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**If you are in any doubt about the action you should take, you should consult your stockbroker, bank manager, solicitor, accountant or an independent financial adviser duly authorised under the FSMA if you are located in the United Kingdom, or, if you are located outside the United Kingdom, an appropriately authorised independent financial adviser.**

Subject to the restrictions set out below, if you sell or otherwise transfer or have sold or otherwise transferred all of your Existing Melrose Shares, you should send this Supplementary Circular, if and when received, as soon as possible to the purchaser or transferee, or to the stockbroker, bank or other agent through whom the sale or transfer was effected, for transmission to the purchaser or transferee. This document should not, however, be distributed, forwarded or transmitted in or into any jurisdiction where to do so might constitute a violation of local securities laws or regulations. If you sell or otherwise transfer or have sold or otherwise transferred only part of your holding of Existing Melrose Shares, you should immediately consult the stockbroker, bank or other agent through whom the sale or transfer was effected.

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## **Melrose Industries PLC**

*(Incorporated and registered in England and Wales with Registered No. 9800044)*

### **Supplementary Circular to Melrose Shareholders in connection with the acquisition of GKN plc and the Melrose General Meeting**

**This supplementary circular (the “Supplementary Circular”) is supplemental to and must be read in conjunction with the circular dated 2 February 2018 previously sent to Melrose Shareholders and available on Melrose’s website ([www.melroseplc.net](http://www.melroseplc.net)) which provides notice of the Melrose General Meeting relating to the Acquisition to be held at Barber-Surgeons’ Hall, Monkwell Square, Wood Street, London EC2Y 5BL on 8 March 2018 at 11.00 a.m (the “Circular”).**

Your attention is drawn to the risk factors relating to the Acquisition, GKN, the Melrose Group and the Enlarged Group set out in the Circular on pages 13 to 20, which Melrose Shareholders should carefully consider before deciding whether or not to vote in favour of the Resolutions to be proposed at the Melrose General Meeting.

The Existing Melrose Shares are listed on the Official List with a premium listing maintained by the FCA and traded on the London Stock Exchange’s main market for listed securities. Applications will be made for the admission of the New Melrose Shares to the Official List with a premium listing and to trading on the London Stock Exchange’s main market for listed securities. It is expected that Admission of the New Melrose Shares will become effective and that dealings (for normal settlement) in the New Melrose Shares will commence on the London Stock Exchange at 8.00 a.m. on the Effective Date (whereupon an announcement will be made by the Company to a Regulatory Information Service). A Prospectus Equivalent Document has been published on 1 February 2018 by Melrose in connection with the issue and Admission of the New Melrose Shares.

This Supplementary Circular does not constitute or form part of any offer or invitation to purchase, otherwise acquire, subscribe for, sell, otherwise dispose of or issue, or any solicitation of any offer to sell, otherwise dispose of, issue, purchase, otherwise acquire or subscribe for, any security.

The distribution of this Supplementary Circular into jurisdictions other than the United Kingdom may be restricted by law. Persons into whose possession this Supplementary Circular come should inform themselves about and observe any such restrictions. Any failure to comply with these restrictions may constitute a violation of the securities laws of any such jurisdiction. This Supplementary Circular has been prepared for the purposes of

complying with English law and the Listing Rules and the information disclosed herein may not be the same as that which would have been disclosed if this Supplementary Circular had been prepared in accordance with the laws and regulations of any jurisdiction outside of the United Kingdom.

**Neither this Supplementary Circular nor any other document has been approved or disapproved by the SEC, any state securities commission in the United States or any US regulatory authority, nor have authorities passed upon or endorsed the merits of the Acquisition or the accuracy or adequacy of this Supplementary Circular. Any representation to the contrary is a criminal offence in the United States.**

**THE CONTENTS OF THIS SUPPLEMENTARY CIRCULAR OR ANY SUBSEQUENT COMMUNICATION FROM THE COMPANY OR THE FINANCIAL ADVISER OR ANY OF THEIR RESPECTIVE AFFILIATES, OFFICERS, DIRECTORS, EMPLOYEES OR AGENTS ARE NOT TO BE CONSTRUED AS LEGAL, FINANCIAL OR TAX ADVICE. EACH PROSPECTIVE INVESTOR SHOULD CONSULT HIS, HER OR ITS OWN SOLICITOR, INDEPENDENT FINANCIAL ADVISER OR TAX ADVISER FOR LEGAL, FINANCIAL OR TAX ADVICE.**

Without limitation, the contents of the websites of the Company or GKN do not form part of this Supplementary Circular.

Capitalised terms used but not defined in this Supplementary Circular have the meanings given to them in the Circular.

This Supplementary Circular is dated 27 February 2018.

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**PART I**  
**LETTER FROM THE CHAIRMAN OF MELROSE**



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

*Directors:*

Christopher Miller (*Chairman*)  
David Roper (*Vice-Chairman*)  
Simon Peckham (*Chief Executive*)  
Geoffrey Martin (*Group Finance Director*)  
Justin Dowley (*Non-executive Director*)  
Elizabeth Hewitt (*Non-executive Director*)  
David Lis (*Non-executive Director*)  
Archie. G Kane (*Non-executive Director*)

*Registered Office:*

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The Colmore Building  
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27 February 2018

**ACQUISITION OF GKN**  
**INTRODUCTION TO THE SUPPLEMENTARY CIRCULAR**

Dear Shareholder,

On 1 February 2018 Melrose posted its Offer Document to GKN Shareholders containing the full terms and conditions of its firm offer to acquire the entire issued and to be issued share capital of GKN.

On 2 February 2018 Melrose posted its circular providing details of the Acquisition and notice of the Melrose General Meeting relating to the Acquisition convened for 11.00 a.m. on 8 March 2018 at Barber-Surgeons' Hall, Monkswell Square, Wood Street, London EC2Y 5BL (the "**Circular**").

Melrose and GKN each announced their full year results for the financial year ended 31 December 2017 on 20 February 2018 and 27 February 2018 respectively.

In Part I of the Circular it was noted that the Company expected to publish a supplementary circular following the GKN results announcement on 27 February 2018 setting out details of those results.

Accordingly, the purpose of this Supplementary Circular is to provide such details to Melrose Shareholders. GKN's full year results announcement is set out in full in Appendix II (*GKN preliminary full year results for the year ended 31 December 2017*).

Shareholders are referred to the Circular dated 2 February 2018 for further information including the recommendation from the Board of Melrose to vote in favour of the Acquisition.

Yours sincerely,

Christopher Miller

## **PART II**

### **IMPORTANT INFORMATION**

#### **Responsibility**

The Company and the Melrose Board, whose names appear in Part I of this Supplementary Circular, accept responsibility for the information contained in this Supplementary Circular, except that the only responsibility accepted by the Melrose Board in relation to information relating to GKN, which has been compiled from published sources, is to ensure that such information is correctly and fairly produced and presented. To the best of the knowledge and belief of the Company and the Melrose Board (which has taken all reasonable care to ensure that such is the case) the information contained in this Supplementary Circular (other than the information contained in this Supplementary Circular relating to GKN) is in accordance with the facts and does not omit anything likely to affect the import of such information.

#### **Forward-looking statements**

This Supplementary Circular may contain forward looking statements that are based on current expectations or beliefs, as well as assumptions about future events. Generally, words such as “anticipate”, “believe”, “could”, “estimate”, “expect”, “goals”, “intend”, “may”, “objectives”, “outlook”, “plan”, “probably”, “project”, “risks”, “seek”, “should”, “target”, “will” and similar terms and phrases identify forward-looking statements. These statements are based on the current expectations of management and are naturally subject to risks, uncertainties and changes in circumstances. Undue reliance should not be placed on any such statements because, by their very nature, they are subject to known and unknown risks and uncertainties and can be affected by other factors that could cause actual results, and management’s plans and objectives, to differ materially from those expressed or implied in the forward looking statements.

There are several factors which could cause actual results to differ materially from those expressed or implied in forward looking statements. Among the factors that could cause actual results to differ materially from those described in the forward looking statements include (but are not limited to): (a) changes in demand for Melrose’s and/or GKN’s products; (b) currency fluctuations; (c) loss of market share and industry competition; (d) risks associated with the identification of suitable potential acquisition properties and targets, and successful negotiation and completion of such transactions; and (e) changes in trading conditions.

All forward looking statements contained in this Supplementary Circular are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. Readers should not place undue reliance on forward looking statements which are subject to inherent uncertainties, including both economic and business risk factors underlying any such forward-looking information.

Melrose does not undertake any obligation (except as required by the Prospectus Rules, the Listing Rules, the Disclosure Requirements and Disclosure Guidance and Transparency Rules and the rules of the London Stock Exchange and as other may be required by applicable law) to revise or update any forward looking statement contained in this Supplementary Circular, regardless of whether that statement is affected as a result of new information, future events or otherwise.

#### **Market and economic data**

This Supplementary Circular contains information regarding Melrose’s, GKN’s and the Enlarged Group’s businesses and the markets in which they operate and compete, which Melrose has obtained from various third party sources. Where information has been sourced from a third party it has been accurately reproduced and, so far as Melrose is aware and is able to ascertain from the information published by that third party, no facts have been omitted which would render the reproduced information inaccurate or misleading and the source of such information has been disclosed.

#### **No profit forecasts or estimates**

No statement in this Supplementary Circular is intended as a profit forecast, profit estimate or quantified financial benefits statement for the purposes of Rule 28 of the City Code, and no statement should be interpreted as such.

**Rounding**

Certain figures included in this Supplementary Circular have been subjected to rounding adjustments. Accordingly, figures shown for the same category presented in different tables or forms may vary slightly and figures shown as totals in certain tables or forms may not be an arithmetic aggregation of the figures that precede them.

**No access**

Melrose and its advisers have not had access to GKN's non-public information or documentation and accordingly have been unable to perform any due diligence on such information or documentation. All information relating to GKN and the GKN Group contained in this Supplementary Circular has been sourced from publicly available information and has not been subject to comment or verification by GKN or the relevant member of the GKN Group or their respective directors.

## APPENDIX I ADDITIONAL INFORMATION

On 1 February 2018 Melrose posted its Offer Document to GKN Shareholders containing the full terms and conditions of its firm offer to acquire the entire issued and to be issued share capital of GKN.

In accordance with Rule 27.2 of the City Code, Melrose is required to provide details of any material changes to the matters set out in Rule 27.2(b) of the City Code since publication of the Offer Document on 1 February 2018.

Save as set out in this Supplementary Circular and other than information relating to GKN set out in GKN's response circular dated 15 February 2018, Melrose confirms that there have been no changes in information detailed in any previously published document relating to the Acquisition which are material in the context of that document and there have been no material changes to the matters set out in Rule 27.2(b) of the City Code since 1 February 2018.

Set out below are details of material changes that have occurred following the publication of the Offer Document on 1 February 2018 in relation to certain of the matters set out in Rule 27.2(b) of the City Code.

1. Profit forecasts and quantified financial benefits statements (Rule 24.3(d)(xviii) of the City Code):

The Melrose Profit Estimate contained in Part 6 of the Offer Document is no longer outstanding following publication on 20 February 2018 of Melrose's preliminary results for the financial year ended 31 December 2017.

2. Interests and dealings in relevant securities (Rule 24.4 of the City Code)

In this paragraph 2 "disclosure date" shall mean 26 February 2018, being the latest practicable date prior to the publication of this Supplementary Circular.

The Offer Document included a reference to 13,865 GKN Shares held by Investec Capital and Investments (Ireland) Limited. These GKN Shares are in fact held by Investec Capital and Investments (Ireland) Limited as nominee on behalf of such shares' beneficial owner.

Paragraph 4 of Part 4 of the Offer Document is supplemented as set out below. Where not included below, the disclosure in respect of the relevant person set out in the Offer Document remains unchanged.

Dealings in relevant securities of Melrose by Royal Bank of Canada:

<b>Starting date</b>	<b>Ending date</b>	<b>Shares purchased</b>	<b>Shares disposed</b>	<b>Net transactions</b>	<b>Highest price</b>	<b>Lowest price</b>
1 February 2018	26 February 2018	0	37,200	(37,200)	£2.18944771	£2.0965254
<b>Total</b>		<b>0</b>	<b>37,200</b>	<b>(37,200)</b>		

**APPENDIX II**  
**GKN PRELIMINARY FULL YEAR RESULTS FOR THE YEAR ENDED 31 DECEMBER 2017**

Set out below are the GKN preliminary full year results for the financial year ended 31 December 2017 as announced on 27 February 2018.



**GKN plc Results Announcement for the year ended 31 December 2017**
**Group Highlights<sup>(a)</sup>**

- Results in line with previous guidance
  - Management sales up 11% (organic sales up 6%), exceeding £10 billion for the first time;
  - Excluding £112 million North American Aerospace balance sheet review adjustments:
    - Operating profit (management basis) of £774 million (2016: £773 million);
    - Earnings per share up 2% to 31.7 pence (2016: 31.0 pence);
  - Reported profit before tax £658 million (2016: £292 million), a rise of 125%<sup>(c)</sup>;
  - Pensions progress - UK defined benefit scheme closed to future accrual, £250 million lump sum paid to reduce the deficit and the level of future deficit recovery payments;
  - Free cash flow of £207 million (2016: £201 million).
- Technology investments continue to deliver business results
  - Strong technology pipeline; innovation recognised by customer and industry awards;
  - Order book on electrified drivelines reaches more than £2 billion;
  - Ramp up of new engine deliveries to increase significantly;
  - Breakthrough contracts in place in GKN Powder Metallurgy additive manufacturing for major auto OEMs; selling product profitably today.
- New product segment strategy and Project Boost announced and being implemented
  - Expected to generate £340 million p.a. of recurring cash benefit from end of 2020<sup>1</sup>;
  - Targeting up to £2.5 billion cash return to shareholders over the next three years<sup>2</sup>;
  - New core segment trading margin targets for 2020<sup>3</sup>: GKN Aerospace at least 14%, GKN Driveline at least 9.5%, Group 11%;
  - Aim to formally separate GKN Aerospace and GKN Driveline into two listed companies via a demerger in the middle of 2019.

	Management basis <sup>(a)</sup>			Statutory basis		
	2017 <sup>(b)</sup> £m	2016 £m	Change %	2017 £m	2016 £m	Change %
Sales	<b>10,409</b>	9,414	+11	<b>9,671</b>	8,822	+10
Operating profit	<b>662</b>	773	-14	<b>699</b>	335	+109 <sup>(c)</sup>
Trading margin (%)	<b>6.4%</b>	8.2%	-180bps			
Profit before tax	<b>572</b>	678	-16	<b>658</b>	292	+125 <sup>(c)</sup>
Earnings per share	<b>26.6p</b>	31.0p	-14	<b>29.3p</b>	14.1p	+108 <sup>(c)</sup>
Dividend per share	<b>9.30p</b>	8.85p	+5	<b>9.30p</b>	8.85p	+5
Free cash flow	<b>207</b>	201				
Net debt	<b>889</b>	704				

<sup>(a)</sup> Financial information set out in this announcement, unless otherwise stated, is presented on a management basis as defined on pages 16 to 18.

<sup>(b)</sup> Including £112 million North American Aerospace balance sheet review adjustments.

<sup>(c)</sup> Primarily higher due to mark to market valuation of FX contracts.

Commenting on the results, Anne Stevens, Chief Executive of GKN said:

“GKN has fantastic businesses which have grown organically above our key markets, demonstrating once again our strong positions and leading technology. However as I set out two weeks ago, we now need to change our emphasis and ensure that those orders deliver world class financial performance with a renewed focus on strong margins and cash generation.

“With Project Boost, I have laid out how we plan to achieve this, through detailed product segment strategies and an emphasis on manufacturing and functional excellence. We are excited about delivering these plans.”

## **Highlights**

### **Group**

- Strong sales growth continued, up 6% organically;
- Accounting deficit for UK pension reduced by 44% to £675 million, with deficit recovery payments falling to £36 million p.a. from 2018;
- Trading margin reduced to 7.4% (2016: 8.2%, including £39 million restructuring costs), excluding the £112 million North American Aerospace balance sheet review adjustments, of which £4 million are included in corporate costs.

### **GKN Aerospace**

- Headline sales growth of 6%; 2% organic growth was ahead of the market;
- Around \$4.1 billion of new and replacement work packages won over contract lives;
- China JV MOU signed with Comac and AVIC;
- Additive manufacturing (AM) partnerships with US Department of Energy's Oak Ridge National Laboratory and Saab;
- Trading margin of 7.8% (2016: 9.9%), excluding the £108 million balance sheet review adjustment. The most significant factor was the performance of the US Standard Aerostructures business which reported a trading loss for the year.

### **GKN Driveline**

- Organic sales growth of 9%, significantly ahead of global auto production, helped by our broad geographic footprint and strong positions on high growth global platforms;
- eDrive order book extended to over £2 billion;
- PACE Innovation Award for the integrated co-axial eAxle on the Volvo XC90 T8 twin engine;
- Electrified driveline programmes launched in China JV (SDS);
- Trading margin of 7.1% (2016: 7.2%, restated), with a good performance in Europe offset by reduced profitability in the North American AWD business, increased eDrive R&D investment to drive future growth, warranty claims and raw material headwind.

### **GKN Powder Metallurgy**

- Organic sales growth of 5%;
- Acquisition of Tozmetal in Turkey;
- Titanium powder production for AM started with partner TLS Technik;
- Launched InstAMetal, digitized metal AM quoting, design and prototyping experience;
- Trading margin of 10.6% (2016: 11.4%), principally reflecting higher raw material surcharge and investment in high-end powder capability in China.

## **New strategy and “Project Boost”**

As set out in our announcement of 14 February 2018, the Board of GKN has concluded a wide-ranging strategic and operational review, which started in 2017. This review focused on both capital allocation discipline and a transformation programme aimed at improving cash flow and margin (“Project Boost”).

This new strategy differentiates core product segments into improve, grow and develop, with each strategy having different capital expenditure targets and different expectations for growth, margin improvement, cash generation and return on investment. Core division margin targets for 2020 have been set, at least 14% for GKN Aerospace, at least 9.5% for GKN Driveline and 11% for the Group<sup>3</sup>. The Project Boost transformation plan is expected to deliver recurring annual cash benefits of £340 million from the end of 2020<sup>1</sup>.

The new strategy has a clear framework that is expected to result in significant cash returns to GKN shareholders. The strategy includes a plan to sell Powder Metallurgy, as well as a number of other non-core businesses. GKN's progressive dividend policy will be to target an average payout of 50% of free cash flow over the period of 2018 to 2020. In addition, GKN expects to distribute surplus cash to shareholders, subject to maintaining an investment grade credit rating. In total, GKN is targeting returns of up to £2.5 billion to shareholders over the next three years, with a significant part expected to come from divestments executed within the first 12 to 18 months, including the sale of Powder Metallurgy.

## **Outlook**

The Group's revenue expectations in the short term are unchanged.

GKN Aerospace's underlying trading margin is expected to show a slight improvement in 2018, despite some further contractual price downs and increased investment in new engine programmes. In 2019, the trading margin is expected to reach around 10% for the Division, on the way to the 2020 target of at least 12% for the Division and 14% for the core aerospace segment, together with strong cash conversion.

In GKN Driveline, solid trading margin progression is expected in both 2018 and 2019 as the Division works towards achieving its core segment trading margin target of at least 9.5% in 2020. Cash conversion is expected to improve significantly during 2018 and thereafter.

GKN Powder Metallurgy's trading margin is expected to show steady progression in 2018 and 2019 as it works towards achieving its 2020 target of at least 11%. Its future is expected to be very strong with great prospects in China, Brazil and India in addition to the good opportunities on high end technology business in Europe and North America. Operating cash flow is expected to remain strong.

## **Separation**

GKN is today providing further information on its plans to separate its Aerospace and Driveline businesses. GKN is in the process of separating operationally and the Board has determined to formally separate GKN Aerospace and GKN Driveline into two listed companies via a demerger. The aim is to complete the demerger in the middle of 2019, creating two strong companies with investment grade balance sheets that can support their share of the Group's pension liabilities. The basis on which to progress these discussions has been agreed with the UK Pension Trustees.

A demerger represents GKN's base case separation structure for a number of reasons, including that the timetable is within GKN's control, it allows GKN to allocate liabilities appropriately and it is tax efficient.

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<sup>1</sup> This statement includes a quantified financial benefits statement which has been reported on for the purposes of the City Code on Takeovers and Mergers ("City Code") (see Appendix 2 to the announcement entitled "Moving GKN to world class performance" dated 14 February 2018 available at [www.gkn.com](http://www.gkn.com)). This does not take account of one-off associated incentive payments, which are estimated to be in the region of £70m (to be satisfied in GKN ordinary shares) and which have not been reported on for the purposes of the City Code. Excludes any impact of potential disposals.

<sup>2</sup> A significant part expected to come from divestments executed within the first 12 to 18 months.

<sup>3</sup> The trading margin targets for 2020 should not be construed as a profit forecast or interpreted as such.

## **Cautionary Statement**

This announcement contains forward looking statements which are made in good faith based on the information available at the time of its approval. It is believed that the expectations reflected in these statements are reasonable but they may be affected by a number of risks and uncertainties that are inherent in any forward looking statement which could cause actual results to differ materially from those currently anticipated. Nothing in this document should be regarded as a profits forecast.

## **Publication on a website**

A copy of this announcement will be published on the GKN website ([www.gkn.com](http://www.gkn.com)) by no later than 12 noon on 28 February 2018. The content of the website referred to in this announcement is not incorporated into and does not form part of this announcement.

## **No material changes**

For the purposes of Rule 27.2(a) of the City Code, there have been no material changes: (i) in the information disclosed in the response circular published by GKN on 15 February 2017 (the “**Defence Document**”) which are material in the context of the Defence Document; and (ii) to the matters listed in Rule 27.2(c) of the City Code since the publication of the Defence Document.

## **Further Enquiries**

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There will be an analyst and investor meeting today at 8.45am at UBS, 5 Broadgate, London, EC2M 2QS in the Auditorium located on the ground floor. The presentation will cover the 2017 full year results and more detail on GKN Aerospace, including its plans within Project Boost. A more detailed presentation regarding GKN Driveline will be held in due course.

A live videocast of today’s presentation will be available at <http://lps.ggwebcast.com/gkn/35>

Slides will be put onto the GKN website approximately 60 minutes before the presentation is due to begin, and will be available to download from the GKN website at: [www.gkn.com](http://www.gkn.com)

A live dial in facility will be available by telephoning: +44 (0) 2071 928000, Conf ID: 8298024

Following the event, a replay of the conference call will be uploaded onto the GKN website and the on-demand archive webcast will be available via [www.gkn.com](http://www.gkn.com)

*Note: Questions will only be taken at the event and the webcast and dial in facility will be turned off before the Q&A session commences. If permitted, the Q&A session will be uploaded to the website later.*

GKN plc LEI: 213800QNZ22GS95OSW84

## NEWS RELEASE

### GKN plc Results Announcement for the year ended 31 December 2017

#### Group Overview

##### Markets

*The Group operates in the global aerospace and automotive markets. GKN Aerospace sells to manufacturers of commercial and military aircraft, aircraft engines and equipment. In the automotive market, GKN Driveline sells to manufacturers of passenger cars and light vehicles. Around 80% of GKN Powder Metallurgy sales are also to the automotive market, with the balance to other industrial customers.*

##### Results<sup>(a)</sup>

Group	2017	2016	Change (%)	
			Headline	Organic
Sales (£m)	<b>10,409</b>	9,414	11	6
Trading profit (£m)	<b>662</b>	773	(14)	(4) <sup>(b)</sup>
Trading margin (%)	<b>6.4%</b>	8.2%		
Return on average invested capital (%)	<b>13.0%</b>	16.0%		

<sup>(a)</sup> Financial information set out in this announcement, unless otherwise stated, is presented on a management basis as defined on pages 16 to 18.

<sup>(b)</sup> Excluding £112 million North American Aerospace balance sheet review adjustments.

Management sales increased organically by £626 million (6%), with currency translation contributing £456 million offset by an £87 million net reduction from acquisitions/divestments, principally relating to the sale of Stromag.

Overall, organic trading profit reduced by £145 million, primarily due to the £112 million balance sheet review charge and associated costs in North American Aerospace and claims of £38 million partly offset by the absence of £40 million restructuring costs incurred in 2016. There was a benefit from currency translation of £43 million and a £9 million net reduction due to acquisitions/divestments.

The Group trading margin reduced to 6.4% (2016: 8.2%), or 7.4% excluding the £112 million North American Aerospace balance sheet review adjustments. The adjustments also impacted the return on average invested capital (ROIC), which reduced to 13.0% (2016: 16.0%).

At 31 December 2017, the Group had net debt of £889 million (31 December 2016: £704 million) and the total deficit on post-employment obligations totalled £1,504 million (2016: £2,033 million). During the year, the Group issued a new £300 million 3.375% annual unsecured bond, £250 million of which was paid into the GKN2 UK pension scheme.

#### Divisional Performance

##### GKN Aerospace

*GKN Aerospace is a leading global tier one supplier of airframe and engine structures, landing gear, electrical interconnection systems, transparencies and aftermarket services. Its technology influences the performance and efficiency of the world's leading commercial and military aircraft.*

The latest Teal data suggest that overall aerospace industry sales were flat in 2017, with commercial sales up 1% and military down 2%. In commercial, single aisle aircraft deliveries grew 7%, while wide-body aircraft declined 3% and regional aircraft fell 8%. Military production was lower as the 12% decline in rotorcraft and 4% fall in transport aircraft more than offset the 9% increase in fighters.

The key financial results for the year are as follows:

GKN Aerospace	2017	2016	Change (%)	
			Headline	Organic
Sales (£m)	<b>3,638</b>	3,423	6	2
Trading profit (£m)	<b>175</b>	339	(48)	(21) <sup>(a)</sup>
Trading margin (%)	<b>7.8%</b> <sup>(a)</sup>	9.9%		
Return on average invested capital (%)	<b>7.5%</b>	14.6%		

<sup>(a)</sup> Excluding £108 million North American balance sheet review adjustments.

Overall, GKN Aerospace's organic sales were £76 million higher (2%). There was a £143 million benefit from currency translation and a £4 million reduction due to disposals. During the year GKN Aerospace completed the sales of its Bandy Machining site in Burbank, California and the Applied Composites business in Linköping, Sweden. GKN Aerospace's sales were split 72% commercial and 28% military.

GKN Aerospace's organic commercial sales declined 1%, principally due to the greater exposure to the wide-body market. Reduced sales were reported on the A380, Boeing 737 MAX (due to the end of a temporary development contract in 2016), business jets, Boeing 777 and CFM56 engine. This was partly offset by stronger production of the A350 and A320, including the PW PurePower® Geared Turbofan™ (GTF) engines. Military sales were organically 11% higher, primarily due to an increase in production of the F-35 and F/A-18 Super Hornet, as well as development sales for advanced proprietary military programmes.

Trading profit was £175 million (2016: £339 million, including £10 million restructuring costs), reflecting the £108 million North American balance sheet review adjustments, an organic profit decline of £73 million, a benefit from a favourable currency translation impact of £16 million and a £1 million improvement due to divestments. The £108 million North American balance sheet review adjustments comprised inventory writedowns of £64 million, charges for onerous contracts of £18 million, re-assessment of customer receivables and claims of £19 million, and correction to fixed asset carrying value of £7 million.

The most significant factor affecting GKN Aerospace's profitability was the performance of the US Standard Aerostructures business which reported a trading loss for the year, due to declining legacy programmes, price pressure, the end of a development contract and operational issues.

In addition, organic trading profit in the year was impacted by a number of factors which net out to around a £15 million negative impact on underlying trading profit. This includes: the £15 million charge in Alabama; a £28 million claim associated with engine programme delays; and recognising £6 million of lower trading profits from the SABCA equity accounted investment. These were partly offset by programme pricing adjustments of £13 million within the engines business and £19 million within the US Standard Aerostructures business.

The engine business performed well and investment continues in the PW PurePower® Geared Turbofan™ (GTF) engines across four different platforms. Fokker also delivered strong results, with good organic growth and achieving the 10% trading margin target set at the time of acquisition, a year ahead of original plans.

Trading margin was 7.8%, excluding the North American balance sheet review adjustments (2016: 9.9%). Return on average invested capital, was 7.5% (2016: 14.6%).

Progress in the development and application of additive manufacturing (AM) continued in the year. Momentum increased in both free form and powder bed with both technologies in production, new orders won and parts now flying on seven platforms across the commercial, military and space markets. This is a key area of focus for the Group.

During the year, new and replacement work packages totalling \$4.1 billion over their contract lives have been won and a number of important milestones were achieved, including:

- Integrated the European structures business with Fokker structures;
- Signed a joint venture memorandum of understanding with Comac and AVIC, in China;
- Secured new work packages and extensions of long-term agreements on key engine platforms;
- Won a three year contract extension worth over \$180 million, covering the technical product support, maintenance and parts supply for the Gripen RM12 Engines used in Sweden, Hungary, Czech Republic, Thailand and South Africa;
- Signed a contract with Honda Aircraft Company to manufacture the complete electrical wiring and interconnection system for the market-leading HondaJet;
- Secured a long-term agreement with Kawasaki Heavy Industries to supply Low-Pressure Compressor Vanes for the PW1100G-JM and PW1400G-JM PurePower® Geared Turbofan™ engines;
- Delivered the first advanced 2.5m diameter Ariane 6 nozzle (SWAN) to ArianeGroup for the Vulcain 2.1 engine incorporating laser-welded technology and AM structures; resulting in 90% fewer component parts, 40% cost reduction and 30% improvement in production time; and
- Signed a research agreement with the U.S. Department of Energy's Oak Ridge National Laboratory, focused on AM in order to progress its use in the manufacture of major, structural components for aircraft and celebrated one year of collaboration with Saab, which has already resulted in the delivery and certification of AM components now flying on Saab aircraft.

## Automotive market

Light vehicle production in 2017 increased 2.2% to 95.1 million vehicles (2016: 93.1 million), with all major markets, except North America, increasing output.

Car and light vehicle production (rounded millions of units)			Growth (%) <sup>(#)</sup>
	2017	2016	
Europe	22.2	21.5	3.2
North America	17.1	17.8	-4.3
Brazil	2.7	2.1	26.1
Japan	9.2	8.8	5.4
China	27.7	27.0	2.6
India	4.5	4.2	6.8
Others	11.7	11.7	0.9
Total – global	95.1	93.1	2.2

Source: February 2018, IHS Markit Production Forecast; <sup>(#)</sup> Growth is derived from unrounded production figures

In 2017, European production increased 3.2% with stronger than expected demand and new model launches providing growth in Western Europe, while the recovering Russian market helped demand in Eastern Europe.

Production in North America was down due to a weaker US market, reflecting a significant reduction in demand for passenger cars. Cheap credit and the low price of fuel continued to support increased demand and production for full-size pickups and Sport Utility Vehicles (SUVs). Production in Brazil rose strongly as recovery in the local market gathered pace and exports increased.

Production growth in China slowed as a result of an increase in the sales tax on small cars and a general slowdown in the market. Solid growth in Japan resulted from the improved economy, following weak demand in 2016. In India, a solidly expanding domestic market helped production increase 6.8%.

## GKN Driveline

*GKN Driveline is the world's leading supplier of automotive driveline systems and solutions. As a global business serving the leading vehicle manufacturers, it develops, builds and supplies an extensive range of automotive driveline products and systems, for use in everything from the smallest low-cost car to the most sophisticated premium vehicles that demand complex driving dynamics. Off-Highway Powertrain is a global supplier of power management products, systems and service solutions for the world's leading off highway and industrial equipment manufacturers. Its technologies deliver efficiencies in the agricultural, construction, mining, utility and industrial markets.*

The key financial results for the year are as follows:

GKN Driveline	2017	2016 <sup>(a)</sup>	Change (%)	
			Headline	Organic
Sales (£m)	<b>5,308</b>	4,614	15	9
Trading profit (£m)	<b>377</b>	330	14	8
Trading margin (%)	<b>7.1%</b>	7.2%		
Return on average invested capital (%)	<b>18.7%</b>	18.3%		

<sup>(a)</sup> Restated to include Off-Highway Powertrain, previously part of GKN Land Systems

Organic sales increased by £457 million (9%), substantially ahead of global light vehicle production which was up 2.2%. The beneficial effect from currency translation was £237 million. Constant Velocity Jointed (CVJ) Systems accounted for 65% of GKN Driveline's sales, all-wheel drive (AWD) and eDrive sales were 28%, and Off-Highway Powertrain sales represented 7%.

GKN Driveline's market outperformance was mainly in China and in North America. In China, significant growth was achieved following new programme launches with additional content from AWD sales, including to a number of domestic manufacturers, and an unusually strong sales performance in the fourth quarter. In North America, sales grew well above the market, reflecting strong recent programme gains and in Europe, production continued slightly ahead of the market, benefitting from good demand for premium vehicles. In Japan, GKN Driveline's sales grew at a slower rate than the market due to vehicle mix. Off-Highway Powertrain delivered strong sales growth and significantly improved trading profit.

Overall, GKN Driveline trading profit increased £47 million to £377 million, including the favourable impact of currency translation of £20 million. The organic increase in trading profit was £27 million, with the increased investment in eDrive of £36 million (2016: £16 million) being offset by the non-recurrence of restructuring charges in 2016 of £22 million (restated to include Off-Highway Powertrain, previously part of GKN Land Systems). The North American AWD business continued to improve operationally, although profitability reduced as new launches increasingly replaced mature, higher margin, programmes. During 2018, the focus will be on driving margin improvement.

Other costs incurred, include £10 million of warranty claims and net raw material price headwinds of £12 million. GKN Driveline's trading margin was 7.1% (2016: 7.2%). Return on average invested capital was 18.7% (2016: 18.3%).

GKN Driveline's European plants continue to operate at very high capacity utilisation with a strong conversion on the additional sales. In China, margin reduced as expected, with the benefit of increased sales being offset by pricing pressure and the on-going investment in new programmes, engineering and technology localisation, particularly to support AWD and eDrive growth. In the Americas, operations were helped by strong growth in Brazil, USA and Mexico with an associated increase in launch investments being made to support a high number of new programmes.



The trend towards electrification of passenger vehicles continues to accelerate, which is an area of significant strength to GKN. GKN Driveline is already a market leader having delivered over 725,000 eDrive systems, serving premium and global customer brands with its award-winning technology and world leading vehicle and systems integration capability. The order book for eDrive technologies stood at £2 billion at the end of 2017 following a series of significant programme wins with major global automakers. During the year £35 million of eDrive sales were reported, with sales expected to reach £500 million by 2022.

During the year, around £600 million of annualised sales in new and replacement business was secured and a number of important milestones achieved, including:

- Launched the third application of the new lightweight VL3 constant velocity joint (CVJ) on the new BMW X3;
- Commenced production of its latest technologies in China, through its joint venture: a complete AWD disconnect system for small to medium-sized vehicles, as well as production of its Disconnect four-wheel drive system;
- Established dedicated Industry 4.0 team and pilot cells launched in all regions;
- Created digital operational reporting to link all GKN Driveline plants to one global system;
- Deployed web-based, on-line, digital programme management system on all AWD and eDrive programmes;
- New management team installed in the largest (USA) AWD plant and experienced CEO appointed to run the global CVJ business;
- Won an Automotive News PACE Innovation Award for the integrated co-axial eAxle on the Volvo XC90 T8 twin engine;
- Received “Machine of the year-Special Award” at Agritechnica for the GKN Walterscheid Hydraulic Top-Link;
- Received the highest-ever number of Global customer awards in 2017 (22 vs 17 in 2016);
- Announced that China will become a global production hub for electrified driveline in 2018, when production of the latest eDrive technologies commences;
- Opened a new winter test facility in Michigan, USA to complement the existing proving grounds for extreme cold-weather testing in Sweden and China;
- Announced at the IAA Frankfurt Motor Show, the new eTwinstarX, two-speed eAxle with Twinstar technology which is delivering exceptional performance during GKN’s winter test programme. eTwinstarX will bring torque vectoring and improved handling, performance and efficiency to the next generation of electric vehicles; and
- Agreed a multi-year partnership with Panasonic Jaguar Racing, providing design, manufacturing and engineering services to the Formula E team.

## GKN Powder Metallurgy

*GKN Powder Metallurgy comprises GKN Sinter Metals and Hoeganaes. GKN Sinter Metals is the world’s leading manufacturer of precision automotive sintered components as well as components for industrial and consumer applications. Hoeganaes is one of the world’s leading manufacturers of metal powder, the essential raw material for powder metallurgy.*

The key financial results for the year are as follows:

GKN Powder Metallurgy	2017	2016	Change (%)	
			Headline	Organic
Sales (£m)	1,174	1,032	14	5
Trading profit (£m)	125	118	6	(2)
Trading margin (%)	10.6%	11.4%		
Return on average invested capital (%)	19.7%	21.0%		

Organic sales were £55 million higher, including £33 million pass through to customers of higher scrap steel prices and other commodities. There was a £60 million benefit from currency translation and a £27 million increase from the acquisitions of a majority share of a powder manufacturer in China and a Turkish metal parts company.

Organic sales growth before raw material pass through was 2%, in line with global light vehicle production. Strong underlying sales growth was achieved in China, Europe and Brazil but sales in North America fell due to weaker automotive demand.

Trading profit increased £7 million to £125 million, benefiting from favourable currency translation of £7 million. The organic reduction in trading profit was £3 million and there was a £3 million profit from acquisitions.

The divisional trading margin was 10.6% (2016: 11.4%), reflecting the £8 million impact of higher raw material prices, ongoing investment in China and tougher market conditions in the US. Return on average invested capital was 19.7% (2016: 21.0%).

The European business, principally focused on small parts, grew well increasing its sales into the automotive market. Good progress continues in Asia with double digit sales growth. North America was tougher reflecting a slowdown in the automotive market. Digitisation across the shop floor is assisting with productivity gains across GKN Powder Metallurgy.

Commercial titanium powder production for AM started in Cinnaminson, USA as part of the venture with TLS Technik. Interest in powder continues to be strong and a number of production orders have been received from key customers for both standard and customised titanium AM powder alloys. There is also increased demand for AM parts for use in the automotive and industrial sectors.

During the year, more than £200 million of annualised sales in new and replacement business was secured (particularly in the well-performing “small” product segment and Asia) and a number of important milestones achieved, including:

- Completed the acquisition of Turkish powder metal parts manufacturer Tozmetal Ticaret Ve Sanayi AS (Tozmetal), adding pump part capacity;
- Made further steps towards Industry 4.0 by fully implementing global connectivity on more than 2,500 assets to support quality, productivity and most effective asset utilization;
- Launched a new e-commerce platform, InstAMetal, a revolutionary digitized quoting and design experience for metal AM that will bring speed and simplicity of online ordering to engineering prototypes;
- Agreed partnerships with GE and EOS in AM;
- Received the Best Supplier Award for quality performance by Somfy for the high-class planetary gears and components that it supplies for electrical shutter motors; and
- Received two prestigious Grand Prize Design Excellence Awards from the Metal Powder Industries Federation in the Automotive Transmission category (planetary carrier assembly for Ford Motor Company) and the Automotive Chassis category (copper-steel output pulley for Nidec Automotive Motor Americas).

## **Other Businesses and corporate costs**

GKN's Other Businesses comprise Wheels and Structures (previously part of GKN Land Systems) and Cylinder Liners (a 59% owned venture mainly in China, manufacturing engine liners for the truck market in the US, Europe and China). 2016 comparators are restated for the inclusion of Stromag and Wheels and Structures, previously part of GKN Land Systems.

GKN's Other Businesses reported combined sales in the period of £289 million (2016: £345 million). The change reflects a £38 million organic increase in sales due to good growth in Cylinder Liners and Wheels, a £16 million benefit from currency translation and a reduction due to the disposal of Stromag of £110 million.

A trading profit of £16 million was reported (2016: £7 million) including a £1 million benefit from currency translation. Organic trading profit was £21 million higher, reflecting a strong performance in Cylinder Liners and the absence of a restructuring charge in 2016. Trading profit was £13 million lower due to the disposal of Stromag.

Corporate costs, which comprise the costs of stewardship of the Group and operating charges and credits associated with the Group's legacy businesses, were £31 million (2016: £21 million), principally due to £4 million of additional costs associated with the North American balance sheet review, £4 million of additional costs associated with closure of the UK pension scheme and the absence of a pension gain of £5 million in 2016. There was also a £1 million adverse currency translation impact.

## **Other Financial Information**

### **Items excluded from management trading profit**

In order to achieve consistency and comparability of underlying results between reporting periods, certain items are presented separately from management basis results which are used in many of the Group's Key Performance Indicators. In addition, management basis results aggregate the sales and trading profit of subsidiaries with the Group's share of the sales and trading profits of equity accounted investments.

The Group uses management measures, which are non-GAAP measures, for certain remuneration targets and to assess operating performance on a consistent basis, as we believe this gives a fairer assessment from period to period of the underlying activity of the business. The use of management measures allows the Group to chart progress, make decisions and allocate resources based on the actions for which management is responsible or can influence, without volatility arising from significant one-time trading and portfolio change transactions or the mark to market valuation of currency hedges.

The items excluded from management basis results are adjusted because of their size or nature. The Group considers the following matters when assessing the nature of items to be excluded; whether the charge or income is significantly impacted by fair value movements outside of management control (change in value of derivative and other financial instruments and fair value changes on cross currency interest rate swaps), it is non-cash (interest charge on post-employment benefits and unwind of discounts) or it does not relate to trading performance but rather acquisition or divestment activity (amortisation of non-operating intangible assets arising on business combinations, gains and losses on changes in Group structure and acquisition-related restructuring charges).

### **Change in value of derivative and other financial instruments**

The change in value of derivative and other financial instruments during the year resulted in a credit of £364 million (2016: £154 million charge).

When the business wins long term customer contracts that are in a foreign currency, the Group seeks to mitigate the potential volatility of the future cash flows by hedging through forward foreign currency exchange contracts. At each period end, the Group is required to mark to market these contracts even though it has no intention of closing them out in advance of their maturity dates. At 31 December 2017, the net fair value of such instruments was a liability of £117 million (2016: £482 million liability) and the change in fair value during the year was a £364 million credit (2016: £135 million charge).

There was also a £6 million charge arising from the change in fair value of embedded derivatives in the year (2016: £4 million credit) and a net gain of £6 million attributable to the currency impact on Group funding balances (2016: £23 million net loss).

### **Amortisation of non-operating intangible assets arising on business combinations**

The charge for amortisation of non-operating intangible assets arising on business combinations (for example, customer contracts, order backlog, technology and intellectual property rights) was £100 million (2016: £103 million).

## **Gains and losses on changes in Group structure**

The net loss on changes in Group structure was £2 million (2016: £9 million loss).

On 29 December 2017, the Group sold its GKN Applied Composites AB business for a cash consideration of £7 million before professional fees. The profit on sale of £3 million comprises profit on disposal of net assets only with no impact from reclassification of previous currency variations from other reserves.

On 14 August 2017, the Group sold its GKN Aerospace Bandy Machining, Inc. business for a cash consideration of £1 million before professional fees. The loss on sale of £1 million comprises £5 million loss on disposal of net assets and £3 million gain from reclassification of previous currency from other reserves.

## **Acquisition-related restructuring charges**

There were no charges regarding acquisition-related restructuring in the year (2016: £31 million).

## **Impairment charges**

Consistent with previous years, all goodwill, together with cash generating units (CGUs) where there were indicators of impairment, was tested for impairment. An impairment charge of £131 million (2016: £52 million) has been recorded in the Income Statement as an adjusting and therefore non-trading item within the line 'impairment charges' in respect of seven CGUs all within the Aerospace division.

## **Post-tax earnings of equity accounted investments**

On a management basis, the sales and trading profits of equity accounted investments are included pro-rata in the individual divisions to which they relate, although shown separately post-tax in the statutory income statement.

The Group's share of post-tax earnings on a management basis was £80 million (2016: £73 million), with trading profit of £94 million (2016: £89 million). The Group's share of the tax and net financing costs amounted to £14 million (2016: £16 million). Trading profit increased £5 million, primarily due to an unusually strong performance in the fourth quarter in China.

## **Net financing costs**

Net financing costs totalled £121 million (2016: £116 million) and comprise the net interest payable of £76 million (2016: £79 million), the interest charge on post-employment benefits of £47 million (2016: £53 million), a credit from fair value changes on cross currency interest rate swaps of £4 million (2016: £18 million credit) and charge for unwind of discounts of £2 million (2016: £2 million). The non-cash charge on post-employment benefits, fair value changes on cross currency interest rate swaps and unwind of discounts are not included in management figures. Details of the assumptions used in calculating post-employment costs are provided in note 15.

Interest payable was £86 million (2016: £86 million), whilst interest receivable was £10 million (2016: £7 million) resulting in net interest payable of £76 million (2016: £79 million).

## **Profit before tax**

Management profit before tax was £572 million (2016: £678 million) and £684 million excluding the impact of the Aerospace North America balance sheet review adjustments. Profit before tax on a statutory basis was £658 million (2016: £292 million). The main differences between management and statutory figures for 2017 are the change in value of derivative and other financial instruments, amortisation of non-operating intangible assets arising on business combinations, impairment charges and non-cash charge on post-employment benefits. Further details are provided in note 3 to the financial statements.

## **Taxation**

The book tax rate on management profits of subsidiaries was 22% (2016: 24%), arising as a £110 million tax charge (2016: £144 million) on management profits of subsidiaries of £492 million (2016: £605 million).

The theoretical average tax rate reduced in 2017, largely due to tax losses arising in the US. The book tax rate is slightly higher than the theoretical weighted average tax rate, principally due to the tax on items excluded from management profit and changes in deferred tax assets.

The tax rate on statutory profits of subsidiaries was 26% (2016: 22%) arising as a £149 million tax charge (2016: £48 million) on statutory profits of subsidiaries of £578 million (2016: £219 million).

## **Non-controlling interests**

The profit attributable to non-controlling interests was £6 million (2016: £2 million).

## **Earnings per share**

Management earnings per share was 26.6 pence, or 31.7 pence excluding the after tax impact of the £112 million North American Aerospace balance sheet review adjustments (2016: 31.0 pence). Average shares outstanding in 2017 were 1,714.7 million (2016: 1,712.1 million).

On a statutory basis earnings per share was 29.3 pence (2016: 14.1 pence), impacted by a significant credit from the change in value of derivatives and other financial instruments.

## **Dividend**

The Board has decided to recommend a final dividend of 6.2 pence per share (2016: 5.9 pence per share). The total dividend for the year will, therefore, be 9.3 pence per share (2016: 8.85 pence per share), an increase of 5%. The final dividend is payable on 14 May 2018 to shareholders on the register on 6 April 2018. Shareholders may choose to use the Dividend Reinvestment Plan (DRIP) to reinvest the final dividend. The closing date for receipt of new DRIP mandates is 20 April 2018.

The Group's progressive dividend policy will be to target an average payout of 50% of free cash flow over the period of 2018 to 2020.

## **Cash flow**

Operating cash flow, which is defined as cash generated from operations of £600 million (2016: £778 million) adjusted for capital expenditure (net of proceeds from capital grants) of £519 million (2016: £494 million), repayment of principal on government refundable advances of £8 million (2016: £6 million) and proceeds from the sale/realisation of fixed assets of £8 million (2016: £37 million), was an inflow of £81 million (2016: £315 million).

Management operating cash flow, which is operating cash flow adjusted for pension deficit funding and cash flow associated with restructuring charges excluded from management trading profit, was £397 million (2016: £388 million).

Cash generated from operations includes movements in working capital and provisions totalling £48 million (2016: £130 million). The 2017 movement was impacted by the £105 million working capital write-offs related to the North American Aerospace balance sheet review adjustments and the £15 million Alabama write-off.

Capital expenditure (net of proceeds from capital grants) on both tangible and intangible assets totalled £519 million (2016: £494 million). Of this, £440 million (2016: £410 million) was on tangible fixed assets and was 1.5 times (2016: 1.6 times) the depreciation charge. Expenditure on intangible assets, mainly initial non-recurring costs on Aerospace programmes, totalled £79 million (2016: £84 million).

The Group invested £201 million in the year (2016: £186 million) on research and development activities not qualifying for capitalisation, net of £61 million (2016: £59 million) customer and government funding.

Net interest paid totalled £71 million (2016: £76 million) including £6 million receipts related to favourable tax case settlements. Tax paid in the year was £113 million (2016: £93 million).

### **Free cash flow**

Free cash flow, which is operating cash flow including equity accounted investment dividends and after interest, tax, dividends paid to non-controlling interests but before dividends paid to GKN shareholders, was an inflow of £207 million (2016: £201 million inflow).

### **Net debt**

At the end of the year, the Group had net debt of £889 million (2016: £704 million). The Group has a series of cross currency interest rate swaps, used to better align its foreign currency income receipts with its debt coupon payments. The fair value of these derivative instruments at 31 December 2017 was a liability of £151 million (2016: liability of £214 million) which is included in the net debt figure of £889 million. The benefit from these derivative instruments was primarily offset by the issuance of a new £300 million unsecured bond with an annual fixed interest rate of 3.375% maturing in May 2032, and the subsequent lump-sum pension contribution of £250 million.

### **Pensions and post-employment obligations**

GKN operates a number of defined benefit pension schemes and historical retiree medical plans across the Group.

At 31 December 2017, the total deficit on post-employment obligations of the Group totalled £1,504 million (2016: £2,033 million), comprising deficits on funded obligations of £782 million (2016: £1,322 million) and on unfunded obligations of £722 million (2016: £711 million). In total, the deficit has decreased £529 million since 31 December 2016, primarily due to changes in the actuarial assumptions and the pension contributions made.

The amount included within trading profit for the year comprises current service cost of £38 million (2016: £48 million) and administrative costs of £5 million (2016: £3 million). The interest charge on net defined benefit plans, which is excluded from management figures, was £47 million (2016: £53 million).

Cash contributions to the various defined benefit pension schemes and retiree medical arrangements totalled £344 million (2016: £121 million), including a £250 million lump sum contribution to the GKN2 scheme.

### **UK pensions**

The accounting deficit for UK defined benefit pension schemes decreased to £675 million (2016: £1,204 million).

During the year, the Group's two UK defined benefit pension schemes completed their triennial funding valuations as at 5 April 2016 for GKN2 and 31 December 2016 for GKN3.

The outcome of these discussions resulted in a lump sum contribution of £250 million paid in October 2017, in addition to the £42 million annual contribution. From 2018, the annual contribution will be £36 million per annum.

During the year, a decision was also taken to close GKN 2 to future accrual and following a consultation process with the scheme members, the closure took place effective 30 June 2017. UK pension benefits are now provided on a Defined Contribution basis.

### ***Defined contribution pension schemes***

In addition to defined benefit pension schemes, the Group also operates a number of defined contribution schemes for which the income statement charge was £84 million (2016: £62 million).

### **Net assets**

Net assets of £2,580 million were £418 million higher than the December 2016 year end figure of £2,162 million. The increase is driven by management profit after tax (£462 million), a gain on remeasurement of defined benefit plans, net of tax (£227 million), and changes in value of derivative and other financial instruments (£364 million), which have been partially offset by amortisation of non-operating intangible assets arising on business combinations (£100 million), currency (including fair value changes in net investment hedging) movements in other comprehensive income, net of tax (£163 million), impairment charges (£131 million) and dividends paid to equity shareholders (£154 million).

### **Exchange rates**

Exchange rates used for currencies most relevant to the Group's operations are:

	Average		Year End	
	2017	2016	2017	2016
Euro	1.14	1.22	1.12	1.17
US dollar	1.29	1.35	1.35	1.23

The approximate impact on 2017 trading profit of subsidiaries and equity accounted investments of a 1% movement in the average rate would be euro - £2 million, US dollar - £2 million.

### **Funding, liquidity and going concern**

At 31 December 2017, UK committed bank facilities were £844 million (2016: £863 million). Within this amount there are committed revolving credit facilities of £800 million (2016: £800 million) and a £32 million (2016: £48 million) eight-year amortising facility from the European Investment Bank (EIB). The revolving credit facilities of £800 million mature in 2019, whilst the third of five equal, annual £16 million EIB repayments was paid in 2017. At 31 December 2017, £32 million of the EIB facility was drawn (2016: £48 million drawn) and there were no drawings on any of the UK revolving credit facilities (2016: no drawings).

Capital market borrowings at 31 December 2017 and 31 December 2016 comprised a £350 million 6.75% annual unsecured bond maturing in October 2019 and a £450 million 5.375% semi-annual unsecured bond maturing in September 2022. During the period, the Group issued a new £300 million 3.375% annual unsecured bond maturing in May 2032.

As at 31 December 2017, the Group had net debt of £889 million (2016: £704 million).

All of the Group's committed credit facilities have financial covenants requiring EBITDA of subsidiaries to be at least 3.5 times net interest payable and for net debt to be no greater than 3 times EBITDA of subsidiaries. The covenants are tested every six months using the previous 12 months' results. For the 12 months to 31 December 2017, EBITDA was 12.5 times greater than net interest payable, whilst net debt was 0.9 times EBITDA.

The Group has a series of cross currency interest rate swaps to better align its foreign currency income receipts in US Dollars and Euros with its debt and had the effect of converting its Sterling bonds into US Dollars (\$951 million) and Euros (€284 million). The cross currency interest rate swaps have been designated as a net investment hedge of the Group's US Dollar and Euro net assets.

A limited number of Group trade receivables are subject to non-recourse factoring and customer supply chain finance arrangements, from seven banks. As at 31 December 2017, the facilities totalled £248 million (2016: £258 million) with drawings of £189 million (2016: £209 million).

The Group also has a limited supply chain finance programme for its suppliers from five banks. As at December 2017, total facilities were £150 million (2016: £101 million) with drawings of £94 million (2016: £73 million).

The Directors have taken into account both divisional and Group forecasts for the 18 months from the balance sheet date to assess the future funding requirements of the Group and compared them to the level of committed available borrowing facilities, described above. The Directors have concluded that the Group will have a sufficient level of headroom in the foreseeable future and that the likelihood of breaching covenants in this period is remote, such that it is appropriate for the financial statements to be prepared on a going concern basis.

## **Definitions and management measures**

Financial information set out in this announcement, unless otherwise stated, is presented on a management basis which excludes certain items. The items excluded from management trading results and the reasons for their exclusion are set out on pages 11 and 12.

Management use non-GAAP measures, commonly referred to as Alternative performance measures (APMs), in the preparation and presentation of the financial information which are not defined or specified under the requirements of IFRS.

The Group uses management measures to provide additional useful information to assess the operating performance on a comparable basis and are not intended to be a substitute for, or superior to, IFRS measures.

Management measures are consistent with how information is reported to the board and enables management to chart progress, make decisions and allocate resources based on the same underlying performance of the Group, without volatility arising from significant non-trading items such as impairment charges, portfolio change transactions or change in value of derivatives and other financial instruments.



## Management measures used comprise:

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### **Management measure:** management results

		<b>2017</b>	<b>2016</b>
		<b>£m</b>	<b>£m</b>
Management sales are sales of subsidiaries with the Group's share of the sales of equity accounted investments (EAI).	Sales of subsidiaries Sales of EAI <b>Management sales</b>	9,671 738 <b>10,409</b>	8,822 592 <b>9,414</b>
Management trading profit is trading profit, (defined as operating profit excluding the impact of non-trading items, see note 3) of subsidiaries with the Group's share of the trading of EAI.	Trading profit of subsidiaries Trading profit of EAI <b>Management trading profit</b>	£m 568 94 <b>662</b>	£m 684 89 <b>773</b>
Management profit before tax is management trading profit less net subsidiary interest payable and receivable; the Group's share of net interest payable and receivable and taxation of EAI.	Management trading profit Net subsidiary interest Group share of EAI interest Group share of EAI tax <b>Management profit before tax</b>	£m 662 (76) 2 (16) <b>572</b>	£m 773 (79) (1) (15) <b>678</b>
Management trading margin is management trading profit expressed as a percentage of management sales.	Management sales Management trading profit <b>Management trading margin</b>	£m 10,409 662 <b>6.4%</b>	£m 9,414 773 <b>8.2%</b>
Management earnings per share is management profit after tax attributable to owners of the parent divided by the weighted average number of ordinary shares in issue (excluding treasury shares).	Management profit after tax Weighted average number of shares <b>Management earnings per share</b>	£m 456 1,714.7 <b>26.6p</b>	£m 530 1,712.1 <b>31.0p</b>

These are key internal management metrics used to assess the Group as a whole including its equity accounted investments enabling full view of the overall performance.

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### **Management measure:** organic sales growth

		<b>£m</b>	<b>£m</b>
Management sales measured both in absolute terms and on an underlying basis (excluding the effects of currency translation, acquisitions and divestments relative to the prior year). Organic sales growth is organic change as a percentage of management sales, currency impact and divestments.	Group management sales Currency impact Divestments	9,414 456 (114)	7,689 862 –
		<b>9,756</b>	<b>8,551</b>
	Acquisitions Organic change	27 626	654 209
	Group management sales <b>Organic sales growth</b>	10,409 <b>6.4%</b>	9,414 <b>2.4%</b>

This enables readers to understand the underlying sales growth rate on a comparable basis without the effect of those items mentioned which could impact the rate of growth.

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**Management measure:** organic trading profit growth

		£m	£m
Management trading profit measured both in absolute terms and on an underlying basis (excluding the effects of currency translation, acquisitions and divestments relative to the prior year). Organic trading profit growth is organic change as a percentage of prior year management trading profit, currency impact and divestments. In 2017 this excludes the impact of the North American Aerospace balance sheet review.	Group management trading profit	773	679
	Currency impact	43	89
	Divestments	(12)	–
		804	768
	Acquisitions	3	62
	North American Aerospace balance sheet review	(112)	–
	Organic change	(33)	(57)
	Group management trading profit	662	773
	<b>Organic trading profit decline</b>	<b>(4.1)%</b>	<b>(7.4)%</b>

This enables readers to understand the underlying trading profit growth rate on a comparable basis without the effect of those items mentioned which could impact the rate of growth.

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**Management measure:** operating cash flow

		£m	£m
Cash generated from operations adjusted for capital expenditure (tangible and intangible), government capital grants, proceeds from disposal of fixed assets and government refundable advances.	Cash generated from operations	600	778
	Capital expenditure	(521)	(500)
	Government capital grants	2	6
	Proceeds from fixed asset disposals	8	37
	Government refundable advances	(8)	(6)
	<b>Operating cash flow</b>	<b>81</b>	<b>315</b>

This measure shows the cash generated by the Group following the inclusion of capital items.

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**Management measure:** free cash flow

		£m	£m
Operating cash flow including interest, tax, equity accounted investment dividends, special pension payments and amounts paid to non-controlling interests, but excluding dividends paid to GKN shareholders.	Operating cash flow	81	315
	Dividends from EAI	60	57
	Interest	(71)	(76)
	Tax	(113)	(93)
	Special pension repayment	250	–
	Dividends paid to NCI	–	(2)
	<b>Free cash flow</b>	<b>207</b>	<b>201</b>

This measure shows the cash generated and retained by the Group in the year available for distribution to shareholders.

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**Management measure:** management operating cash flow

		£m	£m
Operating cash flow adjusted for pension deficit funding and cash flows associated with restructuring charges excluded from management trading profit.	Operating cash flow	81	315
	Pension deficit funding	292	57
	Acquisition related restructuring	13	16
	Portfolio change restructuring	11	–
	<b>Management operating cash flow</b>	<b>397</b>	<b>388</b>

This measure allows clarity of operating cash flow excluding the impact of large one-off items in the year.

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**Management measure:** return on average invested capital (ROIC)

		£m	£m
Management trading profit as a percentage of average total net assets, which is defined as the net assets of the Group excluding post-employment obligations, tax, borrowings and derivatives throughout the year.	Management trading profit	662	773
	Average invested capital	5,076	4,823
	<b>ROIC</b>	<b>13.0%</b>	<b>16.0%</b>

This allows ROIC to be calculated on the operating assets of the business within the control of management.

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**Management measures:** impact of the North American balance sheet review

Given the significance of the £112 million charge booked as a result of the North American balance sheet review certain management measures have been included to avoid possible distortion of prior year comparisons. The additional 2017 measures are noted below.

	£m
Management trading profit (as adjusted for £112 million)	774
Management profit before tax (as adjusted for £112 million)	684
Management earnings per share (as adjusted for the after tax effect of the £112 million)	31.7p
Aerospace organic trading profit decline (as adjusted for £108 million)	(20.5)%

## APPENDICES

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## Consolidated Income Statement

For the year ended 31 December 2017

	Notes	2017 £m	2016 £m
<b>Sales</b>	2	<b>9,671</b>	8,822
<i>Trading profit</i>	2	<b>568</b>	684
<i>Change in value of derivative and other financial instruments</i>	4	<b>364</b>	(154)
<i>Amortisation of non-operating intangible assets arising on business combinations</i>	5	<b>(100)</b>	(103)
<i>Gains and losses on changes in Group structure</i>	6	<b>(2)</b>	(9)
<i>Acquisition-related restructuring charges</i>	7	<b>–</b>	(31)
<i>Impairment charges</i>	8	<b>(131)</b>	(52)
<b>Operating profit</b>		<b>699</b>	335
<b>Share of post-tax earnings of equity accounted investments</b>		<b>80</b>	73
Interest payable		<b>(86)</b>	(86)
Interest receivable		<b>10</b>	7
Other net financing charges		<b>(45)</b>	(37)
<b>Net financing costs</b>	9	<b>(121)</b>	(116)
<b>Profit before taxation</b>		<b>658</b>	292
<b>Taxation</b>	10	<b>(149)</b>	(48)
<b>Profit after taxation for the year</b>		<b>509</b>	244
Profit attributable to non-controlling interests		<b>6</b>	2
Profit attributable to owners of the parent		<b>503</b>	242
		<b>509</b>	244
<b>Earnings per share – pence</b>	11		
Continuing operations – basic		<b>29.3</b>	14.1
Continuing operations – diluted		<b>29.1</b>	14.0

# Consolidated Statement of Comprehensive Income

For the year ended 31 December 2017

	Notes	2017 £m	2016 £m
Profit after taxation for the year		<b>509</b>	244
Other comprehensive income			
<b>Items that may be reclassified to profit or loss</b>			
Currency variations – subsidiaries			
Arising in year		<b>(214)</b>	671
Reclassified in year	6	<b>(3)</b>	2
Currency variations – equity accounted investments			
Arising in year		<b>(4)</b>	22
Net investment hedge changes in fair value			
Arising in year		<b>55</b>	(177)
Taxation	10	<b>3</b>	(14)
		<b>(163)</b>	504
<b>Items that will not be reclassified to profit or loss</b>			
Remeasurement of defined benefit plans			
Subsidiaries	15	<b>291</b>	(396)
Taxation	10	<b>(64)</b>	63
		<b>227</b>	(333)
Other comprehensive income for the year		<b>64</b>	171
Total comprehensive income for the year		<b>573</b>	415
Total comprehensive income attributable to non-controlling interests		<b>4</b>	6
Total comprehensive income attributable to owners of the parent		<b>569</b>	409
		<b>573</b>	415

# Consolidated Statement of Changes in Equity

For the year ended 31 December 2017

	Notes					Other reserves			Equity attributable to equity holders of the parent £m	Non-controlling interests £m	Total equity £m
		Share capital £m	Capital redemption reserve £m	Share premium account £m	Retained earnings £m	Exchange reserve £m	Hedging reserve £m	Other reserves £m			
<b>At 1 January 2017</b>		<b>173</b>	<b>298</b>	<b>330</b>	<b>981</b>	<b>881</b>	<b>(402)</b>	<b>(134)</b>	<b>2,127</b>	<b>35</b>	<b>2,162</b>
Profit for the year		–	–	–	<b>503</b>	–	–	–	<b>503</b>	<b>6</b>	<b>509</b>
Other comprehensive income/(expense):											
Remeasurement of defined benefit plans and related tax		–	–	–	<b>227</b>	–	–	–	<b>227</b>	–	<b>227</b>
Currency variations and related tax		–	–	–	–	<b>(204)</b>	–	–	<b>(204)</b>	<b>(2)</b>	<b>(206)</b>
Net investment hedge changes in fair value and related tax		–	–	–	–	–	<b>43</b>	–	<b>43</b>	–	<b>43</b>
		–	–	–	<b>227</b>	<b>(204)</b>	<b>43</b>	–	<b>66</b>	<b>(2)</b>	<b>64</b>
Total comprehensive income		–	–	–	<b>730</b>	<b>(204)</b>	<b>43</b>	–	<b>569</b>	<b>4</b>	<b>573</b>
Share-based payments		–	–	–	<b>4</b>	–	–	–	<b>4</b>	–	<b>4</b>
Purchase of own shares by Employee Share Ownership Plan Trust		–	–	–	<b>(6)</b>	–	–	–	<b>(6)</b>	–	<b>(6)</b>
Share options exercised		–	–	–	<b>1</b>	–	–	–	<b>1</b>	–	<b>1</b>
Dividends paid to equity shareholders	12	–	–	–	<b>(154)</b>	–	–	–	<b>(154)</b>	–	<b>(154)</b>
<b>At 31 December 2017</b>		<b>173</b>	<b>298</b>	<b>330</b>	<b>1,556</b>	<b>677</b>	<b>(359)</b>	<b>(134)</b>	<b>2,541</b>	<b>39</b>	<b>2,580</b>
At 1 January 2016		173	298	330	1,217	243	(264)	(134)	1,863	23	1,886
Profit for the year		–	–	–	<b>242</b>	–	–	–	<b>242</b>	<b>2</b>	<b>244</b>
Other comprehensive income/(expense):											
Remeasurement of defined benefit plans and related tax		–	–	–	<b>(333)</b>	–	–	–	<b>(333)</b>	–	<b>(333)</b>
Currency variations and related tax		–	–	–	–	<b>638</b>	–	–	<b>638</b>	<b>4</b>	<b>642</b>
Net investment hedge changes in fair value and related tax		–	–	–	–	–	<b>(138)</b>	–	<b>(138)</b>	–	<b>(138)</b>
		–	–	–	<b>(333)</b>	<b>638</b>	<b>(138)</b>	–	<b>167</b>	<b>4</b>	<b>171</b>
Total comprehensive income		–	–	–	<b>(91)</b>	<b>638</b>	<b>(138)</b>	–	<b>409</b>	<b>6</b>	<b>415</b>
Share-based payments		–	–	–	<b>5</b>	–	–	–	<b>5</b>	–	<b>5</b>
Share options exercised		–	–	–	<b>1</b>	–	–	–	<b>1</b>	–	<b>1</b>
Addition of non-controlling interest		–	–	–	–	–	–	–	–	<b>9</b>	<b>9</b>
Purchase of non-controlling interest		–	–	–	<b>(1)</b>	–	–	–	<b>(1)</b>	<b>(1)</b>	<b>(2)</b>
Dividends paid to equity shareholders	12	–	–	–	<b>(150)</b>	–	–	–	<b>(150)</b>	–	<b>(150)</b>
Dividends paid to non-controlling interests		–	–	–	–	–	–	–	–	<b>(2)</b>	<b>(2)</b>
<b>At 31 December 2016</b>		<b>173</b>	<b>298</b>	<b>330</b>	<b>981</b>	<b>881</b>	<b>(402)</b>	<b>(134)</b>	<b>2,127</b>	<b>35</b>	<b>2,162</b>

Other reserves include accumulated reserves where distribution has been restricted due to legal or fiscal requirements and accumulated adjustments in respect of piecemeal acquisitions.

# Consolidated Balance Sheet

At 31 December 2017

	Notes	2017 £m	2016 £m
<b>Assets</b>			
<b>Non-current assets</b>			
Goodwill		492	588
Other intangible assets		1,179	1,320
Property, plant and equipment		2,677	2,670
Equity accounted investments		249	233
Other receivables and investments		153	49
Derivative financial instruments		37	25
Deferred tax assets		374	557
		<b>5,161</b>	<b>5,442</b>
<b>Current assets</b>			
Inventories		1,431	1,431
Trade and other receivables		1,748	1,648
Current tax assets		68	7
Derivative financial instruments		28	19
Other financial assets	13	5	5
Cash and cash equivalents	13	421	411
		<b>3,701</b>	<b>3,521</b>
<b>Total assets</b>		<b>8,862</b>	<b>8,963</b>
<b>Liabilities</b>			
<b>Current liabilities</b>			
Borrowings	13	(38)	(64)
Derivative financial instruments		(78)	(206)
Trade and other payables		(2,333)	(2,186)
Current tax liabilities		(132)	(142)
Provisions		(80)	(71)
		<b>(2,661)</b>	<b>(2,669)</b>
<b>Non-current liabilities</b>			
Borrowings	13	(1,126)	(842)
Derivative financial instruments		(248)	(521)
Deferred tax liabilities		(184)	(227)
Trade and other payables		(485)	(427)
Provisions		(74)	(82)
Post-employment obligations	15	(1,504)	(2,033)
		<b>(3,621)</b>	<b>(4,132)</b>
<b>Total liabilities</b>		<b>(6,282)</b>	<b>(6,801)</b>
<b>Net assets</b>		<b>2,580</b>	<b>2,162</b>
<b>Shareholders' equity</b>			
Share capital		173	173
Capital redemption reserve		298	298
Share premium account		330	330
Retained earnings		1,556	981
Other reserves		184	345
Equity attributable to equity holders of the parent		<b>2,541</b>	<b>2,127</b>
Non-controlling interests		39	35
<b>Total equity</b>		<b>2,580</b>	<b>2,162</b>

## Consolidated Cash Flow Statement

For the year ended 31 December 2017

	Notes	2017 £m	2016 £m
<b>Cash flows from operating activities</b>			
Cash generated from operations	14	600	778
Interest received		8	7
Interest paid		(79)	(83)
Tax paid		(113)	(93)
Dividends received from equity accounted investments		60	57
		<b>476</b>	<b>666</b>
<b>Cash flows from investing activities</b>			
Purchase of property, plant and equipment		(442)	(416)
Receipt of government capital grants		2	6
Purchase of intangible assets		(79)	(84)
Repayment of government refundable advance		(8)	(6)
Proceeds from sale and realisation of fixed assets		8	37
Payment of deferred and contingent consideration		(2)	(1)
Acquisition of subsidiaries (net of cash acquired)		(25)	(17)
Costs associated with disposal of subsidiaries		(2)	–
Purchase of investment		–	(5)
Proceeds from disposal of subsidiary, net of cash		6	151
Equity accounted investments loan settlement		–	4
		<b>(542)</b>	<b>(331)</b>
<b>Cash flows from financing activities</b>			
Purchase of own shares by Employee Share Ownership Plan Trust		(6)	–
Purchase of non-controlling interests		–	(2)
Proceeds from exercise of share options		1	1
Proceeds from borrowing facilities		302	102
Repayment of other borrowings		(37)	(243)
Dividends paid to shareholders		(154)	(150)
Dividends paid to non-controlling interests		–	(2)
		<b>106</b>	<b>(294)</b>
<b>Movement in cash and cash equivalents</b>		<b>40</b>	<b>41</b>
Cash and cash equivalents at 1 January		385	291
Currency variations on cash and cash equivalents		(13)	53
<b>Cash and cash equivalents at 31 December</b>	14	<b>412</b>	<b>385</b>



# Notes to the News Release

For the year ended 31 December 2017

## 1 Basis of preparation

The financial information for the year ended 31 December 2017 contained in this News Release was approved by the Board on 26 February 2018. This announcement does not constitute statutory financial statements of the Company within the meaning of Section 435 of the Companies Act 2006, but is derived from those financial statements, which have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed and adopted for use by the European Union.

This information has been prepared under the historical cost method except where other measurement bases are required to be applied under IFRS, using all standards and interpretations required for financial periods beginning 1 January 2017. No standards or interpretations have been adopted before the required implementation date. Whilst the financial information included within this announcement has been prepared in accordance with the recognition and measurement criteria of IFRS, it does not comply with all disclosure requirements.

Statutory financial statements for the year ended 31 December 2016 have been delivered to the Registrar of Companies. Statutory financial statements for the year ended 31 December 2017, which have been prepared on a going concern basis, will be delivered to the Registrar of Companies following the Company's Annual General Meeting.

The auditors have reported on those financial statements. Their reports were not qualified, did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report, and did not contain a statement under Section 498 (2) or (3) of the Companies Act 2006.

## 2 Segmental analysis

### (a) Sales

	Automotive			Total £m
	Aerospace £m	Driveline £m	Powder Metallurgy £m	
<b>2017</b>				
Subsidiaries	3,556	4,652	1,174	
Equity accounted investments	82	656	–	
	<b>3,638</b>	<b>5,308</b>	<b>1,174</b>	<b>10,120</b>
Other businesses				289
Management sales				<b>10,409</b>
Less: equity accounted investments sales				<b>(738)</b>
Income statement – sales				<b>9,671</b>
<b>2016 – restated*</b>				
Subsidiaries	3,352	4,109	1,032	
Equity accounted investments	71	505	–	
	<b>3,423</b>	<b>4,614</b>	<b>1,032</b>	<b>9,069</b>
Other businesses				345
Management sales				9,414
Less: equity accounted investments sales				(592)
Income statement – sales				<b>8,822</b>

Subsidiary sales comprise £9,016 million (2016: £8,281 million) from the manufacture of product and £655 million (2016: £541 million) from the sale of services.

\* As previously announced, following disposal of its Stromag business on 30 December 2016 the Group changed its segments to remove Land Systems for reporting in 2017. The two businesses remaining in the Group that were part of Land Systems have been reported as follows: Wheels and Structures in Other Businesses and Driveshafts and Aftermarket Services, now renamed Off-Highway Powertrain, in Driveline. For the purpose of comparative information in 2016, Stromag has been included in Other Businesses. There is no change to Aerospace or Powder Metallurgy segmental reporting.

## 2 Segmental analysis (continued)

### (b) Trading profit

	Aerospace £m	Automotive		Total £m
		Driveline £m	Powder Metallurgy £m	
<b>2017</b>				
Trading profit before depreciation and amortisation	330	445	176	
Depreciation of property, plant and equipment	(92)	(151)	(49)	
Amortisation of operating intangible assets	(61)	(13)	(2)	
Trading profit – subsidiaries	177	281	125	
Trading (loss)/profit – equity accounted investments	(2)	96	–	
	175	377	125	677
Other businesses				16
Corporate and unallocated costs				(31)
Management trading profit				662
Less: equity accounted investments trading profit				(94)
Income statement – trading profit				568

During the year, the Group has recorded net charges in the trading profit of Aerospace amounting to £119 million which are set out below.

The results of the overall North American Aerospace balance sheet review (£108 million) and the initial inventory and other asset write-downs at the Alabama plant (£15 million) total £123 million. This combined charge contains inventory write-downs of £79 million, charges for onerous contracts of £18 million, re-assessment of customer recoveries and claims of £19 million and corrections to fixed asset carrying values of £7 million.

Additionally, the Aerospace trading profit has absorbed the impact of costs of £28 million associated with performance-related claims arising from a risk and revenue sharing partnership within the Engine Systems business. In the year credits amounting to £32 million arose from programme pricing adjustments; £19 million in the North American Aerostructures business and £13 million in the Engine Systems business.

As highlighted in our Trading Update in November 2017, the Driveline trading profit has borne estimated product warranty charges amounting to £10 million.

Professional fees associated with the North American Aerospace balance sheet review, £4 million, are charged in corporate and unallocated costs.

	Aerospace £m	Automotive		Total £m
		Driveline £m	Powder Metallurgy £m	
<b>2016 – restated*</b>				
Trading profit before depreciation and amortisation	464	388	164	
Depreciation of property, plant and equipment	(78)	(128)	(44)	
Amortisation of operating intangible assets	(51)	(12)	(2)	
Trading profit – subsidiaries	335	248	118	
Trading profit – equity accounted investments	4	82	–	
	339	330	118	787
Other businesses				7
Corporate and unallocated costs				(21)
Management trading profit				773
Less: equity accounted investments trading profit				(89)
Income Statement – trading profit				684

No income statement items between trading profit and profit before tax are allocated to management trading profit, which is the Group's segmental measure of profit or loss (see note 3).

During the year ended 31 December 2016, the Group recorded a charge of £39 million in trading profit in respect of a Group-wide restructuring programme. The charge arose in: Aerospace £10 million, Driveline £22 million, Powder Metallurgy £3 million, Other Businesses £2 million and Corporate costs £2 million.

### 3 Adjusted performance measures

#### (a) Reconciliation of reported and management performance measures

	2017			
	As reported £m	Equity accounted investments £m	Adjusting and non- trading items £m	Management basis £m
<b>Sales</b>	<b>9,671</b>	<b>738</b>	<b>–</b>	<b>10,409</b>
<i>Trading profit</i>	<b>568</b>	<b>94</b>	<b>–</b>	<b>662</b>
<i>Change in value of derivative and other financial instruments</i>	<b>364</b>	<b>–</b>	<b>(364)</b>	<b>–</b>
<i>Amortisation of non-operating intangible assets arising on business combinations</i>	<b>(100)</b>	<b>–</b>	<b>100</b>	<b>–</b>
<i>Gains and losses on changes in Group structure</i>	<b>(2)</b>	<b>–</b>	<b>2</b>	<b>–</b>
<i>Acquisition-related restructuring charges</i>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>
<i>Impairment charges</i>	<b>(131)</b>	<b>–</b>	<b>131</b>	<b>–</b>
<b>Operating profit</b>	<b>699</b>	<b>94</b>	<b>(131)</b>	<b>662</b>
<b>Share of post-tax earnings of equity accounted investments</b>	<b>80</b>	<b>(94)</b>	<b>–</b>	<b>(14)</b>
Interest payable	<b>(86)</b>	<b>–</b>	<b>–</b>	<b>(86)</b>
Interest receivable	<b>10</b>	<b>–</b>	<b>–</b>	<b>10</b>
Other net financing charges	<b>(45)</b>	<b>–</b>	<b>45</b>	<b>–</b>
<b>Net financing costs</b>	<b>(121)</b>	<b>–</b>	<b>45</b>	<b>(76)</b>
<b>Profit before taxation</b>	<b>658</b>	<b>–</b>	<b>(86)</b>	<b>572</b>
<b>Taxation</b>	<b>(149)</b>	<b>–</b>	<b>39</b>	<b>(110)</b>
<b>Profit after tax for the year</b>	<b>509</b>	<b>–</b>	<b>(47)</b>	<b>462</b>
Profit attributable to non-controlling interests	<b>(6)</b>	<b>–</b>	<b>–</b>	<b>(6)</b>
Profit attributable to owners of the parent	<b>503</b>	<b>–</b>	<b>(47)</b>	<b>456</b>
Earnings per share – pence	<b>29.3</b>	<b>–</b>	<b>(2.7)</b>	<b>26.6</b>
2016				
<b>Sales</b>	<b>8,822</b>	<b>592</b>	<b>–</b>	<b>9,414</b>
<i>Trading profit</i>	<b>684</b>	<b>89</b>	<b>–</b>	<b>773</b>
<i>Change in value of derivative and other financial instruments</i>	<b>(154)</b>	<b>–</b>	<b>154</b>	<b>–</b>
<i>Amortisation of non-operating intangible assets arising on business combinations</i>	<b>(103)</b>	<b>–</b>	<b>103</b>	<b>–</b>
<i>Gains and losses on changes in Group structure</i>	<b>(9)</b>	<b>–</b>	<b>9</b>	<b>–</b>
<i>Acquisition-related restructuring charges</i>	<b>(31)</b>	<b>–</b>	<b>31</b>	<b>–</b>
<i>Impairment charges</i>	<b>(52)</b>	<b>–</b>	<b>52</b>	<b>–</b>
<b>Operating profit</b>	<b>335</b>	<b>89</b>	<b>349</b>	<b>773</b>
<b>Share of post-tax earnings of equity accounted investments</b>	<b>73</b>	<b>(89)</b>	<b>–</b>	<b>(16)</b>
Interest payable	<b>(86)</b>	<b>–</b>	<b>–</b>	<b>(86)</b>
Interest receivable	<b>7</b>	<b>–</b>	<b>–</b>	<b>7</b>
Other net financing charges	<b>(37)</b>	<b>–</b>	<b>37</b>	<b>–</b>
<b>Net financing costs</b>	<b>(116)</b>	<b>–</b>	<b>37</b>	<b>(79)</b>
<b>Profit before taxation</b>	<b>292</b>	<b>–</b>	<b>386</b>	<b>678</b>
<b>Taxation</b>	<b>(48)</b>	<b>–</b>	<b>(96)</b>	<b>(144)</b>
<b>Profit after tax for the year</b>	<b>244</b>	<b>–</b>	<b>290</b>	<b>534</b>
Profit attributable to non-controlling interests	<b>(2)</b>	<b>–</b>	<b>(2)</b>	<b>(4)</b>
Profit attributable to owners of the parent	<b>242</b>	<b>–</b>	<b>288</b>	<b>530</b>
Earnings per share – pence	<b>14.1</b>	<b>–</b>	<b>16.9</b>	<b>31.0</b>

Basic and management earnings per share use a weighted average number of shares of 1,714.7 million (2016: 1,712.1 million). Also see note 7.

#### (b) Summary of management performance measures by segment

	2017			2016 – restated*		
	Sales £m	Trading profit £m	Margin	Sales £m	Trading profit £m	Margin
Aerospace	<b>3,638</b>	<b>175</b>	<b>4.8%</b>	3,423	339	9.9%
Driveline	<b>5,308</b>	<b>377</b>	<b>7.1%</b>	4,614	330	7.2%
Powder Metallurgy	<b>1,174</b>	<b>125</b>	<b>10.6%</b>	1,032	118	11.4%
Other businesses	<b>289</b>	<b>16</b>		345	7	
Corporate and unallocated costs	<b>–</b>	<b>(31)</b>		<b>–</b>	<b>(21)</b>	
	<b>10,409</b>	<b>662</b>	<b>6.4%</b>	9,414	773	8.2%

**4 Change in value of derivative and other financial instruments**

	2017 £m	2016 £m
Forward currency contracts (not hedge accounted)	364	(135)
Embedded derivatives	(6)	4
	358	(131)
Net gains and losses on intra-group funding		
Arising in year	6	(23)
	364	(154)

**5 Amortisation of non-operating intangible assets arising on business combinations**

	2017 £m	2016 £m
Marketing-related	(3)	(4)
Customer-related	(71)	(67)
Technology-based	(26)	(32)
	(100)	(103)

**6 Gains and losses on changes in Group structure**

	2017 £m	2016 £m
Business disposed	2	9
Business closures	(4)	(18)
	(2)	(9)

On 29 December 2017, the Group sold its GKN Applied Composites AB business for a cash consideration of £7 million before professional fees. The profit on sale of £3 million comprises profit on disposal of net assets including £2 million cash, with no impact from reclassification of previous currency variations from other reserves.

On 14 August 2017, the Group sold its GKN Aerospace Bandy Machining, Inc. business for a cash consideration of £1 million before professional fees. The loss on sale of £1 million comprises £5 million loss on disposal of net assets and £3 million gain from reclassification of previous currency from other reserves.

On 30 December 2016, the Group sold its Stromag business (part of the Land Systems division) to Altra Industrial Motion Corp. for cash consideration of £159 million excluding an overdraft disposed of £7 million and before professional and completion fees (£1 million). The profit on sale of £9 million comprises an £11 million profit on disposal of net assets and £2 million loss from reclassification of previous currency variations from other reserves.

On 17 November 2016, the Group confirmed the closure of its Aerospace business in Yeovil. The company previously had a contract to make airframes for the Royal Navy AW159 Wild Cat helicopters but its main customer which assembles the helicopters, announced that it was taking this contract in-house. The site closure has resulted in a further charge in 2017 of £4 million comprising: transition costs of £2 million and other associated costs of £2 million. In 2016, a reorganisation charge of £12 million was recorded, comprising: redundancy of £4 million; impairment of property, plant and equipment of £4 million; write down of inventories of £2 million; and other associated costs of £2 million. Cash flows in 2017 amounted to £7 million. There was a further decision in 2016 to curtail operations of a Driveline business with an associated reorganisation charge of £6 million comprising redundancy of £4 million and impairment of goodwill of £2 million. Redundancy cash flows in 2017 amounted to £4 million.

**7 Acquisition-related restructuring charges**

	2017 £m	2016 £m
Redundancy and other employee-related amounts	–	(27)
Integration and other expenses	–	(4)
Restructuring charges	–	(31)

In 2016, restructuring charges, separately identified, relate to the acquisition of Fokker Technologies Group B.V. business within Aerospace in 2015. The cash flows related to this totalled £13 million in 2017.

## 8 Impairment charges

	2017 £m	2016 £m
Goodwill	(72)	(38)
Other intangible assets	(2)	–
Property, plant and equipment	(57)	(14)
	<b>(131)</b>	<b>(52)</b>

Consistent with previous years, all goodwill, together with CGUs where there were indicators of impairment, was tested for impairment. An impairment charge of £131 million (2016: £52 million) has been recorded in the Income Statement as an adjusting and therefore non-trading item within the line 'impairment charges' in respect of seven CGUs all within the Aerospace division.

CGU	Impairment charge	Rationale	Remaining recoverable amount	Pre-tax discount rate	Sensitivity
Engine Products – West, North America	£88 million – Goodwill (£72 million) – Property, plant and equipment (£14 million) – Intangible assets (£2 million)	Performance in the year behind previously agreed forecasts	£32 million	10% (2016: 13%)	Most sensitive to a 5% reduction in operating cash flows, which would have increased the impairment charge by £3 million
St. Louis, North America	£24 million – Property, plant and equipment (£24 million)	Loss of key business in the year and lower than expected margins on certain contracts	£7 million	10% (2016: 13%)	Most sensitive to 5% reduction in operating cash flows, which would have increased the impairment charge by £4 million
Cincinnati, North America	£5 million – Property, plant and equipment (£5 million)	Conclusion of key programmes in 2017 and 2018, which have not been replaced, coinciding with operational issues	£0 million	10% (2016: 13%)	–
Astech, North America	£9 million – Property, plant and equipment (£9 million)	Loss of key business in the year and operational issues	£0 million	10% (2016: 13%)	–

There were further impairment charges in three other Aerospace businesses totalling £5 million, comprising only property, plant and equipment.

## 9 Net financing costs

	2017 £m	2016 £m
<b>(a) Interest payable and fee expense</b>		
Short-term bank and other borrowings	(13)	(12)
Interest on debt repayable within five years	(61)	(41)
Interest on debt repayable after five years	(6)	(27)
Government refundable advances	(6)	(6)
	<b>(86)</b>	<b>(86)</b>
Interest receivable		
Short-term investments, loans and deposits	4	7
Tax case interest recoveries (see note 6)	6	–
	<b>10</b>	<b>7</b>
<b>Net interest payable and receivable</b>	<b>(76)</b>	<b>(79)</b>

Short-term bank and other borrowings includes a finance cost of £7 million (2016: £5 million) for factoring and customer supply chain finance programmes.

	2017 £m	2016 £m
<b>(b) Other net financing charges</b>		
Interest charge on net defined benefit plans	(47)	(53)
Fair value changes on cross currency interest rate swaps	4	18
Unwind of discounts	(2)	(2)
	<b>(45)</b>	<b>(37)</b>

## 10 Taxation

### (a) Tax expense

	2017 £m	2016 £m
<b>Analysis of charge in year</b>		
Current tax (charge)/credit		
Current year charge	(113)	(67)
Utilisation of previously unrecognised tax losses and other assets	–	1
Net movement on provisions for uncertain tax positions	30	9
Adjustments in respect of prior years	–	9
	<b>(83)</b>	<b>(48)</b>
Deferred tax (charge)/credit		
Origination and reversal of temporary differences	52	–
Tax on change in value of derivative financial instruments	(79)	14
Other changes in unrecognised deferred tax assets	(51)	(3)
Adjustments in respect of prior years	12	(11)
	<b>(66)</b>	<b>–</b>
<b>Total tax charge for the year</b>	<b>(149)</b>	<b>(48)</b>

Analysed as:

	2017 £m	2016 £m
<b>Tax in respect of management profit</b>		
Current tax	(72)	(40)
Deferred tax	(38)	(104)
	<b>(110)</b>	<b>(144)</b>
<b>Tax in respect of items excluded from management profit</b>		
Current tax	(11)	(8)
Deferred tax	(28)	104
	<b>(39)</b>	<b>96</b>
<b>Total for tax charge for the year</b>	<b>(149)</b>	<b>(48)</b>

#### Book tax rate

The net movement on provisions for uncertain tax positions of £30 million principally follows successful resolution of disputes in Italy and a release of the provision created in 2015 against the use of previously unrecognised tax losses, partially offset by an increase in provisions for issues currently being audited by the tax authorities.

#### Management tax rate

The tax charge arising on management profit before tax less the share of post tax earnings of EAI of £492 million (2016: £605 million) was £110 million (2016: £144 million) giving an effective tax rate of 22% (2016: 24%).

	2017		2016	
<b>Tax reconciliation</b>	£m	%	£m	%
Profit before taxation	658		292	
Less share of post-tax earnings of equity accounted investments	(80)		(73)	
Profit before taxation excluding equity accounted investments	578		219	
Tax charge calculated at 19.25% (2016: 20%) standard UK corporate tax rate	(111)	(19)	(44)	(20)
Differences between UK and overseas corporate tax rates	(16)	(3)	(30)	(13)
Non-deductible and non-taxable items	(16)	(3)	36	16
Recognition of previously unrecognised tax losses	–	–	–	–
Utilisation of previously unrecognised tax losses and other assets	1	–	1	–
Changes in tax rates	6	1	(17)	(8)
Other changes in deferred tax assets	(55)	(9)	(1)	–
Tax charge before prior year and adjustment and movement in uncertain tax positions	(191)	(33)	(55)	(25)
Net movement on provision for uncertain tax positions	30	5	9	4
Adjustments in respect of prior years	12	2	(2)	(1)
<b>Total tax charge for the year</b>	<b>(149)</b>	<b>(26)</b>	<b>(48)</b>	<b>(22)</b>

## 10 Taxation (continued)

### (b) Tax included in other comprehensive income

	2017 £m	2016 £m
<b>Analysis of (charge)/credit in year</b>		
Deferred tax on post-employment obligations	(89)	60
Deferred tax on hedged foreign currency gains and losses	(12)	39
Deferred tax on other foreign currency gains and losses on intra-group funding	–	(3)
Current tax on post-employment obligations	25	3
Current tax on foreign currency gains and losses on intra-group funding	15	(50)
	<b>(61)</b>	<b>49</b>

### (c) Recognised deferred tax

The movements in deferred tax assets and liabilities (prior to the offsetting of balances within the same jurisdiction as permitted by IAS 12) during the year are shown below:

	Assets			Liabilities		
	Post-employment obligations	Tax losses	Other	Fixed assets	Other	Total
	£m	£m	£m	£m	£m	£m
<b>At 1 January 2017</b>	<b>325</b>	<b>177</b>	<b>229</b>	<b>(391)</b>	<b>(10)</b>	<b>330</b>
Businesses disposed	–	–	–	–	–	–
Included in the income statement	1	(60)	(75)	63	5	(66)
Included in other comprehensive income	(89)	–	(12)	–	–	(101)
Currency variations	3	7	(6)	23	–	27
<b>At 31 December 2017</b>	<b>240</b>	<b>124</b>	<b>136</b>	<b>(305)</b>	<b>(5)</b>	<b>190</b>
At 1 January 2016	245	176	157	(339)	(8)	231
Businesses disposed	(1)	1	(1)	15	–	14
Included in the income statement	(2)	(19)	18	5	(2)	–
Included in other comprehensive income	60	–	36	–	–	96
Currency variations	23	19	19	(72)	–	(11)
At 31 December 2016	325	177	229	(391)	(10)	330

## 11 Earnings per share

	2017			2016		
	Earnings £m	Weighted average number of shares million	Earnings per share pence	Earnings £m	Weighted average number of shares million	Earnings per share pence
Basic	503	1,714.7	29.3	242	1,712.1	14.1
Dilutive securities	–	13.5	(0.2)	–	13.9	(0.1)
<b>Diluted</b>	<b>503</b>	<b>1,728.2</b>	<b>29.1</b>	<b>242</b>	<b>1,726.0</b>	<b>14.0</b>

Management basis earnings per share of 26.6p (2016: 31.0p) is presented in note 3 and uses the weighted average number of shares consistent with basic earnings per share calculations. The diluted management basis earnings per share is 26.4p (2016: 30.7p).

## 12 Dividends

	Paid or proposed in respect of		Recognised		
	2017 pence	2016 pence	2018 £m	2017 £m	2016 £m
2015 final dividend paid	–	–	–	–	99
2016 interim dividend paid	–	2.95	–	–	51
2016 final dividend paid	–	5.9	–	101	–
2017 interim dividend paid	3.1	–	–	53	–
2017 final dividend proposed	6.2	–	106	–	–
	<b>9.3</b>	<b>8.85</b>	<b>106</b>	<b>154</b>	<b>150</b>

The 2017 final proposed dividend will be paid on 14 May 2018 to shareholders who are on the register of members at close of business on 6 April 2018.

### 13 Net borrowings

#### (a) Analysis of net borrowings

	Current	Non-current			Total	
	Within one year	One to two years	Two to five years	More than five years	Total	
	£m	£m	£m	£m	£m	£m
<b>2017</b>						
Unsecured capital market borrowings						
£450 million 5¼% 2022 unsecured bond	–	–	(447)	–	(447)	(447)
£350 million 6¾% 2019 unsecured bond	–	(349)	–	–	(349)	(349)
£300 million 3¾% 2032 unsecured bond	–	–	–	(296)	(296)	(296)
Unsecured committed bank borrowings						
European Investment Bank	(16)	(16)	–	–	(16)	(32)
2019 Committed Revolving Credit Facility	–	–	–	–	–	–
Other (net of unamortised issue costs)	(2)	(2)	(6)	(2)	(10)	(12)
Finance lease obligations	(1)	(1)	(3)	(4)	(8)	(9)
Bank overdrafts	(9)	–	–	–	–	(9)
Other short-term bank borrowings	(10)	–	–	–	–	(10)
<b>Borrowings</b>	<b>(38)</b>	<b>(368)</b>	<b>(456)</b>	<b>(302)</b>	<b>(1,126)</b>	<b>(1,164)</b>
Bank balances and cash	257	–	–	–	–	257
Short-term bank deposits	164	–	–	–	–	164
<b>Cash and cash equivalents</b>	<b>421</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>421</b>
Other financial assets – bank deposits	5	–	–	–	–	5
<b>Net borrowings (excluding cross currency interest rate swaps)</b>	<b>388</b>	<b>(368)</b>	<b>(456)</b>	<b>(302)</b>	<b>(1,126)</b>	<b>(738)</b>
Cross currency interest rate swaps	–	(76)	(75)	–	(151)	(151)
<b>Net debt</b>	<b>388</b>	<b>(444)</b>	<b>(531)</b>	<b>(302)</b>	<b>(1,277)</b>	<b>(889)</b>
<b>2016</b>						
Unsecured capital market borrowings						
£450 million 5¼% 2022 unsecured bond	–	–	–	(446)	(446)	(446)
£350 million 6¾% 2019 unsecured bond	–	–	(349)	–	(349)	(349)
Unsecured committed bank borrowings						
European Investment Bank	(16)	(16)	(16)	–	(32)	(48)
2019 Committed Revolving Credit Facility	–	–	–	–	–	–
Other (net of unamortised issue costs)	–	(2)	(7)	(4)	(13)	(13)
Finance lease obligations	(1)	–	–	(2)	(2)	(3)
Bank overdrafts	(26)	–	–	–	–	(26)
Other short-term bank borrowings	(21)	–	–	–	–	(21)
<b>Borrowings</b>	<b>(64)</b>	<b>(18)</b>	<b>(372)</b>	<b>(452)</b>	<b>(842)</b>	<b>(906)</b>
Bank balances and cash	236	–	–	–	–	236
Short-term bank deposits	175	–	–	–	–	175
Cash and cash equivalents	411	–	–	–	–	411
Other financial assets – bank deposits	5	–	–	–	–	5
<b>Net borrowings (excluding cross currency interest rate swaps)</b>	<b>352</b>	<b>(18)</b>	<b>(372)</b>	<b>(452)</b>	<b>(842)</b>	<b>(490)</b>
Cross currency interest rate swaps	–	–	(122)	(92)	(214)	(214)
<b>Net debt</b>	<b>352</b>	<b>(18)</b>	<b>(494)</b>	<b>(544)</b>	<b>(1,056)</b>	<b>(704)</b>

Unsecured capital market borrowings include: an unsecured £350 million (2016: £350 million) 6¾% bond maturing in 2019 less unamortised issue costs of £1 million (2016: £1 million) and an unsecured £450 million (2016: £450 million) 5¼% bond maturing in 2022 less unamortised issue costs of £3 million (2016: £4 million) and a new unsecured £300 million 3¾% bond maturing in 2032 less unamortised issue costs of £4 million.

Unsecured committed bank borrowings include £32 million (2016: £48 million) drawn under the Group's European Investment Bank (EIB) unsecured facility which attracts a fixed interest rate of 4.1% per annum payable annually in arrears and a borrowing of £12 million (2016: £15 million) drawn against a KfW amortising unsecured facility which attracts a fixed interest rate of 1.65%. On 22 June 2017, the Group repaid the third of five annual instalments of £16 million on the EIB facility. There were no drawings (2016: nil) at the year end against the Group's 2019 Committed Revolving Credit Facilities of £800 million (2016: £800 million). Unamortised issue costs on the 2019 Committed Revolving Credit Facilities were £2 million (2016: £3 million).



14 **Cash flow reconciliations**

	2017	2016
	£m	£m
<b>Cash generated from operations</b>	<b>699</b>	<b>335</b>
Operating profit	699	335
Adjustments for:		
Depreciation, impairment and amortisation of fixed assets		
Charged to trading profit		
Depreciation	302	263
Amortisation	78	67
Amortisation of non-operating intangible assets arising on business combinations	100	103
Impairment charges	131	52
Change in value of derivative and other financial instruments	(364)	154
Gains and losses on changes in Group structure	2	9
Amortisation of government capital grants	(2)	(2)
Net profits on sale and realisation of fixed assets	(2)	(3)
Charge for share-based payments	4	5
Movement in post-employment obligations	(300)	(75)
Change in inventories	(57)	(78)
Change in receivables	(258)	(151)
Change in payables and provisions	267	99
	<b>600</b>	<b>778</b>
<b>Movement in net debt</b>		
Movement in cash and cash equivalents	40	41
Net movement in other borrowings and deposits	(268)	141
Movement on finance leases	(6)	–
Movement on cross currency interest rate swaps	63	(145)
Movement on other net investment hedges	1	(17)
Amortisation of debt issue costs	(2)	(2)
Currency variations	(13)	47
Movement in year	(185)	65
Net debt at beginning of year	(704)	(769)
<b>Net debt at end of year</b>	<b>(889)</b>	<b>(704)</b>
<b>Reconciliation of cash and cash equivalents</b>		
Cash and cash equivalents per balance sheet	421	411
Bank overdrafts included within 'current liabilities – borrowings'	(9)	(26)
<b>Cash and cash equivalents per cash flow</b>	<b>412</b>	<b>385</b>

	At 1 January	Cash	Non-cash movements				At 31
	2017	flows	Acquisition	Currency	Fair value	Lease	December
			and disposals	movements	changes	movements	2017
Long-term borrowings	(840)	(278)	–	–	–	–	(1,118)
Short-term borrowings	(63)	29	(3)	–	–	–	(37)
Lease liabilities	(3)	–	–	–	–	(6)	(9)
Cross currency interest rate swaps	(214)	–	–	–	63	–	(151)
<b>Total liabilities from financing activities</b>	<b>(1,120)</b>	<b>(249)</b>	<b>(3)</b>	<b>–</b>	<b>63</b>	<b>(6)</b>	<b>(1,315)</b>
Cash and cash equivalents	411	21	2	(13)	–	–	421
Other financial assets – bank deposits	5	–	–	–	–	–	5
<b>Net debt</b>	<b>(704)</b>	<b>(228)</b>	<b>(1)</b>	<b>(13)</b>	<b>63</b>	<b>(6)</b>	<b>(889)</b>

## 15 Post-employment obligations

		2017 £m	2016 £m
Post-employment obligations as at the year end comprise:			
Pensions	– funded	(743)	(1,285)
	– unfunded	(675)	(662)
Medical	– funded	(39)	(37)
	– unfunded	(47)	(49)
		<b>(1,504)</b>	<b>(2,033)</b>

The Group's pension arrangements comprise various defined benefit and defined contribution schemes throughout the world. In addition, in the US and UK various plans operate which provide members with post-retirement medical benefits. The Group's post-employment plans in the UK, US and Germany together account for 98% of plan assets and 98% of plan liabilities.

The Group's post-employment plans include both funded and unfunded arrangements. The UK pension schemes are funded, albeit in deficit in common with many other UK pension schemes, with the scheme assets held in trustee-administered funds. The German and other European plans are generally unfunded, with pension payments made from company funds as they fall due, rather than from scheme assets. The US schemes include a combination of funded and unfunded pension and medical plans, while Japan also operates a funded pension plan.

The Group's defined benefit pension arrangements provide benefits to members in the form of an assured level of pension payable for life. The level of benefits provided typically depends on length of service and salary levels in the years leading up to retirement. In the UK and Germany, pensions in payment are generally updated in line with inflation, whereas in the US pensions generally do not receive inflationary increases once in payment. The UK and German schemes are closed to new entrants, while the US schemes are closed to future accrual.

Independent actuarial valuations of all major defined benefit scheme assets and liabilities were carried out at 31 December 2017. The present value of the defined benefit obligation and the related service cost elements were measured using the projected unit credit method.

### (a) Defined benefit schemes – assumptions and estimates

Estimating the post-employment obligation involves a number of significant assumptions, which are detailed below.

#### Key assumptions and estimates:

	UK		Americas %	Europe %	ROW %
	GKN2 %	GKN3 %			
<b>2017</b>					
Rate of increase in pensionable salaries (past service)	n/a	n/a	n/a	2.50	–
Rate of increase in payment and deferred pensions	3.00	3.00	n/a	1.75	n/a
Discount rate (past service)	2.60	2.40	3.60	1.70	0.50
Inflation assumption (past service)	3.20	3.15	n/a	1.75	n/a
Rate of increase in medical costs:					
Initial/long-term	5.4/5.4		6.5/5.0	n/a	n/a
<b>2016</b>					
Rate of increase in pensionable salaries (past/future service)	4.30/4.25	n/a	n/a	2.50	–
Rate of increase in payment and deferred pensions	3.20	3.30	n/a	1.75	n/a
Discount rate (past/future service)	2.60/2.70	2.45	4.10	1.60	0.50
Inflation assumption (past/future service)	3.30/3.25	3.35	n/a	1.75	n/a
Rate of increase in medical costs:					
Initial/long-term	5.4/5.4		6.75/5.0	n/a	n/a

In prior years, there were separate assumptions for past and future service in relation to the UK pension scheme. However, following the closure of GKN2 to future accrual from 1 July 2017, this is no longer relevant.

The UK schemes each use a duration-specific discount rate derived from the LCP Treasury Model, which is based on corporate bonds with two or more AA-ratings. The European discount rate was calculated with reference to Aon Hewitt's German discount rate yield curve. For the US, the discount rate referenced the Citigroup intermediate pension liability index, the Merrill Lynch US corporate AA 10+ years index and the Towers Watson Rate:LINK benchmark. The approach taken in Europe and the US is consistent with the prior year.

The underlying mortality assumptions for the major schemes, are as follows:

#### UK

The key current year mortality assumptions for both GKN2 and GKN3 use S2PA year of birth mortality tables (adjusted for GKN experience) with CMI 2016 improvements and a 1.25% per annum long-term improvement trend. These assumptions give the following expectations for each scheme: for GKN3 a male aged 65 lives for a further 22.0 years and a female aged 65 lives for a further 24.6 years, while a male aged 40 is expected to live a further 24.8 years from age 65 and a female aged 40 is expected to live a further 26.5 years from age 65. For GKN2 a male aged 65 lives for a further 22.3 years and a female aged 65 lives for a further 25.1 years, while a male aged 40 is expected to live a further 24.2 years from age 65 and a female aged 40 is expected to live a further 27.0 years from age 65.

#### Overseas

In the US, RP-2014 tables have been used, while in Germany the RT2005-G tables have been used. In the US, the longevity assumption for a male aged 65 is that he lives a further 20.7 years (female 22.7 years), while in Germany a male aged 65 lives for a further 19.1 years (female 23.2 years). The longevity assumption for a US male currently aged 45 is that he also lives for a further 22.3 years once attaining 65 years (female 24.2 years), with the German equivalent assumption for a male being 21.8 years (female 25.7 years). These assumptions are based on the prescribed tables, rather than GKN experience.

## 15 Post-employment obligations (continued)

### Assumption sensitivity analysis

The impact of a one percentage point movement in the primary assumptions (longevity: 1 year) on the defined benefit obligations as at 31 December 2017 is set out below:

	UK	Americas	Europe	ROW
	Liabilities	Liabilities	Liabilities	Liabilities
	£m	£m	£m	£m
Discount rate +1%	478	39	102	2
Discount rate -1%	(622)	(48)	(132)	(1)
Rate of inflation +1%	(525)	(1)	(89)	—
Rate of inflation -1%	407	—	74	—
Life expectancy +1 year	(122)	(10)	(25)	—
Life expectancy -1 year	124	10	23	—
Health cost trend +1%	(2)	(2)	—	—
Health cost trend -1%	2	1	—	—

### Pension partnership interest

During the year, the Group has paid £30 million (2016: £30 million) to the UK pension schemes through its pension partnership arrangement and this is included within the amount of contributions/benefits paid.

### Funding update and closure of GKN2 to future accrual

During the year, the Group's two UK defined benefit pension schemes completed their triennial funding valuations as at 5 April 2016 for GKN2 and 31 December 2016 for GKN3.

The outcome of these discussions resulted in a lump sum contribution of £250 million paid in October 2017 to GKN2, and annual contributions of £6 million until 2022 to GKN3. These contributions along with investment outperformance is expected to close the deficits on the Trustee's funding basis by April 2022 for GKN3 and June 2031 for GKN2.

During the year, a decision was also taken to close GKN2 to future accrual and following a consultation process with the scheme members, the closure took place effective 30 June 2017. UK pension benefits are now provided on a defined contribution basis.

## (b) Defined benefit schemes – reporting

The amounts included in operating profit are:

	2017 £m	2016 £m
Current service cost and administrative expenses	(43)	(51)
Settlements/curtailments	—	5
	(43)	(46)

The amounts recognised in the balance sheet are:

	2017					2016
	UK £m	Americas £m	Europe £m	ROW £m	Total £m	£m
Present value of unfunded obligations	(16)	(40)	(662)	(4)	(722)	(711)
Present value of funded obligations	(3,293)	(321)	(38)	(31)	(3,683)	(3,902)
Fair value of plan assets	2,618	224	34	25	2,901	2,580
Net obligations recognised in the balance sheet	(691)	(137)	(666)	(10)	(1,504)	(2,033)

The triennial funding valuations for the UK defined benefit pension schemes were completed during the year. Following the completion of these valuations, in order to fund the deficits, the Company agreed to make a lump sum contribution of £250 million to GKN2 and annual contributions of £6 million to GKN3 until 2022 in addition to the distributions from the UK pension partnership.

The contribution for deficit funding expected to be paid by the Group during 2018 to the UK schemes is £6 million. In addition, a distribution of £30 million is expected to be made from the UK pension partnership to GKN2 in the first half of 2018, which brings the total expected UK cash requirement for 2018 to £36 million. The expected 2018 contribution to overseas schemes is £35 million.

Cumulative remeasurement of defined benefit plan differences recognised in equity are as follows:

	2017 £m	2016 £m
At 1 January	(1,469)	(1,073)
Remeasurement of defined benefit plans	291	(396)
At 31 December	(1,178)	(1,469)

**Movement in schemes' obligations (funded and unfunded) during the year**

	UK £m	Americas £m	Europe £m	ROW £m	Total £m
<b>At 1 January 2017</b>	<b>(3,514)</b>	<b>(375)</b>	<b>(688)</b>	<b>(36)</b>	<b>(4,613)</b>
Current service cost	(24)	(1)	(11)	(2)	(38)
Employee contributions	–	(1)	–	–	(1)
Administrative expenses	(4)	(1)	–	–	(5)
Interest	(89)	(15)	(11)	–	(115)
Remeasurement of defined benefit plans	174	(22)	13	–	165
Benefits and administrative expenses paid	148	21	27	2	198
Currency variations	–	33	(30)	1	4
<b>At 31 December 2017</b>	<b>(3,309)</b>	<b>(361)</b>	<b>(700)</b>	<b>(35)</b>	<b>(4,405)</b>
At 1 January 2016	(3,234)	(319)	(531)	(34)	(4,118)
Current service cost	(35)	(1)	(9)	(3)	(48)
Businesses disposed	–	–	12	–	12
Settlements and curtailments	268	–	2	–	270
Administrative expenses	(3)	–	–	–	(3)
Interest	(119)	(15)	(13)	–	(147)
Remeasurement of defined benefit plans	(540)	5	(82)	5	(612)
Benefits and administrative expenses paid	149	17	22	3	191
Currency variations	–	(62)	(89)	(7)	(158)
At 31 December 2016	(3,514)	(375)	(688)	(36)	(4,613)

**Movement in schemes' assets during the year**

	UK £m	Americas £m	Europe £m	ROW £m	Total £m
<b>At 1 January 2017</b>	<b>2,293</b>	<b>227</b>	<b>37</b>	<b>23</b>	<b>2,580</b>
Interest	58	9	1	–	68
Employee contributions	–	1	–	–	1
Remeasurement of defined benefit plans	102	21	–	3	126
Contributions by Group	308	7	–	2	317
Benefits paid	(143)	(21)	(5)	(2)	(171)
Currency variations	–	(20)	1	(1)	(20)
<b>At 31 December 2017</b>	<b>2,618</b>	<b>224</b>	<b>34</b>	<b>25</b>	<b>2,901</b>
At 1 January 2016	2,322	186	33	19	2,560
Interest	85	8	1	–	94
Settlements and curtailments	(263)	–	(2)	–	(265)
Businesses disposed	–	–	(1)	–	(1)
Remeasurement of defined benefit plans	207	7	2	–	216
Contributions by Group	87	6	1	2	96
Benefits paid	(145)	(17)	(2)	(2)	(166)
Currency variations	–	37	5	4	46
At 31 December 2016	2,293	227	37	23	2,580

Remeasurement gains and losses in relation to schemes' obligations are as follows

	UK £m	Americas £m	Europe £m	ROW £m	Total £m
<b>2017</b>					
Experience gains and losses	10	(3)	4	–	11
Changes in financial assumptions	64	(20)	9	–	53
Change in demographic assumptions	100	1	–	–	101
	<b>174</b>	<b>(22)</b>	<b>13</b>	<b>–</b>	<b>165</b>
<b>2016</b>					
Experience gains and losses	210	6	1	–	217
Changes in financial assumptions	(715)	(8)	(83)	5	(801)
Change in demographic assumptions	(35)	7	–	–	(28)
	<b>(540)</b>	<b>5</b>	<b>(82)</b>	<b>5</b>	<b>(612)</b>

## 15 Post-employment obligations (continued)

The fair values of the assets in the schemes were:

	UK £m	Americas £m	Europe £m	ROW £m	Total £m
<b>At 31 December 2017</b>					
Equities (including hedge funds)	507	106	–	14	627
Diversified growth funds	824	–	–	–	824
Bonds – government	464	50	–	–	514
Bonds – corporate	315	62	–	8	385
Property	127	–	–	–	127
Cash, derivatives and net current assets	214	6	–	–	220
Other assets	167	–	34	3	204
	<b>2,618</b>	<b>224</b>	<b>34</b>	<b>25</b>	<b>2,901</b>
<b>At 31 December 2016</b>					
Equities (including hedge funds)	607	107	–	12	726
Diversified growth funds	558	–	–	–	558
Bonds – government	540	53	–	9	602
Bonds – corporate	245	63	–	–	308
Property	138	–	–	–	138
Cash, derivatives and net current assets	23	4	–	–	27
Other assets	182	–	37	2	221
	<b>2,293</b>	<b>227</b>	<b>37</b>	<b>23</b>	<b>2,580</b>

### (c) Defined contribution schemes

The Group operates a number of defined contribution schemes. The charge to the income statement in the year was £84 million (2016: £62 million).

## 16 Contingent liabilities

Aside from an unrecognised contingent asset in respect of Franked Investment Income, related to advance corporate tax payments and corporate tax paid on certain foreign dividends, there were no other material contingent assets at 31 December 2017 or 31 December 2016.

There is a known risk that future delivery schedule commitments, negotiated as part of the performance related claims settlement noted in note 2(b), may not be met and as such further penalties be levied on the risk and revenue sharing partnership. The Group's programme share of these potential penalties is not reliably quantifiable.

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