

Section 172 statement

This is an overview of how the Directors performed their duty to promote the success of the Company under section 172 of the Companies Act 2006.

Our purpose, strategy and values

Melrose was founded in 2003 to empower businesses to unlock their full potential for the benefit of all stakeholders, whilst providing shareholders with a superior return on their investment. This has been delivered through our “Buy, Improve, Sell” strategy, whereby we acquire high quality but underperforming manufacturing businesses and invest in them heavily to improve performance and productivity, so that they become stronger, better businesses under our responsible stewardship. At the appropriate time, we find them a new home for the next stage of their development and return the proceeds to shareholders.

The Company’s purpose and strategy remain underpinned by the principles and values on which it was founded. We act with integrity, honesty, transparency and decisiveness, and believe in a lean operating model and high productivity. We invest in the businesses we own as if we are going to own them forever, and we do not shy away from difficult decisions. We provide the space and resources to empower people to perform and reward them well when they do. We provide the focus and investment to improve our businesses’ sustainability, for the benefit of all stakeholders. We work with them to set meaningful sustainability targets alongside financial metrics, provide the investment to achieve them, and hold each business and their management team accountable for their progress. These principles lie at the heart of our success, and are the basis on which we strive for future success.

The Board is ultimately accountable to the Company’s shareholders for setting the Group’s strategy and for overseeing the Group’s financial and operational performance in line with Melrose’s strategic objectives. Implementation of the Group’s strategic objectives, as determined and overseen by the Board, is delegated to the Melrose senior management team, and with day-to-day operational management delegated to the business unit executive teams. The Board has established an organisational structure with clear reporting procedures, lines of responsibility and delegated authority, as depicted in the diagram on page 44 and in line with the Group’s governance framework, which the Board reviews regularly.

In setting the Company’s strategy, the Directors take into account the principal risks facing the Group, which are described on pages 46 to 53 of this Annual Report.

SECTION 172(1) STATEMENT

This section, together with those pages incorporated by reference, acts as the Company’s Section 172(1) statement. You will find more information about engagement with stakeholders, building relationships, considering the likely long-term consequences of decisions and safeguarding our reputation, incorporated throughout this Annual Report and financial statements.

This statement has been prepared in accordance with the requirements of The Companies (Miscellaneous Reporting) Regulations 2018, which require the Company to describe how the Directors have had regard to the matters set out in section 172 of the Companies Act 2006 during the financial year under review.

Duty to promote the success of the Company

In executing the Company’s strategy, the Directors must act in accordance with a set of general duties detailed in section 172 of the Companies Act 2006. These general duties include a duty to promote the success of the Company, and specifically to act in a way that the Director considers, in good faith, would be most likely to promote the success of the Company for the benefit of its shareholders as a whole and, in doing so, having regard (amongst other matters) to:

- the likely consequences of any decisions in the long term;
- the interests of the Company’s employees;
- the need to foster the Company’s business relationships with suppliers, customers and others;
- the impact of the Company’s operations on the community and environment;
- the desirability of the Company maintaining a reputation for high standards of business conduct; and
- the need to act fairly as between shareholders of the Company.

These pages 54 to 57, and the pages incorporated by reference, describe how the Directors took these factors into account in their decision-making in 2020.

Our key stakeholders

The Board cultivates strong relationships with its key stakeholders so that it is well placed and sufficiently informed to take their considerations into account when making decisions, where appropriate, in order to discharge their duties and to pursue the Company’s strategic objectives. Our purpose is to create long-term value for stakeholders and in order to do this, we need to understand our stakeholders and what matters to them. Stakeholder engagement is regularly on the Board’s agenda to assess whether the identities and priorities of our principal stakeholders have changed, and whether the Board has sufficient engagement with each principal stakeholder group.

We consider our key stakeholders to fall into the following broad categories, each of which is considered in this statement: shareholders, employees, customers and suppliers, and communities.

Long-term decision making

The Board is ultimately responsible for determining and reviewing Melrose’s “Buy, Improve, Sell” strategy. In line with this strategy, Melrose’s core purpose is to acquire good manufacturing businesses with strong market positions that are underperforming their potential, with a view to investing in those businesses and empowering their management teams to unlock operational improvements and to drive value and performance for the benefit of all stakeholders. Although our strategy necessarily means that new owners are eventually found for all our businesses at the appropriate time, during our ownership we invest in them as if we were going to own them forever and act as responsible stewards of those businesses.

Although this approach did not change during 2020, clearly the outbreak of the COVID-19 pandemic meant that the implementation of the Melrose strategy was different from previous years. The global situation changed very quickly and the world was facing very difficult health and economic circumstances. The impact of the COVID-19 outbreak caused significant uncertainty across global markets and in each of our businesses, which were (and continue to be) impacted differently by the pandemic. The Board was required to react quickly to rapidly changing circumstances in order to protect the health and wellbeing of the Group’s employees, customers and suppliers, and to ensure that the businesses dealt with the crisis in the best manner possible for all stakeholders. This resulted in the Board focusing on and prioritising actions to ensure that the Group was able to withstand the immediate impact of the pandemic and be in the best position as we emerged from the crisis.

Although such decisions were taken to ensure that the Group was protected in the short to medium-term, the Board was fully cognisant of the long-term impacts of these decisions.

Financial resilience, ordinarily an important part of our value creation process, was even more critical during 2020. During the height of the crisis, the Board met on a weekly basis to review the Group's operations, trading, cash position and working capital, based on detailed bottom-up financial information from the businesses. The Melrose senior management team met with the businesses on a weekly basis to analyse trading, cash and working capital. Significant and accelerated management actions were put in place across all businesses in the Group, to reduce cost and preserve cash until the market conditions improved. Although clearly a temporary measure, this was done in order to keep the Group on a stable footing and ensure that it emerged from the crisis in the best position to drive long-term value. Strong cash management was prioritised until market conditions showed signs of improvement. Operational initiatives to generate efficiency improvements in working capital were intensified. Right at the outset, our supportive banking syndicate agreed to temporary covenant relief giving the flexibility, if required, over the medium-term to continue to improve the businesses. Restructuring projects are well underway, which the Board expects will significantly improve the Group's trading performance in 2021. There are substantial margin improvement opportunities across the GKN businesses.

While the pandemic has been challenging for all of our businesses, the Group has sought to protect investment in research and development and to continue to develop world-leading technologies that seek to address longer-term global sustainability challenges. GKN Aerospace is investing in ground-breaking technologies for both electric and hydrogen powered aircraft. GKN Automotive pressed ahead with investment in its e-Drive auto systems. GKN Powder Metallurgy has continued to develop its Hy2green technology, which is expected to be officially launched to market in 2021. Nortek Global HVAC is continuing to maximise the full potential of its revolutionary StatePoint Technology®. Further development of these and other exciting projects are key to the successful development of the Group, and are further detailed on pages 62 to 67 of the Sustainability report.

Employees

Employees are central to the Group's success and for our businesses to perform well and exceed their potential, it is important to nurture an engaged, capable and passionate workforce. The workforce advisory panel ("WAP") continued to operate during 2020 and was very helpful in promoting effective engagement with, and encouraging participation from, the Group's workforce. The structure of the WAP deliberately reflects the decentralised nature of the Melrose model and ensures that the voice of the workforce is heard where it is most effective in the business unit executive decision-making process. The WAP met twice during the year and the outcomes were fed back to the Board accordingly. Further details about the WAP and its actions during 2020 can be found in the Sustainability report on page 79.

The Board continued to monitor the nature of issues reported through the whistleblowing hotlines operated by the Group on a consistent approach with 2019. The integrity of this process is an important part of the Company's governance arrangements and the Board will review this once again in 2021 to ensure it remains effective. Further details about the Group's whistleblowing procedures can be found in the Sustainability report on page 86.

There has been a heightened focus since the start of the pandemic on health and safety. Keeping workers safe has always been a top priority, but never more so than during the global pandemic. We focused intensely on securing all necessary PPE and implemented changes to processes and other measures to protect our employees as our sites across the globe, like the wider community, experienced cases of the virus. In addition, within Melrose and many of our businesses, senior salaried staff, and the entire Melrose Board, took a temporary 20% pay cut to help support the Group. The Board is extremely grateful for these efforts, which contributed to the Group delivering the results that are reflected in this Annual Report.

Once we became aware that the impact of the pandemic was going to be prolonged, we took steps to reshape the businesses to adapt to the new demand levels. We acknowledge that these necessary actions are difficult for those affected, but we ensure that we treat people fairly and strive for clear and transparent communication.

The funding position of the GKN pension schemes has continued to improve. The significantly increased cash contributions that have been made to the GKN UK defined benefit pension schemes under our ownership have helped to reduce the funding deficit of these schemes that we inherited at the time of acquisition by over 80% to approximately £0.1 billion since acquisition. We will continue in our efforts to improve this position further, to make members more secure for the rest of their lives.

Suppliers and customers

Fostering positive and open business relationships with customers and suppliers is key to the success of our businesses, even more so in times of crisis. Our businesses worked hard to maintain their strong relationships with suppliers and customers as the pandemic impacted them, primarily through continued robust channels of communication.

Our businesses have invested heavily in their relationships with suppliers and customers throughout 2020, and details of this are set out on pages 62 to 67 of the Sustainability report.

During the year, we published our fourth Modern Slavery Statement. We remain committed to addressing the potential risks of modern slavery and human rights abuses, to acting in an ethical manner with integrity and transparency in all business dealings, and to investing in the creation of effective systems and controls across the Group to safeguard against adverse human rights impacts. The Board also approved the implementation of a Group-wide conflict minerals policy in 2020, to ensure that our businesses comply with applicable laws as well as customer expectations in relation to 3TG minerals. Further details can be found in the Sustainability report on pages 67 and 86 to 87.

Shareholders

Shareholder support is integral to the successful execution of our "Buy, Improve, Sell" strategy. Melrose has attracted long-term support from key shareholders since its establishment in 2003, none of which is taken for granted. Given that we often need to move quickly to secure the opportunities that we feel will be (and have been) critical to Melrose's success, we rely on the in-depth understanding amongst our investors of our business model and strategy, which feeds into other aspects of our governance structure, such as executive remuneration.

Melrose has always prided itself on the timeliness and transparency of the information we provide to our shareholders. Key for our shareholders is the resilience of our business model through varied economic cycles and through a crisis. Consequently, shareholders have wanted to understand the impact of the COVID-19 pandemic and the economic environment on the Group. The Board felt it was particularly important to keep investors updated during 2020, as the Group was adapting to the quickly-changing external circumstances presented by the pandemic. Trading updates were published more frequently to ensure that investors were appropriately informed as to the Group's performance, and there was an increase in the number of bespoke interactions between investors, analysts and members of management, given the absence of the more formal interactions that we would run in a normal year, such as the capital markets days and in-person investor roadshows.

The views of key analysts and shareholders continue to be reported to the Board directly by individual Directors or via the Company's brokers. This helps to ensure that all members of the Board develop an understanding of the views and any concerns of shareholders. The Chairman and other Non-executive Directors are also available to meet institutional shareholders, where requested.

Further details on the Board's programme of shareholder engagement in 2020 are detailed throughout this Annual Report, including in the Sustainability report on page 61, the Governance overview on page 91, the Corporate Governance report on page 97, and the Directors' remuneration report on page 111.

Environment and community

Improving the sustainability performance of our businesses is central to our “Buy, Improve, Sell” strategy. We acquire good manufacturing businesses that are underperforming their potential with respect to their financial, operational and sustainability performance. We then invest heavily to improve their longer-term financial and operational performance in a sustainable manner, and find them suitable owners for the future, generating significant value for our shareholders.

Following publication of the Company’s inaugural ESG report last year, the Board has been extremely focused on continuing improvement in respect of both the substantive actions being taken in the businesses to reduce the impact of the Group’s operations on the community and environment, and on improving the quality and transparency of our disclosures in reporting on matters relating to sustainability. The Board understands that sustainability is high on the agenda for our key stakeholders and it is important that we are providing clear and fulsome disclosure in respect of these matters. In order to better understand market expectations, which we appreciate are still in a state of fluctuation, the Board is engaging more regularly with a range of stakeholders including shareholders, sustainability analysts and rating agencies on a number of sustainability topics that are relevant for our businesses.

The Board has supported continued investment in the businesses to develop products and services that deliver environmental improvements and benefits to their customers. Some of these products and services, such as GKN Aerospace’s early investment in Eviation Alice, the world’s first electric commuter aircraft, GKN Automotive’s eDrive system, and Nortek Global HVAC’s cutting-edge StatePoint Technology®, have demonstrated our businesses’ commitment to long-term innovation in, and their continued development of, ground-breaking technology. For further details, please refer to the Divisional reviews on pages 14 to 33.

Cultivating the technical and innovation capabilities and foresight to provide effective solutions to the emerging sustainability challenges that our customers face is another key focus for our businesses. We are already taking active steps to anticipate how climate change will affect our businesses, as described in the Sustainability report, and to encourage firm progress from our businesses in respect of positive climate action. We will continue to strengthen our understanding of the specific climate-related risks that our businesses face as we work to mitigate these risks. We are also encouraging our businesses to identify the reporting metrics that are the most important for their businesses and which they believe will add value.

During 2020, it was more important than ever for our businesses to support their local communities. Our Sustainability report highlights examples of actions the businesses took during 2020 to engage with their communities. On a more national scale, GKN Aerospace and GKN Automotive were at the heart of the VentilatorChallengeUK consortium of manufacturing companies making medical ventilators required by NHS hospitals as a result of the pandemic. Further details of this initiative are included on page 85 of the Sustainability report.

Government bodies

The Group has multiple interactions with government bodies in a number of jurisdictions across the world, many of which are of strategic importance to the Group’s long-term success. In the UK, the Company has regular dialogue with the Department for Business, Energy and Industrial Strategy (BEIS), the Ministry of Defence and the UK Panel on Takeovers and Mergers regarding ongoing compliance with the undertakings and other continuing obligations given to the UK Government and other regulatory bodies in connection with the acquisition of GKN.

Corporate governance agencies and independent reporting bodies

The Company continued to invest significant time in speaking regularly to the key corporate governance bodies regarding the central aspects of our governance framework that the Board considers to be of long-term strategic importance, including executive remuneration and diversity. A large part of our shareholder community subscribes to these governance bodies and it is important to us that we have their support in relation to areas of corporate governance. The Company has also engaged with independent reporting bodies supported by the UK Government, including the Parker Review and the Hampton-Alexander Review. Our stakeholders expect us to act as responsible stewards and engage with such bodies, and we are keen to highlight our demonstrable commitment to promoting diversity at all levels, including within our senior leadership.

Maintaining a reputation for high standards of business conduct

This remained an area of key focus for the Board in 2020. Regardless of macro-economic circumstances, it is critical that our businesses understand the importance of maintaining high standards of business conduct, not only for the purposes of financial success, but to ensure that they continue to maintain strong reputations in their respective industries as good partners to deal with.

The Board continued to play an active oversight role in terms of how the businesses manage compliance during the year. In particular, an in-depth review of the Melrose Code of Ethics and Group compliance policies was undertaken in 2020, which will be rolled out by the businesses during 2021. The Board gave particular thought to the Melrose Code of Ethics and this was refreshed to ensure that it reflects the Company’s expectations of its business, employees and certain other parties in doing business. In addition, the Board approved the implementation of the Group’s inaugural conflict minerals policy. Further detail on the Group’s policies and compliance framework can be found on pages 86 to 87 of the Sustainability report.

During 2020, the Group continued to work closely with external audit firms to monitor and verify performance at Group and business unit levels, in respect of both financial and non-financial performance. In times of economic uncertainty, where enhanced focus is, rightly, on financial results and performance, the Board nevertheless considers it to be of the utmost importance that our businesses continue to uphold the highest standards of business conduct possible, and continue to pursue improvements in this area.

Acting fairly as between the Company’s shareholders

The Company continues to have one class of ordinary shares, which have the same rights as regards voting, distributions and on a liquidation. Full alignment with shareholders remains the case, with management continuing to be significant shareholders in the Company, holding approximately 1.5% of the register as at 31 December 2020 (together putting them in the top 20 shareholders).

On the basis of the above, the members of the Board consider, both individually and together, that they have acted in the way they consider, in good faith, would be most likely to promote the success of the Company for the benefit of its members as a whole (having regard to the stakeholders and matters set out in s172(1)(a-f) of the Companies Act 2006) in the decisions taken during the year ended 31 December 2020.