in its new environment; and the continuation of costs relating to rationalisation projects commenced in the previous year.

- A charge of £60 million (2019: £83 million) within the Automotive division as the business has accelerated its efforts to address its high cost base, inherited on acquisition, and best position itself as it recovers post COVID-19.

- A charge of £48 million (2019: £19 million) within the Powder Metallurgy division including costs associated with realigning the business for future demand, along with consolidation actions started in 2019 and the commencement during 2020 of the closure of a site in its underperforming North American Structural business.

- A net charge of £2 million (2019: £57 million) within the Nortek Air Management, Other Industrial and Corporate divisions which includes the completion of a factory consolidation within the HVAC business; the finalisation of the changes made in the Nortek Control business (formerly the Security & Smart Technology business) to move to a third party contract manufacturing model; and the profit from the disposal of a Dutch property held within the Brush business left vacant following the factory consolidation programme commenced in 2018.

The write down of assets in the year of £184 million, mostly recognised in the second quarter of the year as a result of the impact of COVID-19, of which £133 million was within the Aerospace division. As a result of the impact of the pandemic, a review of the operating assets of the Group was performed, and resulted in £159 million of fixed assets and £25 million of other net operating assets being written down across certain sites within the businesses, as they adapted to new levels of industry demand. The write down of these assets is shown as an adjusting item due to the unprecedented nature of the COVID-19 pandemic, its non-trading nature and size. The charge of £179 million, recognised in 2019, related to impairment of goodwill allocated to the Nortek Control group of CGUs.

The net release of fair value items in the year of £118 million (2019: £153 million) where items have been resolved for more favourable amounts than first anticipated. During the year this included a net release of £101 million in respect of loss-making contract provisions held within the GKN businesses, where either contractual terms have been renegotiated with the relevant customer or operational efficiencies have been identified and demonstrated for a sustained period. The net release of fair value items is shown as an adjusting item, avoiding positively distorting adjusted results.

Movements in the fair value of derivative financial instruments (primarily forward foreign currency exchange contracts where hedge accounting is not applied) entered into within the GKN businesses to mitigate the potential volatility of future cash flows, on long-term foreign currency customer and supplier contracts, along with foreign exchange movements on the associated financial assets and liabilities. This totalled a credit of £182 million (2019: £55 million) in the year and is shown as an adjusting item because of its volatility and size.

Other adjusting items of £48 million (2019: £41 million) include items consistent with prior years, the largest of which is an adjustment of £30 million (2019: £28 million) to gross up the post-tax profits of EAIs to be consistent with the adjusted operating profits of subsidiaries within the Group.

STATUTORY AND ADJUSTED RESULTS BY REPORTING SEGMENT

The following table shows revenue split by reporting segment, including EAIs for adjusted revenue:

	Aerospace £m	Automotive £m	Powder Metallurgy £m	Nortek Air Mgmt. £m	Other Industrial £m	Total £m
Statutory revenue	**2,798**	**3,231**	**886**	**1,227**	**628**	**8,770**
Reconciling item:						
Revenue from EAIs	6	566	19	-	-	591
Adjusted revenue	**2,804**	**3,797**	**905**	**1,227**	**628**	**9,361**

The following table shows operating (loss)/profit split by reporting segment. Adjusting items are described earlier in this review.

	Aerospace £m	Automotive £m	Powder Metallurgy £m	Nortek Air Mgmt. £m	Other Industrial £m	Corporate £m	Total £m
Statutory operating (loss)/profit	**(410)**	**(183)**	**(57)**	**149**	**34**	**129**	**(338)**
Reconciling item:							
Adjusting items	424	265	96	39	29	(175)	678
Adjusted operating profit/(loss)	**14**	**82**	**39**	**188**	**63**	**(46)**	**340**

The performances of each of the reporting segments are discussed in the Chief Executive's Review. The adjusted operating loss in the corporate cost centre of £46 million (2019: £52 million) included £34 million (2019: £32 million) of operating costs and £12 million (2019: £20 million) of costs relating to divisional cash-based long-term incentive plans, which have been re-evaluated following the impact of COVID-19 on the businesses.

FINANCE COSTS AND INCOME – CONTINUING OPERATIONS

Total net finance costs in the year ended 31 December 2020 were £197 million (2019: £212 million), £187 million (2019: £213 million) shown within the adjusted results and £10 million of charges (2019: credit of £1 million) treated as adjusting items.

Net interest on external bank loans, bonds, overdrafts and cash balances was £133 million (2019: £143 million). The Group uses interest rate swaps to fix the majority of the interest rate exposure on its drawn debt. More detail on these swaps is given in the finance cost risk management section of this review.

In addition, finance charges included: a £12 million (2019: £11 million) amortisation charge relating to the arrangement costs of raising the Group's current bank facility; an interest charge on net pension liabilities of £19 million (2019: £31 million); a charge on lease liabilities of £21 million (2019: £21 million); and a charge for the unwind of discounting on long-term provisions of £2 million (2019: £7 million).

Adjusting items:

Adjusting items, within finance costs and income, include a charge of £2 million (2019: credit of £1 million) relating to the fair value changes on cross-currency swaps, and £8 million (2019: £nil) relating to costs incurred renegotiating the Group's financial covenants with its banking facility syndicate in response to the impact of COVID-19. These charges are shown as adjusting items because of their volatility and non-trading nature.

DISCONTINUED OPERATIONS

Discontinued operations include the GKN Wheels & Structures business results which was classified as held for sale at 31 December 2019 and subsequently disposed on 25 November 2020 for total proceeds of £21 million, resulting in a loss on disposal in the year of £8 million.

In the prior year, discontinued operations also included the results of Walterscheid Powertrain Group up to the date of disposal on 25 June 2019.

For the year ended 31 December 2020 discontinued operations show revenue of £144 million (2019: £423 million), a statutory operating loss of £nil (2019: £80 million) and a statutory loss before tax of £nil (2019: £82 million).

TAX – CONTINUING OPERATIONS

The statutory results show a tax credit of £12 million (2019: charge of £51 million) which arises on a statutory loss before tax of £535 million (2019: profit of £106 million), a statutory tax rate of 2% (2019: 48%). During the year, the Ergotron division was legally separated from the Nortek tax group, realising an adjusting tax charge of £71 million, of which £20 million will be settled in cash in 2021, with the remainder being settled by the utilisation of tax assets held within the Group. In addition to this adjusting tax charge, several of the adjusting items, discussed earlier in this review, do not give rise to tax deductions, meaning that the statutory tax rate is lower than the adjusted tax rate.

The effective rate on the adjusted profit before tax for the year ended 31 December 2020 was 22% (2019: 21%).

The Group has tax losses and other deferred tax assets with a value of £810 million (31 December 2019: £819 million). These are offset by deferred tax liabilities on intangible assets of £1,161 million (31 December 2019: £1,243 million) and £201 million (31 December 2019: £188 million) of other deferred tax liabilities. Most of the tax losses and other deferred tax assets will generate future cash tax savings, whereas the deferred tax liabilities on intangible assets are not expected to give rise to cash tax payments.

Cash tax receipts from the refund of advance payments and the closure of enquiries offset cash tax payments made in the year. Net cash tax in the year ended 31 December 2020 was £nil (2019: net payments of £117 million).

MELROSE EMPLOYEE SHARE PLAN

The Melrose 2017 Incentive Plan ("2017 Plan") expired on 31 May 2020 with no value payable to its participants, despite being on track to generate a share reward before the impact of COVID-19.

A new Melrose Employee Share Plan ("2020 Plan") was approved on 21 January 2021 which mirrors the previous 2017 Plan, in most respects, with a three year performance period and a further two year holding period. Details of the 2020 Plan are included in the Directors' Remuneration report in the 2020 Annual Report.

The charge in respect of the 2020 Plan will be £16 million per annum (2017 Plan: £13 million), excluding the associated employer's tax charge.

CASH GENERATION AND MANAGEMENT

Robust cash management was set as the top commercial priority for the Group this year as the realisation of the significant impact that COVID-19 would have on the global economy and the Group's businesses materialised. Comprehensive cash preservation actions were successfully implemented in each business in the first half of the year and strong cash management continued throughout the second half as certain businesses within the Group showed some signs of recovery.

As a result, an adjusted free cash inflow of £628 million before restructuring spend (2019: £591 million before restructuring spend and one-off special contributions to defined benefit pension plans), was generated in the year, 6% more than the adjusted free cash generated in 2019.

An analysis of the adjusted free cash flow is shown in the table below:

	2020 £m	**2019 £m**
Adjusted operating profit	340	1,102
Adjusted operating profit from EAIs	(62)	(66)
Depreciation and amortisation	492	498
Lease obligation payments	(76)	(70)
Positive non-cash impact from loss-making contracts	(59)	(81)
Working capital movements	424	58
Adjusted operating cash flow (pre-capex)	**1,059**	**1,441**
Net capital expenditure	(292)	(495)
Net interest and net tax paid	(162)	(295)
Defined benefit pension contributions – ongoing	(111)	(72)
Defined benefit pension contributions – special contribution	-	(111)
Restructuring	(172)	(190)
Dividend income from equity accounted investments	54	67
Net other	80	(55)
Free cash flow	**456**	**290**
Adjusted free cash flow	**628**	**591**

Net working capital was reduced by £424 million in the year (2019: £58 million), mainly by reducing inventory and receivables levels in the businesses, along with net capital expenditure in the year being £292 million (2019: £495 million), representing 0.7x depreciation of owned assets.

Net interest paid in the period was £162 million (2019: £178 million), net tax payments were £nil as explained in the tax section of this review (2019: £117 million) and ongoing contributions to defined benefit pension schemes were £111 million (2019: £72 million), which included £60 million paid into the GKN UK pension plans.

Free cash flow in the year, after restructuring spend of £172 million (2019: £190 million), was an inflow of £456 million (2019: £290 million), contributing to the reduction in net debt (as defined in the glossary to the Financial Statements) of 13% in the year.

The movement in net debt is summarised as follows:

	2020 £m	2019 £m
At 1 January	**(3,283)**	**(3,482)**
Non-trading items and discontinued operations:		
Net cash flow from acquisition and disposal related activities	(11)	103
Dividend paid to Melrose shareholders	-	(231)
Foreign exchange and other non-cash movements	(2)	74
Discontinued operations	(7)	(37)
Cash flow from non-trading items and discontinued operations	**(20)**	**(91)**
Free cash flow	456	290
At 31 December at closing exchange rates	**(2,847)**	**(3,283)**
At 31 December at 12 month average exchange rates	**(2,953)**	**(3,385)**

Group net debt at 31 December 2020, translated at closing exchange rates (being US $1.37 and €1.12), was £2,847 million (31 December 2019: £3,283 million, translated at closing exchange rates at 31 December 2019).

The movement in net debt during the year included a free cash inflow of £456 million, being partly offset by £11 million of net spend on acquisition and disposal related activities, primarily relating to the acquisition of FORECAST 3D in the Powder Metallurgy division and proceeds relating to the disposed GKN Wheels & Structures business, and a £2 million increase to net debt in respect of foreign exchange and other non-cash movements.

For bank covenant purposes the Group's net debt is calculated at average exchange rates for the previous twelve months, to better align the calculation with the currency rates used to calculate profits, and was £2,953 million.

The Group net debt leverage was not required to be tested at 31 December 2020 following a waiver for this test date being unanimously agreed with the Group's lending banks earlier in the year as the initial impact of COVID-19 on the businesses was being understood. Group net debt leverage was 4.1x EBITDA at 31 December 2020 (31 December 2019: 2.3x EBITDA) and will be next tested at 31 December 2021, when the bank covenant test level will be 5.25x.

ASSETS AND LIABILITIES

The summarised Melrose Group assets and liabilities are shown below:

	2020 £m	2019 £m
Goodwill and intangible assets acquired with business combinations	8,790	9,342
Tangible fixed assets, computer software and development costs	3,541	3,874
Equity accounted investments	430	436
Net working capital	346	821
Retirement benefit obligations	(838)	(1,121)
Provisions	(1,021)	(1,087)
Deferred tax and current tax	(717)	(698)
Lease obligations	(555)	(582)
Net other	(19)	(151)
Total	**9,957**	**10,834**

These assets and liabilities are funded by:

	2020 £m	2019 £m
Net debt	(2,847)	(3,283)
Equity	(7,110)	(7,551)
Total	**(9,957)**	**(10,834)**

Net debt shown in the table above is defined in the glossary to the Financial Statements and is consistent with the banking facility covenant testing definition.

GOODWILL, INTANGIBLE ASSETS AND IMPAIRMENT REVIEW

The total value of goodwill as at 31 December 2020 was £3,640 million (31 December 2019: £3,653 million) and intangible assets acquired with business combinations was £5,150 million (31 December 2019: £5,689 million). These items are split by reporting segment as follows:

31 December 2020	Aerospace £m	Automotive £m	Powder Metallurgy £m	Nortek Air Mgmt. £m	Other Industrial £m	Total £m
Goodwill	942	1,026	524	575	573	3,640
Intangible assets acquired with business combinations	2,793	1,146	628	302	281	5,150
Total goodwill and acquired intangible assets	**3,735**	**2,172**	**1,152**	**877**	**854**	**8,790**

The Group's goodwill and intangible assets have been tested for impairment, and in accordance with IAS 36 "Impairment of assets" the recoverable amount has been assessed as being the higher of the fair value less costs to sell and the value in use.

Under IAS 36, the value in use basis for calculating the recoverable amount prohibits the inclusion of future uncommitted restructuring plans, whilst the fair value less costs to sell basis of valuation allows the inclusion of these plans if it is deemed that a market participant would also restructure.

With the future benefits of restructuring projects currently forming a material part of valuations for certain businesses within the Group, because they are substantially reducing their cost structure to align with the new levels of demand post COVID-19, the fair value less costs to sell basis gives the higher valuation at this point in time and therefore in accordance with IAS 36, has been used in assessing the recoverable amount for these businesses.

Sensitivity analysis and increased disclosures have been provided in the Financial Statements for the Aerospace, Automotive, Powder Metallurgy, Ergotron and Nortek Control businesses, being the businesses showing the tightest headroom.

Whilst the headroom on impairment testing has inevitably reduced in certain businesses compared to the previous year, the Board is comfortable that no impairment is required in respect of the valuation of goodwill and intangible assets in its businesses as at 31 December 2020.

PROVISIONS

Total provisions at 31 December 2020 were £1,021 million (31 December 2019: £1,087 million).

The following table details the movement in provisions in the year:

	Total £m
At 1 January 2020	**1,087**
Spend against provisions	(277)
Net charge to adjusted operating profit	169
Net charge shown as adjusting items	188
Release of loss-making contract provision to adjusting items	(101)
Utilisation of loss-making contract provision	(59)
Other (including foreign exchange)	14
At 31 December 2020	**1,021**

The net charge to adjusted operating profit in the year of £169 million is primarily in respect of ongoing warranty, product liability and workers' compensation charges which are closely matched by similar cash payments in the year, such that the provision for these categories has not changed significantly during the year.

The net charge shown as adjusting items in the Income Statement of £188 million primarily includes costs associated with restructuring actions of £203 million, discussed within the adjusting items section of this review, net of a release, mainly relating to fair value items settled for an amount more favourable than first anticipated.

The utilisation of the loss-making contract provision was £59 million in the year (31 December 2019: £83 million). Furthermore, £101 million, approximately 30%, of the remaining loss-making contract provision was released as an adjusting item in the year, either because contracts have been favourably resolved following positive negotiations with customers or because operational efficiencies have been demonstrated for a sustained period of time. At 31 December 2020 the loss-making contract provision was £241 million, 60% lower than when GKN was acquired in 2018.

During the period £172 million of cash was spent on restructuring.

Included within Other for the Group are foreign exchange movements of £7 million, the unwind of discounting on certain provisions of £6 million and the provisions acquired with FORECAST 3D in the year totalling £1 million.

PENSIONS AND POST-EMPLOYMENT OBLIGATIONS

Melrose operates a number of defined benefit pension schemes and retiree medical plans across the Group, accounted for using IAS 19 Revised: "Employee Benefits".

The values of the Group plans were updated at 31 December 2020 by independent actuaries to reflect the latest key assumptions. A summary of the assumptions used are shown in the Financial Statements.

At 31 December 2020 total plan assets of the Melrose Group's defined benefit pension plans were £3,775 million (31 December 2019: £3,412 million) and total plan liabilities were £4,613 million (31 December 2019: £4,533 million), a net deficit of £838 million (31 December 2019: £1,121 million).

The most significant pension plans in the Group are the GKN Group Pension Schemes (Numbers 1 - 4) created when the GKN UK 2012 pension plan was split into four schemes, two of which are allocated to the Aerospace division and two to the Automotive division. At 31 December 2020 in total these four pension plans had aggregate gross assets of £2,556 million (31 December 2019: £2,243 million), gross liabilities of £2,755 million (31 December 2019: £2,711 million) and a net deficit of £199 million (31 December 2019: £468 million), split 58% of the deficit held within Aerospace and 42% within Automotive.

The GKN Group Pension Schemes (Numbers 1 - 4) are closed to new members and to the accrual of future benefits for current members.

In total ongoing contributions to the Group defined benefit pension plans and post-employment medical plans in the year ended 31 December 2020 were £111 million and are expected to be approximately £98 million in 2021.

The Group's ongoing annual contributions include £60 million to the GKN UK plans. The Group has also committed to contribute 10% of the net proceeds from disposal of GKN businesses (other than Powder Metallurgy) and 5% of the net proceeds from disposal of non-GKN businesses. Additionally, the Group has committed to contribute £270 million to the GKN UK plans when Powder Metallurgy is sold. These commitments cease when the funding target, which has been agreed with the Trustees, is achieved, being gilts plus 25 basis points for the GKN UK 2016 plan and gilts plus 75 basis points for the GKN Group Pension Schemes (Numbers 1 - 4). At 31 December 2020, the funding target on the GKN UK 2016 plan had been achieved, and the funding deficit on the GKN Group Pension Schemes (Numbers 1 - 4) was approximately £370 million.

It is noted that a 0.1 percentage point decrease in the discount rate would increase the retirement benefit accounting liabilities of the Group, on an IAS 19 basis, by £78 million, or 2%, and a 0.1 percentage point increase to inflation would increase the liabilities by £46 million, or 1%. Furthermore, an increase by one year in the expected life of a 65 year old member would increase the pension liabilities on these plans by £250 million, or 5%.

FINANCIAL RISK MANAGEMENT

The financial risks the Group faces continue to be considered and policies are implemented to appropriately deal with each risk. The most significant financial risks are considered to be liquidity risk, finance cost risk, exchange rate risk, contract and warranty risk and commodity cost risk.

These are discussed in turn below.

Liquidity risk management

Following the impact of COVID-19 on the Group's businesses and their end markets, the liquidity of the Group has been a key focus in the year.

The Group's net debt position at 31 December 2020 was £2,847 million (31 December 2019: £3,283 million).

The Group's committed bank funding includes: a multi-currency denominated term loan of £100 million and US$960 million that was due to mature in April 2021; and a multi-currency denominated revolving credit facility of £1.1 billion, US$2.0 billion and €0.5 billion that matures in January 2023. In February 2021, the Company exercised its option to extend the term loan for a further three years to April 2024.

As at 31 December 2020, the term loan was fully drawn and there remains a significant amount of headroom on the multi-currency committed revolving credit facility. Applying the exchange rates at 31 December 2020, the headroom equated to £1,632 million (31 December 2019: £1,136 million applying the exchange rates at 31 December 2019).

In addition to the headroom on the multi-currency committed revolving credit facility, cash, deposits and marketable securities, net of overdrafts, in the Group amounted to £160 million at 31 December 2020 (31 December 2019: £317 million).

The Group also holds capital market borrowings as at 31 December 2020 consisting of:

Maturity date	Notional amount £m	Coupon % p.a.	Cross-currency swaps million	Interest rate on swaps % p.a.
September 2022	450	5.375%	US$373	5.70%
			€284	3.87%
May 2032	300	4.625%	n/a	n/a

The committed bank funding has two financial covenants, being a net debt to adjusted EBITDA covenant and an interest cover covenant, both of which are normally tested half-yearly in June and December.

During the year the Group agreed, with its lending banks, a waiver for its net debt to adjusted EBITDA covenant test as at 31 December 2020 and 30 June 2021. The Group also renegotiated the net debt to adjusted EBITDA covenant test level to be 5.25x at 31 December 2021; 4.75x at 30 June 2022; and 4.0x at 31 December 2022, before returning to 3.5x at 30 June 2023 and onwards. At 31 December 2020 the Group net debt leverage was 4.1x.

Similarly, the interest cover bank covenant test was renegotiated such that at 31 December 2020 the test is set at 2.5x; 3.0x at 30 June 2021 and 31 December 2021; and 3.25x at 30 June 2022, before returning to 4.0x from 31 December 2022 onwards. At 31 December 2020 the Group interest cover was 5.1x, affording comfortable headroom.

Following the completion of a material disposal from within the Group, the net debt to adjusted EBITDA covenant test level would be adjusted downwards to be 4.25x at 31 December 2021; 4.0x at 30 June 2022; and 3.75x at 31 December 2022, before returning to 3.5x at 30 June 2023 and onwards. No such adjustment would be made to the interest cover bank covenant test following a material disposal.

A limited number of Group trade receivables are subject to non-recourse factoring and customer supply chain finance arrangements, taking advantage of facilities where the cost of finance is cheaper than the Group's own cost of funds and where OEMs have extended their own programmes to support their supply chain through the COVID-19 global pandemic. As at 31 December 2020, these amounted to £314 million (31 December 2019: £200 million), and the net cash benefit in the year was approximately £60 million.

In addition, some suppliers have access to utilise the Group's supplier finance programmes, which are provided by a number of the Group's banks. As at 31 December 2020 there were drawings on these facilities of £62 million (31 December 2019: £75 million). There is no cost to the Group for providing these programmes as the cost is borne by the suppliers. These programmes allow suppliers to choose whether they want to accelerate the payment of their invoices, by the financing banks, at a low interest cost, based on the credit rating of the Group as determined by the financing banks. If the Group exited these arrangements or the banks ceased to fund the programmes there could be a potential impact of approximately £30 million (31 December 2019: approximately £35 million) on the Group's cash flows. The risk of this happening is considered low as the Group has extended the number of banks that provide this type of financing to ensure there is not a significant exposure to any one bank.

Finance cost risk management

The bank margin on the bank facility depends on the Group leverage, and ranges from 0.75% to 2.0% on the term loan, and 0.95% to 2.25% on the revolving credit facility. As at 31 December 2020 the margin was 2.0% (31 December 2019: 1.4%) on the term loan and 2.25% (31 December 2019: 1.65%) on the revolving credit facility.

In addition to the cross-currency swaps associated with the fixed rate capital market borrowings, inherited as part of the GKN acquisition, the Group holds interest rate swap instruments to fix the cost of LIBOR on borrowings under the bank facility. The policy of the Board is to fix approximately 70% of the interest rate exposure of the Group. Under the terms of the existing swap arrangements and excluding the bank margin, the Group will pay a weighted average fixed cost of approximately 2% until the swaps terminate on 17 January 2023.

The Group also holds cross-currency swaps used to convert US Dollar bank debt into Euro borrowings and at 31 December 2020, US $507 million had been swapped into €425 million. These swaps are rolled on a monthly basis and help to reduce the cost of the Group's borrowings.

At 31 December 2020, the fair value liability of all cross-currency swaps held by the Group was £89 million (31 December 2019: £80 million).

The average cost of the debt for the Group is expected to be approximately 4.2% over the next 12 months.

Exchange rate risk management

The Group trades in various countries around the world and is exposed to movements in a number of foreign currencies. The Group therefore carries exchange rate risk that can be categorised into three types: transaction, translation and disposal related risk, as described in the paragraphs below. The Group's policy is designed to protect against the majority of the cash risks but not the non-cash risks.

The most common exchange rate risk is the transaction risk the Group takes when it invoices a customer or purchases from suppliers in a different currency to the underlying functional currency of the relevant business. The Group's policy is to review transactional foreign exchange exposures, and place necessary hedging contracts, quarterly on a rolling basis. To the extent the cash flows associated with a transactional foreign exchange risk are committed, the Group will hedge 100% at the time the cash flow becomes committed. For forecast and variable cash flows, the Group hedges a proportion of the expected cash flows, with the percentage being hedged lowering as the time horizon lengthens. The average time horizons are longer for GKN Aerospace, GKN Automotive and GKN Powder Metallurgy to reflect the longer-term nature of the contracts within these divisions. Typically, in total the Group hedges around 90% of foreign exchange exposures expected over the next twelve months and approximately 60% to 80% of exposures expected between 12 and 24 months. This policy does not eliminate the cash risk but does bring some certainty to it.

The translation rate risk is the effect on the Group results in the period due to the movement of exchange rates used to translate foreign results into Sterling from one period to the next. No specific exchange instruments are used to protect against the translation risk because it is a non-cash risk to the Group, until foreign currency is subsequently converted to Sterling. However, the Group utilises its multi-currency revolving credit facility and cross-currency swaps, where relevant, to maintain an appropriate mix of debt in each currency. The hedge of having debt drawn in these currencies funding the trading units with US Dollars or Euro functional currencies protects against some of the Balance Sheet and banking covenant translation risk.

Lastly, exchange rate risk arises when a business that is predominantly based in a foreign currency is sold. The proceeds for those businesses may be received in a foreign currency and therefore an exchange rate risk may arise on conversion of foreign currency proceeds into Sterling, for instance to pay a Sterling dividend or Capital Return to shareholders. Protection against this risk is considered on a case by case basis and, if appropriate, hedged at the time.

Exchange rates for currencies most relevant to the Group in the year were:

US Dollar	**Average rate**	**Closing rate**
2020	1.28	1.37
2019	1.28	1.33
Euro		
2020	1.13	1.12
2019	1.14	1.18

A 10 percent strengthening of the major currencies within the Group, if this were to happen in isolation against all other currencies, would have the following impact on the re-translation of adjusted operating profit into Sterling:

£m	**USD**	**EUR**	**CNY**	**Other**
Increase in adjusted operating profit	45	12	7	11
% impact on adjusted operating profit	7%	2%	1%	2%

The impact from transactional foreign exchange exposures is not material in the short term due to hedge coverage being approximately 90%.

A 10 percent strengthening in either the US Dollar or Euro would have the following impact on debt as at 31 December 2020:

	USD	**EUR**
Increase in debt - £ million	187	72
Increase in debt	6%	2%

Contract and warranty risk management

Under Melrose management a suitable bid and contract management process exists in the businesses, which includes thorough reviews of contract terms and conditions, contract-specific risk assessments and clear delegation of authority for approvals. These processes aim to ensure effective management of risks associated with complex contracts. The financial risks connected with contracts and warranties include the consideration of commercial, legal and warranty terms and their duration, which are all considered carefully by the businesses and Melrose centrally before being entered into.

Commodity cost risk management

The cumulative expenditure on commodities is important to the Group and the risk of base commodity costs increasing is mitigated, wherever possible, by passing on the cost increases to customers or by having suitable purchase agreements with suppliers which fix the price over a certain period. These risks are also managed through sourcing policies, including the use of multiple suppliers, where possible, and procurement contracts where prices are agreed in advance to limit exposure to price volatility. Occasionally, businesses within the Group enter financial instruments on commodities when this is considered to be the most efficient way of protecting against price movements.

GOING CONCERN

As part of their consideration of going concern, the Directors have reviewed the Group's future cash forecasts and profit projections, which are based on market data and internal information and recent past experience. Given the global political and economic continuing uncertainty resulting from the COVID-19 pandemic, it is difficult to estimate with precision the impact on the Group's prospective financial performance.

The Group has modelled a reasonably possible downside scenario against these future cash forecasts and throughout this scenario the Group would not breach any of the revised financial covenants and would not require any additional sources of financing.

The long-term impact of COVID-19 remains uncertain and the impacts of the pandemic on trading conditions could be more prolonged or severe than that which the Directors have considered in this reasonably possible downside scenario.

However, the Group's current committed bank facility headroom, its access to liquidity, and the sensible levels of bank covenants agreed with the Group's supportive lending banks, allow the Directors to consider it appropriate that the Group can manage its business risks successfully and adopt a going concern basis in preparing the Financial Statements.

Geoffrey Martin
Group Finance Director
4 March 2021

CAUTIONARY STATEMENT

This announcement contains forward-looking statements. These statements are made in good faith based on the information available up to the time of the approval of this announcement, and should be treated with caution due to the inherent uncertainties, including both economic and business risk factors, underlying any such forward-looking information. Accordingly, readers are cautioned not to place undue reliance on any such forward-looking statements. Subject to compliance with applicable laws and regulations, the Company does not undertake any obligation to update any forward-looking statement to reflect events or circumstances after the date of this announcement. This announcement has been prepared solely to provide information to shareholders to assess the Company's strategies and the potential for those strategies to succeed, and neither the Company nor its directors accept any liability to any other person save as would arise under English law.

Consolidated Income Statement

Continuing operations	Notes	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Revenue	3	**8,770**	10,967
Cost of sales		**(7,492)**	(8,732)
Gross profit		**1,278**	2,235
Share of results of equity accounted investments	9	**32**	38
Net operating expenses		**(1,648)**	(1,955)
Operating (loss)/profit	3, 4	**(338)**	318
Finance costs		**(200)**	(221)
Finance income		**3**	9
(Loss)/profit before tax		**(535)**	106
Tax	5	**12**	(51)
(Loss)/profit after tax for the year from continuing operations		**(523)**	55
Discontinued operations			
Loss for the year from discontinued operations		**(10)**	(106)
Loss after tax for the year		**(533)**	(51)
Attributable to:			
Owners of the parent		**(536)**	(60)
Non-controlling interests		**3**	9
		(533)	(51)
Earnings per share			
Continuing operations			
– Basic	7	**(10.8)p**	0.9p
– Diluted	7	**(10.8)p**	0.9p
Continuing and discontinued operations			
– Basic	7	**(11.0)p**	(1.2)p
– Diluted	7	**(11.0)p**	(1.2)p

Adjusted[(1)] results from continuing operations

Adjusted revenue	3	**9,361**	11,592
Adjusted operating profit	3, 4	**340**	1,102
Adjusted profit before tax	4	**153**	889
Adjusted profit after tax	4	**120**	699
Adjusted basic earnings per share	7	**2.4p**	14.3p
Adjusted diluted earnings per share	7	**2.4p**	14.3p

(1) Defined in note 2.

Consolidated Statement of Comprehensive Income

	Notes	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Loss after tax for the year		**(533)**	(51)
Items that will not be reclassified subsequently to the Income Statement:			
Net remeasurement gain/(loss) on retirement benefit obligations		**244**	(32)
Fair value loss on investments in equity instruments		**(16)**	–
Income tax (charge)/credit relating to items that will not be reclassified	5	**(42)**	15
		186	(17)
Items that may be reclassified subsequently to the Income Statement:			
Currency translation on net investments		**(42)**	(346)
Share of other comprehensive income/(expense) from equity accounted investments		**16**	(23)
Transfer to Income Statement from equity of cumulative translation differences on disposal of foreign operations		**–**	(13)
Derivative losses on hedge relationships		**(99)**	(17)
Transfer to Income Statement on hedge relationships		**8**	–
Income tax credit/(charge) relating to items that may be reclassified	5	**9**	(19)
		(108)	(418)
Other comprehensive income/(expense) for the year		**78**	(435)
Total comprehensive expense for the year		**(455)**	(486)
Attributable to:			
Owners of the parent		**(458)**	(494)
Non-controlling interests		**3**	8
		(455)	(486)

Consolidated Statement of Cash Flows

	Notes	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Operating activities			
Net cash from operating activities from continuing operations	12	**768**	769
Net cash used in operating activities from discontinued operations	12	**(4)**	(20)
Net cash from operating activities		**764**	749
Investing activities			
Disposal of businesses, net of cash disposed		**10**	169
Purchase of property, plant and equipment		**(275)**	(465)
Proceeds from disposal of property, plant and equipment		**25**	24
Purchase of computer software and capitalised development costs		**(42)**	(54)
Dividends received from equity accounted investments		**54**	67
Purchase of investments		**(2)**	(50)
Settlement of derivatives used in net investment hedging		**–**	(100)
Acquisition of subsidiaries, net of cash acquired		**(19)**	–
Interest received		**3**	9
Net cash used in investing activities from continuing operations		**(246)**	(400)
Net cash used in investing activities from discontinued operations	12	**(2)**	(15)
Net cash used in investing activities		**(248)**	(415)
Financing activities			
Repayment of borrowings		**(598)**	(456)
New bank loans raised		**–**	350
Costs of raising debt finance		**(1)**	–
Repayment of principal under lease obligations		**(76)**	(70)
Dividends paid to non-controlling interests		**–**	(6)
Dividends paid to owners of the parent	6	**–**	(231)
Net cash used in financing activities from continuing operations		**(675)**	(413)
Net cash used in financing activities from discontinued operations	12	**(1)**	(2)
Net cash used in financing activities		**(676)**	(415)
Net decrease in cash and cash equivalents, net of bank overdrafts		**(160)**	(81)
Cash and cash equivalents, net of bank overdrafts at the beginning of the year	12	**317**	415
Effect of foreign exchange rate changes	12	**3**	(17)
Cash and cash equivalents, net of bank overdrafts at the end of the year	12	**160**	317

As at 31 December 2020, the Group had net debt of £2,847 million (31 December 2019: £3,283 million). A definition and reconciliation of the movement in net debt is shown in note 12.

Consolidated Balance Sheet

	Notes	31 December 2020 £m	Restated(1) 31 December 2019 £m	Restated(1) 31 December 2018 £m
Non-current assets				
Goodwill and other intangible assets		**9,198**	9,784	11,098
Property, plant and equipment		**3,133**	3,432	3,171
Investments		**34**	48	–
Interests in equity accounted investments		**430**	436	492
Deferred tax assets		**180**	160	132
Derivative financial assets		**101**	38	26
Trade and other receivables		**439**	424	504
		13,515	14,322	15,423
Current assets				
Inventories		**1,126**	1,332	1,489
Trade and other receivables		**1,658**	1,970	2,328
Derivative financial assets		**47**	19	15
Current tax assets		**23**	20	74
Cash and cash equivalents		**311**	512	511
Assets classified as held for sale		**–**	65	–
		3,165	3,918	4,417
Total assets	3	**16,680**	18,240	19,840
Current liabilities				
Trade and other payables		**2,456**	2,461	2,583
Interest-bearing loans and borrowings		**165**	284	473
Lease obligations		**81**	71	5
Derivative financial liabilities		**58**	106	204
Current tax liabilities		**188**	106	137
Provisions	10	**415**	412	391
Liabilities associated with assets held for sale		**–**	46	–
		3,363	3,486	3,793
Net current (liabilities)/assets		**(198)**	432	624
Non-current liabilities				
Trade and other payables		**421**	444	762
Interest-bearing loans and borrowings		**2,926**	3,464	3,378
Lease obligations		**474**	511	52
Derivative financial liabilities		**210**	216	227
Deferred tax liabilities		**732**	772	874
Retirement benefit obligations	11	**838**	1,121	1,413
Provisions	10	**606**	675	1,080
		6,207	7,203	7,786
Total liabilities	3	**9,570**	10,689	11,579
Net assets		**7,110**	7,551	8,261
Equity				
Issued share capital		**333**	333	333
Share premium account		**8,138**	8,138	8,138
Merger reserve		**109**	109	109
Other reserves		**(2,330)**	(2,330)	(2,330)
Translation and hedging reserve		**(30)**	78	495
Retained earnings		**861**	1,197	1,492
Equity attributable to owners of the parent		**7,081**	7,525	8,237
Non-controlling interests		**29**	26	24
Total equity		**7,110**	7,551	8,261

(1) Cash and cash equivalents and current interest-bearing loans and borrowings have been restated to meet the requirements of IAS 32 as further described in note 1. This has had no impact on net assets.

The Financial Statements were approved and authorised for issue by the Board of Directors on 4 March 2021 and were signed on its behalf by:

Geoffrey Martin
Group Finance Director
4 March 2021

Simon Peckham
Chief Executive
4 March 2021

Consolidated Statement of Changes in Equity

	Issued share capital £m	Share premium account £m	Merger reserve £m	Other reserves £m	Translation and hedging reserve £m	Retained earnings £m	**Equity attributable to owners of the parent £m**	Non-controlling interests £m	**Total equity £m**
At 1 January 2019	333	8,138	109	(2,330)	495	1,492	**8,237**	24	**8,261**
(Loss)/profit for the year	–	–	–	–	–	(60)	**(60)**	9	**(51)**
Other comprehensive expense	–	–	–	–	(417)	(17)	**(434)**	(1)	**(435)**
Total comprehensive (expense)/income	–	–	–	–	(417)	(77)	**(494)**	8	**(486)**
Dividends paid	–	–	–	–	–	(231)	**(231)**	(6)	**(237)**
Equity-settled share-based payments	–	–	–	–	–	13	**13**	–	**13**
At 31 December 2019	333	8,138	109	(2,330)	78	1,197	**7,525**	26	**7,551**
(Loss)/profit for the year	–	–	–	–	–	(536)	**(536)**	3	**(533)**
Other comprehensive (expense)/income	–	–	–	–	(108)	186	**78**	–	**78**
Total comprehensive (expense)/income	–	–	–	–	(108)	(350)	**(458)**	3	**(455)**
Equity-settled share-based payments	–	–	–	–	–	14	**14**	–	**14**
At 31 December 2020	**333**	**8,138**	**109**	**(2,330)**	**(30)**	**861**	**7,081**	**29**	**7,110**

Notes to the Financial Statements

1. Corporate information

The financial information included within this Preliminary Announcement does not constitute the Company's statutory Financial Statements for the years ended 31 December 2020 or 31 December 2019 within the meaning of s435 of the Companies Act 2006, but is derived from those Financial Statements. Statutory Financial Statements for the year ended 31 December 2019 have been delivered to the Registrar of Companies and those for the year ended 31 December 2020 will be delivered to the Registrar of Companies during April 2021. The auditor has reported on those Financial Statements; their reports were unqualified, did not draw attention to any matters by way of emphasis and did not contain statements under s498(2) or (3) of the Companies Act 2006.

While the financial information included in this Preliminary Announcement has been prepared in accordance with the recognition and measurement criteria of International Financial Reporting Standards ("IFRSs") adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union in addition to IFRSs as issued by the IASB, this announcement does not itself contain sufficient information to comply with IFRSs. The Company expects to publish full Financial Statements that comply with IFRSs during April 2021.

Corporate structure

On 2 January 2020, the Powder Metallurgy division completed the acquisition of FORECAST 3D, a leading US specialist in plastic additive manufacturing and 3D printing services offering a full range of services from concept to series production for consideration of up to £29 million. The acquisition furthers Powder Metallurgy's ambition to achieve global market leadership in industrialising additive manufacturing.

On 25 November 2020, the Group completed the disposal of the Wheels & Structures business to Aurelius Group AG, and in the prior year completed the disposal of the Walterscheid Powertrain Group. The Wheels & Structures business is shown as a discontinued operation in these Consolidated Financial Statements prior to its disposal.

Prior year restatement of cash and cash equivalents and bank overdrafts

During the year, the Group changed the presentation of cash and cash equivalents and bank overdrafts within the Balance Sheet relating to cash pooling arrangements. While the Group has the legal right to offset amounts under these cash pooling arrangements, it was determined that the appropriate current and prior year presentation should be on a gross basis in line with the requirements of IAS 32: "Financial Instruments: Presentation" and other associated interpretations. Prior year comparatives have been restated accordingly. The impact of this change is to increase both cash and cash equivalents and bank overdrafts within current interest-bearing loans and borrowings by £195 million as at 31 December 2019, and by £96 million as at 31 December 2018 in the Balance Sheet. This has no impact on net assets or other primary statements.

Going concern

The Consolidated Financial Statements have been prepared on a going concern basis as the Directors consider that adequate resources exist for the Company to continue in operational existence for the foreseeable future.

The Group's liquidity and funding arrangements are described in the Finance Director's Review. There is significant liquidity headroom in excess of £1.6 billion at 31 December 2020 and sufficient headroom throughout the going concern forecast period. There has been a greater focus on forecast covenant compliance which is considered further below.

Covenants

The Group's banking facility has two financial covenants being a net debt to adjusted EBITDA covenant and an interest cover covenant, both of which are tested half yearly in June and December. The net debt to adjusted EBITDA covenant test was originally set at 3.5x and the interest cover covenant was originally set at 4.0x for each of the half yearly measurement dates for the remainder of the term of the facility.

Due to the pervasive impact of COVID-19 on certain of the Group's businesses, it was necessary to formally renegotiate the financial covenants with lending banks. The revised financial covenants during the period of assessment for going concern are as follows:

	31 December 2020	30 June 2021	31 December 2021
Net debt to adjusted EBITDA	**Waived**	Waived	5.25x
Interest cover	**2.5x**	3.0x	3.0x

Testing

The Group has modelled two scenarios in its assessment of going concern; a base case and a reasonably possible sensitised case. Please refer to note 8 for further details of the Group's forecasting considerations.

The base case takes into account the estimated impact of the COVID-19 global pandemic as well as other end market and operational factors throughout the going concern period and has been monitored against the actual results and cash generation in the year. Due to the severe impact on trading during the second quarter of 2020, along with ways of working to accommodate social distancing and other regulations in factories, it is difficult to estimate with precision the impact on the Group's prospective financial performance although improvements were seen in certain businesses within the Group in the second half of 2020.

The reasonably possible sensitised case models a reduction in sales in 2021 and the first half of 2022 compared to the base case. A 5% decline in revenue in 2021 and 9% decline in H1 2022 over and above the base case has been included, taking into account the different businesses and geographies affected, with an impact on adjusted operating profit of between 27% and 41% of absolute revenue changes. This does not take into account the potential outcome of further factory closures for any significant length of time.

Under the reasonably possible sensitised case, no covenant is breached at any of the forecast testing dates being; 30 June 2021 and 31 December 2021, with the testing at 30 June 2022 also favourable, and the Group will not require any additional sources of finance.

The reasonably possible sensitised case has also been used as a 'reverse stress test' to consider the point at which the covenants may be breached. This reverse stress test indicates that a significant reduction in sales, beyond what is considered reasonable, would be required in order to breach covenants. In this remote situation, management could take further mitigating actions to protect profits and conserve cash, including reducing capital expenditure to minimum maintenance levels. Annual adjusted operating profit would need to fall by c.£150 million from that achieved in the year ended 31 December 2020 or by c.£350 million from the annualised amount achieved in the second half of the year, before a covenant breach would occur in the assessment period.

2. Alternative Performance Measures

The Group presents Alternative Performance Measures ("APMs") in addition to the statutory results of the Group. These are presented in accordance with the Guidelines on APMs issued by the European Securities and Markets Authority ("ESMA").

APMs used by the Group are set out in the glossary to this Preliminary Announcement and the reconciling items between statutory and adjusted results are listed below and described in more detail in note 4.

Adjusted revenue includes the Group's share of revenue from equity accounted investments ("EAIs").

Adjusted profit measures exclude items which are significant in size or volatility or by nature are non-trading or non-recurring, any item released to the Income Statement that was previously a fair value item booked on an acquisition, and include adjusted profit from EAIs.

On this basis, the following are the principal items included within adjusting items impacting operating profit:

- Amortisation of intangible assets that are acquired in a business combination, excluding computer software and development costs;
- Significant restructuring costs and other associated costs, including losses incurred following the announcement of closure for identified businesses, arising from significant strategy changes that are not considered by the Group to be part of the normal operating costs of the business;
- Acquisition and disposal related costs;
- Impairment charges that are considered to be significant in nature and/or value to the trading performance of the business;
- Movement in derivative financial instruments not designated in hedging relationships, including revaluation of associated financial assets and liabilities;
- Removal of adjusting items, interest and tax on equity accounted investments to reflect operating results;
- The charge for the Melrose equity-settled compensation scheme, including its associated employer's tax charge;
- Costs associated with the gender equalisation of guaranteed minimum pension ("GMP") for occupational schemes; and
- The net release of fair value items booked on acquisitions.

Further to the adjusting items above, adjusting items impacting profit before tax include:

- Acceleration of unamortised debt issue costs written off as a consequence of Group refinancing; and
- The fair value changes on cross-currency swaps, entered into by GKN prior to acquisition, relating to cost of hedging which are not deferred in equity.

In addition to the items above, adjusting items impacting profit after tax include:

- The net effect on tax of significant restructuring from strategy changes that are not considered by the Group to be part of the normal operating costs of the business; and
- The tax effects of adjustments to profit/(loss) before tax.

The Board considers the adjusted results to be an important measure used to monitor how the businesses are performing as this provides a meaningful reflection of how the businesses are managed and measured on a day-to-day basis and achieves consistency and comparability between reporting periods, when all businesses are held for a complete reporting period.

The adjusted measures are used to partly determine the variable element of remuneration of senior management throughout the Group and are also in alignment with performance measures used by certain external stakeholders. The adjusted measures are also taken into account when valuing individual businesses as part of the "Buy, Improve, Sell" Group strategy model.

Adjusted profit is not a defined term under IFRS and may not be comparable with similarly titled profit measures reported by other companies. It is not intended to be a substitute for, or superior to, GAAP measures. All APMs relate to the current year results and comparative periods where provided.

3. Segment information

Segment information is presented in accordance with IFRS 8: "Operating Segments" which requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reported to the Group's Chief Operating Decision Maker ("CODM"), which has been deemed to be the Group's Board, in order to allocate resources to the segments and assess their performance.

The operating segments are as follows:

Aerospace – a multi-technology global tier one supplier of both civil and defence airframes and engine structures.

Automotive – a global technology and systems engineer which designs, develops, manufactures and integrates an extensive range of driveline technologies, including electric vehicle components.

Powder Metallurgy – a global leader in precision powder metal parts for the automotive and industrial sectors, as well as the production of powder metal.

Nortek Air Management – comprises the Group's Air Management businesses, which includes the Air Quality and Home Solutions business ("AQH") and the Global Heating, Ventilation & Air Conditioning business ("HVAC"). AQH is a leading manufacturer of ventilation products for the professional remodelling and replacement markets, residential new construction market and DIY market. HVAC manufactures and sells split-system and packaged air conditioners, heat pumps, furnaces, air handlers and parts for the residential replacement and new construction markets along with custom designed and engineered products and systems for data centres and non-residential applications.

Other Industrial – comprises the Group's Ergotron, Brush and Nortek Control (formerly Security & Smart Technology) businesses.

In addition, there are central cost centres which are also reported to the Board. The central corporate cost centres contain the Melrose Group head office costs and charges related to the divisional management long-term incentive plans.

Reportable segment results include items directly attributable to a segment as well as those which can be allocated on a reasonable basis. Inter-segment pricing is determined on an arm's length basis in a manner similar to transactions with third parties.

The Group's geographical segments are determined by the location of the Group's non-current assets and, for revenue, the location of external customers. Inter-segment sales are not material and have not been disclosed.

The following tables present the results and certain asset and liability information regarding the Group's operating segments and central cost centres for the year ended 31 December 2020.

a) Segment revenues

The Group derives its revenue from the transfer of goods and services over time and at a point in time. The Group has assessed that the disaggregation of revenue recognised from contracts with customers by operating segment is appropriate as this is the information regularly reviewed by the CODM in evaluating financial performance. The Group also believes that presenting this disaggregation of revenue based on the timing of transfer of goods or services provides useful information as to the nature and timing of revenue from contracts with customers.

Year ended 31 December 2020 **Continuing operations**	Aerospace £m	Automotive £m	Powder Metallurgy £m	Nortek Air Management £m	Other Industrial £m	Total £m
Adjusted revenue	**2,804**	**3,797**	**905**	**1,227**	**628**	**9,361**
Equity accounted investments	(6)	(566)	(19)	–	–	(591)
Revenue	**2,798**	**3,231**	**886**	**1,227**	**628**	**8,770**
Timing of revenue recognition						
At a point in time	1,704	3,231	886	1,155	624	7,600
Over time	1,094	–	–	72	4	1,170
Revenue	**2,798**	**3,231**	**886**	**1,227**	**628**	**8,770**

Year ended 31 December 2019 Continuing operations	Aerospace £m	Automotive £m	Powder Metallurgy £m	Nortek Air Management £m	Other Industrial £m	Total £m
Adjusted revenue	**3,852**	**4,739**	**1,115**	**1,178**	**708**	**11,592**
Equity accounted investments	(16)	(593)	(16)	–	–	(625)
Revenue	**3,836**	**4,146**	**1,099**	**1,178**	**708**	**10,967**
Timing of revenue recognition						
At a point in time	2,644	4,146	1,099	1,157	705	9,751
Over time	1,192	–	–	21	3	1,216
Revenue	**3,836**	**4,146**	**1,099**	**1,178**	**708**	**10,967**

b) Segment operating profit

Year ended 31 December 2020 **Continuing operations**	Aerospace £m	Automotive £m	Powder Metallurgy £m	Nortek Air Management £m	Other Industrial £m	Corporate[(2)] £m	Total £m
Adjusted operating profit/(loss)	**14**	**82**	**39**	**188**	**63**	**(46)**	**340**
Items not included in adjusted operating profit[(1)]:							
Amortisation of intangible assets acquired in business combinations	(256)	(147)	(52)	(36)	(35)	–	(526)
Restructuring costs	(110)	(60)	(48)	(3)	3	(2)	(220)
Impairment of assets	(133)	(21)	(30)	–	–	–	(184)
Equity accounted investments adjustments	–	(30)	–	–	–	–	(30)
Melrose equity-settled compensation scheme charges	–	–	–	–	–	(11)	(11)
Acquisition and disposal costs	–	–	–	–	–	(5)	(5)
Impact of GMP equalisation on UK pension schemes	(1)	(1)	–	–	–	–	(2)
Movement in derivatives and associated financial assets and liabilities	(9)	(2)	–	–	–	193	182
Net release and changes in discount rates of fair value items	85	(4)	34	–	3	–	118
Operating (loss)/profit	**(410)**	**(183)**	**(57)**	**149**	**34**	**129**	**(338)**
Finance costs							(200)
Finance income							3
Loss before tax							**(535)**
Tax							12
Loss for the year from continuing operations							**(523)**

Year ended 31 December 2019 Continuing operations	Aerospace £m	Automotive £m	Powder Metallurgy £m	Nortek Air Management £m	Other Industrial £m	Corporate[2] £m	Total £m
Adjusted operating profit/(loss)	**409**	**367**	**117**	**175**	**86**	**(52)**	**1,102**
Items not included in adjusted operating profit[1]:							
Amortisation of intangible assets acquired in business combinations	(261)	(148)	(48)	(36)	(41)	–	(534)
Restructuring costs	(79)	(83)	(19)	(11)	(37)	(9)	(238)
Impairment of assets	–	–	–	–	(179)	–	(179)
Equity accounted investments adjustments	(1)	(27)	–	–	–	–	(28)
Melrose equity-settled compensation scheme charges	–	–	–	–	–	(17)	(17)
Net release and changes in discount rates of fair value items	34	79	28	11	1	–	153
Movement in derivatives and associated financial assets and liabilities	2	(2)	–	–	–	55	55
Acquisition and disposal costs	–	–	(1)	–	–	5	4
Operating profit/(loss)	**104**	**186**	**77**	**139**	**(170)**	**(18)**	**318**
Finance costs							(221)
Finance income							9
Profit before tax							**106**
Tax							(51)
Profit for the year from continuing operations							**55**

(1) Further details on adjusting items are discussed in note 4.
(2) Corporate adjusted operating loss of £46 million (2019: £52 million), includes £12 million (2019: £20 million) of costs in respect of divisional long-term incentive plans.

c) Segment total assets and liabilities

	Total assets		Total liabilities	
	31 December 2020 £m	Restated[1] 31 December 2019 £m	**31 December 2020 £m**	Restated[1] 31 December 2019 £m
Aerospace	**6,614**	7,478	**2,691**	3,089
Automotive	**5,172**	5,391	**2,407**	2,304
Powder Metallurgy	**1,816**	1,906	**476**	472
Nortek Air Management	**1,436**	1,415	**500**	362
Other Industrial	**1,129**	1,237	**215**	259
Corporate	**513**	748	**3,281**	4,157
Total continuing operations	**16,680**	18,175	**9,570**	10,643
Discontinued operations	**–**	65	**–**	46
Total	**16,680**	18,240	**9,570**	10,689

(1) Cash and cash equivalents and current interest-bearing loans and borrowings have been restated to meet the requirements of IAS 32 as further described in note 1. This impacts the total assets and total liabilities within Corporate.

d) Segment capital expenditure and depreciation

	Capital expenditure[1]		Depreciation of owned assets[1]		Depreciation of leased assets	
	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Aerospace	**98**	178	**121**	139	**28**	30
Automotive	**130**	231	**199**	194	**18**	16
Powder Metallurgy	**33**	55	**61**	59	**9**	8
Nortek Air Management	**23**	37	**26**	23	**13**	11
Other Industrial	**6**	8	**10**	11	**5**	6
Corporate	**–**	–	**1**	–	**1**	1
Total continuing operations	**290**	509	**418**	426	**74**	72
Discontinued operations	**–**	11	**–**	12	**–**	1
Total	**290**	520	**418**	438	**74**	73

(1) Including computer software and development costs. Capital expenditure excludes lease additions.

e) Geographical information

The Group operates in various geographical areas around the world. The parent company's country of domicile is the UK and the Group's revenues and non-current assets in the rest of Europe and North America are also considered to be material.

The Group's revenue from external customers and information about its segment assets (non-current assets excluding deferred tax assets; non-current trade and other receivables; and non-current derivative financial assets) by geographical location are detailed below:

	Revenue[(1)] from external customers		**Segment assets**	
	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m	**31 December 2020 £m**	31 December 2019 £m
UK	**646**	1,048	**2,166**	2,319
Rest of Europe	**1,989**	2,426	**4,871**	5,136
North America	**5,004**	6,073	**4,535**	4,917
Other	**1,131**	1,420	**1,223**	1,328
Continuing operations	**8,770**	10,967	**12,795**	13,700
Discontinued operations	**144**	423	**–**	–
Total	**8,914**	11,390	**12,795**	13,700

(1) Revenue is presented by destination.

4. Reconciliation of adjusted profit measures

As described in note 2, adjusted profit measures are an alternative performance measure used by the Board to monitor the operating performance of the Group.

a) Operating profit

Continuing operations	Notes	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Operating (loss)/profit		**(338)**	318
Amortisation of intangible assets acquired in business combinations	a	**526**	534
Restructuring costs	b	**220**	238
Impairment of assets	c	**184**	179
Equity accounted investments adjustments	d	**30**	28
Melrose equity-settled compensation scheme charges	e	**11**	17
Acquisition and disposal costs	f	**5**	(4)
Impact of GMP equalisation on UK pension schemes	g	**2**	–
Movement in derivatives and associated financial assets and liabilities	h	**(182)**	(55)
Net release and changes in discount rate of fair value items	i	**(118)**	(153)
Total adjustments to operating (loss)/profit		**678**	784
Adjusted operating profit		**340**	1,102

a. The amortisation charge on intangible assets acquired in business combinations of £526 million (2019: £534 million) is excluded from adjusted results due to its non-trading nature and to enable comparison with companies that grow organically. However, where intangible assets are trading in nature, such as computer software and development costs, the amortisation is not excluded from adjusted results.

b. Restructuring and other associated costs in the year totalling £220 million (2019: £238 million) are shown as adjusting items due to their size and non-trading nature. During the year ended 31 December 2020 these included:

- A charge of £110 million (2019: £79 million) within the Aerospace division primarily relating to costs incurred globally to reduce the business' headcount and cost structure in reaction to the significant impact that COVID-19 is having on the aerospace industry. This charge also included costs in respect of the continuation of the business' global integration, announced last year, to create "One Aerospace", ensuring the business is well positioned and able to react to changes in its new environment; and the continuation of costs relating to rationalisation projects commenced in the previous year.

- A charge of £60 million (2019: £83 million) within the Automotive division, as the business has accelerated its efforts to address its high cost base, inherited on acquisition, and best position itself as it recovers post COVID-19.

- A charge of £48 million (2019: £19 million) within the Powder Metallurgy division including costs associated with realigning the business for future demand, along with consolidation actions started in 2019 and the commencement during 2020 of the closure of a site in its underperforming North American Structural business.

- A net charge of £2 million (2019: £57 million) within the Nortek Air Management, Other Industrial and Corporate divisions which includes the completion of a factory consolidation within the HVAC business; the finalisation of the changes made in the Nortek Control business to move to a third party contract manufacturing model; and the profit from the disposal of a Dutch property held within the Brush business left vacant following the factory consolidation programme commenced in 2018.

c. The write down of assets in the year of £184 million, mostly recognised in the second quarter of the year as a result of the impact of COVID-19, includes £133 million within the Aerospace division. As a result of the impact of the pandemic, a review of the operating assets of the Group was performed and resulted in £159 million of fixed assets and £25 million of other net operating assets being written down across certain sites within the businesses, as they adapted to new levels of industry demand. The write down of these assets is shown as an adjusting item due to the unprecedented nature of the COVID-19 pandemic, its non-trading nature and size. The charge of £179 million, recognised in 2019, related to impairment of goodwill allocated to the Nortek Control group of CGUs.

d. The Group has a number of equity accounted investments ("EAIs") in which it does not hold full control, the largest of which is a 50% interest in Shanghai GKN HUAYU Driveline Systems ("SDS"), within the Automotive business. The EAIs generated £591 million (2019: £625 million) of revenue in the year, which is not included in the statutory results but is shown within adjusted revenue so as not to distort the operating margins reported in the businesses when the adjusted operating profit earned from these EAIs is included.

   In addition, the profits and losses of EAIs, which are shown after amortisation of acquired intangible assets, interest and tax in the statutory results, are adjusted to show the adjusted operating profit consistent with the adjusted operating profits of the subsidiaries of the Group. The revenue and profit of EAIs are adjusted because they are considered to be significant in size and are important in assessing the performance of the business.

e. The charge for the Melrose equity-settled Employee Share Scheme, including its associated employer's tax charge, of £11 million (2019: £17 million) is excluded from adjusted results due to its size and volatility. The shares that would be issued, based on the Scheme's current value at the end of the reporting period, are included in the calculation of the adjusted diluted earnings per share, which the Board considers to be a key measure of performance.

f. Acquisition and disposal related costs of £5 million (2019: net credit of £4 million), arose in the year. These items are excluded from adjusted results due to their non-trading nature.

g. During the year the Company incurred a further £2 million in respect of gender equalisation of guaranteed minimum pensions for occupational pension schemes in the UK. This charge resulted from amendments made in 2020 to a High Court judgment from October 2018. For consistency with the accounting treatment in 2018 and because of its non-trading nature the charge is excluded from adjusted results.

h. Movements in the fair value of derivative financial instruments (primarily forward foreign currency exchange contracts where hedge accounting is not applied) entered into within the GKN businesses to mitigate the potential volatility of future cash flows, on long-term foreign currency customer and supplier contracts, along with foreign exchange movements on the associated financial assets and liabilities is shown as an adjusting item because of its volatility and size. This totalled a credit of £182 million (2019: £55 million) in the year.

i. The net release of fair value items in the year of £118 million (2019: £153 million) where items have been resolved for more favourable amounts than first anticipated is shown as an adjusting item, avoiding positively distorting adjusted operating profit. During the year this included a net release of £101 million in respect of loss-making contract provisions, held within the GKN businesses, where either contractual terms have been renegotiated with the relevant customer or operational efficiencies have been identified and demonstrated for a sustained period.

b) Profit before tax

Continuing operations	Notes	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
(Loss)/profit before tax		**(535)**	106
Adjustments to operating (loss)/profit as above		**678**	784
Bank facility negotiation fees	j	**8**	–
Fair value changes on cross-currency swaps	k	**2**	(1)
Total adjustments to (loss)/profit before tax		**688**	783
Adjusted profit before tax		**153**	889

j. Following the impact of COVID-19, the Group paid fees in negotiating waivers and amendments to its bank facility covenants for the remaining period of the facilities. These fees were immediately written off and are shown as an adjusting item because of their non-trading nature.

k. The fair value changes on cross-currency swaps relating to cost of hedging which are not deferred in equity, is shown as an adjusting item because of its volatility and non-trading nature.

c) Profit after tax

Continuing operations	Notes	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
(Loss)/profit after tax		**(523)**	55
Adjustments to (loss)/profit before tax as above		**688**	783
Tax effect of adjustments to (loss)/profit before tax	5	**(115)**	(123)
Tax effect of significant restructuring	5	**78**	(9)
Equity accounted investments – tax	l	**(8)**	(7)
Total adjustments to (loss)/profit after tax		**643**	644
Adjusted profit after tax		**120**	699

l. As explained in paragraph d above, the profits and losses of EAIs are shown after interest and tax in the statutory results. They are adjusted to show the profit before tax and the profit after tax, consistent with the subsidiaries of the Group.

5. Tax

Continuing operations	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Analysis of tax (credit)/charge in the year:		
Current tax		
Current year tax charge	**88**	156
Adjustments in respect of prior years	**(12)**	(10)
Total current tax charge	**76**	146
Deferred tax		
Origination and reversal of temporary differences	**(188)**	(89)
Adjustments in respect of prior years	**–**	5
Tax on the change in value of derivative financial instruments	**41**	(10)
Adjustments to deferred tax attributable to changes in tax rates	**(6)**	(2)
Non-recognition of deferred tax	**65**	17
Recognition of previously unrecognised deferred tax assets	**–**	(16)
Total deferred tax credit	**(88)**	(95)
Tax (credit)/charge on continuing operations	**(12)**	51
Tax charge on discontinued operations	**2**	3
Total tax (credit)/charge in the year	**(10)**	54

Analysis of (credit)/charge on continuing operations in the year:	**£m**	£m
Tax charge in respect of adjusted profit before tax	**33**	190
Tax credit recognised as an adjusting item	**(45)**	(139)
Total tax (credit)/charge on continuing operations	**(12)**	51

The tax charge of £33 million (2019: £190 million) arising on adjusted profit before tax of £153 million (2019: £889 million), results in an effective tax rate of 21.6% (2019: 21.4%).

The £45 million (2019: £139 million) tax credit recognised as an adjusting item includes £115 million (2019: £123 million) in respect of tax credits on adjustments to (loss)/profit before tax of £688 million (2019: £783 million), £8 million (2019: £7 million) in respect of the tax on equity accounted investments and a charge of £78 million (2019: credit of £9 million) in respect of restructuring, being a £71 million (2019: £nil) tax charge arising on the legal separation of the Nortek Air Management and Ergotron businesses and a £7 million charge (2019: credit of £9 million) arising from other internal Group restructuring.

The tax (credit)/charge for the year for continuing and discontinued operations can be reconciled to the (loss)/profit before tax per the Income Statement as follows:

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
(Loss)/profit before tax:		
Continuing operations	**(535)**	106
Discontinued operations	**–**	(82)
	(535)	24
Tax (credit)/charge on (loss)/profit before tax at the weighted average rate of 27.0% (2019: 21.0%)	**(144)**	5
Tax effect of:		
Disallowable expenses and other permanent differences within adjusted profit	**–**	6
Disallowable items included within adjusting items	**3**	54
Temporary differences not recognised in deferred tax	**65**	17
Recognition of previously unrecognised deferred tax assets	**–**	(16)
Tax credits, withholding taxes and other rate differences	**6**	4
Adjustments in respect of prior years	**(12)**	(5)
Tax charge/(credit) classified within adjusting items	**78**	(9)
Effect of changes in tax rates	**(6)**	(2)
Total tax (credit)/charge for the year	**(10)**	54

The reconciliation has been performed at a blended Group tax rate of 27.0% (2019: 21.0%) which represents the weighted average of the tax rates applying to profits and losses in the jurisdictions in which those results arose in 2020.

Tax charges included in Other Comprehensive Income are as follows:

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Deferred tax on retirement benefit obligations	**42**	(15)
Deferred tax on hedge relationship gains and losses	**(9)**	16
Deferred tax on foreign currency gains and losses	**–**	3
Total charge for the year	**33**	4

6. Dividends

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Final dividend for the year ended 31 December 2019	**–**	–
Interim dividend for the year ended 31 December 2020	**–**	–
Final dividend for the year ended 31 December 2018 of 3.05p	**–**	148
Interim dividend for the year ended 31 December 2019 of 1.7p	**–**	83
	–	231

Proposed final dividend for the year ended 31 December 2020 of 0.75p per share totalling £36 million. The initially proposed final dividend for the year ended 31 December 2019 of 3.4p per ordinary share was withdrawn as announced on 7 May 2020.

The final dividend of 0.75p per share was proposed by the Board on 4 March 2021 and in accordance with IAS 10: "Events after the reporting period", has not been included as a liability in the Consolidated Financial Statements.

7. Earnings per share

Earnings attributable to owners of the parent	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Earnings for basis of earnings per share	**(536)**	(60)
Less: loss for the year from discontinued operations	**10**	106
Earnings for basis of earnings per share from continuing operations	**(526)**	46

	Year ended 31 December 2020 Number	Year ended 31 December 2019 Number
Weighted average number of ordinary shares for the purposes of basic earnings per share (million)	**4,858**	4,858
Further shares for the purposes of diluted earnings per share (million)	**–**	–
Weighted average number of ordinary shares for the purposes of diluted earnings per share (million)	**4,858**	4,858

Earnings per share	Year ended 31 December 2020 pence	Year ended 31 December 2019 pence
Basic earnings per share		
From continuing and discontinued operations	**(11.0)**	(1.2)
From continuing operations	**(10.8)**	0.9
From discontinued operations	**(0.2)**	(2.1)
Diluted earnings per share		
From continuing and discontinued operations	**(11.0)**	(1.2)
From continuing operations	**(10.8)**	0.9
From discontinued operations	**(0.2)**	(2.1)

Adjusted earnings from continued operations	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Adjusted earnings for the basis of adjusted earnings per share(1)	**117**	693

(1) Adjusted earnings for the year ended 31 December 2020 comprises adjusted profit after tax of £120 million (2019: £699 million) (note 4), net of an allocation to non-controlling interest of £3 million (2019: £6 million).

Adjusted earnings per share from continuing operations

	Year ended 31 December 2020 pence	Year ended 31 December 2019 pence
Adjusted basic earnings per share	**2.4**	14.3
Adjusted diluted earnings per share	**2.4**	14.3

8. Goodwill and other intangible assets

Goodwill acquired in business combinations, net of impairment, has been allocated to the businesses, each of which comprises several cash-generating units ("CGUs").

Goodwill	**31 December 2020 £m**	31 December 2019 £m
AQH	**345**	355
HVAC	**230**	237
Nortek Control	**167**	172
Ergotron	**406**	418
Aerostructures(1)	**605**	595
Aerospace Engine Systems	**337**	346
Aerospace	**942**	941
Automotive Driveline	**690**	688
Automotive ePowertrain	**336**	339
Automotive	**1,026**	1,027
Powder Metallurgy	**524**	503
	3,640	3,653

(1) Reflects the revised groups of CGUs effective 1 January 2020 whereby the Aerostructures and Aerospace Special Technologies groups of CGUs were organised into one group of CGUs.

Impairment testing

The Group tests goodwill annually or more frequently if there are indications that goodwill might be impaired. In accordance with IAS 36: "Impairment of assets" the Group values goodwill at the recoverable amount, being the higher of the value in use basis and the fair value less costs to sell basis. Due to the maturity of the different groups of CGUs within Melrose's strategic life cycle of "Buy, Improve, Sell" the value in use methodology generally yields a higher recoverable amount for businesses owned for a longer time and fair value less costs to sell give a higher value where the improvement phase is ongoing.

Value in use calculations have been used to determine the recoverable amount of goodwill and other relevant net assets allocated to the AQH, HVAC and Ergotron groups of CGUs. The calculation used the latest approved forecasts extrapolated into perpetuity using growth rates shown below, which do not exceed the long-term growth rate for the relevant market.

Fair value less costs to sell calculations have been used to determine the recoverable amount of goodwill and other relevant net assets allocated to the Aerostructures, Aerospace Engine Systems, Automotive Driveline, Automotive ePowertrain, Powder Metallurgy and Nortek Control groups of CGUs. When applying the fair value less cost to sell methodology, it has been difficult to assess a sale value using observable market inputs (level 1) or inputs based on market evidence (level 2) in the current environment and so unobservable inputs (level 3) have been used. A combination of discounted cash flows and EBITDA multiples have been used to establish fair values for each of the groups of CGUs.

Under IAS 36, the value in use basis prohibits inclusion of benefits from future uncommitted restructuring plans although this is permitted when applying the fair value less costs to sell basis, to the extent that similar actions would be carried out by a market participant.

Based on impairment testing completed no impairment was identified in respect of any of the groups of CGUs. Impairment testing has been performed for both the groups of CGUs as at 31 October 2020, as well as those revised groups of CGUs as at 31 December 2020. There is no reasonably possible change in key assumptions that could result in an impairment in the AQH and HVAC groups of CGUs.

The COVID-19 pandemic is having a significant impact on global end markets in which certain of the Group's businesses operate which has resulted in reduced levels of headroom, such that sensitivity analysis has been provided in respect of reasonably possible changes to key assumptions.

Significant assumptions and estimates

The basis of impairment tests and the key assumptions are set out in the tables below:

	31 December 2020(1)			31 December 2019		
Groups of CGUs – value in use	**Pre-tax discount rates**	**Long-term growth rates**	**Years in forecast**	Pre-tax discount rates	Long-term growth rates	Years in forecast
AQH	**9.5%**	**3.0%**	**3**	11.0%	3.3%	3
HVAC	**9.5%**	**2.8%**	**3**	11.2%	3.1%	3
Ergotron	**9.4%**	**3.0%**	**3**	10.9%	3.4%	3

	31 December 2020(1)			31 December 2019		
Groups of CGUs – fair value less costs to sell	**Post-tax discount rates(3)**	**Long-term growth rates**	**Years in forecast**	Pre-tax discount rates(3)	Long-term growth rates	Years in forecast
Nortek Control	**7.8%**	**2.9%**	**3**	11.5%	3.5%	3
Aerostructures(2)	**7.5%**	**2.9%**	**5**	9.4%	2.9%	5
Aerospace Engine Systems	**7.0%**	**2.7%**	**5**	9.4%	3.0%	5
Automotive Driveline	**9.8%**	**2.5%**	**5**	13.5%	2.5%	5
Automotive ePowertrain	**7.8%**	**2.4%**	**5**	10.0%	2.8%	5
Powder Metallurgy	**9.0%**	**2.5%**	**5**	11.8%	2.5%	5

(1) Shows discount rates used in the annual impairment test for the year ended 31 December 2020, which was performed on 31 October 2020.
(2) Reflects the revised groups of CGUs effective 1 January 2020 whereby the Aerostructures and Aerospace Special Technologies groups of CGUs were organised into one group of CGUs.
(3) The groups of CGUs tested in 2020 had a higher recoverable amount under the fair value less costs to sell methodology, which requires the use of post-tax discount rates. The groups of CGUs tested in 2019 had a higher recoverable amount under the value in use methodology, which requires the use of pre-tax discount rates, and so pre-tax discount rates are shown as a comparative.

Risk adjusted discount rates
Cash flows within the AQH, HVAC and Ergotron groups of CGUs are discounted using a pre-tax discount rate specific to each group of CGUs. Cash flows within the Aerostructures, Aerospace Engine Systems, Automotive Driveline, Automotive ePowertrain, Powder Metallurgy and Nortek Control groups of CGUs are discounted using a post-tax discount rate specific to each group of CGUs. Discount rates reflect the current market assessments of the time value of money and the territories in which the group of CGUs operates. In determining the cost of equity, the Capital Asset Pricing Model ("CAPM") has been used. Under CAPM, the cost of equity is determined by adding a risk premium, based on an industry adjustment ("Beta"), to the expected return of the equity market above the risk-free return. The relative risk adjustment reflects the risk inherent in each group of CGUs relative to all other sectors and geographies on average.

The cost of debt is determined using a risk-free rate based on the cost of government bonds, and an interest rate premium equivalent to a corporate bond with a similar credit rating to Melrose.

Assumptions applied in financial forecasts
The Group prepares cash flow forecasts derived from financial budgets and medium-term forecasts. Each forecast has been prepared using a cash flow period deemed most appropriate by management, considering the nature of each group of CGUs. The key assumptions used in forecasting cash flows relate to future budgeted revenue and operating margins likely to be achieved and the expected rates of long-term growth by market sector. Underlying factors in determining the values assigned to each key assumption are shown below:

Revenue growth and operating margins:
Revenue growth assumptions in the forecast period are based on financial budgets and medium-term forecasts by management, taking into account industry growth rates and management's historical experience in the context of wider industry and economic conditions. Projected sales are built up with reference to markets and product categories. They incorporate past performance, historical growth rates, projections of developments in key markets, secured orders and orders forecast to be achieved in the short to medium term given trends in the relevant market sector. Revenue assumptions are made using external market data, where available, and also consider the recovery period to return to pre COVID-19 levels, and have been disclosed where appropriate for groups of CGUs within the sensitivities below.

Operating margins have been forecast based on historical levels achieved considering the likely impact of changing economic environments and competitive landscapes on volumes and revenues and the impact of management actions on costs. Projected margins reflect the impact of all initiated projects to improve operational efficiency and leverage scale and increase from returning sale volumes. The projections do not include the impact of future restructuring projects to which the Group is not yet committed, where testing has been performed using a value in use methodology. Where testing has been performed using the fair value less costs to sell methodology, the assumptions to derive operating profit margins take into account both normal cost saving activities and a significant contribution from planned restructuring activity. Forecasts for other operating costs are based on inflation forecasts and supply and demand factors.

Aerospace – The key drivers for growth in revenue and operating margins are global demand for commercial and military aircraft. Consumer spending, passenger load factors, raw material input costs, market expectations for aircraft production requirements, technological advancements, and other macro-economic factors influence demand for these products.

Automotive – The key drivers for growth in revenue and operating margins are global demand for a large range of cars including smaller low-cost cars to larger premium vehicles. Demand is influenced by technological advancements particularly in electric and full hybrid vehicles, market expectations for global vehicle production requirements, fuel prices, raw material input costs, consumer spending, credit availability, and other macro-economic factors.

Powder Metallurgy – The key drivers for growth in revenue and operating margins are trends in the automotive and industrial markets. Market expectations for global light vehicle production requirements, raw material input costs, technological advancements, particularly in additive manufacturing, influence demand for these products along with other macro-economic factors.

HVAC and AQH – The key drivers for growth in revenue and operating margins are the levels of residential remodelling and replacement activity, data centre global expansion and the levels of residential and non-residential new construction in the markets in which these businesses operate. New residential and non-residential construction activity and, to a lesser extent, residential remodelling and replacement activity are affected by seasonality and cyclical factors such as interest rates, credit availability, inflation, consumer spending, employment levels and other macro-economic factors.

Nortek Control – The key driver for growth in revenue and operating margins is global demand for newly-launched security and home automation products. Consumer spending, employment levels, regulation, technological advancements and the evolution of the traditional security market towards home automation and other macro-economic factors influence demand for these products.

Ergotron – The key driver for growth in revenue and operating margins is demand for technology and wellness products in the markets in which Ergotron operates. Seasonal factors, public authority spending, corporate and consumer spending, employment levels, the public awareness of wellness, regulation, technological advancements and other macro-economic factors influence demand for these products.

Long-term growth rates:
Long-term growth rates are based on long-term forecasts for growth in the sectors and geography in which the group of CGUs operates. Long-term growth rates are determined using long-term growth rate forecasts that take into account the international presence and the markets in which each business operates.

Sensitivity analysis impacting certain groups of CGUs
Due to the impact of COVID-19, certain businesses are mitigating the impact of lower levels of demand through cost reduction and efficiency actions, including restructuring. The Aerospace groups of CGUs remain the most severely affected by the pandemic, and as such management are not assuming that revenue returns to pre COVID-19 levels within the five year forecast period. Other groups of CGUs are assumed to recover within their forecast period.

Aerostructures group of CGUs – sensitivity analysis
The forecasts show headroom of £309 million above the carrying amount for the Aerostructures group of CGUs. Sensitivity analysis has been carried out and a reasonably possible change in the discount rate and long-term growth rate from 7.5% to 8.2% or from 2.9% to 2.1% respectively would reduce headroom to £nil. A failure to execute restructuring plans or a delay in currently anticipated market recovery would impact operating profit and operating margin assumptions and a reduction in the terminal operating profit of 14% would reduce the terminal operating margin by 1.0 percentage points and would reduce headroom to £nil. A reasonably possible change to revenue in the final year of the forecast period of 16% would also reduce the headroom to £nil.

Aerospace Engine Systems group of CGUs – sensitivity analysis

The forecasts show headroom of £437 million above the carrying amount for the Aerospace Engine Systems group of CGUs. Sensitivity analysis has been carried out and a reasonably possible change in the discount rate and long-term growth rate from 7.0% to 7.7% or from 2.7% to 1.9% respectively would reduce headroom to £nil. A delay in the forecast market recovery or execution of restructuring plans would impact operating profit and operating margin assumptions and a reduction in the terminal operating profit of 15% would reduce the terminal operating margin by 2.9 percentage points and would reduce headroom to £nil. A reasonably possible change to revenue in the final year of the forecast period of 16% would also reduce the headroom to £nil.

Powder Metallurgy group of CGUs – sensitivity analysis

The forecasts show headroom of £186 million above the carrying amount for the Powder Metallurgy group of CGUs. Sensitivity analysis has been carried out and a reasonably possible change in the discount rate and long-term growth rate from 9.0% to 9.8% or from 2.5% to 1.4% respectively would reduce headroom to £nil. Executing restructuring plans and optimising market penetration are key to margin assumptions and a reduction in the terminal operating profit of 13% would reduce the terminal operating margin by 1.8 percentage points and would reduce headroom to £nil.

Automotive Driveline group of CGUs – sensitivity analysis

The forecasts show headroom of £288 million above the carrying amount for the Automotive Driveline group of CGUs. Sensitivity analysis has been carried out and a reasonably possible change in the discount rate and long-term growth rate from 9.8% to 10.6% or from 2.5% to 1.3% respectively would reduce headroom to £nil. If restructuring plans are not appropriately executed or if there is a change in the market dynamics this could impact margin assumptions and a reduction in the terminal operating profit of 11% would reduce the terminal operating margin by 1.3 percentage points and would reduce headroom to £nil.

Automotive ePowertrain group of CGUs – sensitivity analysis

The forecasts show headroom of £213 million above the carrying amount for the Automotive ePowertrain group of CGUs. Sensitivity analysis has been carried out and a reasonably possible change in the discount rate and long-term growth rate from 7.8% to 8.7% or from 2.4% to 1.1% respectively would reduce headroom to £nil. If restructuring plans are not competed on a timely basis or there is a change in the electric vehicle market dynamics these could impact margin assumptions and a reduction in the terminal operating profit of 18% would reduce the terminal operating margin by 1.5 percentage points and would reduce headroom to £nil.

Nortek Control – sensitivity analysis

The forecasts show headroom of £135 million above the carrying amount for the Nortek Control group of CGUs. Sensitivity analysis has been carried out and a reasonably possible change in the discount rate and long-term growth rate from 7.8% to 9.8% or from 2.9% to 0.5% respectively would reduce headroom to £nil. A failure to deliver the successful launch of a new product and exploit potential market share could impact margin assumptions and a reduction in the terminal operating profit of 31% would reduce the terminal operating margin by 3.2 percentage points and would reduce headroom to £nil.

Ergotron – sensitivity analysis

As part of an internal reorganisation during the year, the Ergotron group of CGUs was valued at a little above its carrying amount. A failure to rebalance sales mix or exploit potential market share could impact margin assumptions and a reasonably possible small reduction in discount rate, growth rate or the terminal operating margin would reduce headroom to £nil.

9. Equity accounted investments

Group share of results from continuing operations	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Revenue	**591**	625
Operating costs	**(529)**	(559)
Adjusted operating profit	**62**	66
Adjusting items	**(22)**	(21)
Profit before tax	**40**	45
Tax	**(8)**	(7)
Share of results of equity accounted investments	**32**	38

10. Provisions

	Loss-making contracts £m	Property related costs £m	Environmental and litigation £m	Warranty related costs £m	Restructuring £m	Other £m	Total £m
At 1 January 2020	384	45	155	324	114	65	1,087
Utilised	(59)	(2)	(52)	(48)	(172)	(3)	(336)
Charge to operating profit(1)	15	1	108	83	216	15	438
Release to operating profit(2)	(108)	(2)	(17)	(34)	(13)	(8)	(182)
Unwind of discount(3)	6	–	–	–	–	–	6
Acquisition of businesses	–	1	–	–	–	–	1
Exchange adjustments	3	–	(3)	5	2	–	7
31 December 2020	**241**	**43**	**191**	**330**	**147**	**69**	**1,021**
Current	44	5	95	135	126	10	415
Non-current	197	38	96	195	21	59	606
	241	**43**	**191**	**330**	**147**	**69**	**1,021**

(1) Includes £234 million of adjusting items and £204 million recognised in adjusted operating profit.
(2) Includes £147 million of adjusting items and £35 million recognised in adjusted operating profit.
(3) Includes £2 million within finance costs relating to the time value of money and £4 million relating to changes in discount rates on loss-making contract provisions recognised as fair value items on the acquisition of GKN, which has been included as an adjusting item within operating profit (note 4).

Loss-making contracts

Provisions for loss-making contracts are considered to exist where the Group has a contract under which the unavoidable costs of meeting the obligations exceed the economic benefits expected to be received under it. This obligation has been discounted and will be utilised over the period of the respective contracts, which is up to 15 years.

Calculation of loss-making contract provisions is based on contract documentation and delivery expectations, along with an estimate of directly attributable costs and represents management's best estimate of the unavoidable costs of fulfilling the contract.

Utilisation during the year of £59 million (2019: £83 million) has benefited adjusted operating profit with £32 million recognised in Aerospace, £21 million recognised in Automotive, £5 million recognised in Powder Metallurgy and £1 million recognised in Other Industrial. In addition, £93 million has been released on a net basis with a net £101 million shown as an adjusting item, as described in note 4, as part of the release of fair value items split; £72 million in Aerospace, £36 million in Powder Metallurgy and a charge of £7 million in Automotive.

Property related costs

The provision for property related costs represents dilapidation costs for ongoing leases and is expected to result in cash expenditure over the next eight years. Calculation of dilapidation obligations are based on lease agreements with landlords and external quotes, or in the absence of specific documentation, management's best estimate of the costs required to fulfil obligations.

Environmental and litigation

Environmental and litigation provisions relate to the estimated remediation costs of pollution, soil and groundwater contamination at certain sites and estimated future costs and settlements in relation to legal claims and associated insurance obligations. Liabilities for environmental costs are recognised when environmental assessments are probable and the associated costs can be reasonably estimated.

Provisions are recorded for product and general liability claims which are probable and for which the cost can be reliably estimated. These liabilities include an estimate of claims incurred but not yet reported and are based on actuarial valuations using claim data. Due to their nature, it is not possible to predict precisely when these provisions will be utilised.

The Group has on occasion been required to take legal or other actions to defend itself against proceedings brought by other parties. Provisions are made for the expected costs associated with such matters, based on past experience of similar items and other known factors, considering professional advice received. This represents management's best estimate of the likely outcome. The timing of utilisation of these provisions is frequently uncertain, reflecting the complexity of issues and the outcome of various court proceedings and negotiations. Contractual and other provisions represent management's best estimate of the cost of settling future obligations and reflect management's assessment of the likely settlement method, which may change over time. However, no provision is made for proceedings which have been, or might be, brought by other parties against Group companies unless management, considering professional advice received, assess that it is more likely than not that such proceedings may be successful.

Warranty related costs

Provisions for the expected cost of warranty obligations under local sale of goods legislation are recognised at the date of sale of the relevant products and subsequently updated for changes in estimates as necessary. The provision for warranty related costs represents the best estimate of the expenditure required to settle the Group's obligations, based on past experience, recent claims and current estimates of costs relating to specific claims. Warranty terms are, on average, between one and five years.

Restructuring

Restructuring provisions relate to committed costs in respect of restructuring programmes, as described in note 4, usually resulting in cash spend within one year. A restructuring provision is recognised when the Group has developed a detailed formal plan for the restructuring and has raised a valid expectation in those affected that it will carry out the restructuring by either starting to implement the plan or by announcing its main features to those affected by it. The measurement of a restructuring provision includes only the direct expenditures arising from the restructuring, which are those amounts that are necessarily entailed by the restructuring programmes.

Other

Other provisions include long-term incentive plans for divisional senior management and the employer tax on equity-settled incentive schemes which are expected to result in cash expenditure in the next five years.

Where appropriate, provisions have been discounted using discount rates between 0% and 7% (31 December 2019: 0% and 7%) depending on the territory in which the provision resides and the length of its expected utilisation.

11. Retirement benefit obligations

Defined benefit plans

The Group sponsors defined benefit plans for qualifying employees of certain subsidiaries. The funded defined benefit plans are administered by separate funds that are legally separated from the Group. The Trustees of the funds are required by law to act in the interest of the fund and of all relevant stakeholders in the plans. The Trustees of the pension funds are responsible for the investment policy with regard to the assets of the fund.

Contributions

The Group committed on acquisition of GKN to contribute, and during 2019 completed payment of, £150 million in total to the GKN UK pension plans in the first 12 months of ownership, as well as ongoing annual contributions of £60 million. In addition, the Group has committed to contribute £270 million upon the disposal of Powder Metallurgy, 10% of the proceeds from disposal of other GKN businesses and 5% of the proceeds from disposal of non-GKN businesses to the GKN UK pension plans. These commitments cease when the funding target which has been agreed with Trustees is achieved, being gilts plus 25 basis points for the GKN UK 2016 plan and gilts plus 75 basis points for the GKN Group Pension Schemes (Numbers 1 – 4).

The Group contributed £111 million (2019: £185 million, including the remaining £94 million of the £150 million commitment on acquisition of GKN and a £17 million special contribution paid on disposals) to defined benefit pension plans and post-employment plans in the year ended 31 December 2020. The Group expects to contribute £98 million to defined benefit pension plans and post-employment plans in 2021.

Actuarial assumptions

The major assumptions used by the actuaries in calculating the Group's pension liabilities are as set out below:

	Rate of increase of pensions in payment % per annum	**Discount rate % per annum**	**Price inflation (RPI/CPI) % per annum**
31 December 2020			
GKN Group Pension Schemes (Numbers 1 – 4)	**2.4**	**1.4**	**2.7/2.2**
GKN UK 2016 Pension Plan	**1.9**	**1.4**	**2.7/2.2**
GKN US plans	**n/a**	**2.4**	**n/a**
GKN Europe plans	**1.4**	**0.6**	**1.4/1.4**
Brush UK Pension Plan	**3.1**	**1.4**	**2.7/2.2**
31 December 2019			
GKN Group Pension Schemes (Numbers 1 – 4)	2.8	2.0	2.9/2.1
GKN UK 2016 Pension Plan	2.8	2.0	2.9/2.1
GKN US plans	n/a	3.1	n/a
GKN Europe plans	1.5	1.1	1.5/1.5
Brush UK Pension Plan	2.8	2.0	2.9/2.1

Balance Sheet disclosures

The amount recognised in the Consolidated Balance Sheet arising from net liabilities in respect of defined benefit plans was as follows:

	31 December 2020 £m	31 December 2019 £m
Present value of funded defined benefit obligations	**(3,930)**	(3,899)
Fair value of plan assets	**3,775**	3,412
Funded status	**(155)**	(487)
Present value of unfunded defined benefit obligations	**(683)**	(634)
Net liabilities	**(838)**	(1,121)

The net retirement benefit obligation is attributable to Aerospace: liability of £171 million (2019: £353 million), Automotive: liability of £693 million (2019: £753 million), Powder Metallurgy: liability of £47 million (2019: £48 million), Nortek Air Management: liability of £21 million (2019: £28 million), Other Industrial: asset of £30 million (2019: £17 million) and Corporate: asset of £64 million (2019: £44 million).

The plan assets and liabilities at 31 December 2020 were as follows:

	UK Plans(1) £m	US Plans £m	European Plans £m	Other Plans £m	**Total £m**
Plan assets	3,442	271	27	35	**3,775**
Plan liabilities	(3,560)	(408)	(603)	(42)	**(4,613)**
Net liabilities	(118)	(137)	(576)	(7)	**(838)**

(1) Includes a net liability in respect of the GKN Group Pension Schemes (Numbers 1 – 3), GKN post-employment medical plans, and the Nortek UK plan, and a net asset in respect of the Brush UK Pension Plan, the GKN UK 2016 Pension Plan and the GKN Pension Scheme Number 4.

12. Cash flow statement

	Notes	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Reconciliation of operating (loss)/profit to net cash from operating activities generated by continuing operations			
Operating (loss)/profit		**(338)**	318
Adjusting items	4	**678**	784
Adjusted operating profit	4	**340**	1,102
Adjustments for:			
Depreciation of property, plant and equipment		**435**	434
Amortisation of computer software and development costs		**57**	64
Share of adjusted operating profit of equity accounted investments	9	**(62)**	(66)
Restructuring costs paid and movements in provisions		**(150)**	(320)
Defined benefit pension contributions paid(1)		**(111)**	(183)
Change in inventories		**187**	(12)
Change in receivables		**250**	72
Change in payables		**(13)**	(2)
Acquisition costs and associated transaction taxes		**–**	(16)
Tax paid		**–**	(117)
Interest paid on loans and borrowings		**(144)**	(166)
Interest paid on lease obligations		**(21)**	(21)
Net cash from operating activities		**768**	769

(1) In the year ended 31 December 2019, the Company made one-off contributions of £111 million, being the £94 million balance of the £150 million upfront commitment on acquisition of GKN, and a £17 million contribution following the disposal of the Walterscheid Powertrain Group.

Reconciliation of cash and cash equivalents, net of bank overdrafts	31 December 2020 £m	31 December 2019 £m
Cash and cash equivalents per Balance Sheet	**311**	512
Bank overdrafts included within current interest-bearing loans and borrowings	**(151)**	(195)
Cash and cash equivalents, net of bank overdrafts per Statement of Cash Flows	**160**	317

Cash flow information relating to discontinued operations is as follows:

Cash flow from discontinued operations	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Net cash used in discontinued operations	**(3)**	(16)
Defined benefit pension contributions paid	**–**	(2)
Interest paid on lease obligations	**–**	(1)
Tax paid	**(1)**	(1)
Net cash used in operating activities from discontinued operations	**(4)**	(20)
Purchase of property, plant and equipment	**(2)**	(12)
Disposal costs	**–**	(3)
Net cash used in investing activities from discontinued operations	**(2)**	(15)
Repayment of principal under lease obligations	**(1)**	(2)
Net cash used in financing activities from discontinued operations	**(1)**	(2)

Net debt reconciliation

Net debt consists of interest-bearing loans and borrowings (excluding any acquisition related fair value adjustments), cross-currency swaps and cash and cash equivalents. Currency denominated balances within net debt are translated to Sterling at swapped rates where hedged by cross-currency swaps.

Net debt is considered to be an alternative performance measure as it is not defined in IFRS. The most directly comparable IFRS measure is the aggregate of interest-bearing loans and borrowings (current and non-current) and cash and cash equivalents. A reconciliation from the most directly comparable IFRS measure to net debt is given below:

	31 December 2020 £m	Restated[1] 31 December 2019 £m
Interest-bearing loans and borrowings – due within one year	**(165)**	(284)
Interest-bearing loans and borrowings – due after one year	**(2,926)**	(3,464)
External debt	**(3,091)**	(3,748)
Less:		
Cash and cash equivalents	**311**	512
	(2,780)	(3,236)
Adjustments:		
Impact of cross-currency swaps	**(89)**	(80)
Non-cash acquisition fair value adjustments	**22**	33
Net debt	**(2,847)**	(3,283)

(1) Cash and cash equivalents and current interest-bearing loans and borrowings have been restated to meet the requirements of IAS 32 as further described in note 1. This has had no impact on net debt.

The table below shows the key components of the movement in net debt:

	At 31 December 2019 £m	Cash flow £m	Acquisitions and disposals £m	Other non-cash movements £m	Effect of foreign exchange £m	**At 31 December 2020 £m**
External debt (excluding bank overdrafts)	(3,553)	552	–	–	61	**(2,940)**
Cross-currency swaps	(80)	46	–	–	(55)	**(89)**
Non-cash acquisition fair value adjustments	33	–	–	(11)	–	**22**
	(3,600)	598	–	(11)	6	**(3,007)**
Cash and cash equivalents, net of bank overdrafts	317	(149)	(11)	–	3	**160**
Net debt	(3,283)	449	(11)	(11)	9	**(2,847)**

Glossary

Alternative Performance Measures ("APMs")

In accordance with the Guidelines on APMs issued by the European Securities and Markets Authority ("ESMA"), additional information is provided on the APMs used by the Group below.

In the reporting of financial information, the Group uses certain measures that are not required under IFRS. These additional measures (commonly referred to as APMs) provide additional information on the performance of the business and trends to stakeholders. These measures are consistent with those used internally, and are considered important to understanding the financial performance and financial health of the Group. APMs are considered to be an important measure to monitor how the businesses are performing because this provides a meaningful comparison of how the business is managed and measured on a day-to-day basis and achieves consistency and comparability between reporting periods.

These APMs may not be directly comparable with similarly titled measures reported by other companies and they are not intended to be a substitute for, or superior to, IFRS measures. All Income Statement and cash flow measures are provided for continuing operations unless otherwise stated.

Income Statement Measures

APM
Adjusted revenue

Closest equivalent statutory measure
Revenue

Reconciling items to statutory measure
Share of revenue of equity accounted investments (note 3)

Definition and purpose
Adjusted revenue includes the Group's share of revenue of equity accounted investments ("EAIs"). This enables comparability between reporting periods.

Revenue	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Revenue	**8,770**	10,967
Share of revenue of equity accounted investments (note 3)	**591**	625
Adjusted revenue	**9,361**	11,592

APM
Adjusting items

Closest equivalent statutory measure
None

Reconciling items to statutory measure
Adjusting items (note 4)

Definition and purpose
Those items which the Group excludes from its adjusted profit metrics in order to present a further measure of the Group's performance.

These include items which are significant in size or volatility or by nature are non-trading or non-recurring, any item released to the Income Statement that was previously a fair value item booked on an acquisition, and includes adjusted profit from EAIs.

This provides a meaningful comparison of how the business is managed and measured on a day-to-day basis and provides consistency and comparability between reporting periods.

APM
Adjusted operating profit

Closest equivalent statutory measure
Operating (loss)/profit[1]

Reconciling items to statutory measure
Adjusting items (note 4)

Definition and purpose
The Group uses adjusted profit measures to provide a useful and more comparable measure of the ongoing performance of the Group. Adjusted measures are reconciled to statutory measures by removing adjusting items, the nature of which are disclosed above and further detailed in note 4.

Operating profit	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Operating (loss)/profit	**(338)**	318
Adjusting items to operating (loss)/profit (note 4)	**678**	784
Adjusted operating profit	**340**	1,102

APM
Adjusted operating margin

Closest equivalent statutory measure
Operating margin[2]

Reconciling items to statutory measure
Share of revenue of equity accounted investments (note 3) and adjusting items (note 4).

Definition and purpose
Adjusted operating margin represents Adjusted operating profit as a percentage of Adjusted revenue. The Group uses adjusted profit measures to provide a useful and more comparable measure of the ongoing performance of the Group.

APM
Adjusted profit before tax

Closest equivalent statutory measure
(Loss)/profit before tax

Reconciling items to statutory measure
Adjusting items (note 4)

Definition and purpose
Profit before the impact of adjusting items and tax. As discussed above, adjusted profit measures are used to provide a useful and more comparable measure of the ongoing performance of the Group. Adjusted measures are reconciled to statutory measures by removing adjusting items, the nature of which are disclosed above and further detailed in note 4.

Profit before tax	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
(Loss)/profit before tax	**(535)**	106
Adjusting items to (loss)/profit before tax (note 4)	**688**	783
Adjusted profit before tax	**153**	889

APM
Adjusted profit after tax

Closest equivalent statutory measure
(Loss)/profit after tax

Reconciling items to statutory measure
Adjusting items (note 4)

Definition and purpose
Profit after tax but before the impact of the adjusting items. As discussed above, adjusted profit measures are used to provide a useful and more comparable measure of the ongoing performance of the Group. Adjusted measures are reconciled to statutory measures by removing adjusting items, the nature of which are disclosed above and further detailed in note 4.

Profit after tax	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
(Loss)/profit after tax	**(523)**	55
Adjusting items to (loss)/profit after tax (note 4)	**643**	644
Adjusted profit after tax	**120**	699

APM
Adjusted EBITDA for leverage covenant purposes

Closest equivalent statutory measure
Operating (loss)/profit(1)

Reconciling items to statutory measure
Adjusting items (note 4), depreciation of property, plant and equipment and amortisation of computer software and development costs, imputed lease charge, share of non-controlling interests and other adjustments required for covenant purposes(3)

Definition and purpose
Adjusted operating profit for 12 months prior to the reporting date, before depreciation and impairment of property, plant and equipment and before the amortisation and impairment of computer software and development costs.

Adjusted EBITDA for covenant purposes is a measure used by external stakeholders to measure performance.

Adjusted EBITDA for leverage covenant purposes	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Adjusted operating profit	**340**	1,102
Depreciation of property, plant and equipment and amortisation of computer software and development costs	**492**	498
Imputed lease charge	**(97)**	(91)
Non-controlling interests	**(3)**	(6)
Other adjustments required for covenant purposes(3)	**(8)**	2
Adjusted EBITDA for leverage covenant purposes	**724**	1,505

APM
H2 annualised adjusted EBITDA for proforma leverage

Closest equivalent statutory measure
Operating (loss)/profit[(1)]

Reconciling items to statutory measure
Adjusting items (note 4), depreciation of property, plant and equipment and amortisation of computer software and development costs, imputed lease charge, share of non-controlling interests and other adjustments required for covenant purposes[(3)]

Definition and purpose
Adjusted operating profit for the six months prior to the reporting date, before depreciation and impairment of property, plant and equipment and before the amortisation and impairment of computer software and development costs. This is doubled to give a H2 annualised adjusted EBITDA for proforma leverage.

H2 annualised adjusted EBITDA for proforma leverage is a useful indicator to measure performance considering the pervasive impact of COVID-19 on the Group's results for the first half of the year.

H2 annualised adjusted EBITDA for proforma leverage	**31 December 2020 £m**
Adjusted EBITDA for leverage covenant purposes	**724**
Less: Adjusted EBITDA for leverage covenant purposes for six months to 30 June 2020	**(266)**
Adjustment to H2 2020 average foreign exchange rates	**–**
H2 adjusted EBITDA for proforma leverage	**458**
H2 annualised adjusted EBITDA for proforma leverage	**916**

APM
Adjusted tax rate

Closest equivalent statutory measure
Effective tax rate

Reconciling items to statutory measure
Adjusting items, adjusting tax items and the tax impact of adjusting items (note 4 and note 5)

Definition and purpose
The income tax charge for the Group excluding adjusting tax, and the tax impact of adjusting items, divided by adjusted profit before tax.

This measure is a useful indicator of the ongoing tax rate for the Group.

Adjusted tax rate	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Tax credit/(charge) per Income Statement	**12**	(51)
Adjusted for:		
Tax impact of adjusting items	**(115)**	(123)
Tax impact of restructuring	**78**	(9)
Tax impact of EAIs	**(8)**	(7)
Adjusted tax charge	**(33)**	(190)
Adjusted profit before tax	**153**	889
Adjusted tax rate	**21.6%**	21.4%

APM
Adjusted basic earnings per share

Closest equivalent statutory measure
Basic earnings per share

Reconciling items to statutory measure
Adjusting items (note 4 and note 7)

Definition and purpose
Profit after tax attributable to owners of the parent and before the impact of adjusting items, divided by the weighted average number of ordinary shares in issue during the financial year.

APM
Adjusted diluted earnings per share

Closest equivalent statutory measure
Diluted earnings per share

Reconciling items to statutory measure
Adjusting items (note 4 and note 7)

Definition and purpose
Profit after tax attributable to owners of the parent and before the impact of adjusting items, divided by the weighted average number of ordinary shares in issue during the financial year adjusted for the effects of any potentially dilutive options.

The Board considers this to be a key measure of performance when all businesses are held for the complete reporting period.

APM
Interest cover

Closest equivalent statutory measure
None

Reconciling items to statutory measure
Not applicable

Definition and purpose
Adjusted EBITDA calculated for covenant purposes (including EBITDA of businesses disposed) as a multiple of net interest payable on bank loans and overdrafts.

This measure is used for bank covenant testing.

Interest cover	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Adjusted EBITDA for leverage covenant purposes	**724**	1,505
Adjusted EBITDA from businesses disposed in the year	**2**	36
Adjusted EBITDA for interest cover	**726**	1,541
Interest on bank loans and overdrafts	**(136)**	(152)
Finance income	**3**	9
Other interest for covenant purposes[(4)]	**(9)**	–
Net finance charges for covenant purposes	**(142)**	(143)
Interest cover	**5.1x**	10.8x

Balance Sheet Measures

APM
Working capital

Closest equivalent statutory measure
Inventories, trade and other receivables less trade and other payables

Reconciling items to statutory measure
Not applicable

Definition and purpose
Working capital comprises inventories, current and non-current trade and other receivables and current and non-current trade and other payables. This measure provides additional information in respect of working capital management.

APM
Net debt

Closest equivalent statutory measure
Cash and cash equivalents less interest-bearing loans and borrowings and finance related derivative instruments

Reconciling items to statutory measure
Reconciliation of net debt (note 12)

Definition and purpose
Net debt comprises cash and cash equivalents, interest-bearing loans and borrowings and cross-currency swaps but excludes non-cash acquisition fair value adjustments.

Net debt is one measure that could be used to indicate the strength of the Group's Balance Sheet position and is a useful measure of the indebtedness of the Group.

APM
Bank covenant definition of net debt at average rates and leverage

Closest equivalent statutory measure
Cash and cash equivalents less interest-bearing loans and borrowings and finance related derivative instruments

Reconciling items to statutory measure
Impact of foreign exchange and adjustments for bank covenant purposes

Definition and purpose
Net debt (as above) is presented in the Balance Sheet translated at year end exchange rates.

For bank covenant testing purposes net debt is converted using average exchange rates for the previous 12 months.

Leverage is calculated as the bank covenant definition of net debt divided by adjusted EBITDA for leverage covenant purposes. This measure is used for bank covenant testing.

Net debt	31 December 2020 £m	31 December 2019 £m
Net debt at closing rates (note 12)	**2,847**	3,283
Impact of foreign exchange	**106**	94
Net debt at average rates	**2,953**	3,377
Other adjustments required for covenant purposes	**–**	8
Bank covenant definition of net debt at average rates	**2,953**	3,385
Leverage	**4.1x**	2.25x

APM
Net debt at H2 average rates and H2 annualised proforma leverage

Closest equivalent statutory measure
Cash and cash equivalents less interest-bearing loans and borrowings and finance related derivative instruments

Reconciling items to statutory measure
Impact of foreign exchange and adjustments for bank covenant purposes

Definition and purpose
Net debt (as above) is presented in the Balance Sheet translated at year end exchange rates.

H2 annualised proforma leverage is calculated as net debt at H2 average rates divided by H2 annualised adjusted EBITDA for proforma leverage.

H2 annualised proforma leverage is a useful measure of performance considering the pervasive impact of COVID-19 on the Group's results for the first half of the year.

Net debt	**31 December 2020 £m**
Net debt at closing rates (note 12)	**2,847**
Impact of foreign exchange	**85**
Net debt at H2 average rates	**2,932**
H2 annualised proforma leverage	**3.2x**

Cash Flow Measures

APM
Adjusted operating cash flow (pre-capex) and Adjusted operating cash flow (pre-capex) conversion

Closest equivalent statutory measure
Net cash from operating activities

Reconciling items to statutory measure
Non-working capital items (note 12)

Definition and purpose
Adjusted operating cash flow (pre-capex) is calculated as adjusted operating profit before depreciation and amortisation attributable to subsidiaries, repayment of principal under lease obligations, the positive non-cash utilisation from loss-making contracts and movements in working capital.

Adjusted operating cash flow (pre-capex) conversion is adjusted operating cash flow (pre-capex) divided by adjusted profit before depreciation and amortisation attributable to subsidiaries, less repayment of principal under lease obligations and the positive non-cash utilisation from loss-making contracts.

This measure provides additional useful information in respect of cash generation and is consistent with how business performance is measured internally.

Adjusted operating cash flow (pre-capex)	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Adjusted operating profit	**340**	1,102
Share of adjusted operating profit of equity accounted investments	**(62)**	(66)
Depreciation of owned property, plant and equipment and amortisation of computer software and development costs	**418**	426
Depreciation of leased property, plant and equipment and amortisation of leased computer software and development costs	**74**	72
Repayment of principal under lease obligations	**(76)**	(70)
Positive non-cash utilisation from loss-making contracts	**(59)**	(81)
	635	1,383
Change in inventories	**187**	(12)
Change in receivables	**250**	72
Change in payables	**(13)**	(2)
Adjusted operating cash flow (pre-capex)	**1,059**	1,441
Adjusted operating cash flow (pre-capex) conversion	**167%**	104%

APM
Movement in net working capital and percentage change

Closest equivalent statutory measure
Change in inventories, change in receivables and change in payables as included within net cash from operating activities (note 12).

Reconciling items to statutory measure
Not applicable.

Definition and purpose
Movement in working capital represents the cash flow from inventories, receivables and payables during the year. The percentage reduction in net working capital is the movement in working capital divided by net working capital as at the prior Balance Sheet date.

Movement in working capital	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Change in inventories (note 12)	**187**	(12)
Change in receivables (note 12)	**250**	72
Change in payables (note 12)	**(13)**	(2)
Movement in working capital	**424**	58

	Year ended 31 December 2019	Year ended 31 December 2018
Net working capital comprises:		
Inventories	**1,332**	1,489
Current trade and other receivables	**1,970**	2,328
Non-current trade and other receivables	**424**	504
Current trade and other payables	**(2,461)**	(2,583)
Non-current trade and other payables	**(444)**	(762)
Net working capital	**821**	976
Percentage reduction in net working capital	**52%**	6%

APM
Free cash flow

Closest equivalent statutory measure
Net increase/decrease in cash and cash equivalents

Reconciling items to statutory measure
Acquisition related cash flows, dividends paid to owners of the parent, foreign exchange, discontinued operating cash flows and other non-cash movements

Definition and purpose
Free cash flow represents cash generated from trading from continuing businesses after all costs including restructuring, pension contributions, tax and interest payments.

Free cash flow	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Adjusted operating cash flow (pre-capex)	**1,059**	1,441
Net capital expenditure	**(292)**	(495)
Net interest and tax paid	**(162)**	(295)
Defined benefit pension contributions paid	**(111)**	(183)
Restructuring costs paid	**(172)**	(190)
Dividends received from EAIs	**54**	67
Trading net other cash flows[(5)]	**80**	(55)
Free cash flow	**456**	290

APM
Adjusted free cash flow

Closest equivalent statutory measure
Net increase/decrease in cash and cash equivalents

Reconciling items to statutory measure
Free cash flow, as defined above, adjusted for special pension contributions and restructuring cash flows

Definition and purpose
Adjusted free cash flow represents free cash flow adjusted for special pension contributions and restructuring cash flows.

Adjusted free cash flow	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Free cash flow	**456**	290
Special pension contributions[(6)]	**–**	111
Restructuring costs paid	**172**	190
Adjusted free cash flow	**628**	591
Increase in adjusted free cash flow compared to 2019	**6%**	n/a

APM
Capital expenditure (capex)

Closest equivalent statutory measure
None

Reconciling items to statutory measure
Not applicable

Definition and purpose
Calculated as the purchase of owned property, plant and equipment and computer software and expenditure on capitalised development costs during the year, excluding any assets acquired as part of a business combination.

Net capital expenditure is capital expenditure net of proceeds from disposal of property, plant and equipment.

APM
Capital expenditure to depreciation ratio

Closest equivalent statutory measure
None

Reconciling items to statutory measure
Not applicable

Definition and purpose
Net capital expenditure divided by depreciation of owned property, plant and equipment and amortisation of computer software and development costs.

APM
Dividend per share

Closest equivalent statutory measure
Dividend per share

Reconciling items to statutory measure
Not applicable

Definition and purpose
Amounts payable by way of dividends in terms of pence per share.

(1) Operating (loss)/profit is not defined within IFRS but is a widely accepted profit measure being (loss)/profit before finance costs, finance income and tax.
(2) Operating margin is not defined within IFRS but is a widely accepted profit measure being derived from operating (loss)/profit[(1)] divided by revenue.
(3) Included within other adjustments required for covenant purposes are dividends received from equity accounted investments, the removal of adjusted operating profit of equity accounted investments and the inclusion of adjusted operating profit in respect of businesses classified as held for sale.
(4) Other interest for covenant purposes includes bank facility renegotiation fees and debt issue costs paid during the year.
(5) Trading net other cash flows include non-cash movements included in adjusted operating profit, cash paid against provisions and dividends paid to non-controlling interests.
(6) Special pension contributions in 2019 included £111 million of one-off payments, being the £94 million balance of the £150 million upfront commitment on acquisition of GKN, and a £17 million contribution following the disposal of the Walterscheid Powertrain Group.